TELEFONICA BRASIL S.A.
Form 6-K
March 28, 2014

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 6-K

REPORT OF FOREIGN PRIVATE ISSUER PURSUANT TO RULE 13a-16 OR 15d-16 UNDER THE SECURITIES EXCHANGE ACT OF 1934

For the month of March, 2014

Commission File Number: 001-14475

TELEFÔNICA BRASIL S.A.

(Exact name of registrant as specified in its charter)

TELEFONICA BRAZIL S.A.

(Translation of registrant's name into English)

Av. Eng° Luís Carlos Berrini, 1376 - 28º andar

São Paulo, S.P.

Federative Republic of Brazil

(Address of principal executive office)

Indicate by check mark whether the registrant files or will file annual reports under cover of Form 20-F or Form 40-F:

Form 20-F	X	Form 40-F	

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(1):

Yes		No	X

Indicate by check mark if the registrant is submitting the Form 6-K in paper as permitted by Regulation S-T Rule 101(b)(7):

Yes		No	X

TELEFÔNICA BRASIL S.A.

QUARTERLY INFORMATION

DECEMBER 31, 2013

INDEPENDENT AUDITORS' REPORT

ON THE FINANCIAL STATEMENTS

To the Shareholders and Management of

TELEFÔNICA BRASIL S.A.

São Paulo - SP

We have examined the individual and consolidated financial statements of **TELEFÔNICA BRASIL S.A.**, identified as Parent Company and Consolidated, respectively, which comprises the balance sheet as at December 31, 2013 and the respective statement of income, of comprehensive income, of changes in shareholders' equity and of cash flows for the period then ended, as well as a summary of the main accounting practices and other notes.

Management's responsibility on the financial statements

The Entity's management is responsible for the preparation and adequate presentation of the individual financial statements in accordance with the accounting practices adopted in Brazil and the consolidated financial statements in accordance with the International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board – IASB, and in accordance with the accounting practices adopted in Brazil, as well as for the internal controls it has determined as necessary to allow the preparation of financial statements free of material misstatements caused by fraud or error.

Responsibility of the Independent Auditors

Our responsibility is to issue an opinion on these financial statements based on our audit, conducted in accordance with Brazilian and international accounting standards. Those standards require that ethical demands are met and that the audit be planned and executed to obtain reasonable assurance that the financial statements are free of material misstatement.

An audit involves the execution of selected procedures to obtain evidence related to the amounts and disclosures presented in the financial statements. The selected procedures depend on the auditor's professional judgment, including the assessment of risks of material misstatement in the financial statement caused by fraud or error. In this risk assessment, the auditor considers the internal controls which are relevant to the preparation and adequate presentation of the financial statements of the Association to plan the audit procedures appropriate to the circumstances, but not to express an opinion on the effectiveness of the Association's internal controls. An audit also includes the assessment of adequacy of the accounting practices used and the reasonableness of the accounting estimates made by the management, as well as the evaluation of the presentation of the financial statements made as a group.

We believe that the audit evidence obtained is sufficient and appropriate to base our opinion.

Opinion on the individual financial statements

In our opinion, the individual financial statements referred to above adequately present, in all relevant aspects, the financial position of **TELEFÔNICA BRASIL S.A.** as at December 31, 2013, the performance of its operations and cash flows for the year then ended, in accordance with the accounting practices adopted in Brazil.

Opinion on the consolidated financial statements

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In our opinion, the consolidated financial statements referred to above adequately present, in all relevant aspects, the consolidated financial position of **TELEFÔNICA BRASIL S.A.** as at December 31, 2013, the consolidated performance of its operations and cash flows for the year then ended, in accordance with the international financial reporting standards (IFRS) issued by the International Accounting Standards Board – IASB and accounting practices adopted in Brazil.

Emphases

Investments Evaluation

According to note 2, the individual financial statements were prepared according to the accounting practices adopted in Brazil. In the case of **TELEFÔNICA BRASIL S.A.**, these practices differ from IFRSs, applicable to the separate financial statements, solely referring to the evaluation of investments in subsidiaries and joint subsidiaries by the equity method, however, for IFRS purposes, they would be evaluated at cost or fair value. Our opinion is not with exception due to this matter.

Restatement of corresponding amounts

As mentioned in Note 2, as a consequence of a change in the accounting practice introduced by the adoption of IFRS 11, the consolidated balance sheet referring to the year ended on December 31, 2012 and the respective consolidated statements of income, of comprehensive income, of changes in shareholders’ equity and of cash flows, for the year then ended, presented for comparison purposes, were adjusted and are being restated in accordance with CPC 23 – Accounting Policies, Changes in Estimates and Correction of Error and CPC 26 (R1) – Presentation of the Financial Statements. Our opinion is not changed regarding this matter.

Other Matters

Statement of Value Added

We have also examined the individual and consolidated statement of value added (SVA), referring to the period ended December 31, 2013, prepared under the Company’s management responsibility, the presentation of which is required according to the Brazilian corporate law for listed companies, and, as supplementary information by the IFRSs, which do not require the presentation of the SVA. These statements were submitted to the same audit procedures previously described and, in our opinion, they are adequately presented, in all material aspects, in relation to the financial statements as a whole.

São Paulo, 25 February 2014.

CRC Nº 2SP013002/O-3

Clóvis Ailton Madeira

CTCRC Nº 1SP106895/O-1 "S"

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TELEFÔNICA BRASIL S. A.
Balance sheets
At December 31, 2013, 2012 and january 1st, 2012
(In thousands of reais)

		Company		**Consolidated**					**Co**
ASSETS	**Note**	**12.31.13**	**12.31.12**	**12.31.13**	**12.31.12** restated	**1.1.12**	**LIABILITIES AND EQUITY**	**Note**	**12.31.1**
CURRENT ASSETS		**15,632,730**	**6,515,094**	**15,936,633**	**16,209,181**	**11,759,744**	**CURRENT LIABILITIES**		**13,862,2**
Cash and cash equivalents	5	6,311,299	3,079,282	6,543,936	7,133,485	2,889,543	Personnel, social charges and benefits	15	427,0
Trade accounts receivable, net	6	5,541,023	2,150,724	5,802,859	5,546,938	5,128,142	Trade accounts payable	16	6,948,9
Inventories	7	469,586	24,403	505,615	387,809	471,721	Taxes, charges and contributions	17	1,269,1
Taxes recoverable	8.1	2,168,797	602,328	2,191,962	2,052,421	2,495,065	Loans, financing and lease	18.1	1,236,7
Judicial deposits and garnishments	9	204,165	-	204,165	126,625	116,421	Debentures	18.2	286,9
Derivative transactions	36	89,499	39,197	89,499	41,109	1,840	Dividend and interest on equity	19	1,187,5
Prepaid expenses	10	254,743	26,610	257,286	248,337	255,056	Provisions	20	561,4
Dividend and interest on equity	19	60,346	394,105	1,140	1,140	772	Derivative transactions	36	44,4
Other assets	11	533,272	198,445	340,171	671,317	401,184	Deferred revenue	21	812,8
							Payable from reverse split of fractional shares		389,2
NONCURRENT ASSETS		**53,982,379**	**51,067,347**	**53,604,442**	**54,041,911**	**53,728,817**	Authorization license		95,7
Short-term investments pledged as collateral	5	106,239	23,920	106,455	109,708	124,668	Other liabilities	22	602,1

Trade accounts receivable, net	6	160,478	-	257,086	93,378	84,855			
Taxes recoverable	8.1	368,388	549,225	368,388	738,965	1,014,959	**NONCURRENT LIABILITIES**		**12,858,37**
Deferred taxes	8.2	-	-	210,294	1,027,888	1,427,499	Personnel, social charges and benefits	15	18,69
Judicial deposits and garnishments	9	4,123,584	3,068,256	4,148,355	3,909,268	3,374,490	Taxes, charges and contributions	17	52,25
Derivative transactions	36	329,652	21,465	329,652	286,278	225,935	Deferred taxes	8.2	722,63
Prepaid expenses	10	24,879	16,720	25,364	31,396	32,138	Loans, financing and lease	18.1	3,215,15
Other assets	11	127,567	75,587	127,793	92,308	96,049	Debentures	18.2	4,014,68
Investments	12	**11,089,918**	**21,561,061**	**86,349**	**142,881**	**152,256**	Provisions	20	4,042,78
Property, plant and equipment, net	13	**18,377,905**	**10,020,263**	**18,441,647**	**17,604,144**	**17,146,521**	Derivative transactions	36	24,80
Intangible assets, net	14	**19,273,769**	**15,730,850**	**29,503,059**	**30,005,697**	**30,049,447**	Deferred revenue	21	252,35
							Liabilities for post-retirement benefit plans	35	370,35
							Other liabilities	22	144,65
							TOTAL EQUITY		**42,894,44**
							EQUITY		**42,894,44**
							Capital	23	37,798,1
							Capital reserves	23	2,686,89
							Income reserves	23	1,287,49
							Bonus on acquisition of interest from non-controlling shareholders	23	(70,44
							Other comprehensive income	23	16,84
							Additional dividend proposed	23	1,175,53
							Non-controlling interest		

TOTAL ASSETS	**69,615,109**	**57,582,441**	**69,541,075**	**70,251,092**	**65,488,561**	**TOTAL LIABILITIES AND EQUITY**	**69,615,1**

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TELEFÔNICA BRASIL S. A.
Income statements
Years ended December 31, 2013 and 2012
(In thousands of reais)

		Company		Consolidated	
	Note	**2013**	**2012**	**2013**	**2012** restated
NET OPERATING REVENUE	24	**23,189,261**	**12,883,541**	**34,721,897**	**33,919,656**
Cost of sales	25	(12,452,247)	(7,716,553)	(17,542,167)	(16,557,444)
GROSS PROFIT		**10,737,014**	**5,166,988**	**17,179,730**	**17,362,212**
OPERATING INCOME (EXPENSES)		**(6,421,993)**	**(122,127)**	**(12,302,606)**	**(10,150,704)**
Selling expenses	26	(6,591,404)	(3,094,834)	(9,686,170)	(8,693,696)
General and administrative expenses	27	(1,313,365)	(695,824)	(2,177,891)	(2,145,308)
Equity pickup	12	1,913,508	3,995,228	(55,150)	588
Other operating income (expenses), net	28	(430,732)	(326,697)	(383,395)	687,712
OPERATING INCOME BEFORE FINANCIAL INCOME (EXPENSES)		**4,315,021**	**5,044,861**	**4,877,124**	**7,211,508**
Financial income	29	1,243,109	534,786	1,748,277	1,281,105
Financial expenses	29	(1,512,178)	(677,478)	(1,963,037)	(1,572,369)
INCOME BEFORE TAXES		**4,045,952**	**4,902,169**	**4,662,364**	**6,920,244**
Income and social contribution taxes	30	(330,007)	(448,596)	(946,419)	(2,468,063)
NET INCOME FOR THE YEAR		**3,715,945**	**4,453,573**	**3,715,945**	**4,452,181**
Attributable to					
Non-controlling interests		-	-	-	(1,392)
Controlling interest		3,715,945	4,453,573	3,715,945	4,453,573
Basic and diluted earnings per common share		3.10	3.72		
Basic and diluted earnings per preferred share		3.41	4.09		

TELEFÔNICA BRASIL S. A.
Statements of changes in equity
Years ended December 31, 2013 and 2012
(In thousands of reais)

		Capital reserves					Inc
	Capital	**Premium on acquisition of noncontrolling interests**	**Special goodwill reserve**	**Other**	**Treasury stock**	**L res**
Balances at December 31, 2011	**37,798,110**	**(29,929)**	**63,074**	**2,735,930**	**(79,339)**	**877**
Additional dividend proposed for 2011	-	-	-	-	-	
Unclaimed dividend and interest on equity	-	-	-	-	-	
Other changes	-	-	-	-	-	
Repurchase of shares	-	-	-	-	(32,768)	
Non-controlling interests	-	(40,519)	-	-	-	
Other comprehensive income	-	-	-	-	-	
Net income for the year	-	-	-	-	-	
Allocation of income:						
Legal reserve	-	-	-	-	-	222
Interim dividend	-	-	-	-	-	
Additional dividend proposed	-	-	-	-	-	
Balances at December 31, 2012	**37,798,110**	**(70,448)**	**63,074**	**2,735,930**	**(112,107)**	**1,100**
Additional dividend proposed for 2012	-	-	-	-	-	
Unclaimed dividend and interest on equity	-	-	-	-	-	
DIPJ adjustment - Tax incentives	-	-	-	-	-	
Other comprehensive income	-	-	-	-	-	
Net income for the year	-	-	-	-	-	
Allocation of income:						
Legal reserve	-	-	-	-	-	185
Interim interest on equity	-	-	-	-	-	
Interim dividend	-	-	-	-	-	
Additional dividend proposed	-	-	-	-	-	
Balances at December 31, 2013	**37,798,110**	**(70,448)**	**63,074**	**2,735,930**	**(112,107)**	**1,285**

Outstanding shares (in thousands)
VPA - Net book value of Company's shares

TELEFÔNICA BRASIL S. A.
Cash flow statements
Years ended December 31, 2013 and 2012
(In thousands of reais)

	Company		Conso
	2013	**2012**	**2013**
Cash generated by operating activities			
Income before taxes	**4,045,952**	**4,902,169**	**4,662,364**
Items not affecting cash			
Expenses (revenues) not representing changes in cash	**4,363,283**	**(648,026)**	**8,440,826**
Depreciation and amortization	4,135,668	2,634,616	5,643,310
Foreign exchange (gains) losses on loans	70,612	6,815	98,105
Monetary (gains) losses	135,624	(12,493)	142,289
Equity pickup	(1,913,508)	(3,995,228)	55,150
Losses on write-off/sale of goods	(46,235)	(10,747)	(122,598)
Provision for impairment - accounts receivable	480,373	267,453	741,274
Provision (reversal) of trade accounts payable	498,835	(148,914)	579,225
Provision (Write-offs and reversals of) provision for impairment - inventories	(14,728)	(4,351)	(5,901)
Pension plans and other post-employment benefits	27,106	9,906	26,986
Provisions for tax, labor, civil and regulatory contingencies	493,965	336,677	660,771
Interest expense	489,145	274,047	596,292
Provision for (reversal of) divestiture	3,268	(195)	19,437
Provisions for customer loyalty program	2,154	-	8,915
Other	1,004	(5,612)	(2,429)
(Increase) decrease in operating assets:	**(710,357)**	**777,537**	**(1,673,802)**
Trade accounts receivable	(870,569)	(131,541)	(1,160,903)
Inventories	15,997	11,784	(111,905)
Taxes recoverable	(75,609)	771,854	(399,105)
Other current assets	325,239	100,937	37,703
Other noncurrent assets	(105,415)	24,503	(39,592)
Increase (decrease) in operating liabilities:	**(1,102,498)**	**(787,012)**	**(1,853,108)**
Personnel, social charges and benefits	16,629	(38,658)	20,625
Trade accounts payable	(522,289)	(166,024)	(490,538)
Taxes, charges and contributions	229,493	(87,935)	487,854
Interest paid	(501,335)	(221,609)	(625,624)
Income and social contribution taxes paid	-	(9,483)	(868,395)
Other current liabilities	(343,670)	(226,518)	(341,427)
Other noncurrent liabilities	18,674	(36,785)	(35,603)
Total cash generated by operating activities	**6,596,380**	**4,244,668**	**9,576,280**

Cash generated by (used in) investing activities

Future capital contribution in subsidiaries	(85,250)	(96,607)	-
Additions to PP&E and intangible assets (net of donations)	(3,814,802)	(2,051,106)	(5,837,172)
Cash received from sale of PP&E items	47,437	40,628	436,386
Cash received from divestitures	-	7,551	-
Redemption of (investments in) investments in guarantee	267,220	-	22,485
Redemption of (increase in) judicial deposits	(67,098)	(101,725)	(168,075)
Dividend and interest on equity received	1,323,026	2,647,353	2,577
Effect of cash and cash equivalents due to merger/split	3,371,178	-	-
Total cash generated by (used in) investing activities	**1,041,711**	**446,094**	**(5,543,799)**
Cash used in (generated by) financing activities			
Payment of loans, financing and debentures	(2,111,360)	(858,201)	(2,336,023)
Loans and debetures raised	2,211,138	2,000,000	2,229,134
Payment net of derivative agreements	29,956	(9,244)	20,667
Payment for reverse split of shares	(289)	-	(289)
Dividend and interest on equity paid	(4,535,519)	(3,493,997)	(4,535,519)
Acquisition of non-controlling interest	-	(44,172)	-
Repurchase of treasury stock	-	(32,768)	-
Total cash used in (generated by) financing activities	**(4,406,074)**	**(2,438,382)**	**(4,622,030)**
Increase (decrease) in cash and cash equivalents	**3,232,017**	**2,252,380**	**(589,549)**
Cash and cash equivalents at beginning of year	**3,079,282**	**826,902**	**7,133,485**
Cash and cash equivalent at end of year	**6,311,299**	**3,079,282**	**6,543,936**
Changes in cash and cash equivalents for the year	**3,232,017**	**2,252,380**	**(589,549)**

TELEFÔNICA BRASIL S. A.
Statements of comprehensive income
Years ended December 31, 2013 and 2012
(In thousands of reais)

	Company		**Consolidate**	
	2013	**2012**	**2013**	
				res
Net income for the year	**3,715,945**	**4,453,573**	**3,715,945**	**4,452**
Unrealized losses on investments available for sale	(13,466)	(5,536)	(13,466)	(5
Taxes	4,578	1,882	4,578	1
	(8,888)	(3,654)	(8,888)	(3
Cumulative translation adjustments - operations in foreign currency	11,525	5,731	11,525	5
Other comprehensive income to be reclassified to gains (losses) for subsequent periods	**2,637**	**2,077**	**2,637**	**2**
Actuarial gains (losses) and limitation effect of the assets of surplus plans	18,993	(83,309)	21,612	(69
Taxes	(6,458)	28,325	(7,348)	23
	12,535	(54,984)	14,264	(46
Gains (losses) - derivative transactions	(5,424)	-	(5,424)	12
Taxes	1,844	-	1,844	(4
	(3,580)	-	(3,580)	8
Interest in comprehensive income of subsidiaries	1,729	17,123	-	
Other comprehensive income not to be reclassified to gains (losses) for subsequent periods	**10,684**	**(37,861)**	**10,684**	**(37**
Comprehensive income for the year, net of taxes	**3,729,266**	**4,417,789**	**3,729,266**	**4,416**
Attributable to:				
Non-controlling interests	-	-	-	(1
Controlling interest	3,729,266	4,417,789	3,729,266	4,417

TELEFÔNICA BRASIL S. A.
Statements of value added
Years ended December 31, 2013 and 2012
(In thousands of reais)

	Company		Consolidated	
	2013	**2012**	**2013**	**2012** restated
Revenues	**30,969,784**	**17,204,211**	**46,970,960**	**46,210,727**
Sales	31,019,867	17,146,952	47,095,810	46,066,465
Other revenues	430,290	324,712	616,424	798,535
Provision for impairment - accounts receivable	(480,373)	(267,453)	(741,274)	(654,273)
Inputs acquired from third parties	**(12,710,787)**	**(7,559,445)**	**(18,027,763)**	**(15,693,801)**
Cost of sales and resales	(7,815,422)	(5,328,483)	(10,714,033)	(9,956,264)
Materials, electric energy, outsourced services and other	(4,949,919)	(2,297,993)	(7,433,734)	(6,837,558)
Loss/recovery of asset values	54,554	67,031	120,004	1,100,021
Gross value added	**18,258,997**	**9,644,766**	**28,943,197**	**30,516,926**
Retentions	**(4,135,668)**	**(2,634,616)**	**(5,643,310)**	**(5,491,776)**
Depreciation and amortization	(4,135,668)	(2,634,616)	(5,643,310)	(5,491,776)
Net value added generated	**14,123,329**	**7,010,150**	**23,299,887**	**25,025,150**
Value added received in transfer	**3,156,617**	**4,530,014**	**1,693,127**	**1,281,692**
Equity pickup	1,913,508	3,995,228	(55,150)	588
Financial income	1,243,109	534,786	1,748,277	1,281,104
Total value added to be distributed	**17,279,946**	**11,540,164**	**24,993,014**	**26,306,842**
Distribution of value added	**(17,279,946)**	**(11,540,164)**	**(24,993,014)**	**(26,306,842)**
Personnel, social charges and benefits	(1,572,734)	(860,657)	(2,334,734)	(2,184,470)
Direct compensation	(1,028,607)	(588,540)	(1,498,143)	(1,467,379)
Benefits	(439,614)	(203,092)	(698,907)	(589,334)
FGTS	(104,513)	(69,025)	(137,684)	(127,757)
Taxes, charges and contributions	(8,649,666)	(4,851,019)	(14,496,157)	(15,929,169)
Federal	(2,663,044)	(1,556,796)	(4,849,278)	(6,368,854)
State	(5,924,082)	(3,235,821)	(9,519,257)	(9,462,721)
Municipal	(62,540)	(58,402)	(127,622)	(97,594)
Debt remuneration	(2,605,080)	(811,014)	(3,615,099)	(2,982,774)
Interest	(1,486,003)	(633,515)	(1,934,369)	(1,527,077)
Rental	(1,119,077)	(177,499)	(1,680,730)	(1,455,697)
Equity remuneration	(3,715,945)	(4,453,573)	(3,715,945)	(4,452,181)
Interest on equity	(1,738,000)	-	(1,738,000)	-
Dividend	(746,000)	(1,122,522)	(746,000)	(1,122,522)

Retained profit	(1,231,945)	(3,331,051)	(1,231,945)	(3,331,051)
Non-controlling interests	-	-	-	1,392
Other	(736,521)	(563,901)	(831,079)	(758,248)
Provisions for tax, labor, civil and regulatory contingencies	(736,521)	(563,901)	(831,079)	(758,248)

Telefônica Brasil S. A.

NOTES TO FINANCIAL STATEMENTS

Years ended December 31, 2013 and 2012

(In thousands of reais)

1. OPERATIONS

a. Background information

Telefônica Brasil S.A. (Company or Telefônica Brasil) is a publicly-traded corporation operating in telecommunication services and in the performance of activities that are necessary or useful in the rendering of such services in conformity with the concessions, authorizations and permits it has been or shall be granted. The Company, headquartered at Avenida Engenheiro Luiz Carlos Berrini, nº 1376, in the city of São Paulo, State of São Paulo, Brazil, is a member of Telefonica Group (Group), the telecommunications industry leader in Spain, also being present in several European and Latin American countries. At December 31, 2013 and 2012, Telefónica S.A., holding company of the Group, held a total of73.81% direct and indirect interest in the Company, excluding treasury stock, including 91.76% common shares and 64.60% preferred shares.

b. Corporate restructuring

In order to streamline the Company's organizational structure, to rationalize the services provided by its subsidiaries and to concentrate service provision into two operating entities, namely the Company and its wholly-owned subsidiary (Telefônica Data S.A., TData or subsidiary), on March 15, 2012, the Company filed with the Brazilian National Telecommunications Agency (ANATEL) a request for previous approval of corporate restructuring, which became legally feasible due to legislation changes applicable to Fixed Switched Telephone Service (STFC) operators through Law No. 12485.

This corporate restructuring process was approved by ANATEL under Act No. 3043, of May 27, 2013, as published in the Federal Official Gazette (DOU) of May 29, 2013, subject to the conditions thereunder.

The Board of Directors' meeting of June 11, 2013 approved the terms and conditions of the corporate restructuring process involving the Company's wholly-owned subsidiaries and subsidiaries.

The corporate restructuring included spin-offs and mergers of subsidiaries and of companies directly or indirectly controlled by the Company, so that the economic activities other than telecommunications services, including the provision of Value Added Services as defined in article 61 of the General Telecommunications Law (LGT) (with such activities being jointly and generally referred to as SVAs), provided by the various wholly-owned subsidiaries/subsidiaries were concentrated in TData and the telecommunication services were consolidated by the Company.

All of the spin-offs or split-ups, as the case may be, and the merger of the net assets of the companies involved in the restructuring process took place on the same date and had the same base date (April 30, 2013), as follows: the Company merged (i) the net assets of TData, arising from its spin-off, corresponding to the activities related to the provision of service of Multimedia Communication Service (SCM); (ii) the net assets of Vivo S.A. (Vivo), arising from its split-up, corresponding to the use of Personal Communication Services (SMP), Multimedia Communication Services (SCM) and STFC in local, domestic and international long distance calls in regions I and II of the General Service Concession Plan (PGO); (iii) the net assets of ATelecom S.A. (ATelecom), arising from its split-up, corresponding to the activities related to the provision of Conditional Access Audiovisual Services (SEAC) (through DTH technology) and SCM; and (iv) Telefônica Sistema de Televisão S.A. (TST), which concentrated the activities related to the provision of SEAC and SCM services before its merger into the Company.

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The organization chart before the corporate restructuring is summarized as follows:

Please find below a brief description of spin-offs and mergers of companies involved in the Company's corporate restructuring process.

Merger of Lemontree Participações S.A. (Lemontree), GTR-T Participações e Empreendimentos S.A. (GTR-T), Ajato Telecomunicações Ltda (Ajato), Comercial Cabo TV São Paulo S.A. (CaTV) and TVA Sul Paraná S.A. (TVA) pela TST: Immediately before the merger of TST into the Company, yet on the same date, TST merged its subsidiary Ajato and the Company's wholly-owned subsidiaries Lemontree and GTR-T as well as their related subsidiaries Sul Paraná and CaTV. These entities were valued under the provisions of article 227 of Law No. 6404/76, based on their respective book values as at April 30, 2013, as ratified by the general meeting held by TST. Merger thereof resulted in a R$102,512 increase in TST capital, under the terms of the Merger Protocol of these entities and of TST. After the merger into TST of Lemontree, GTR-T, Ajato, CaTV and Sul Paraná ceased to exist. Except for the Company and TST, aforementioned companies were wholly-owned by T Brasil; therefore, the merger of these companies did not result in any refund to or protection of noncontrolling shareholders of the companies involved.

Merger of TST into the Company: TST was valued under the provisions of article 227 of Law No. 6404/76, based on its respective book value as at April 30, 2013. Considering the merger of Lemontree, GTR-T, Ajato, CaTV and Sul Paraná into TST immediately before the merger of TST into the Company, the total amount of TST net assets (corresponding to the sum of net assets of TST and of the companies merged into it) merged by the Company totaled R$226,106.

Merger of TData net assets: The net assets of TData related to SCM services were spun off and merged into T Brasil, in order to concentrate in its equity the net assets related to SVAs. The amount of TData net assets merged by the Company was valued under the terms of article 227 of Law No. 6404/76, based on its respective book value at April 30, 2013, as ratified by the Company's general meeting. TData spun-off net assets totaled R$34,724.

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<u>Merger of Vivo net assets:</u> Vivo was split up in order to segregate the operation of SMP, SCM and STFC activities in local, domestic and international long distance calls in regions I and II of PGO, with the related net assets being merged by the Company. Value-added services (SVAs) and other non-telecommunication services were merged into TData and Vivo ceased to exist. The amount of Vivo net assets merged by the Company was valued under the terms of article 227 of Law No. 6404/76, based on its respective book value at April 30, 2013, as ratified by the Company's general meeting. These net assets totaled R$10,228,352.

<u>Merger of ATelecom net assets:</u> ATelecom was split up in order to segregate the net assets related to value-added services provided by ATelecom, which were merged into TData. The net assets of ATelecom's remaining activities were merged into the Company and ATelecom ceased to exist. The amount of ATelecom net assets merged by the Company was valued under the terms of article 227 of Law No. 6404/76, based on its respective book value at April 30, 2013, as ratified by the Company's general meeting. These net assets totaled R$348,624.

The merger of companies and net assets previously described did not result in any capital increase or issue of new Company shares; accordingly, the corporate restructuring did not result in any changes in interests currently held by Company shareholders.

There is no question of replacing shares of noncontrolling shareholders of the spun-off companies with shares of the merging company, since the Company was, upon the merger of net assets and/or companies, as the case may be, the sole shareholder of the companies spun off/ merged. Accordingly, an equity valuation report at market price was not prepared for calculating the noncontrolling share replacement ratio as defined in article 264 of Law No. 6404/76 and item VI, paragraph 1, article 2 of CVM Ruling No. 319/99, based on recent understandings expressed by the Brazilian Securities and Exchange Commission (CVM) regarding consultations in connection with similar restructuring processes and based on CVM Rule No. 559, of November 18, 2008.

The merger of entities and spun-off amounts previously described did not interrupt the operations and telecommunication services provided to their customers, and such services were entirely succeeded by the Company.

Company General Shareholders' Meeting held on July 1, 2013 approved aforementioned corporate restructuring and the organization chart is now as follows:

The restructuring has been accounted for as a reorganization of entities under common control without any substantive change to the equity value of the Company, since all of the entities involved were wholly-owned immediately before and immediately after the restructuring. Accordingly, the restructuring was recorded at the book values of the entities involved. However, as a result of the restructuring, the Company recognized a tax benefit and corresponding deferred tax asset for R$ 319.996, relating to certain tax attributes that were not expected to be realized by certain of the entities prior to the restructuring.

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c. Operations

The Company is primarily engaged in the rendering of land-line telephone and data services in the state of São Paulo, under Fixed Switched Telephone Service Concession Arrangement (STFC) and Multimedia Communication Service (SCM) authorizations, respectively. Also, the Company is authorized to render STFC services in Regions I and II of the General Service Concession Plan (PGO/2008) and other telecommunications services, such as SCM (data communication, including broadband internet), SMP (Personal Communication Services) and SEAC (Conditional Access Audiovisual Services) (especially by means of DTH and cable technologies).

Service concessions and authorizations are granted by Brazil's Telecommunications Regulatory Agency (ANATEL), under the terms of Law No. 9472, of July 16, 1997 – General Telecommunications Law ("Lei Geral das Telecomunicações" - LGT), amended by Laws No. 9986, of July 18, 2000 and No. 12485, of September 12, 2011. Operation of such concessions and authorizations is subject to supplementary regulations and plans issued.

c.1) STFC service concession arrangement

The Company is the grantee on an STFC concession to render land-line services in the local network and national long distance calls originated in sector 31 of region III, which comprises the state of São Paulo (except for cities within sector 33), as established in the General Service Concession Plan (PGO/2008).

The Company's current STFC service concession arrangement is effective until December 31, 2025, and may be subject to reviews on December 31, 2015 and December 31, 2020.

In accordance with the service concession arrangement, every two years, during the arrangement's 20-year term, the Company shall pay a fee equivalent to 2% (two percent) of its prior-year STFC revenue, net of applicable taxes and social contributions.

c.2) Authorizations and frequencies related to mobile telephone services

Frequency authorizations granted by ANATEL for mobile telephone services may be renewed only once, over a 15-year period, through payment, every two years after the first renewal, of fees equivalent to 2% (two percent) of the Company's prior-year revenue, net of taxes and social contributions, related to the application of the Basic and Alternative Plans of Service.

In August 2013, the Company and ANATEL executed the authorization terms for the nonexclusive use of radiofrequency blocks, on a primary basis, as a result of the realignment of the "L" band in sub-bands from 1,975 MHz to 1,980 MHz for the mobile station transmission and from 2,165 MHz to 2,170 MHz for nodal station transmission.

These authorizations were issued for the remaining terms established under item 1.9 of Public Notice No. 002/2007/SPV-Anatel, of October 23, 2007, for valuable consideration, associated to the authorization for the rendering of SMP services, amendment No. 01 to authorization No. 078/2012/PVCP/SPV-Anatel of August 14, 2013, published in the Federal Official Gazette of August 16, 2013, effective until April 29, 2023, and may be extended only once, over a 15-year period. Effectiveness of these authorizations is subject to the compliance with the requirements defined in the agreements.

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The Company paid R$451,121 for the aforementioned authorizations, which were recorded as licenses under intangible assets (Note 14) and will be amortized over the remaining periods of the licenses.

Of the lots offered in the sale auctions of national 2.5 GHz bandwidths, linked to the 450 MHz bandwidth, conducted by ANATEL on June 12 and 13, 2012, Vivo (merged into the Company on July 1, 2013) was the winning bidder of lot 3, in accordance with public notice No. 004/2012/PVCP/SPV-Anatel for the sale of 4G broadband. The price offered for lot 3 was R$1,050,000.

On October 11, 2012, through Act No. 5907, ANATEL's Board decided to approve the nonexclusive use of radiofrequency blocks, on a primary basis, in sub-bands 2550 through 2570 MHz / 2670 through 2690 MHz, in connection with the authorizations to operate the Personal Communications Service (SMP) granted to Vivo (merged into the Company on July 1, 2013), as well as of other radiofrequencies in the 2.5 GHz band by the respective winning bidders of the lots mentioned in the bid. The authorization terms of the above-mentioned radiofrequency bands were executed on October 16, 2012 and published in the Federal Official Gazette (DOU) on October 18, 2012.

Accordingly, upon the actual awarding of such lot, Vivo (merged into the Company on July 1, 2013) increased its service provision capacity powered by 4G technology nationwide and has since then operated in the 2.5GHz bandwidth, with 20+20 MHz band. In addition to the 2.5GHz bandwidth, the acquired lot includes a 450 MHz bandwidth for rural areas in the Brazilian states of Alagoas, Ceará, Minas Gerais, Paraíba, Pernambuco, Piauí, Rio Grande do Norte, São Paulo and Sergipe.

In the fourth quarter of 2012, the total amount of R$1,050,000 was adjusted in accordance with the remaining life of licenses and recorded as licenses in intangible assets (Note 14).

The Company operates SMP services, in accordance with the authorizations given as follows:

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<u>Operation Area</u>	**License Expiration**						
	450 MHz	**800 MHz (1)**	**900 MHz**	**1800 MHz**	**1900 MHz (2)**	**2100 MHz (3)**	**2.5 GHz**
<u>Region 1</u>							
Rio de Janeiro	-	Bandwidth A – 11/29/20	Extension 1 - 04/30/23	Extensions 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Espírito Santo	-	Bandwidth A - 11/30/23	Extension 1 - 04/30/23	Extensions 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Amazonas, Roraima, Amapá, Pará and Maranhão	-	Bandwidth B - 11/29/28	Extension 2 - 04/30/23	Extensions 7, 9 and 10 - 04/30/23	-	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Minas Gerais (except *Triângulo Mineiro*)	10/18/27	Bandwidth A - 04/29/23	Extension 2 - 04/30/23	Extensions 11 to 14 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Minas Gerais (*Triângulo Mineiro*)	10/18/27	-	Bandwidth E -04/28/20	Bandwidth E - 04/28/20	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Bahia	-	Bandwidth A - 06/29/23	Extension 1 - 04/30/23	Extensions 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Sergipe	10/18/27	Bandwidth A - 12/15/23	Extension 1 - 04/30/23	Extensions 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Alagoas, Ceará, Paraíba, Pernambuco,	10/18/27	-	-	Bandwidth E - 04/30/23 Extensions 9 and 10 -	Bandwidth L -12/07/22	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27

Piauí and Rio Grande do Norte				04/30/23			
Region 2							
Paraná (except for Sector 20) and Santa Catarina	-	Bandwidth B - 04/08/28	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Paraná Sector 20 - Londrina and Tamarana (5)	-	Bandwidth B - 04/08/28	-	Bandwidth M - 04/30/23 Extension 10 - 04/30/23	-	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Rio Grande do Sul (except for Sector 30)	-	Bandwidth A - 12/17/22	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Rio Grande do Sul - Sector 30 (Pelotas, Morro Redondo, Capão do Leão and Turuçu)	-	-	-	Bandwidths D and M - 04/30/23	Bandwidth L - 12/07/22	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Federal District	-	Bandwidth A - 07/24/21	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Goiás and Tocantins	-	Bandwidth A - 10/29/23	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Goiás (Sector 25) (7)	-	-	-	Bandwidth M - 04/30/23 Extensions 7 to 10 - 04/30/23	Bandwidth L - 12/07/22	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Mato Grosso	-	Bandwidth A - 03/30/24	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
	-						

Mato Grosso do Sul (except for Sector 22) (6)		Bandwidth A - 09/28/24	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Mato Grosso do Sul (Sector 22 - Paranaíba)	-	-	-	Bandwidth M - 04/30/23 Extensions 7, 9 and 10 - 04/30/23	Bandwidth L - 12/07/22	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Rondônia	-	Bandwidth A - 07/21/24	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Acre	-	Bandwidth A - 07/15/24	Extension 1 - 04/30/23	Bandwidth M - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
Region 3							
São Paulo (4)	10/18/27	Bandwidth A - 08/05/23	-	Extensions 9 and 10 - 04/30/23	Bandwidth L - 30/04/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
São Paulo (Ribeirão Preto, Guatapará and Bonfim Paulista) (4)	10/18/27	Bandwidth A - 01/20/24	-	Extensions 5, 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
São Paulo (Franca area and region) (4)	10/18/27	Bandwidth A - 08/08/23	-	Extensions 5, 9 and 10 - 04/30/23	Bandwidth L - 04/30/23	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27
São Paulo (Sector 33) (8)	-	-	-	Extensions 9 and 10 - 04/30/23	Bandwidth L - 12/07/22	Bandwidth J - 04/30/23	Bandwidth X - 10/18/27

(1) - All Licence Terms for Bandwidths A and B have already been renewed for another 15 years. Therefore, no further extension is permitted (30 year-license completed).
(2) - The License Terms for Bandwith L linked to Bandwidth A or B were renewed in the same period for those Bandwidths.
(3) - Bandwidths "L", which were realigned with Bandwidth J, now have the same extension date as the latter (this issue has been considered for the realignment price calculation.
(4) - In SP, only in municipalities with CN from 13 to 19, VIVO has 450 MHz licenses expiring at 10/18/27.
(5) - Paraná - Sector 20 of PGO - Londrina and Tamarana.
(6) - Mato Grosso do Sul - Sector 22 of PGO - Paranaíba.

(7) - Goiás - Sector 25 do PGO - Buriti Alegre, Cachoeira Dourada, Inaciolândia, Itumbiara, Paranaiguara and São Simão.
(8) - São Paulo - Sector 33 of PGO - Altinópolis, Aramina, Batatais, Brodosqui, Buritizal, Cajuru, Cássia dos Coqueiros, Colômbia, Franca, Guaíra, Guará, Ipuã, Ituverava, Jardinópolis, Miguelópolis, Morro Agudo, Nuporanga, Orlândia, Ribeirão Corrente, Sales de Oliveira, Santa Cruz da Esperança, Santo Antônio da Alegria and São Joaquim da Barra.

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d. Share trading on stock exchanges

The Company is listed in the Brazilian Securities and Exchange Commission (CVM) as a publicly-held company under Category A (issuers authorized to trade any marketable securities) and has shares traded on the São Paulo Stock Exchange (BM&FBovespa). It is also listed in the US Securities and Exchange Commission (SEC*)*, and its level II American Depositary Shares (ADS), backed by preferred shares only, are traded on the New York Stock Exchange (NYSE).

d.1) Shares traded on BM&F Bovespa

On September 21, 1998, the Company started trading its shares on BM&F Bovespa, under tickers TLPP3 and TLPP4, for common and preferred shares, respectively.

In the Special Shareholders’ Meeting of Vivo Participações S.A. (Vivo Part.) and Telecomunicações de São Paulo S. A. (Telesp) held on October 3, 2011, the merger of Vivo Part. into Telesp was approved. On the same date, its corporate name changed to Telefonica Brasil S.A. and on October 6, 2011, the Company changed its ticker codes to VIVT3 and VIVT4 for common and preferred shares, respectively, and the stock exchange code to Telefonica Brasil.

d.2) Shares traded on NYSE

On November 16, 1998, the Company started trading ADS on NYSE, which currently has the following main characteristics:

- Type of shares: preferred.
- Each ADS represents 1 (one) preferred share.
- Shares are traded as ADS under ticker “VIV” on NYSE.
- Foreign depositary bank: *Citibank N.A*.
- Custodian bank in Brazil: *Citibank N.A*.

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e. Agreement between Telefónica S.A. and Telecom Italia

TELCO S.p.A. (in which Telefónica S.A. held a 46.18% interest) has a 22.4% interest with voting rights in Telecom Italia, being the major shareholder of that company. The Company is an indirect subsidiary of Telefónica S.A., and Telecom Italia holds an indirect interest in TIM Participações S.A. (TIM), a Brazilian telecommunications company. Neither Telefónica S.A., nor Telefonica Brasil or any other affiliate of Telefónica S.A. interfere in, are involved with or have decision-making powers over TIM operations in Brazil, also being lawfully and contractually forbidden to exercise any type of political power derived from indirect interest held as concerns operations in Brazil, directly related to TIM operations. TIM (Brazil) and Telefonica Brasil compete in all markets in which they operate in Brazil under permanent competitive stress and, in this context, as well as in relation to the other economic players in the telecommunications industry, maintain usual and customary contractual relations with one another (many of which are regulated and inspected by ANATEL) and/or which, as applicable, are informed to ANATEL and Brazil's Administrative Council for Economic Defense (CADE), concerning the commitments assumed before these agencies so as to ensure total independence of their operations.

On September 24, 2013, Telefónica S.A., entered into an agreement with the other shareholders of the Italian company TELCO SpA (which holds a 22.4% voting in Telecom Italia SpA), whereby:

1) Telefonica SA subscribed and paid up capital in Telco, SpA through a contribution of 324 million euros, receiving shares without voting rights of TELCO, SpA. As a result of this capital increase, the share capital of Telefónica S.A. voting in Telco, SpA remaining unchanged (remaining at 46.18%), although their economic participation rose to 66%. Thus, the governance of TELCO S.p.A., as well as the obligations of Telefónica S.A. to abstain from participating in or influencing the decisions that impact the industries where they both operate, remained unchanged.

2) Subject to obtaining the required previous approvals from antitrust authorities and telecommunications regulatory agencies as applicable (including Brazil and Argentina), Telefónica S.A. will be involved in another capital increase in TELCO S.p.A. amounting to 117 million Euros, receiving shares with no voting rights of TELCO, SpA. As a result of this capital increase, the share capital of Telefónica S.A. voting in

Telco, SpA increased its total interest to 70%, with the 46.18% interest held in shares with voting rights remaining unchanged.

3) Beginning as of January 1st, 2014, following approvals from antitrust authorities and telecommunications regulatory agencies as applicable (including Brazil and Argentina), Telefónica S.A. will be entitled to convert all or part of nonvoting shares into common shares with voting rights, limited however to a 64.9% interest in TELCO S.p.A. voting capital.

4) Italian shareholders of TELCO S.p.A. granted Telefónica S.A. an option to purchase all of their shares in TELCO S.p.A.. Exercising this call option is also subject to obtaining the required previous approvals from antitrust authorities and telecommunications regulatory agencies as applicable (including Brazil and Argentina), beginning eligible after January 1st 2014, whenever the Shareholders' Agreement remains in full force and effect, except (i) between June 1 and June 30, 2014 and between January 15 and February 15, 2015; and (ii) during certain periods in case the Italian shareholders of TELCO S.p.A. request the entity's spin-off.

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Until the date of preparation of the consolidated financial statements the approval required to implement the transactions agreed on September 24, 2013 by Telefonica S.A. and other shareholders of Italian society TELCO, S.p.A has not been obtained.

On December 4, 2013, the Brazilian Antitrust Enforcement Agency (CADE) announced the following decisions:

1) Approve, subject to the limitations described below, the acquisition, by Telefónica S.A., of the total interest held by Portugal Telecom, SGPS SA e PT Móveis – Serviços de Telecomunicações, SGPS, SA (PT) in Brasilcel NV, which controlled Brazilian mobile telecommunications operator Vivo Participações S.A. (Vivo Part.).

The transaction has been approved by ANATEL and its completion (requiring no prior approval from CADE at the time) took place immediately after approval from ANATEL, on September 27, 2010.

The liminations imposed by CADE on its decision are as follow:

a) a new shareholder share control over Vivo Part. with Telefónica S.A., adopting the same conditions applied to PT when it held an interest in Brasilcel NV., or

b) Telefónica S.A. shall cease to have, either directly or indirectly, an equity interest in TIM Participações S.A..

2) Impose a R$15 million fine on Telefónica S.A. for violating the will and purpose of the agreement executed by and between Telefónica S.A. and CADE (as a requirement to approve the initial purchase transaction of Telecom Italia in 2007), due to the subscription and payment, by Telefónica S.A., of TELCO

S.p.A. nonvoting shares in the context of its recent capital increase. This decision also requires Telefónica S.A. to dispose of its nonvoting shares held in TELCO S.p.A..

The deadline for compliance with the conditions and obligations imposed by CADE in both decisions were classified as confidential by CADE.

At December 13, 2013, Telefónica S.A. published a material news release regarding the decisions made by CADE in the meeting held on December 4, 2013, stating that it considered the measures imposed by that agency to be unreasonable, thus considering the possibility of starting applicable legal proceedings.

In this context, and in order to strengthen its firm commitment to the obligations previously assumed by Telefónica S.A. to keep away from Telecom Italia's business in Brazil, Telefónica S.A. pointed out, in a relevant fact release that Mr. César Alierta Izuel and Mr. Julio Linares López had decided to resign with immediate effect, from the position of Directors at Telecom Italia. Additionally, Mr. Julio Linares López decided to resign, with immediate effect, from his position on the list presented by TELCO S.p.A. for a potential re-election to the Board of Directors of Telecom Italia.

Likewise, Telefónica S.A., notwithstanding the rights defined in the Shareholders' Agreement of TELCO S.p.A, stated in a relevant fact that it decided not to exercise, for now, its right to appoint or suggest two Directors at Telecom Italia.

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2. BASIS OF PREPARATION AND PRESENTATION OF THE FINANCIAL STATEMENTS

2.1 - Basis of preparation and presentation

The Company's financial statements for the years ended December 31, 2013 and 2012 are presented in thousands of reais (unless otherwise stated) and were prepared under a going concern assumption.

The financial statements were prepared on a historical cost basis (except where different criteria are required) and adjusted to reflect the valuation of assets and liabilities measured at fair value or considering the mark-to-market valuation when these items are classified as available for sale.

The financial statements were prepared based on several valuation bases used in accounting estimates. Accounting estimates involved in the preparation of the financial statements are based on objective and subjective factors and management's judgment to determine the adequate amount to be recorded in the financial statements. Significant items subject to these estimates and assumptions include selection of useful lives and recoverability of property and equipment, measurement of financial assets at fair value, credit risk analysis to determine the allowance for doubtful accounts, as well as the analysis of other risks to determine other provisions, including the provision for contingencies.

Settlement of transactions involving these estimates may result in amounts significantly different than those recorded in the financial statements due to the criteria inherent in the estimation process. The Company reviews its estimates at least annually.

The individual financial statements were prepared and are presented in accordance with the accounting policies adopted in Brazil, which comprise the standards issued by the Brazilian Securities and Exchange Commission (CVM) and the pronouncements of the Brazilian FASB (CPC), in conformity with the standards and procedures of the International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board (IASB), except for investments in subsidiaries - valued under the equity accounting method, while under IFRS rules the investments are measure by cost or fair value.

The consolidated financial statements were prepared and are presented in accordance with the International Financial Reporting Standards (IFRS), issued by the International Accounting Standards Board (IASB), which do not differ from the accounting practices adopted in Brazil, comprising the standards issued by the Brazilian Securities and Exchange Commission (CVM) and CPCs.

The financial statements report includes comparative consolidated information in relation to the previous year. Additionally, the Company presents the balance sheet and the cash flow statement at the beginning of the earliest comparative period when it applies an accounting policy retrospectively, makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements. The additional balance sheet as at January 1, 2012 is included in the accompanying financial statements, which are in conformity with the international financial reporting standards issued by the IASB.

Considering the net assets received by the Company as a result of the corporate restructuring process described in Note 1b), the individual financial statements as at December 31, 2013 are not comparable to those as at December 31, 2012.

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The accompanying financial statements were authorized for issue by the Company's management in a meeting held on February 17, 2014, as ratified by the Board of Directors in a meeting held on February 25, 2014.

The Company hereby states that the consolidated financial statements are in conformity with the IFRS as issued by the IASB, in addition to the pronouncements, interpretations and guidelines issued by the CPC in effect as at December 31, 2013, which include the new pronouncements, interpretations and amendments to the following standards, amendments and interpretations published by the IASB and by the IFRS Interpretations Committee (IFRIC), effective as of January 01, 2013:

New IFRS and interpretations of the IFRIC with no significant impact on the financial position shown in these financial statements:

IAS 1 Presentation of Financial Statements - Presentation of Items of Other Comprehensive Income The amendments to IAS 1 introduce a grouping of items presented in other comprehensive income (OCI). Items that could be reclassified (or recycled) to profit or loss at a future point in time (e.g., net gain on hedge of net investment, exchange differences on translation of foreign operations, net movement on cash flow hedges and net loss or gain on available-for-sale financial assets) now have to be presented separately from items that will never be reclassified (e.g., actuarial gains and losses on defined benefit plans and revaluation of land and buildings). The amendments became effective for annual periods beginning on or after July 1, 2012. The application of these amendments affects presentation only and has no impact on the Company's and its subsidiary's financial position or performance.

IAS 19 Employee Benefits (Revised): The IASB has issued a number of amendments to IAS 19. These amendments include not only basic changes, such as the elimination of the "corridor" approach and the concept of expected return on plan assets, but also simple clarifications regarding valuation, devaluation and remeasurement. This amendment became effective for annual periods beginning on or after January 1, 2013. The application of this amendment has no significant impact on the Company's and its subsidiary's financial position or performance.

IAS 28 Accounting for Investments in Associates and Joint Ventures (revised in 2011): As a consequence of the new IFRS 11 and IFRS 12, IAS 28 has been renamed IAS 28 Investments in Associates and Joint Ventures, and describes the application of the equity method to investments in joint ventures in addition to associates. This amendment became effective for annual periods beginning on or after January 1, 2013. The application of this amendment has no impact on the Company's and its subsidiary's financial position or performance.

IFRS 1 First-time Adoption of International Financial Reporting Standards (IFRS): These amendments changed the meaning of effective IFRSs. According to this amendment, an entity may choose to apply either a current standard or a new standard that is not yet mandatory, but that permits early adoption, provided either the standard is applied consistently throughout the periods. The Company did not choose for the early application of any standards.

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IFRS 7 Disclosures - Offsetting Financial Assets and Financial Liabilities (Amendments to IFRS 7): These amendments require an entity to disclose information about rights to set-off and related arrangements (e.g., collateral agreements). The disclosures would provide users with information that is useful in evaluating the effect of netting arrangements on an entity's financial position. The new disclosures are required for all recognized financial instruments that are set off in accordance with IAS 32 Financial Instruments: Presentation. The disclosures also apply to recognized financial instruments that are subject to an enforceable master netting arrangement or similar agreement, irrespective of whether they are set off in accordance with IAS 32. This amendment became effective for annual periods beginning on or after January 1, 2013. The application of these amendments affects presentation only and has no impact on the Company's and its subsidiary's financial position or performance.

IFRS 10 Consolidated Financial Statements, and IAS 27 Separate Financial Statements: IFRS 10 replaces the portion of IAS 27 Consolidated and Separate Financial Statements that addresses the accounting for consolidated financial statements. It also addresses the issues raised in SIC-12 Consolidation -Special Purpose Entities. IFRS 10 establishes a single control model that applies to all entities including special purpose entities. The changes introduced by IFRS 10 require management to exercise significant judgment to determine which entities are controlled and therefore are required to be consolidated by a parent, compared with the requirements that were in IAS 27. This standard became effective for annual periods beginning on or after January 1, 2013. The Company reviewed this standard and did not identify significant impacts on its financial statements.

IFRS 12 Disclosure of Interests in Other Entities: IFRS 12 includes all of the disclosures that were previously in IAS 27 related to consolidated financial statements, as well as all of the disclosures that were previously included in IAS 31 and IAS 28. These disclosures relate to an entity's interests in subsidiaries, joint arrangements, associates and structured entities. This standard became effective for annual periods beginning on or after January 1, 2013. The application of this standard affects disclosures only and has no impact on the Company's and its subsidiary's financial position or performance.

IFRS 13 Fair Value Measurement: IFRS 13 establishes a single source of guidance under IFRS for all fair value measurements. IFRS 13 does not change when an entity is required to use fair value, but rather provides guidance on how to measure fair value under IFRS when fair value is required or permitted. Additionally, at December 12, 2013 amendments to IFRS 13 were introduced with immediate effect. The IASB stated in "Basis for Conclusions" that short-term receivables and account payables with no outstanding interest may be recognized considering the invoice amount where the effect of discounting be quantified as immaterial. This standard became effective for annual periods beginning on or after January 1, 2013. The application of this standard has no impact on the Company upon first-time adoption.

IAS 34 Interim financial reporting: The amendment aligns the disclosure requirements for total segment assets with total segment liabilities in interim financial statements. This clarification also ensures that interim disclosures are aligned with annual disclosures. These improvements became effective for annual periods beginning on or after January 1, 2013. The application of this standard has no impact on the annual financial statements of the Company.

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New IFRS and interpretations of the IFRIC with impact on the financial position shown in these financial statements:

IFRS 11 replaces IAS 31 Interests in Joint Ventures and SIC-13 Jointly-controlled Entities - Non-monetary Contributions by Venturers. IFRS 11 removes the option to account for jointly controlled entities (JCEs) using proportionate consolidation. Instead, JCEs that meet the definition of a joint venture must be accounted for using the equity method. The application of this new standard impacted the Company's financial position and eliminated the proportionate consolidation of Aliança Atlântica Holding B.V. (Aliança), Companhia Aix de Participações (AIX) and Companhia ACT de Participações (ACT). Accordingly, investments in these entities were accounted for using the equity method. This standard became effective for annual periods beginning on or after January 1, 2013, and is to be applied retrospectively for joint arrangements held at the date of initial adoption.

In order to facilitate understanding the effects arising from application of this standard, we present below the consolidated financial statements as at January 1 and December 31, 2012, with corresponding adjustments and some reclassifications for better presentation of the consolidated information:

Consolidated Balance Sheet as at January 1, 2012

ASSETS	**Balance sheet as of 01.01.12, disclosed as of 12.31.12**	**Adjustments for adoption of IFRS 11 and Reclassifications**	**Balance sheet as of 01.01.12., disclosed as of 12.31.13**
Current assets			
Cash and cash equivalents	2,940,342	(50,799)	2,889,543
Trade accounts receivable, net (a)	5,105,860	22,282	5,128,142
Dividend and interest on equity	-	772	772
Taxes recoverable	2,495,066	(1)	2,495,065
Other assets (a)	1,268,850	(22,628)	1,246,222
Total current assets	**11,810,118**	**(50,374)**	**11,759,744**

Noncurrent assets			
Deferred taxes	1,428,878	(1,379)	1,427,499
Judicial deposits and garnishments	3,374,690	(200)	3,374,490
Other assets	1,630,848	(52,244)	1,578,604
Investments	37,835	114,421	152,256
Property, plant and equipment, net	17,153,920	(7,399)	17,146,521
Intangible assets, net	30,053,684	(4,237)	30,049,447
Total noncurrent assets	**53,679,855**	**48,962**	**53,728,817**
Total assets	**65,489,973**	**(1,412)**	**65,488,561**

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NOTES TO FINANCIAL STATEMENTS

Years ended December 31, 2013 and 2012

(In thousands of reais)

LIABILITIES AND EQUITY	Balance sheet as of 01.01.12, disclosed as of 12.31.12	Adjustments for adoption of IFRS 11 and Reclassifications	Balance sheet as of 01.01.12., disclosed as of 12.31.13
Current liabilities			
Personnel, social charges and benefits	495,624	(97)	495,527
Trade accounts payable	6,037,315	834	6,038,149
Taxes, charges and contributions	1,691,991	(254)	1,691,737
Loans, financing and lease (b)	988,413	11,669	1,000,082
Other liabilities (b)	3,526,920	(11,716)	3,515,204
Total current liabilities	**12,740,263**	**436**	**12,740,699**
Noncurrent liabilities			
Personnel, social charges and benefits (d)	-	15,160	15,160
Deferred taxes	788,954	-	788,954
Loans, financing and lease (b)	3,959,115	9,398	3,968,513
Provisions (c)	3,147,085	(309,057)	2,838,028
Liabilities with post-retirement benefit plans (c)	-	308,893	308,893
Other liabilities (b) (d)	1,523,771	(26,242)	1,497,529
Total noncurrent liabilities	**9,418,925**	**(1,848)**	**9,417,077**
Equity	**43,330,785**	**-**	**43,330,785**
Total liabilities and equity	**65,489,973**	**(1,412)**	**65,488,561**

(a) Amounts recorded as other accounts receivable were reclassified from “Other assets” to “Accounts receivable, net” (Notes 11 and 6).

(b) Finance lease amounts were reclassified from “Other obligations” to “Loans, financing and finance lease” (Notes 22 and 18.1).

(c) Actuarial liabilities of post-employment benefit plans were reclassified from “Provisions” to a specific line “Obligations with post-employment benefit plans” (Notes 20 and 35).

(d) Liabilities relating to share-based payment plans were reclassified from “Other obligations” to “Personnel, social charges and benefits” (Notes 22 and 15).

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(In thousands of reais)

Consolidated Balance Sheet as at December 31, 2012

ASSETS	**Balance sheet disclosed as of 12.31.12**	**Adjustments for adoption of IFRS 11 and Reclassifications**	**Balance sheet as of 12.31.12., disclosed as of 12.31.13**
Current assets			
Cash and cash equivalents	7,196,079	(62,594)	7,133,485
Trade accounts receivable, net (a)	5,513,436	33,502	5,546,938
Dividend and interest on equity	-	1,140	1,140
Taxes recoverable	2,052,423	(2)	2,052,421
Other assets (a)	1,510,004	(34,807)	1,475,197
Total current assets	**16,271,942**	**(62,761)**	**16,209,181**
Noncurrent assets			
Deferred taxes	1,029,598	(1,710)	1,027,888
Judicial deposits and garnishments	3,909,474	(206)	3,909,268
Other assets	1,399,830	(47,797)	1,352,033
Investments	23,683	119,198	142,881
Property, plant and equipment, net	17,610,851	(6,707)	17,604,144
Intangible assets, net	30,009,289	(3,592)	30,005,697
Total noncurrent assets	**53,982,725**	**59,186**	**54,041,911**
Total assets	**70,254,667**	**(3,575)**	**70,251,092**

LIABILITIES AND EQUITY	**Balance sheet disclosed as of 12.31.12**	**Adjustments for adoption of IFRS 11 and Reclassifications**	**Balance sheet as of 12.31.12., disclosed as of 12.31.13**
Current liabilities			
Personnel, social charges and benefits	416,355	(103)	416,252
Trade accounts payable	5,889,377	(309)	5,889,068
Taxes, charges and contributions	1,781,480	(230)	1,781,250
Loans, financing and lease (b)	1,255,323	14,799	1,270,122
Other liabilities (b)	4,194,936	(14,836)	4,180,100
Total current liabilities	**13,537,471**	**(679)**	**13,536,792**

Noncurrent liabilities			
Personnel, social charges and benefits (d)	-	13,224	13,224
Loans, financing and lease (b)	3,756,001	18,460	3,774,461
Provisions (c)	3,846,899	(393,262)	3,453,637
Liabilities with post-retirement benefit plans (c)	-	392,269	392,269
Other liabilities (b) (d)	4,433,176	(33,587)	4,399,589
Total noncurrent liabilities	**12,036,076**	**(2,896)**	**12,033,180**
Equity	**44,681,120**	**-**	**44,681,120**
Total liabilities and equity	**70,254,667**	**(3,575)**	**70,251,092**

(a) Amounts recorded as other accounts receivable were reclassified from “Other assets” to “Accounts receivable, net” (Notes 11 and 6).

(b) Finance lease amounts were reclassified from “Other obligations” to “Loans, financing and finance lease” (Notes 22 and 18.1).

(c) Actuarial liabilities of post-employment benefit plans were reclassified from “Provisions” to a specific line “Obligations with post-employment benefit plans” (Notes 20 and 35).

(d) Liabilities relating to share-based payment plans were reclassified from “Other obligations” to “Personnel, social charges and benefits” (Notes 22 and 15).

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Consolidated Income Statement for the year ended December 31, 2012

	Income statement as of 12.31.12, disclosed as of 12.31.12	Adjustments for adoption of IFRS 11 and Reclassifications	Income statement as of 12.31.12, disclosed as of 12.31.13
Net operating revenue	33,931,422	(11,766)	33,919,656
Cost of sales	(16,564,464)	7,020	(16,557,444)
Gross profit	**17,366,958**	**(4,746)**	**17,362,212**
Selling expenses	(8,693,696)	-	(8,693,696)
General and administrative expenses	(2,148,476)	3,168	(2,145,308)
Other operating income, net	687,503	209	687,712
Equity pickup	-	588	588
Income before financial income (expenses)	**7,212,289**	**(781)**	**7,211,508**
Financial income	1,281,554	(449)	1,281,105
Financial expenses	(1,572,369)	-	(1,572,369)
Income before taxes	**6,921,474**	**(1,230)**	**6,920,244**
	(2,469,293)	1,230	(2,468,063)
Net income for the period	**4,452,181**	**-**	**4,452,181**

Consolidated Statement of Cash Flow for the year ended December 31, 2012

	Cash flow statement as of 12.31.12, disclosed as of 12.31.12	Adjustments for adoption of IFRS 11 and Reclassifications	Cash flow statement as of 12.31.12, disclosed as of 12.31.13
Income before taxes	6,921,474	(1,230)	6,920,244

Expenses (revenues) not representing changes in cash	6,139,975	7,947	6,147,922
(Increase) decrease in operating assets:	(557,118)	317,349	(239,769)
Increase (decrease) in operating liabilities:	(2,771,162)	(3,238)	(2,774,400)
Total cash generated by (used in) operating activities	**9,733,169**	**320,828**	**10,053,997**
Cash generated by (used in) investing activities	**(3,397,253)**	**(323,586)**	**(3,720,839)**
Cash generated by (used in) financing activities	**(2,080,179)**	**(9,037)**	**(2,089,216)**
Increase (decrease) in cash and cash equivalents	**4,255,737**	**(11,795)**	**4,243,942**
Cash and cash equivalents at beginning of year	**2,940,342**	**(50,799)**	**2,889,543**
Cash and cash equivalents at end of year	**7,196,079**	**(62,594)**	**7,133,485**
Changes in cash and cash equivalents for the year	**4,255,737**	**(11,795)**	**4,243,942**

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Consolidated Statement of Value Added for the year ended December 31, 2012

	Statement of value added as of 12.31.12, disclosed as of 12.31.12	**Adjustments for adoption of IFRS 11 and Reclassifications**	**Statement of value added as of 12.31.12, disclosed as of 12.31.13**
Revenues	46,224,912	(14,185)	46,210,727
Inputs acquired from third parties	(15,700,903)	7,102	(15,693,801)
Gross value added	**30,524,009**	**(7,083)**	**30,516,926**
Retentions	**(5,493,159)**	**1,383**	**(5,491,776)**
Net value added generated	**25,030,850**	**(5,700)**	**25,025,150**
Value added received in transfer	**1,281,553**	**139**	**1,281,692**
Total value added to be distributed	**26,312,403**	**(5,561)**	**26,306,842**
Distribution of value added	**(26,312,403)**	**5,561**	**(26,306,842)**
Personnel, social charges and benefits	(2,185,653)	1,183	(2,184,470)
Taxes, charges and contributions	(15,933,036)	3,867	(15,929,169)
Debt remuneration	(2,982,393)	(381)	(2,982,774)
Equity remuneration	(4,452,181)	-	(4,452,181)
Other	(759,140)	892	(758,248)

New IFRS and IFRIC interpretations not yet in effect as at December 31, 2013

The following IFRS and IFRIC interpretations had been published by the date of these financial statements, but their application was not mandatory:

IFRS 2 Share-based Payment: These amendments changed the settings relating to the purchase and implementation is effective beginning on or after 1 July 2014. The Company did not expect any significantly impact in its financial statements considering this change.

IFRS 3 Business Combinations: The amendments changed the accounting for contingent consideration in a business combination. Contingent consideration on acquisition of a business that is not classified as equity are subsequently measured at fair value through profit or loss, whether or not included in the scope of IFRS 9 Financial Instruments. These changes are effective for new business combinations after July 1st, 2014 . The Company consider the application of these changes to any business combinations that occur beginning on or after 1 July 2014.

IFRS 8 Operating Segments: The changes are related to the aggregation of operating segments, which can be combined / aggregated whether they are in accordance with the criteria of the rule , in other words, if the segments have similar economic characteristics and are similar in other qualitative aspects. If they are combined, the entity shall disclose the economic characteristics used to assess whether the segments are similar. These amendments take effect beginning on or after 1 July 2014. Considering the fact that the Company and its subsidiaries operates in one operating segment, is not expected to significantly impact its financial statements and disclosure.

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IFRS 9 Financial Instruments: IFRS 9, as issued, reflects the first phase of the IASB's work on the replacement of IAS 39 and applies to classification and measurement of financial assets and financial liabilities as defined in IAS 39. The standard was initially effective for annual periods beginning on or after January 1, 2013, but Amendments to IFRS 9 Mandatory Effective Date of IFRS 9 and Transition Disclosures, issued in December 2011, postponed to a undefined date.. In subsequent phases, the IASB will address hedge accounting and impairment of financial assets. The adoption of the first phase of IFRS 9 will have an effect on the classification and measurement of the Company's financial assets, but will not have an impact on classification and measurements of financial liabilities. The Company will quantify the effect in conjunction with the other phases of IASB project, when the final standard consolidating all phases is issued.

Investment Entities (Amendments to IFRS 10, IFRS 12 and IAS 27): The amendments will be effective for annual periods beginning on or after January 1, 2014, providing an exception to the consolidation requirements for a reporting entity that meets the definition of an investment entity under IFRS 10. This exception requires an investment entity to account for its investments in subsidiaries at fair value in profit or loss. The Company does not expect these amendments to significantly impact its financial statements, given that none of its subsidiaries qualifies as an investment entity.

IFRS 13 Fair Value Measurement: The amendment prospectively after July 1st, 2014 . The change is related to the application of the exception financial assets portfolio, financial liabilities and other contracts. The Company and its subsidiary will evaluate the effect of implementation of new business beginning on or after 1 July 2014.

IAS 16 Property Plant and Equipment and IAS 38 Intangible Assets: The amendment to IAS 16.35 (a) and IAS 38.80 (a) clarifies that a revaluation can be made as follows: i) adjust the gross carrying amount of the asset at market value or , ii) determine the market value and adjust the gross carrying amount proportionally, so that the resulting carrying amount is equal to the market value. IASB also clarified that the accumulated depreciation / amortization is the difference between the gross carrying amount and the carrying amount of the asset (ie gross book value - depreciation / accumulated amortization = book value). The amendment to IAS 16.35 (b) and IAS 38.80 (b) clarifies that the accumulated depreciation / amortization is eliminated so that the gross carrying amount and the book value is equal to market value. The changes will take effect retrospectively beginning on or after 1 July 2014. Implementation of these changes have no impact on the financial or operational condition of the Company and its subsidiary at the time. Whereas the reassessment of fixed assets and intangible assets is not allowed in Brazil, the Company do not expect impact on your financial statements.

IAS 24 Related Party Disclosures: The amendment clarifies that an entity's providing key management personnel services to the reporting entity or to the parent of the reporting entity is a related party of the reporting entity. In addition, an entity that uses a management entity shall disclose the expenses incurred by management services. The changes will take effect retrospectively beginning on or after 1 July 2014. The Company does not expect these amendments significantly impacting its financial statements.

IAS 32 Offsetting Financial Assets and Financial Liabilities - Amendments to IAS 32: These amendments clarify the meaning of “currently has a legally enforceable right to set off the recognized amounts” and the criteria that would qualify for settlement the settlement mechanisms of clearing house systems that are not simultaneous. These amendments will become effective for annual periods beginning on or after January 1, 2014. The Company does not expect these amendments to significantly impact its financial statements.

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IFRIC 21 Levies: IFRIC 21 clarifies that an entity recognizes a liability for a levy when the activity that triggers payment occurs. For a levy that is triggered upon reaching a minimum threshold, the interpretation clarifies that no liability is recognized before the specified minimum threshold is reached. IFRIC 21 becomes effective for annual periods ending on or after January 1, 2014. The Company does not expect IFRIC 21 to significantly impact its financial statements.

IAS 39 Novation of Derivatives and Continuation of Hedge Accounting - Amendments to IAS 39: The amendments provide a relief on the discontinuation of hedge accounting in certain circumstances in which a hedging instrument is to be novated. These amendments will become effective for annual periods beginning on or after January 1, 2014. These amendments shall apply to future novations of derivatives.

IAS 40 Investment Property: This amendment clarifies the relationship between the definitions of IFRS 3 and IAS 40 on the classification of the investment property or owner-occupied property. The description of ancillary services in IAS 40 that differentiates between investment properties and owner occupied property (IFRS 3) is used to determine whether the transaction is a purchase of an asset or a business combination. This amendment is effective prospectively beginning on or after 1 July 2014. The Company will evaluate any possible impact in case of transactions occur after the effective date.

2.2 - Basis of consolidation and significant changes at consolidation level

On consolidation, all intercompany assets, liabilities, income and expenses, as well as equity interests held, are eliminated in full.

Information on investees is described below:

Telefônica Data S.A. (TData): Headquartered in Brazil, the business purpose of this entity is to provide and operate telecommunications services; provide value added services (SVAs); provide integrated business solutions in telecommunications and related activities; manage the provision of technical assistance and maintenance services of telecommunications equipment and network, consulting services regarding telecommunications solutions and related activities, and design, implementation and installation of telecommunication-related projects; sell and lease telecommunications equipment, products and services, value-added services or any other related services, provided or supplied by third parties; provide third parties with telecommunications infrastructure; manage and/or develop activities that are necessary or useful for performing such services in accordance with applicable law; provide business trading services in general and provide technical support services in IT, including consulting, installation and maintenance of goods, applications and services, licensing or sub licensing of any kind of software, and storage and management of data and information. On July 1, 2013, part of its net assets were spun-off and merged into the Company and, on the same date, parts of the net assets of Vivo and ATelecom were merged into TData (Note 1b).

Vivo S.A. (Vivo): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to operate SMP services, including activities necessary or useful for the performance of these services, in conformity with the authorizations it was granted.

Vivo was split up and merged into the Company and TData on July 1, 2013 (Note 1b).

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A. Telecom S.A. (ATelecom): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to manage the rendering of telecommunication and installation services, to operate and maintain Internet, Intranet and Extranet solutions, business representation, mediation, intermediation and distribution of goods, to sell, agency, lease and maintain of telecommunication and general IT systems, equipment and devices, to provide advisory and technical support services regarding specification, implementation and maintenance of new voice, data and image systems, to import and export goods and services that are useful for the performance of its business purpose and to hold interests in the capital of other Brazilian or foreign entities, as a partner, shareholder or member. ATelecom was split up and merged into the Company and TData on July 1, 2013 (Note 1b).

Telefônica Sistema de Televisão S.A. (TST): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to provide Multichannel Multipoint Distribution Service (MMDS) type pay television services, in addition to general telecommunication and Internet services. TST was merged into the Company on July 1, 2013 (Note 1b).

Ajato Telecomunicações Ltda. (Ajato): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to provide telecommunication and IT services, to sell, lease, import, export, maintain and repair related equipment. Ajato was merged into TST (later merged into the Company) on July 1, 2013 (Note 1b).

GTR-T Participações e Empreendimentos S.A. (GTR-T): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to hold interests in other companies engaged in rendering pay and cable television services, telecommunication services in general, acquisition, licensing, import and distribution of own or third-party television programs, replacement parts and equipment, management and operation of telecommunication and pay television service platforms. A GTR-T was merged into TST (later merged into the Company) on July 1, 2013 (Note 1b).

TVA Sul Paraná S.A. (Sul Paraná): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to render pay and cable television services, telecommunication services in general, to acquire, license, import and distribute own or third-party television programs, replacement parts and equipment, to manage and operate telecommunication and pay television service platforms and to publish periodicals. A Sul Paraná was merged into TST (later merged into the Company) on July 1, 2013 (Note 1b).

Lemontree Participações S.A. (Lemontree): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to hold interests in other companies engaged in rendering pay and cable television services, telecommunication services in general, acquisition, licensing, import and distribution of own or third-party television programs, replacement parts and equipment, management, updating and operation of telecommunication and pay television service platforms and management and selling of data. A Lemontree was merged into TST (later merged into the Company) on July 1, 2013 (Note 1b).

Comercial Cabo TV São Paulo S.A. (CaTV): Headquartered in Brazil, the business purpose of this entity was, until June 30, 2013, to render pay television services, to provide general telecommunication advisory and consulting services, to acquire, license, import and distribute own or third-party television programs, replacement parts and equipment, to manage update and operate all types of advertising and publicity. A CaTV was merged into TST (later merged into the Company) on July 1, 2013 (Note 1b).

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Aliança Atlântica Holding B.V. (Aliança): Headquartered in Amsterdam, Netherlands, this entity has a 50% interest held by Telefônica Brasil and cash generated from sale of Portugal Telecom shares in June 2010. Through May 8, 2012, the Company held equity interest in Zon Multimédia, a Portugal Telecom group company that renders services involving pay television, Internet, distribution of audiovisual contents, cinema and telecommunication services. This equity interest was disposed of on May 8, 2012.

Companhia AIX de Participações (AIX): Headquartered in Brazil, this entity is engaged in holding an interest in Refibra consortium, and in performing activities related to the direct and indirect operation of activities related to the construction, completion and operation of underground networks or optical fiber ducts.

Companhia ACT de Participações (ACT): Headquartered in Brazil, this entity is engaged in holding an interest in Refibra consortium, and in performing activities related to the rendering of technical support services for the preparation of projects and completion of networks, by means of studies required to make them economically feasible, and monitor the progress of Consortium-related activities.

Direct and indirect subsidiaries and jointly controlled entities, as well as the percentage of interest held by the Company as of December 31, 2013 and 2012 are as follows:

At December 31, 2013

	Direct ownership interest		
Investees	Investor	Interest held	Total interest held
Wholly-owned subsidiaries			
TData	Telefônica Brasil	100.00%	100.00%

Jointly controlled entities			
Aliança	Telefônica Brasil	50.00%	50.00%
AIX	Telefônica Brasil	50.00%	50.00%
ACT	Telefônica Brasil	50.00%	50.00%

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At December 31, 2012

	Direct ownership interest		Indirect ownership interest		
Investees	Investor	Interest held	Investor	Interest held	Total interest held
Wholly-owned subsidiaries					
Vivo	Telefônica Brasil	100.00%	-	-	100.00%
TData	Telefônica Brasil	100.00%	-	-	100.00%
ATelecom	Telefônica Brasil	100.00%	-	-	100.00%
TST	Telefônica Brasil	100.00%	-	-	100.00%
Ajato	-	-	TST	100.00%	100.00%
GTR-T	Telefônica Brasil	100.00%	-	-	100.00%
Sul Paraná	Telefônica Brasil	79.29%	GTR-T	20.71%	100.00%
Lemontree	Telefônica Brasil	100.00%	-	-	100.00%
CaTV	Telefônica Brasil	78.48%	Lemontree	21.52%	100.00%
Jointly controlled entities					
Aliança	Telefônica Brasil	50.00%	-	-	50.00%
AIX	Telefônica Brasil	50.00%	-	-	50.00%
ACT	Telefônica Brasil	50.00%	-	-	50.00%

The main events and changes at the consolidation level, which, given their significance, should be considered for the purpose of reviewing the consolidated financial information for the years ended December 31, 2013 and 2012 are described below:

2013 - Corporate restructuring

In order to streamline the Company's organizational structure, to rationalize the services provided by its subsidiaries and to concentrate service provision in two operating entities, namely the Company and its wholly-owned subsidiary TData, on March 15, 2012, the Company filed with the ANATEL a request for previous approval of corporate restructuring, which became legally feasible due to legislation changes applicable to STFC operators through Law No. 12485.

This corporate restructuring process was approved by ANATEL under Act No. 3043, of May 27, 2013, as published in the DOU of May 29, 2013, subject to the conditions thereunder (Note 1b).

2012 - Acquisition of Lemontree and GTR-T shares

On June 6, 2012, the Company exercised its option to purchase (a) the remaining 71,330,508 common shares of Lemontree, which controls CaTV, corresponding to 51% of the voting capital; and (ii) the remaining 923,778 common shares of GTR-T, holder of 50.9% of Sul Paraná common shares previously held by Abril group. The call option exercised on that date completes the acquisition of Lemontree and GTR-T remaining shares, which started with the partial exercise of the call option implemented on September 29, 2011, with the acquisition of Lemontree common shares, representing 49% of its capital. Amounts corresponding to the acquisition of the remaining common shares of Lemontree and GTR-T totaled R$37,737 and R$6,434, respectively.

This transaction was accounted for as an acquisition of non-controlling shareholders' interests for the purpose of disclosure and measurement in these financial statements.

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Upon exercising this option, the Company became holder of 100% of the shares representing the voting and total capital of Lemontree and GTR-T and, indirectly, of the cable TV service operators located in the cities of São Paulo, Curitiba, Foz do Iguaçu and Florianópolis.

<u>2012 - Disposal of shares of Zon Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A.</u>

On May 8, 2012, the Company disposed of 1,618,652 (1,196,395 directly and 422,257 indirectly through Aliança Atlântica) common shares representing 0.52% of the voting capital of Zon Multimédia – Serviços de Telecomunicações e Multimédia, SGPS, S.A. (ZON). Consolidated net income (amount obtained from disposal of shares held and divestiture of investments) from this transaction amounted to R$1,486.

3. SUMMARY OF SIGNIFICANT ACCOUNTING PRACTICES

a) <u>Cash and cash equivalents</u>

Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investing or any other purposes. The Company considers cash equivalents to be short-term investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. An investment normally qualifies as a cash equivalent if it has a short-term maturity, e.g. three months or less, from the date of acquisition (Note 5).

b) <u>Accounts receivable, net</u>

Trade accounts receivable are stated at the amount of services rendered under agreed-upon conditions, net of the allowance for doubtful accounts. These include services rendered to customers not yet billed to the balance sheet date, as well as receivables for the sale of cell phones, simcards and accessories. The allowance for doubtful accounts is recognized at an amount sufficient to cover losses, if any, and primarily considers the expected default level (Note 6).

c) Inventories

Inventories are carried at the lower of average acquisition cost and net realizable value, and include cell phones, simcards, prepaid cards, accessories, consumables and supplies. Net realizable value is the selling price in the ordinary course of business, less estimated costs necessary to make the sale (Note 7).

A provision for impairment losses is recognized for supplies and devices deemed obsolete or stored in quantities higher than what the Company usually sells in a given period of time.

d) Prepaid expenses

These are stated at amounts actually disbursed on services acquired but not yet incurred. Prepaid expenses are recognized in the income statement as the related services are provided and the economic benefits flow to the Company (Note 10).

e) Investments

The Company's investments in investees (subsidiaries or jointly-controlled entities) are accounted for using the equity method in the individual financial statements. In the consolidated financial statements investments in subsidiaries are consolidated in full.

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Under the equity method, the investment is carried in the balance sheet at cost plus post-acquisition changes in the Company's share of net assets acquired.

The income statement reflects the share of the results of operations of the investees. Where there has been a change recognized directly in the equity of the investees, the Company recognizes its share of any changes and discloses this, when applicable, in the statement of changes in equity and in the statement of comprehensive income.

The financial statements of the investees are prepared for the same reporting period as the Company. Where necessary, adjustments are made to bring the accounting policies in line with those of the Company.

After application of the equity method, the Company determines whether it is necessary to recognize an additional impairment loss on the Company's investment in its investees. The Company determines at each reporting date whether there is any objective evidence that the investment is impaired. If this is the case the Company calculates the amount of impairment as the difference between the recoverable amount of the investees and their carrying value and recognizes the amount in the income statement.

Upon loss of significant influence over the investee, the Company measures and recognizes any retaining investment at its fair value. Any difference between the carrying amount of the investees upon loss of significant influence and the fair value of the retaining investment and proceeds from disposal is recognized in profit or loss.

On consolidation, all intercompany assets, liabilities, income and expenses, as well as equity interests held, are eliminated in full, considering the Company's proportionate share in the net assets of the investee.

Foreign exchange differences in the net assets of Aliança (jointly-controlled entity) are recognized in the Company's equity as "Cumulative Translation Adjustment".

f) Fixed assets, net

Fixed assets are stated at acquisition and/or construction cost, net of accumulated depreciation and/or accumulated impairment losses, if any. Such cost includes the borrowing costs for long-term construction projects if the recognition criteria are met, and is stated net of ICMS (State VAT) credits, which were recorded as recoverable taxes.

Asset costs are capitalized until the asset becomes operational. Costs incurred after the asset becomes operational and that do not improve the functionality or extend the useful life of the asset are immediately expensed, under the accrual method of accounting. When significant parts of fixed assets are required to be replaced at intervals, the Company recognizes such parts as individual assets with specific useful life and depreciation. Likewise, expenses that represent asset improvement (expanded installed capacity or useful life) are capitalized. All other repair and maintenance costs are recognized in the income statement as incurred.

The present value of the expected cost for the decommissioning of towers and equipment on leased property is capitalized in the cost of the respective asset matched with the provision for dismantling obligations (Note 20) and depreciated over the useful life of the related assets, which do not exceed the lease term.

Depreciation is calculated on a straight-line basis over the useful life of assets, at rates that take into consideration the estimated useful life of assets based on technical studies. The assets’ residual values, useful life and methods of depreciation are reviewed at each financial year end and adjusted prospectively, if appropriate.

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A fixed asset item is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between the net disposal proceeds and the carrying amount of the asset) is included in the income statement when the asset is derecognized.

g) **Intangible assets, net (including goodwill at the consolidated level)**

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is its fair value as at the date of acquisition.

Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses, if any. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is reflected in the income statement in the year in which the expenditure is incurred.

The useful life of intangible assets are assessed as either finite or indefinite, as follows:

- Intangible assets with finite life are amortized over the useful economic life using the straight-line method and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed on an annual basis. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite life is recognized in the income statement in the cost/expense category consistent with the function of the intangible assets. Intangible assets include the rights to use software acquired from third parties, authorizations and licenses granted by ANATEL, customer portfolio, trademarks and other intangible items.

- Intangible assets with indefinite useful life are not amortized, but are tested for impairment annually, either individually or at the cash-generating unit level. The assessment of indefinite life is reviewed annually to determine whether the indefinite life continues to be supportable. If not, the change in useful life from indefinite to finite is made on a prospective basis. Goodwill arising from investment acquisition is assessed as having an indefinite useful life.

Gains and losses arising from derecognition of an intangible asset are measured as the difference between the net disposal proceeds and the carrying amount of the asset and are recognized in the income statement when the asset is derecognized.

h) Leases

The determination of whether an arrangement is, or contains, a lease is based on the substantive aspects regarding the use of a specific asset or assets or the right to use an asset, at inception date.

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Leases which transfer to the Company or subsidiary substantially all the risks and benefits incidental to ownership of the leased item are classified as finance leases. These are capitalized at the commencement of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Initial direct costs incurred in negotiating a lease are added to the carrying amount of the leased asset. Lease payments are apportioned between finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Implicit interest recognized in liabilities is allocated to the income statement over the lease term or using the effective interest rate method.

Amounts recorded as finance leases are depreciated over the estimated useful life of the assets. However, if there is no reasonable certainty that the Company will obtain ownership by the end of the lease term, the asset is depreciated over the shorter of the estimated useful life of the asset and the lease term.

Leases in which a significant part of the risks and benefits of ownership are retained by the lessor are classified as operating leases, and the effects are recognized in the income statement over the lease term.

The Company or subsidiary has lease arrangements classified as finance leases both as a lessor and as a lessee.

• As a lessor: lease of IT equipment (Produto Soluciona TI) for which the Company recognizes revenue, upon inception, at the present value of lease payments matched with accounts receivable.

• As a lessee transmission equipment and media arising from a joint construction agreement with another telecomm operator, based on an optical network linked to the power transmission line, interconnecting the northern Brazilian cities to the Company’s national backbone and lease of towers and rooftops (arising from sale and finance leaseback, for which the net book value of the assets upon disposal remained unchanged, a liability was recognized at the present value of minimum lease payments and deferred income was recorded at the difference between the selling price and the mentioned present value.

The difference between the nominal amount of lease payments and booked accounts receivable/payable is recognized as finance income/expenses using the effective interest rate method over the lease term (Note 18.1).

i) <u>Analysis of the recoverability of non- financial assets</u>

The Company and subsidiary annually review the net book value of assets in order to evaluate events or changes in economic, operating or technological circumstances that may indicate impairment losses. Where such evidence is identified, and the carrying amount of an asset exceeds its recoverable amount, an impairment provision is recognized and the carrying amount is written down to its recoverable amount.

An asset's (or the cash generating unit (CGU) that it belongs) recoverable amount is the higher of its value in use and fair value less costs to sell.

In assessing an asset's or the CGU's value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate (based on the Capital Asset Pricing Model - CAPM) that reflects the weighted average cost of capital and the specific risks of the asset or CGU.

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Fair value less costs to sell is determined considering, whenever possible, outright sale agreements in arm's length transactions between knowledgeable and willing parties less costs of disposal; if no outright sale agreements can be identified, this will be based on the market price of an active market or the price of the most recent transaction involving similar assets.

Impairment losses of continuing operations, including impairment on inventories, are recognized in the income statement in those expense categories consistent with the function of the impaired asset.

For assets excluding goodwill, an assessment is made at each reporting date as to whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased.

A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's or CGU's recoverable amount since the last impairment loss was recognized.

The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceeds the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the income statement.

The following assets have specific characteristics for impairment testing:

i.1) Goodwill: Goodwill is tested for impairment annually at the reporting date or before that when circumstances indicate that the carrying value may be impaired.

Where the recoverable amount is less than the carrying amount, an impairment loss is recognized. Impairment losses relating to goodwill cannot be reversed in future periods i.2) Intangible assets: Intangible assets with indefinite useful life are tested for impairment annually at the reporting date either individually or at the CGU level, as appropriate, and when circumstances indicate that the carrying value may be impaired.

i.3) Determination of value in use: The key assumptions used to estimate value in use are:

- Revenue: Revenue is projected considering the growth in customer base, the evolution of market revenue in view of GDP and the Company's share in this market;
- Operating costs and expenses: Variable costs and expenses are projected in accordance with the dynamics of the customers base, and fixed costs are projected in line with the historical performance of the Company, as well as with revenue growth; and
- Capital investments: Investments in capital goods are estimated considering the technological infrastructure necessary to enable the provision of services.

The key assumptions are based on historical performance of the Company and subsidiary and, reasonable macroeconomic assumptions justified based on financial market projections, documented and approved by the Company's management.

The impairment test of the Company and subsidiary's fixed and intangible assets did not result in recognition of impairment losses for the years ended December 31, 2013 and 2012, since their estimated market value is greater than the net carrying amount as of the estimation date.

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j) Business combination and goodwill

Business combinations are accounted using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred measured at acquisition date fair value and the amount of any non-controlling interest in the acquiree. For each business combination, the acquirer measures the non-controlling interest in the acquiree at fair value or at the proportionate share of the acquiree's identifiable net assets. Acquisition-related costs are expensed as incurred.

When the Company acquires a business, it assesses the financial assets and liabilities assumed for appropriate classification and designation in accordance with the contractual terms, economic circumstances and pertinent conditions as at the acquisition date. This includes the separation of embedded derivatives in host contracts by the acquiree.

If the business combination is achieved in stages, the previously held equity interest is remeasured at its acquisition date fair value and any resulting gain or loss is recognized in profit or loss.

Any contingent consideration to be transferred by the acquirer will be recognized at fair value at the acquisition date. Any subsequent changes in fair value of contingent consideration classified as an asset or liability are to be recognized in either profit or loss or other comprehensive income. Contingent consideration that is classified as equity is not remeasured and subsequent settlement is accounted for within equity.

Goodwill is initially measured at cost, being the excess of the aggregate of the consideration transferred and the amount recognized for non-controlling interest over the net identifiable assets acquired and liabilities assumed. If the fair value of the net assets acquired is in excess of the aggregate consideration transferred, the gain is recognized in profit or loss.

After initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to the cash-generating units that are expected to benefit from the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to those units.

Where goodwill has been allocated to a CGU and part of the operation within that CGU is disposed of, the goodwill associated with the disposed operation is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed in these circumstance is allocated based on the relative fair values of the disposed operation and the portion of the CGU retained.

k) Financial instruments – initial recognition and subsequent measurement

(i) Financial Assets

Initial recognition and measurement

Financial assets are classified as financial assets at fair value through profit or loss, loans and receivables, held-to-maturity investments, available-for-sale financial assets, or as derivatives designated as hedging instruments in an effective hedge, as appropriate. The Company and subsidiary determine the classification of its financial assets at initial recognition, as it becomes an integral part of contractual provisions of the instruments.

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All financial assets are initially recognized at fair value, plus, in case of investments not designated at fair value through profit or loss, transaction costs directly attributable to the acquisition of the financial asset.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the market place (regular way trades) are recognized on the trade date, i.e., the date that the Company and subsidiary commit to purchase or sell the asset.

The Company's and subsidiary financial assets include cash and cash equivalents, trade accounts receivable and other receivables, trade and non-traded financial instruments and derivative financial instruments.

Subsequent measurement

The subsequent measurement of financial assets depends on their classification, which may be as follows:

Financial assets at fair value through profit or loss: These include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling or repurchasing in the near term. This category includes derivative financial instruments taken out by the Company and subsidiary that do not meet the hedge accounting criteria, as defined by applicable standards. Financial assets at fair value through profit or loss are presented in the balance sheet at fair value, with the corresponding gains or losses recognized in the income statement.

Loans and receivables: These are non-derivative financial assets, with fixed or determinable payments, not traded in an active market. After the initial measurement, these financial assets are recorded at amortized cost under the effective interest method (effective interest rate), net of impairment, if and where applicable. The amortized cost is calculated in view of any discount or premium on the acquisition and rates or costs incurred. The amortization under the effective interest method is included in the financial income line in the statement of income. Impairment is recognized as financial expenses in the statement of income, if and where applicable.

Investments held to maturity: These are non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held to maturity whenever the Company and subsidiary expressed the intention and financial capacity to hold them to maturity. After the initial valuation, investments held to maturity are valued at amortized cost under the effective interest method, net of impairment. The amortized cost is calculated in view of any discount or premium on the acquisition and rates or costs incurred. The amortization of effective interest is included in financial income, in the statement of income. Losses on impairment are recognized as financial expenses in the statement of income. The Company and its subsidiaries did not record investments held to maturity during the years ended December 31, 2013 and 2012.

Financial assets available for sale: These are non-derivative financial assets not classified as: (i) loans and receivables, (ii) investments held to maturity or (iii) financial assets at fair value through profit or loss. These financial assets include equity and debt instruments. Debt securities in this category are those that are intended to be held for an indefinite period of time and that may be sold in response to needs for liquidity or in response to changes in the market conditions.

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After the initial measurement, financial assets available for sale are measured at fair value, and unrealized gains and losses are recognized directly in the reserve for assets available for sale in other comprehensive income until the investment is written off, except for impairment losses, interest calculated using the effective interest rate method and foreign exchange gains and losses on monetary assets recognized in the income statement.

When the investment is derecognized or when impairment loss is identified, cumulative gains or losses previously recognized in other comprehensive income (loss) shall be recognized in the income statement.

The fair value of financial assets available for sale denominated in foreign currency is measured in the foreign currency and translated at the spot exchange rate of balance sheet date.

Fair value changes attributable to translation differences are recognized directly in equity.

Derecognition (write-offs)

A financial asset (or, whenever the case, a part of a financial asset, or a part of a group of similar financial assets) is derecognized when:

• The rights to receive the cash flows from the asset have expired;

• The Company and subsidiary has transferred its rights to receive cash flows of the asset or has assumed an obligation to fully pay the cash flows received, without significant delay to a third party under an onlending agreement, and (i) the Company transferred substantially all risks and rewards of the asset, or (ii) the Company has neither transferred nor retained substantially all risks and rewards related to the asset, but has transferred control over the asset.

When the Company or subsidiary has transferred its rights to receive the cash flows from an asset or has entered into a pass-through arrangement, and has neither transferred nor retained substantially all the risks and rewards related to the asset, the asset is recognized to the extent of the Company's continuing involvement in the asset.

(ii) Impairment of financial assets

The Company and subsidiary assesses at the balance sheet dates whether there is any objective evidence of impairment of the financial asset or group of financial assets. A financial asset or group of financial assets is considered to be impaired only if there is an objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (an incurred "loss event") and this loss event impacted the estimated future cash flow of the financial asset or group of financial assets that can be reliably measured.

Evidence of impairment loss may include indication that the borrowing parties are going through significant financial hardship. The probability that they will go bankrupt or other financial reorganization, that there will be default or late payment of interest or principal may be indicated by a measurable drop in the estimated future cash flows, such as changes in maturity or economic conditions related to *defaults*.

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Financial assets at amortized cost

With regard to financial assets at amortized cost, first, the Company or subsidiary individually tests whether there are clear evidence of impairment for each financial asset individually significant or group of financial assets that are not individually significant. If the Company concludes that there is no impairment evidence for a financial asset individually tested, whether significant or not, the asset is included in a group of financial assets with similar characteristics of credit risk and is tested as a whole in relation to impairment. Assets that are individually tested for impairment, and for which impairment loss is or continues to be recognized, are not included in any group of financial assets to be tested for impairment.

When there is clear evidence of impairment, the impairment loss is measured as the difference between the asset book value and the present value of the estimated future cash flows (excluding future credit losses expected but not incurred). The present value of estimated future cash flows is discounted at the original effective interest rate for the financial asset.

The asset book value is decreased by a provision and the loss amount is recognized in the income statement. Loans, jointly with the corresponding provision, are written off when there is no realistic perspective of its future recovery and all guarantees have been realized or transferred to the Company. If in a subsequent year the estimated impairment loss increase or decrease due to an event occurring after the impairment loss recognition, the loss previously recognized is increased or decreased, adjusting itself with the provision. In case of future recovery, if any, of an amount written off, this recovery is recognized in the income statement.

Available for sale financial investments

The Company and subsidiary assesses at the balance sheet dates whether there is objective evidence that an investment is impaired.

In the case of equity investments classified as available-for-sale, objective evidence would include a significant or prolonged decline in the fair value of the investment below its cost.

When there is evidence of impairment, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that investment previously recognized in the income statement – is removed from equity and recognized in the income statement. Increases in their fair value after impairment are recognized directly in other comprehensive income

In the case of debt instruments classified as available for sale, impairment is assessed based on the same criteria as financial assets carried at amortized cost. However, the amount recorded for impairment is the cumulative loss measured as the difference between the amortized cost and the current fair value, less any impairment loss on that investment previously recognized in the income statement.

Future interest income continues to be accrued based on the reduced carrying amount of the asset, using the rate of interest used to discount the future cash flows for the purpose of measuring the impairment loss. The interest income is recorded as part of finance income. If, in a subsequent year, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in the income statement, the impairment loss is reversed through the income statement.

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(iii) Financial liabilities

Initial recognition and measurement

Financial liabilities are initially classified as financial liabilities measured at fair value through profit or loss, loans and financing, accounts payable, or derivatives classified as hedging instruments, as the case may be. The Company and subsidiary determines the classification of its financial liabilities upon their initial recognition.

Financial liabilities are initially recognized at fair value plus, in the case of loans and financing, transaction cost directly attributable thereto.

Company's and subsidiary financial liabilities include trade and other accounts payable, loans and financing agreements, and derivative financial instruments.

Subsequent measurement

Measurement of financial liabilities depends on their classification, which can be as follows:

Financial liabilities at fair value through profit or loss: these include financial liabilities designated upon initial recognition at fair value through profit or loss. This category includes derivative financial instruments taken out by the Company and subsidiary that do not meet the hedge accounting criteria, as defined by applicable standards.

The Company and subsidiary did not designate any financial asset at fair value through profit or loss at the initial recognition.

Loans and financing: After initial recognition, loans and financing subject to interest are subsequently measured at amortized cost, using the effective interest rate method. Gains and losses are recognized in the income statement when the liabilities are derecognized and through the amortization process under the effective interest rate method.

Derecognition (write offs)

A financial liability is written off when the obligation thereunder is discharged, cancelled or expires.

When an existing financial liability is replaced by another from the same lender with substantially different terms, or terms of an existing liability are substantially modified, such replacement or modification is treated as write-off of original liability and recognition of a new liability, and the difference in corresponding carrying amounts is recognized in the income statement.

(iv) Offsetting of financial instruments –net disclosure

Financial assets and financial liabilities are offset and the net amount is reported in the balance sheet if, and only if, there is a current enforceable legal right of offsetting the amounts recognized and if there is the intention to offset or realize the asset and settle the liability simultaneously.

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(v) Fair value of financial instruments

The fair value of financial instruments actively traded in organized financial markets is determined based on purchase prices quoted in the market at close of business at balance sheet date, without any deduction for transaction costs.

The fair value of financial instruments for which there is no active market is determined by using valuation techniques. These techniques may include the use of recent market transactions (on an arm's length basis); reference to the current fair value of another similar instrument, analysis of discounted cash flows or other valuation models.

l) Derivative financial instruments and hedge accounting

The Company uses derivative financial instruments, such as currency and interest rate swaps, to provide hedge against the risk of changes in exchange rates.

Derivative financial instruments designated in hedging transactions are initially recognized at fair value on the date in which the derivative agreement is entered into, being subsequently revaluated also at fair value. Derivatives are presented as financial assets when the fair value of the instrument is positive and as financial liabilities when the fair value is negative.

Any gains or losses arising from changes in the fair value of derivatives are taken directly to profit or loss, except for the effective portion of cash flow hedges, which is recognized in other comprehensive income.

For the purpose of hedge accounting, hedges are classified as: cash flow hedges and fair value hedges.

At the inception of a hedge relationship, the Company formally designates and documents the hedge relationship to which the Company wishes to apply hedge accounting and the risk management objective and strategy for undertaking the hedge. The documentation includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the effectiveness of changes in the hedging instrument’s fair value in offsetting the exposure to changes in the hedged item’s fair value or cash flows attributable to the hedged risk.

As for cash flow hedges, the hedge relationship documentation also includes the highly probable forecast nature of the transaction as well as the periods expected to transfer gains or losses arising from hedge instruments from equity the income statement. Such hedges are expected to be highly effective in achieving offsetting changes in fair value or cash flows and are assessed on an ongoing basis to determine that they actually have been highly effective throughout the financial reporting periods for which they were designated.

The Company’s contracts are classified as cash flow hedges when they protect from changes in cash flows that are attributable to a particular risk associated to a recognized liability that may affect the result of operations, and as fair value hedges when they protect from changes in the fair value of an identified part of certain liabilities that are attributable to a particular risk and may affect the result of operations.

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Cash flow Hedges

Cash flow hedges meeting the recording criteria are accounted for as follows: (i) the portion of gain or loss from the hedge instrument determined as effective hedge shall be recognized directly in equity (in other comprehensive income) and (ii) the ineffective portion of gain or loss from the hedge instrument shall be recognized in the statement of income.

When the Company's documented risk management strategy for a specific hedging relationship excludes from the *hedge* effectiveness evaluation a specific component of gain or loss or the related cash flows from the hedging instrument, this excluded component of gain or loss is promptly recognized in financial income (expense).

The amounts recorded in other comprehensive income are promptly transferred to the income statement when the hedged transaction affects P&L, for instance, when hedged financial income or expense is recognized or when an expected sale takes place. When the hedged item is the cost of a non-financial asset or liability, the amounts recorded in equity are transferred to the initial carrying amount of the non-financial asset or liability.

If the hedging instrument expires or is sold, terminated or exercised without replacement or rollover (as part of the hedging strategy), or if its designation as a hedge is revoked, or when the hedge fails to meet the hedge accounting criteria, any cumulative gain or loss previously recognized in other comprehensive income remains separately in equity until the forecast transaction occurs or the firm commitment is fulfilled.

Fair value hedges

Fair value hedges meeting the recording criteria are accounted for as follows: (i) gain or loss from changes in fair value of a hedge instrument shall be recognized in the income statement as finance costs; and (ii) gain or loss from a hedged item attributable to the hedged risk shall adjust the recorded amount of the hedged item to be recognized in the statement of income, as finance costs.

For fair value hedges relating to items carried at amortized cost, any adjustment to carrying value is amortized through profit or loss over the remaining term of the hedge using the effective interest rate method. The effective interest rate amortization may begin as soon as an adjustment exists and no later than when the hedged item ceases to be adjusted for changes in its fair value attributable to the risk being hedged.

If the hedged item is derecognized, the unamortized fair value is recognized immediately in profit or loss.

When an unrecognized firm commitment is designated as a hedged item, the subsequent cumulative change in the fair value of the firm commitment attributable to the hedged risk is recognized as an asset or liability with a corresponding gain or loss recognized in profit and loss.

Current versus noncurrent classification

Derivative instruments not classified as effective hedge instrument are classified as current or non-current or segregated into short and long term portions based on an evaluation of the contracted cash flows.

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- When the Company and its subsidiary expect to hold a derivative as an economic hedge (and do not apply hedge accounting) for a period beyond 12 months after the reporting date, the derivative is classified as noncurrent (or separated into current and noncurrent portions) consistently with the classification of the underlying item.

- Derivative instruments that are designated as, and are effective hedging instruments, are classified consistently with the classification of the underlying hedged item.

The derivative instrument is separated into a current portion and a noncurrent portion only if a reliable allocation can be made.

m) <u>Fair value measurement</u>

The Company and subsidiary measures financial instruments, such as derivatives and non-financial assets, at fair value at each reporting date.

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value measurement is based on the assumption that the transaction to sell the asset or to transfer the liability will take place either:

- In the principal market for the asset or liability; or

- In the absence of a principal market, in the most advantageous market for the asset or liability.

The Company and subsidiary must have access to the principal (or most advantageous) market.

The fair value of an asset or liability is measured based on the assumption that market participants would use to define the price of an asset or liability, assuming that market participants act in their economic best interest.

A fair value measurement of a non-financial asset takes into account a market participant's ability to generate economic benefits by using the asset in its highest and best use or by selling it to another market participant that would use the asset in its highest and best use.

The Company and its subsidiary use valuation techniques that are appropriate in the circumstances and for which sufficient data are available to measure fair value, maximizing the use of relevant observable inputs and minimizing the use of unobservable inputs.

All the assets and liabilities for which a fair value is measured or disclosed in financial statements are categorized within the fair value hierarchy described below, based on the lowest level input that is significant to the entire fair value measurement.

<u>Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;</u>

<u>Level 2:</u> valuation techniques for which the lowest level input that is significant to the fair value measurement is either directly or indirectly observable.

<u>Level 3:</u> valuation techniques for which the lowest level input that is significant to the fair value measurement is not observable.

For assets and liabilities recognized in the financial statements on a recurring basis, the Company and subsidiary determines whether there have been transfers among hierarchy levels, revaluing their categorization (based on the lowest level input that is significant to the entire fair value measurement) at the end of each reporting period.

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For fair value disclosure purposes, the Company and subsidiary determined classes of assets and liabilities on the basis of the nature, characteristics and risks of the asset or liability and the level of the fair value hierarchy, as described above.

For the year ended December 31, 2013, there were neither transfers between “level 1” and “level 2” fair value measurements nor transfers between “level 3” and “level 2” fair value measurements. The Company has no financial instruments categorized within level 3 of the fair value hierarchy.

The fair values of financial instruments measured at amortized cost are described in Note 36.

n) Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily requires more than 18 months to get ready for its intended use or sale are capitalized as part of the underlying asset cost.

All other borrowing costs are expensed in the period they incur. Borrowing costs include interest expense and other costs incurred by an entity in respect of borrowings.

o) Interest on shareholders´ equity and dividends

Interest on shareholders´ equity

Brazilian legislation allows companies to pay interest on shareholders´ equity, which is similar to payment of dividends; however, this is deductible for income taxes calculation purposes. The amount due accrued by the Company and subsidiary in its accounting records in compliance with Brazilian tax law is matched against the financial expenses account in the income statement for the year and, for the presentation of these financial statements, such expense is reversed against a direct charge to equity, resulting in the same accounting treatment adopted for dividends. The distribution of interest on shareholders´ equity to shareholders is subject to withholding income tax at a 15% rate.

Dividends

The mandatory minimum dividends are recorded in the balance sheets as legal obligations (provisions in current liabilities), and the dividends in excess of such minimum amount, still not approved by the Shareholders' Meeting, are recorded in equity as dividend reserve.

p) Provisions

General

Provisions are recorded when the Company or subsidiary have a present (legal or constructive) obligation arising from past events, the settlement of which is expected to result in an outflow of economic benefits, in an amount that can be reliably estimated. Provisions are adjusted at balance sheet date considering the probable amount of loss and the nature of each contingency (Note 20).

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Provisions for contingencies are presented at their gross amount, less the corresponding judicial deposits, and are classified as provisions for civil, labor, tax and regulatory contingencies. Judicial deposits are classified as assets if the conditions required for their net presentation with the provision are not available.

Provisions for civil, labor, tax and regulatory contingencies

The Company and subsidiary are party to labor, tax, civil and regulatory claims and set up a provision for contingencies likelihood of loss of which was estimated as probable. Assessment of the likelihood of loss includes analysis of available evidence, hierarchy of laws, available case law, recent court rulings and their relevance in the legal system, as well as the evaluation of outside legal advisors. Provisions are reviewed and adjusted to take into account changes in circumstances, such as the applicable statute of limitations, tax audit conclusions or additional exposures identified based on new matters or court decisions.

Provision for demobilization of assets

This refers to costs to be incurred due to the return to the owners of the sites (locations intended for tower and equipment installation at leased property) under the same conditions at the time of execution of the initial lease agreement.

Demobilization costs are provided at the present value of expected costs to settle the obligation using estimated cash flows and are recognized as part of the cost of the particular asset. The cash flows are discounted at a current pre-tax rate that reflects the risks specific to demobilization liability. The unwinding of the discount is expensed as incurred and recognized in the income statement as a finance cost. The estimated future costs of demobilization are reviewed annually and adjusted as appropriate. Changes in the estimated future costs or in the discount rate applied are added to or deducted from the cost of the asset.

Contingent liabilities recognized in a business combination

A contingent liability recognised in a business combination is initially measured at its fair value.

Subsequently, it is measured at the higher of: i) the amount that would be recognized in accordance with the requirements for provisions above or; ii) the amount initially recognised less, when appropriate, cumulative amortization recognized in accordance with the requirements for revenue recognition.

q) <u>Taxes, charges and contributions</u>

Acronyms of the taxes, charges and contributions described in these financial statements are as follows:

CIDE – Contribution Tax for Intervention in the Economic Order – Federal Tax;

COFINS – Contribution Tax on Gross Revenue for Social Security Financing – Federal Tax;

CSLL – Social Contribution Tax on Net Profit – Federal Tax;

FISTEL – Telecommunications Inspection Fund;

FUNTTEL – Telecommunications Technology Development Fund;

FUST – Universal Telecommunication Services Fund;

ICMS – State VAT – State Tax;

IOF – Tax on Financial Transactions – Federal Tax;

IRPJ – Corporate Income Tax – Federal Tax;

IRRF – Withholding Income Tax – Federal Tax;

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ISS – Service Tax – Local Tax;

PIS – Contribution Tax on Gross Revenue for Social Integration Program – Federal Tax;

TFF – Inspection and Operation Fees; and

TFI – Inspection and Installation Fees.

Current income and social contribution taxes

The carrying amount of assets and liabilities related to the current tax of the last year and prior years corresponds to the amount estimated to be recovered from or paid to tax authorities. The tax rates and laws used in calculating the amounts referred to above are those in effect at the balance sheet date. In the balance sheet, current taxes are presented net of prepayments throughout the year.

Current income and social contribution taxes related to items directly recognized in equity are also recognized in equity. Management periodically assesses the tax position for the cases in which tax regulations require interpretation, and sets up provisions when necessary.

Deferred taxes

Deferred tax is generated from temporary differences at the reporting date between the tax bases of assets and liabilities and their carrying amounts.

Deferred tax assets are recognized for all deductible temporary differences and unused tax credits and losses, to the extent that taxable profit will likely be available so that deductible temporary differences can be realized and such unused tax credits and losses can be used, except: (i) when the deferred tax asset related to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction other than a business combination and does not impact, at the transaction date, the book profit or income or loss for tax purposes; and (ii) on deductible temporary differences related to investments in subsidiaries, where deferred tax assets are recognized only to the extent that it is probable that temporary differences will be reversed in the near future and taxable profit will likely be available so that temporary differences can be used.

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Derecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax liabilities are recognized for all temporary tax differences, except: (i) when the deferred tax liability arises from initial recognition of goodwill, or an asset or liability in a transaction other than a business combination, and does not affect book profit or tax income or loss on the transaction date; and (ii) on temporary tax differences related to investments in subsidiaries, in which temporary difference reversal period can be controlled and temporary differences are not likely to be reversed in the near future.

Deferred tax assets and liabilities are measured at the tax rate expected to be applicable for the year the asset will be realized or the liability will be settled, based on tax rates (and tax law) published as of the balance sheet date.

Deferred tax assets and liabilities are not discounted to present value and are classified in the balance sheet as noncurrent, regardless of the expected realization.

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Tax effects of items directly recorded in equity are also recognized in equity. Deferred tax items are recognized based on the transaction in which deferred tax was originated, in comprehensive income or directly in equity.

Deferred tax assets and liabilities are presented net if there is a legal or constructive right to offset tax assets against tax liabilities and when deferred taxes refer to the same taxable entity and are subject to the same tax authority.

Sales taxes

Revenue from services rendered is subject to ICMS or ISS taxation at the rates in force in each area and to PIS and COFINS taxation on a cumulative basis for revenue from telecommunication services, at 0.65% and 3.00%, respectively. Other revenue earned by the Company and subsidiary, including revenue from resale of goods, on a noncumulative basis, is taxed at 1.65% and 7.60% for PIS and COFINS, respectively, and by ICMS at the rates in force in each State.

Prepaid or recoverable taxes are recorded in current or noncurrent assets according to their estimated realization.

Provisional Measure (MP) No. 627

On November 11, 2013 was issued Provisional Measure No. 627 , which introduces a number of changes in the income tax legislation, social contribution, PIS, COFINS, among which are:

i) Repeal of Tax Regime (RTT), established by Law No. 11.941/09 of 27 May 2009, beginning on 1 January 2015, optional basis, beginning on January 1 , 2014 ; and

ii) Amendment of specific provisions of Decree - Law No. 1.598/77 with the objective of adapting the tax law with corporate law and accounting standards, due to the extinction of the RTT and the need to establish a new way of calculating the income tax and social contribution.

As permitted by Article No. 71 of this MP, the Company will opt for adoption of the provisions contained in Articles 1 to 66, when applicable, as of January 1 , 2014 , so the Federal Revenue of Brazil (RFB) define the shape, the term and conditions for that option.

r) <u>Other assets and liabilities</u>

An asset is recognized in the balance sheet when it is likely that its future economic benefits will flow to the Company or subsidiary, and its cost or value can be reliably measured.

A liability is recognized in the balance sheet when the Company or subsidiary have a legal or constructive obligation as a result of a past event and it is probable that an outflow of funds will be required to settle it.

Assets and liabilities are classified as current or noncurrent. An asset is classified as current when:

- it is expected to be realized or it is intended to be sold or used in the regular operating cycle;
- it is held primarily for trading;
- it is expected to be realized within 12 months from the reporting date; or
- cash or cash equivalents, unless there are limitations on its swap or it is used to settle a liability for at least 12 months after the reporting period.

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All other assets are classified as noncurrent.

A liability is classified as current when:

- it is expected to be settled in the regular operating cycle;
- it is held primarily for trading;
- it is expected to be realized within 12 months from the reporting date; or
- there is no unconditional right to defer the settlement of the liability for at least 12 months from the reporting date.

All other liabilities are classified as noncurrent.

s) <u>Present value adjustment of assets and liabilities</u>

Current and noncurrent monetary assets and liabilities are adjusted to present value whenever the effects are considered significant on the overall financial information. The present value adjustment is calculated using contractual cash flows and the explicit interest rate, and in certain cases the implicit interest rate, of respective assets and liabilities.

As such, the interest rates accrued on revenues, expenses and costs associated with these assets and liabilities are discounted with a view to recognizing them on an accrual basis. Subsequently, interest thereof is reallocated to financial income and expenses in the income statements by using the effective interest rate method in relation to the contractual cash flows. Implicit interest rates then applied were determined based on assumptions and are considered accounting estimates.

Based on the analysis performed and on management best estimates, the Company and subsidiary concluded that the adjustment to present value of current monetary assets and liabilities is immaterial in relation to the overall financial statements, and thus did not record any adjustment.

t) <u>Government grants and assistance</u>

Government grants are recognized when there is reasonable assurance that the benefit will be received and the corresponding conditions were met. When the benefit refers to expense item, it will be recorded in income in equal amounts throughout the expected useful life of the corresponding benefit, on a systematic basis in relation to cost of which the benefit intends to settle.

When the Company receives non-monetary benefits, the asset and the benefit are recorded at nominal value and reflected in the income statement over the expected useful life of the asset, at equal annual amounts. The loan or assistance is initially recognized or measured at fair value. A government grant is measured as the difference between the initial carrying amount of the loan and proceeds therefrom. A loan is subsequently measured in accordance with the accounting policy.

When loans or similar assistance are provided by governments or related institutions, with an interest rate below the current applicable market rate, the effect of this favorable interest is regarded as a government grant.

The Brazilian tax legislation (Provisional Executive Order (MP) No. 2199-14, of August 24, 2001, as amended by Law No. 11196, of November 21, 2005), enabled legal entities holding enterprises located in areas under the supervision of Supervisory Authority for Development of the Amazon (SUDAM) and Superintendency for the Development of the Northeast (SUDENE), whose activity fall under an economy sector considered a priority, under the Executive branch ruling, to claim income tax reduction under the terms thereof.

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Through the acquisition of Vivo Part. and Vivo, the Company benefits from a 75% income tax reduction, calculated based on profit from tax incentive operations (*lucro da exploração*) in the north region of Minas Gerais and Vale do Jequitinhonha and in the Brazilian states of Acre, Amapá, Amazonas, Maranhão, Mato Grosso, Pará, Rondônia and Roraima. This benefit will be effective up to 2013.

The profit generated by the portion subject to such benefit was excluded from calculation of dividends and may be only used in cases of capital increase or absorption of losses.

The financing lines through Banco Nacional de Desenvolvimento (BNDES), with interest rates lower than those prevailing in the market, under the scope of IAS 20/CPC 7, are recorded at fair value based on market rates. Adjustment arising from the comparison of the amount measured based on the rate agreed is upon accounted for as deferred revenue (Note 21).

u) <u>Revenue recognition</u>

Revenues substantially correspond to value of considerations received or receivable arising from the provision of telecommunications services and sale of goods are presented net of taxes, discounts and returns (in case of sale of goods) thereon. Revenues and expenses are stated on the accrual basis of accounting.

Revenue is recognized when it is probable that future economic benefits will flow to the Company and subsidiary, when it can be reliably measured, costs incurred in the transaction can be measured, the risks and benefits have been substantially transferred to the buyer and when specific criteria are met for every activity of the Company and subsidiary.

The Company and subsidiary assess its revenue arrangements against specific criteria to determine if it is acting as principal or agent. The Group has concluded that it is acting as a principal in all of its revenue arrangements, except for infrastructure swap revenue.

Revenues of the Company and subsidiary comprise basically the voice portal, data and additional telecommunication services that are offered to customers through fixed-price traffic packs (paid on a monthly basis) or based on customers' consumption, remuneration network usage and sales of goods.

Recognition of revenues from telecommunication services

Revenues from telecommunication services provided are recorded on the accrual basis based on the amounts agreed upon. Local and long-distance calls are billed by the measurement process under the legislation in force. The services billed on fixed monthly amounts are calculated and accounted for on a straight-line basis. Unbilled revenues from the last billing up to the balance sheet date is recognized in the month in which the service is provided.

Revenues related to public phone cards sales are deferred and recognized in the income statement based on the estimated usage of cards.

Revenues related to pre-paid mobile recharge credits, as well as taxes payable due are deferred and recognized in the income statement to the extent services are effectively provided.

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Revenues from equipment lease contracts classified as finance lease agreement are recognized in installation of equipment upon effective transfer of risk. Revenue is recognized at present value of future minimum payments provided for in contract.

Revenues from services are basically subject to the following indirect taxes: ICMS, PIS, COFINS and ISS.

Recognition of revenue and cost of goods sold

Revenues and cost of goods sold (mobile phones, simcards and accessories) are recorded when risks and rewards inherent to such goods are transferred to buyer. Sales made in own stores are recognized upon sale to final consumer. Revenues and costs of goods sold by dealers are recognized in the P&L when the device is activated, limited to 90 days after the date of sale.

Customer loyalty program

The Company has a loyalty points program that enables customers to accumulate points while paying bills regarding the usage of the services offered. The accumulated points may be exchanged for telephone sets or services, conditional upon obtaining a minimum balance of points by customer. The consideration received is allocated to the cost of sets or services at fair value. The fair value of these points is determined by dividing the discount granted by the number of points required for the redemption based on the such fidelity program. The fair value of the accumulated balance of points generated is deferred and recognized as revenue upon redemption of points.

The number of points to be accounted for is determined through statistical techniques that consider assumptions and historical data on expected redemption rates, such as, expiration percentage and cancellation of points. These estimates are subject to variations and uncertainties due to changes in the behavior of customers’ redemptions (Note 21).

Membership fee and promotional campaigns

Participation fees paid for promotional campaigns by customers of the Company are deferred and recorded in P&L throughout the duration of such campaign.

Agreements combining more than one element

Commercial packages offered by the Company that combine different elements are analyzed to determine whether it is necessary to separate the different elements identified, adopting the recognition criteria that is most adequate to each situation. The total revenue generated by the package sale is distributed among its elements, which were identified at their fair values.

The fair value determination of each element then identified implies the need for complex estimates given the nature of the business.

A possible change in fair values estimates could affect the distribution of revenues between components and consequently the deferred revenues.

v) Financial income and expenses

These include interest and monetary and exchange variations arising from short-term investments, derivative transactions, loans, financing, debentures, adjustments to present value of transactions that generate monetary assets and liabilities and other financial transactions. These are recognized on the accrual basis when earned or incurred by the Company or subsidiary.

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For all financial instruments measured at amortized cost and interest bearing financial assets classified as available for sale, interest income is recorded using the effective interest rate (EIR). EIR is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability.

w) Post-retirement benefit plans

The Company and subsidiary individually sponsor pension funds of post-retirement benefits for active and retired employees, in addition to a multiemployer supplementary retirement plan and health care plan to former employees. The contributions are determined on actuarial bases and recorded on the accrual basis. Benefit plans are determined based on actuarial evaluations at the end of each year, in order to ensure that the contributions are sufficient to set up the required reserve for both current and future commitments.

The actuarial liabilities related to defined benefit plans were calculated using the projected unit credit method. Actuarial gains and losses are recognized immediately in equity (in other comprehensive income).

For plans with defined contribution characteristics, the obligation is limited to the payment of contributions, which are recognized in the P&L of the respective years.

The asset or liability related to defined benefit plan to be recognized in financial statements correspond to the present value of the obligation by defined benefit (using a discount rate based on long-term National Treasury Notes “NTNs”), less fair value of plan assets that will be used to settle the obligations. The plan assets are assets held by a privately-held supplementary pension plan entity. The plan assets are not available to the Company’s creditors and cannot be paid directly to the Company. The fair value is based on information on market prices and, in case of securities quoted, on purchase price disclosed. The value of any defined benefit asset then recognized is limited to the present value of any economic benefits available as a reduction in future plan contribution from the Company and subsidiary.

Upon the adoption of IAS 19 (Revised) effective 1 January 2013, pension benefit costs recognized in the Income Statements are limited to service cost and the net interest cost (income) on the net defined benefit plan obligation (asset). All remeasurement effects on the plan assets and obligations are recognized initially in comprehensive income and immediately reclassified permanently in retained earnings.

x) Significant accounting judgment, estimates and assumptions

The preparation of the financial statements requires management to make judgments, estimates and assumptions supported by valuation bases used in accounting estimates. The accounting estimates involved in the preparation of the financial statements were based on objective and subjective factors considering management's judgment to determine the adequate amount to be recorded in the financial statements.

However, uncertainties involving these estimates may result in amounts significantly different from those recorded in the financial statements due to the criteria inherent in the estimation process.

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The key assumptions concerning the future and other key sources of estimation uncertainty at the reporting date, that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are described below:

<u>Impairment of nonfinancial assets</u>

An impairment loss exists when the book value of an asset or cash-generating unit exceeds its recoverable amount, which is the higher of fair value less cost of sales and value in use. The calculation of fair value less cost of sales is based on information available on sales transactions of similar assets or market price less additional costs to dispose of the asset. Calculation of value in use is based on discounted cash flow model. The recoverable value is sensitive to the discount rate used in discounted cash flow method, as well as to the receipt of estimated future cash flows and the growth rate used for extrapolation purposes.

<u>Post-retirement benefit plan</u>

The cost of defined benefit retirement plans and other post-retirement health care benefits and the present value of retirement obligation are determined based on actuarial valuation methods. Actuarial valuations involve the use of assumptions on discount rates, future salary increases, death rates and future increases in pension and retirement plans. The defined benefit obligation is highly sensitive to changes in these assumptions. All assumptions are reviewed annually.

The mortality rate is based on mortality tables available in Brazil. Future increases in wages and pension and retirement benefits are based on the expected future inflation rates for Brazil.

For more details on the assumptions used, see Note 35.

Fair value of financial instruments

Where the fair value of financial assets and financial liabilities recorded in the balance sheet cannot be derived from active markets, their fair value is determined using valuation techniques including the discounted cash flow model. The data for these methods is based on that prevailing in the market, whenever possible. However, when this is not feasible, a certain level of judgment is required to establish the fair value. The judgments include considerations of inputs such as liquidity risk, credit risk and volatility. Changes in assumptions about these factors could affect the reported fair value of financial instruments.

Property, Plant and Equipment and intangible assets, including goodwill

The accounting treatment of investment in fixed and intangible assets includes estimating useful life period for depreciation purposes and the fair value at the date of acquisition, particularly for assets acquired in business combinations.

Useful life determination requires estimates regarding the expected technological developments and alternative uses of assets. The hypotheses related to technological aspect and its future development imply a significant level of analysis, considering the difficulties in forecasting time and nature of future technological changes.

Where impairment is identified amounting to tangible and intangible assets, an adjustment of such amount is recorded in the P&L for the year. The need to record impairment loss is determined through estimates that include, among others, the analysis of the possible impairment causes and the estimated amount thereof. In this regard, factors such as technological obsolescence, suspension of certain services and other changes are also considered in circumstances that demonstrate the need to record a possible impairment.

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The Company and subsidiary periodically analyze the performance of the defined CGUs in order to identify a possible impairment in goodwill. The determination of the recoverable amount of the CGU to which the goodwill is allocated also includes the use of assumptions and estimates and requires a significant level of judgment and criterion.

Taxes

There are uncertainties regarding the interpretation of complex tax regulations and the amount and term of future taxable income. The Company and subsidiary set up provisions based on adequate estimates, for possible audit consequences by tax authorities of the respective jurisdictions in which it operates. The value of these provisions is based on various factors such as past experience with tax audits and different interpretation of tax regulations by the taxpaying entity and the relevant tax authorities. Such differences of interpretation may arise in a wide variety of matters, depending on the conditions prevailing in the respective domicile of the Company and subsidiary.

The Company and subsidiary evaluate the recoverability of deferred tax asset based on estimates of future results. This recoverability ultimately depends on the ability of the Company to generate taxable profits over the period in which the deferred tax asset is deductible. The analysis considers the reversal period of deferred tax liabilities, as well as estimates of taxable profits, based on updated internal projections reflecting the latest trends.

Determining the proper classification of the tax items depends on several factors, including an estimate of the period and the realization of the deferred tax asset and the expected date of payments of these taxes. The actual flow of receipt and shipment of income tax could differ from estimates made by the Company and subsidiary, as a result of changes in tax laws or of unexpected future transactions that may impact tax balances.

Provisions for tax, labor, civil and regulatory proceedings

Provisions are recognized when the Company has a present obligation arising from a past event, of which settlement requires an outflow of resources rated as probable and may be reliably estimated. This obligation can be legal or tacit, derived from, among other factors, regulations, contracts, customary practices or public commitments that expose third parties to a valid expectation that the Company will assume certain responsibility. The determination of the provision is based on the best estimate of the reimbursement required to settle the corresponding obligation, considering the information available on the closing date, including the opinion of independent experts, such as legal counselors.

y) Functional and reporting currency

Company's functional and reporting currency is the Brazilian real. Transactions in foreign currency were translated at the currency exchange rate in force on the date the transaction. Assets and liabilities stated in foreign exchange were translated at the currency exchange rate in force at the balance sheet date. The exchange rate changes arising from transactions in foreign currencies are recognized in P&L as financial income or expenses.

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z) Transactions denominated in foreign currency

The monetary assets and liabilities denominated in foreign currencies are translated to the functional currency (real) at the exchange rate (fx rate) in force on the transaction date and subsequently remeasured based on fx rate effective on the reporting date which, at December 31, 2013 was: US$1.00 = R$2.3426, €1.00 = R$3.23068 and at December 31, 2012, was: US$1.00 = R$2.0435, €1.00 = R$2.693946. Gains and losses resulting from the remeasurement of these assets and liabilities between the foreign exchange rate prevailing at the transaction and reporting dates are recognized in P&L.

aa) Employee profit sharing

The Company and subsidiary have obligations arising from employment contracts, recognizing these provisions during the year. Provisions are recorded to recognize the expense regarding employee profit sharing. These provisions are calculated on the basis of qualitative and quantitative goals set by the management and accounted for in specific accounts according to function in groups of Cost of services, Selling expenses and General and administrative expenses.

bb) Share-based payments

The Company measures the cost of transactions settled with employees and officers based on shares issued by parent company Telefónica S.A., by reference to the fair value of the equity instruments at the date at which they are granted, using the binomial valuation model. This fair value is charged to the income statement over the period until the vesting date.

cc) Treasury shares

Own equity instruments which are reacquired (Treasury shares) are recognized at cost and deducted from shareholders' equity. No gains or losses are recognized in P&L on purchase, sale, issue or cancellation of the Company's own equity instruments.

dd) Noncontrolling interests

Noncontrolling interests represent the portion of profit or loss and equity of subsidiaries not owned by the Company, thus being disclosed in the consolidated balance sheet under equity.

ee) Segment information

Operating segments are defined as components of a venture for which separate financial information is made available and evaluated on a regular basis by the Company's chief operating decision maker involving the allocation of funds to an individual segment and segment performance assessment. Considering that: (i) all officers and managers' decisions are based on consolidated reports; (ii) the Company and subsidiary's mission is to provide its customers with quality telecommunications services; and (iii) all decisions related to strategic planning, finance, shopping, short- and long-term investments are made on consolidated basis, the Company and subsidiary operate in a single operating segment, namely the provision of telecommunications services.

ff) Statements of cash flow and of value added

The statement of cash flows was prepared in accordance with IAS 7/CPC 03 - Cash Flow Statements using the indirect method, and reflects the changes in cash for the years reported.

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The statement of value added is shown as supplementary information, in compliance with Brazilian Corporate Law and was prepared pursuant to CPC09 – Statement of value added. The purpose of the statement of value added is to disclose the wealth generated by the Company during the year and the wealth distribution among its stakeholders.

4. ACQUISITION OF VIVO PARTICIPAÇÕES S.A.

On April 27, 2011 the shareholders meetings held by the Company and Vivo Participações S.A. (Vivo Part.) approved the acquisition of 100% of the shares that the Company held in the latter. Each share of Vivo Part. was substituted for 1.55 shares of the Company. This operation was recorded under the acquisition method.

The Company adopted the fair value of the shares acquired in view of the economic value report prepared by the specialized company engaged by management since it consists of a transaction between two companies under common control, the share value approximates that paid by SP Telecomunicações Participações Ltda. in the equity offering (OPA) of March 2011, which led to the acquisition of 2.65% of capital of Vivo Part., previously held by noncontrolling shareholders.

The fair values of the identifiable assets acquired and liabilities taken on from Vivo Part. were measured and recognized on the acquisition date.

These values were determined through various valuation methods, depending on the type of asset and/or liability in question, as well as the better information available and assisted by specialized advisors.

The methods and hypotheses for determination of these fair values were as follows:

Licenses

The fair value was determined through the *Multi-Period Excess Earnings Method* (MEEM), which is based on a calculation of discount of cash flows of future economic benefits attributable to the licenses, net of the eliminations of the charges relating to the contributing assets implied in the generation of these flows and excluding the flows attributable to the customers portfolio.

This method is based on the assumption that the intangible assets seldom generate profits by its own. Accordingly, the cash flows attributable to the licenses are those remaining after the return of all contributing assets necessary to generate the estimated cash flows. The fair value allocated to the licenses on the acquisition date reached R$12,876,000, which is being amortized for 27.75 years.

Customers portfolio

The customers portfolio also was valued by the MEEM method, which is based on a calculation of discounted cash flows of future economic benefits attributable to the customers base, net of the eliminations of the obligations of contributions implied in their generation. To estimate the useful life remaining from the customers base, an analysis of the average length of the relationship with customers, using a churn rate method was made

This analysis of lives is aimed at estimating a subsistence curve which allows for the future churn profiles associated with the current customers base. As an approximation of the customers subsistence curve, the so-called Iowa curves were considered. The fair value allocated to the customers portfolio on the acquisition date reached R$2,042,000, which is being amortized for an average period of 8.5 years.

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Trademark

The fair value of the "Vivo" trademark was calculated under the "relief-from-royalty" method. In accordance with this method, the value of the asset is determined by capitalizing *royalties* saved in connection with the intellectual property. In other words, the trademark owner obtains profit since it owns the intangible asset instead of paying royalties for its use. Royalties saved was determined by applying a market royalty rate (expressed as a percentage of revenues) to future revenues expected to be obtained from the sale of the products or services associated with the intangible asset. A market royalty rate is usually expressed as a percentage of net revenues which an interested owner would charge an interested user for the use of an asset owned in a free transaction, being both parties duly informed. The fair value allocated to the trademark on the acquisition date reached R$1,642,000, which is being amortized for 19.5 years.

Following are the fair value, the goodwill and the cost of participation of the identifiable assets acquired and liabilities taken on from Vivo Part. on the acquisition date:

Information (in thousands of R$)	Fair Value
Current assets	7,244,124
Noncurrent assets	28,134,683
Deferred tax assets, net[(b)]	417,883
Other noncurrent assets	2,385,177
Property, plant and equipment	6,198,358
Intangible assets [(a)]	19,133,265
Current liabilities	(7,964,209)
Noncurrent liabilities	(5,352,456)
Other noncurrent liabilities [(c)]	(5,352,456)
Net assets	**22,062,142**
Equity expenses	31,222,630
Goodwill on operation	**9,160,488**

(a) Includes the allocation of the fair value attributed to licenses (R$12,876,000), to the trademark (R$1,642,000) and the customers portfolio (R$2,042,000). The Company does not consider the trademark and the customers portfolio as deductible for tax purposes.

(b) Includes the recognition of deferred income tax on (a) and (c).

(c) Includes the allocation of fair value attributed to the contingent liability for R$283,000.

In accordance with IFRS 3(R) – Business Combination, the acquirer must recognize, on the acquisition date, contingent liabilities taken on from a business combination, even if cash outflow is not probable to settle the obligation, provided that a present obligation arising from past events and its fair value may be reliably measured. Meeting former requirements, upon the acquisition contingent liabilities were recognized at fair value of R$283,000, which were determined in view of the estimated cash outflows for settlement on the acquisition date.

Costs incurred with the transaction were posted to P&L, in other operating expenses.

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5. CASH AND CASH EQUIVALENTS

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Cash and banks	101,094	18,398	101,921	94,304	76,316
Short-term investments	6,210,205	3,060,884	6,442,015	7,039,181	2,813,227
Total	**6,311,299**	**3,079,282**	**6,543,936**	**7,133,485**	**2,889,543**

Short-term investments basically correspond to Bank Deposit Certificates (CDB), which are pegged to the Interbank Deposit Certificate (CDI) rate variation, are highly liquid and are kept with first-tier financial institutions.

In addition, not included in the amounts above, the Company has short-term investments in the consolidated amounts of R$106,455 at December 31, 2013 (R$109,708 at December 31, 2012), in noncurrent assets.

6. TRADE ACCOUNTS RECEIVABLE, NET

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Billed amounts	4,081,963	1,622,311	4,485,539	4,066,835	3,695,379
Unbilled amounts	1,777,871	804,965	1,890,485	1,675,091	1,677,708
Interconnection amounts	872,678	338,014	859,894	977,644	896,639
Gross accounts receivable	**6,732,512**	**2,765,290**	**7,235,918**	**6,719,570**	**6,269,726**
Provision for impairment	(1,031,011)	(614,566)	(1,175,973)	(1,079,254)	(1,056,729)
Total	**5,701,501**	**2,150,724**	**6,059,945**	**5,640,316**	**5,212,997**

Current	5,541,023	2,150,724	5,802,859	5,546,938	5,128,142
Noncurrent	160,478	-	257,086	93,378	84,855

The aging list of trade accounts receivable, net of the provision for impairment, is as follows:

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Falling due	4,131,549	1,395,227	4,398,791	4,331,163	4,125,659
Overdue from 1 to 30 days	756,787	377,142	795,389	718,693	631,923
Overdue from 31 to 60 days	266,192	113,042	289,783	215,862	204,775
Overdue from 61 to 90 days	162,436	51,107	166,105	193,291	115,125
Overdue from 91 to 120 days	59,244	27,955	62,122	60,669	49,815
Overdue for more than 120 days	325,293	186,251	347,755	120,638	85,700
Total	**5,701,501**	**2,150,724**	**6,059,945**	**5,640,316**	**5,212,997**

At December 31, 2013 and 2012, no customer represented more than 10% of net trade accounts receivable.

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Changes in the provision for impairment are as follows:

	Company	Consolidated
Balance at December 31, 2011 (Company) and January 01, 2012 (Consolidated)	**(607,736)**	**(1,056,729)**
Additions, net (Note 26)	(267,453)	(654,273)
Write-offs	260,623	631,748
Balance at December 31, 2012	**(614,566)**	**(1,079,254)**
Additions, net (Note 26)	(480,373)	(741,274)
Write-offs	468,058	644,555
Merger/split as of July 1, 2013	(404,130)	-
Balance at December 31, 2013	**(1,031,011)**	**(1,175,973)**

At December 31, 2013, noncurrent consolidated accounts receivable includes R$160,478 referring to the new business model of goods for resale to legal entities, whose term for receipt is up to 24 months. The amount of unrecognized revenue (present value adjustment) on December 31, 2013 was R$18,174.

TData has a product called “Soluciona TI,” which consists of leasing IT equipment to small- and medium-sized enterprises, for which TData receives fixed installments over the lease term. Considering the contractual terms, the Company classified this product as Finance Lease. At December 31, 2013, the consolidated noncurrent accounts receivable balance includes R$96,608 (R$93,378 at December 31, 2012) related to this product.

The consolidated balance of trade accounts receivable, related to finance lease, comprises the following effects:

Consolidated

	12.31.13	12.31.12	01.01.12
Present value of receivables	335,376	294,245	261,933
Unrealized financial income	7,058	7,757	8,941
Gross accounts receivable	**342,434**	**302,002**	**270,874**
Provision for impairment	(99,791)	(86,648)	(69,375)
Net accounts receivable	**242,643**	**215,354**	**201,499**
Current	146,035	121,976	116,644
Noncurrent	96,608	93,378	84,855

At December 31, 2013, the aging list of trade accounts receivable is as follows:

	Consolidated	
	Trade accounts receivable, gross	Present value
Falling due up to one year	238,768	238,768
Falling due up to five years	103,666	96,608
Total	**342,434**	**335,376**

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There are no unsecured residual values resulting in benefits to the lessor nor contingent payments recognized as revenue during the year.

7. INVENTORIES

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Consumer materials	55,431	39,641	58,492	59,417	94,547
Materials for resale (a)	459,949	5,835	498,803	380,163	435,032
Other inventory items	6,481	3,835	6,481	4,005	6,468
Total gross	**521,861**	**49,311**	**563,776**	**443,585**	**536,047**
Provision for impairment and obsolescence	(52,275)	(24,908)	(58,161)	(55,776)	(64,326)
Total	**469,586**	**24,403**	**505,615**	**387,809**	**471,721**

(a) This includes, among others, mobile telephones, simcards (chip) and IT equipment in stock.

Changes in the provision for impairment and obsolescence are as follows:

	Company	Consolidated
Balance at December 31, 2011 (Company) and January 01, 2012 (Consolidated)	**(35,651)**	**(64,326)**
Additions	(4,718)	(35,972)
Reversals	15,461	44,522
Balance at December 31, 2012	**(24,908)**	**(55,776)**
Additions	(14,475)	(29,247)
Reversals	21,785	26,862
Merger/split as of July 1, 2013	(34,677)	-

Balance at December 31, 2013	**(52,275)**	**(58,161)**

Cost of goods sold, which includes amounts regarding provision for impairment and obsolescence, is stated in Note 25.

8. DEFERRED TAXES AND TAXES RECOVERABLE

8.1 Taxes recoverable

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
ICMS (a)	1,553,503	366,211	1,556,452	1,631,088	1,665,896
ICMS agreement No. 39/CAT Admin Ruling No.06 (b)	355,251	178,535	355,251	288,520	307,832
Income and social contribution taxes (c)	374,096	453,933	377,704	528,109	1,143,987
Taxes withheld at source (d)	174,015	106,693	188,659	141,620	152,919
PIS and COFINS	62,449	39,265	63,816	148,092	210,950
Other	17,871	6,916	18,468	53,957	28,440
Total	**2,537,185**	**1,151,553**	**2,560,350**	**2,791,386**	**3,510,024**
Current	2,168,797	602,328	2,191,962	2,052,421	2,495,065
Noncurrent	368,388	549,225	368,388	738,965	1,014,959

(a) Credits arising from additions to property, plant and equipment, subject to offsetting in 48 months.

(b) Refund request for State Value-Added Tax (ICMS) paid for invoices cancelled at a later time.

(c) Mainly prepaid income tax and social contribution, which will be offset against federal taxes to be determined in the future.

(d) Credits on withholding income tax on short-term investments, interest on shareholders´ equity and other, which are used as deduction in operations for the year and social contribution withheld at source on services provided to public entities.

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8.2 Deferred taxes

The Company and its subsidiary calculate deferred income and social contribution tax assets considering the existence of taxable profit for the past five financial years and expected future taxable profit generation, which were based on a technical feasibility study, approved by the Board of Directors.

Significant components of deferred income and social contribution taxes are as follows:

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Deferred tax assets					
Income and social contribution tax losses (a)	122,321	21,290	262,915	21,290	348,576
Merged tax credit (b)	-	9,461	-	9,461	46,962
Income and social contribution taxes on temporary differences (c)					
Provisions for labor, tax and civil contingencies	1,322,244	805,557	1,327,288	1,104,065	950,988
Post-employment retirement plans	143,537	126,605	143,537	133,371	104,856
Provision for impaiment - accounts receivable	241,203	93,442	245,556	169,434	178,433
Provision for modem and other PP&E item losses	164,518	7,467	166,174	210,107	137,829
Profit sharing	71,287	34,888	71,948	62,218	82,564
Accelerated accounting depreciation	154,181	128,070	154,181	421,768	433,512
Provision for impairment - inventories	10,884	8,469	12,885	13,951	17,542
Provision for customer loyalty program	31,199	-	31,199	28,168	23,399
Derivative transactions	-	26,522	-	42,922	69,387

Trade accounts payable and other provisions	338,458	62,314	398,956	290,199	354,916
Income and social contribution taxes on other temporary differences	157,988	81,926	157,313	134,460	109,285
Total deferred tax assets	**2,757,820**	**1,406,011**	**2,971,952**	**2,641,414**	**2,858,249**
Deferred tax liabilities					
Merged tax credit (b)	(337,535)	(269,514)	(337,535)	(269,514)	(207,668)
Income and social contribution taxes on temporary differences (c)					
Technology Innovation Law	(308,490)	(209,185)	(308,490)	(416,700)	(333,156)
Exchange variation	-	(3,383)	-	(3,383)	(14,742)
Customer portfolio	(461,870)	(546,383)	(461,870)	(546,383)	(630,896)
Trademarks and patents	(479,548)	(508,178)	(479,548)	(508,178)	(536,808)
Licenses	(719,780)	(399,878)	(719,780)	(399,878)	(79,976)
Effects of goodwill generated upon merger of Vivo Part.	(568,338)	(344,927)	(568,338)	(344,927)	(258,695)
Vivo Part. Goodwill	(480,366)	(266,870)	(480,366)	(266,870)	(53,374)
Income and social contribution taxes on other temporary differences	(124,527)	(74,344)	(128,365)	(74,344)	(104,389)
Total deferred tax liabilities	**(3,480,454)**	**(2,622,662)**	**(3,484,292)**	**(2,830,177)**	**(2,219,704)**
Total noncurrent assets (liabilities), net	**(722,634)**	**(1,216,651)**	**(512,340)**	**(188,763)**	**638,545**
Deferred tax assets (liabilities), net					
Representado no balanço patrimonial da seguinte forma:					
Noncurrent deferred tax assets, net	**-**	**-**	**210,294**	**1,027,888**	**1,427,499**
Noncurrent deferred tax liabilities, net	**(722,634)**	**(1,216,651)**	**(722,634)**	**(1,216,651)**	**(788,954)**

Deferred taxes were determined considering future realization, as under:

a) Income and social contribution tax losses:this represents the amount recorded by the Company and its subsidiary which, in accordance with Brazilian tax legislation, may be offset to the limit of 30% of the tax bases computed for the following years, with no expiry date.

Following are the amounts of tax credits from losses on income tax and social contribution carry-forwards recognized for the years ended December 31, 2013 and 2012 and, January 1st 2012:

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	Company			Consolidated		
	Income tax	Social contribution tax	Total	Income tax	Social contribution tax	Total
Income and social contribution tax losses at January 1, 2012	-	-	-	1,745,928	1,705,050	3,450,978
Tax credit (25% + 9%)	-	-	-	436,482	153,455	589,937
Tax credit recognized	-	-	-	259,011	89,565	348,576
Unrecognized tax credit (*)	-	-	-	177,471	63,890	241,361
Income and social contribution tax losses at December 31, 2012 (restated)	48,264	102,486	150,750	930,409	997,434	1,927,843
Tax credit (25% + 9%)	12,066	9,224	21,290	232,602	89,769	322,371
Tax credit recognized	12,066	9,224	21,290	12,066	9,224	21,290
Unrecognized tax credit (*)	-	-	-	220,536	80,545	301,081
Income and social contribution tax losses at December 31, 2013	259,106	639,382	898,488	672,523	1,053,155	1,725,678
Tax credit (25% + 9%)	64,777	57,544	122,321	168,131	94,784	262,915
Tax credit recognized	64,777	57,544	122,321	168,131	94,784	262,915

(*) Due to the restructuring process, the T.Data recognized tax credits not recognized over the past years, so there is no credit not recognized in 2013.

b) Merged tax credit: represented by tax benefits arising from corporate restructuring of goodwill for expected future profitability, whose tax use follows the limit set forth in tax legislation.

c) Income and social contribution taxes on temporary differences: amounts will be realized upon payment of provisions, effective impairment or trade receivables, or realization of inventories, as well as upon reversal of other provisions.

Changes in deferred income and social contribution tax assets and liabilities are as follows:

	Company			Consolidated		
Deferred tax assets	Tax losses	Deferred tax assets	Total	Tax losses	Deferred tax assets	Total
Balance at December 31, 2011 (Company) and January 01, 2012 (Consolidated)	**-**	**1,321,848**	**1,321,848**	**348,576**	**2,509,673**	**2,858,249**
Provision	154,657	168,917	323,574	154,657	375,739	530,396
Provision reversal	(133,367)	(106,044)	(239,411)	(481,943)	(265,288)	(747,231)
Balance at December 31, 2012 - Restated	**21,290**	**1,384,721**	**1,406,011**	**21,290**	**2,620,124**	**2,641,414**
Provision	101,031	289,153	390,184	241,625	458,376	700,001
Provision reversal	-	(153,048)	(153,048)	-	(368,537)	(368,537)
Comprehensive income	-	(36)	(36)	-	(926)	(926)
Merger/split as of July 1, 2013	-	1,114,709	1,114,709	-	-	-
Balance at December 31, 2013	**122,321**	**2,635,499**	**2,757,820**	**262,915**	**2,709,037**	**2,971,952**

Deferred tax liabilities	Company	Consolidated
Balance at December 31, 2011 (Company) and January 01, 2012 (Consolidated)	**(2,110,802)**	**(2,219,704)**
Provision	(627,207)	(747,326)
Provision reversal	94,448	123,537
Other changes that did not flow through P&L	(9,308)	(8,071)
Comprehensive income	30,207	21,387
Balance at December 31, 2012 - Restated	**(2,622,662)**	**(2,830,177)**
Provision	(824,830)	(884,798)
Provision reversal	257,687	223,810
Other changes that did not flow through P&L	(21,448)	6,873
Merger/split as of July 1, 2013	(269,201)	-
Balance at December 31, 2013	**(3,480,454)**	**(3,484,292)**

The table below presents deferred income tax and social contribution for items charge or credited directly in net assets during the years ended December 31, 2013 and 2012.

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	Company		Consolidated	
	2013	2012	2013	2012
Non-realized losses on available-for-sale investment	4,578	1,882	4,578	1,882
Actuarial losses and effect of the asset ceiling on plan surplus	(6,458)	28,325	(7,348)	23,726
Gain (losses) on derivative operations	1,844	-	1,844	(4,221)
Total	**(36)**	**30,207**	**(926)**	**21,387**

Following are the expected deadlines to realize net deferred tax assets.

	2014	2015	2016	2017	2018	2019 onwards	Total
Company	(819,636)	(136,081)	(38,855)	(71,332)	(81,336)	424,606	(722,634)
Consolidated	(635,572)	(113,087)	(39,151)	(71,645)	(80,702)	427,817	(512,340)

These amounts are based on projections which may change in the future.

9. JUDICIAL DEPOSITS AND GARNISHMENTS

In some situations, in connection with a legal requirement or presentation of guarantees, judicial deposits are made to secure the continuance of the claims under discussion. These judicial deposits may be required for claims whose likelihood of loss was analyzed by the Company, grounded on the opinion of its legal advisors as a probable, possible or remote loss.

Company	Consolidated

	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Judicial deposits					
Labor	1,030,468	830,081	1,036,055	933,866	789,705
Tax	2,348,179	1,549,738	2,364,913	2,182,513	1,938,270
Civil and reguilatory	852,972	667,646	853,980	866,668	715,285
Total	**4,231,619**	**3,047,465**	**4,254,948**	**3,983,047**	**3,443,260**
Garnishments	96,130	20,791	97,572	52,846	47,651
Total	**4,327,749**	**3,068,256**	**4,352,520**	**4,035,893**	**3,490,911**
Current	204,165	-	204,165	126,625	116,421
Noncurrent	4,123,584	3,068,256	4,148,355	3,909,268	3,374,490

At December 31, 2013, the Company and its subsidiary had a number of tax-related judicial deposits, reaching the consolidated amount of R$2,364,913 (R$2,182,513 at December 31, 2012). Detailed information on the matters from which the main deposits stem, is in Note 20.

A brief description of the main tax-related judicial deposits is as follows:

• Federal contribution taxes on gross revenue for Social Integration Program (PIS) and for Social Security Financing (COFINS)

Company and subsidiary are involved in disputes related to: (i) claim filed for overpayment of tax credits, not recognized by tax authorities; (ii) tax debt arising from underpayment due to differences in ancillary statements (Federal Tax Debt and Credit Return – DCTF); and (iii) disputes referring to changes in rates and increase in tax bases introduced by Law No. 9718/98.

At December 31, 2013, consolidated judicial deposits amounted to R$31,162 (R$62,924 at December 31, 2012).

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NOTES TO FINANCIAL STATEMENTS

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(In thousands of reais)

- Social Contribution Tax for Intervention in the Economic Order (CIDE)

The Company is involved in legal disputes for the exemption of CIDE levied on offshore remittances of funds arising from agreements for the transfer of technology, brand and software licensing, etc.

At December 31, 2013, consolidated judicial deposits amounted to R$144,684 (R$136,211 at December 31, 2012).

- Telecommunications Inspection Fund (FISTEL)

ANATEL collects Installation Inspection Fee (TFI) on extension of licenses granted and on radio base stations, mobile stations and radio links, such collection results from the understanding of ANATEL that said extension would be a triggering event of TFI and that mobile stations, even if owned by third parties, are also subject to TFI. The Company and subsidiary challenge aforesaid fee in court.

At December 31, 2013, the consolidated judicial deposits amounted to R$864,487 (R$818,502 at December 31, 2012).

- Withholding Income Tax (IRRF)

Company is involved in disputes related to: (i) exemption of IRRF payment on offshore remittances for out-coming traffic (land-line operators); (ii) exemption of IRRF payment on interest on shareholders´ equity recognized (mobile operators); and (iii) IRRF levied on earnings from rentals and royalties, wage labor and fixed-income investments.

At December 31, 2013, the consolidated judicial deposits amounted to R$59,343 (R$58,367 at December 31, 2012).

- Corporate Income Tax (IRPJ)

Company is involved in disputes related to: (i) debts stemming from offsetting of IRPJ overpayments not recognized by the Brazilian IRS; and (ii) requirement of IRPJ estimates and lack of payment – debts in the integrated system of economic and tax information (SIEF); and (iii) underpaid IRPJ amounts.

At December 31, 2013, the consolidated judicial deposits amounted to R$28,456 (R$25,422 at December 31, 2012).

- Contribution to Empresa Brasil de Comunicação (EBC)

Sinditelebrasil (Union of Telephony and Mobile and Personal Services) filed an injunction challenging the Contribution to Foster Public Radio Broadcasting payable to EBC, introduced by Law No. 11652/2008. The Company and its subsidiary, as union members, made judicial deposits referring to that contribution.

At December 31, 2013, the consolidated judicial deposits amounted to R$514,127 (R$370,026 at December 31, 2012).

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NOTES TO FINANCIAL STATEMENTS

Years ended December 31, 2013 and 2012

(In thousands of reais)

- Social Security, Work Accident Insurance (SAT) and Funds to Third Parties (INSS)

Company was involved in disputes related to: (i) SAT and funds to third parties (INCRA and SEBRAE); (ii) joint responsibility for contract labor; and (ii) difference in SAT rate (from 1% to 3%).

At December 31, 2013, the consolidated judicial deposits amounted to R$96,736 (R$91,915 at December 31, 2012).

- Unemployment Compensation Fund (FGTS)

The Company filed an injunction in order to represent its right not to pay surtax of 0.5% and 10% for FGTS introduced by Supplementary Law No. 110/2001 levied on deposits made by employers (the proceedings did not result in any reduction of FGTS deposits mad by the Company on behalf of its employees).

At December 31, 2013, the consolidated judicial deposits amounted to R$70,697 (R$66,386 at December 31, 2012).

- Tax on Net Income (ILL)

The Company filed an injunction in order to represent its right to offset amounts unduly paid for ILL purposes against future IRPJ payments.

On December 19, 2013 the Company settled the debt under discussion by including it in the Federal Tax Recovery Program (REFIS), using the judicial deposit then restricted, which is now awaiting conversion into income by the Federal Government.

At December 31, 2013, the consolidated judicial deposits amounted to R$51,648 (R$49,355 at December 31, 2012).

- <u>Universal Telecommunication Services Fund (FUST)</u>

Company and subsidiary filed an injunction in order to have their right declared not to include expenses with interconnection (ITX) and Industrial Use of Dedicated Line (EILD) in FUST tax base for landline phone carriers and not to include revenues from ITX and EILD in FUST tax base for mobile phone carriers, according to Abridgment No. 7, of December 15, 2005, as it does not comply with the provisions contained in sole paragraph of article 6 of Law No. 9998, of August 17, 2000.

At December 31, 2013, the consolidated judicial deposits amounted to R$371,373 (R$341,403 at December 31, 2012).

- <u>Provisional Contribution Tax on Financial Transactions (CPMF)</u>

Given the merger of PTelecom Brasil S.A. into Vivo Part. (later merged into the Company) the judicial deposit balance related to the injunction filed by PTelecom Brasil S.A. was absorbed, so as to reject the requirement for CPMF on pro forma and simultaneous foreign exchange agreements, as required by the Central Bank of Brazil to translate foreign loans into investment.

Telefônica Brasil S. A.

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Years ended December 31, 2013 and 2012

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At December 31, 2013, the petition filed for a writ of mandamus had an unfavorable outcome for the Company, and the aforesaid judicial deposit was converted into income for the payment of the debt under discussion.

At December 31, 2013, the consolidated judicial deposits amounted to R$20,899.

- State Value-Added Tax (ICMS)

Company is involved in disputes related to: (i) ICMS stated but not paid; (ii) ICMS not levied on communication in default; (iii) fine for late voluntary payment of ICMS; (iv) ICMS supposedly levied on access, adhesion, enabling, availability and use of services, as well as supplementary services and additional facilities; (v) right to credit from the acquisition of goods for the PP&E and electric energy; and (vi) activation cards for pre-paid services.

At December 31, 2013, the consolidated judicial deposits amounted to R$38,259 (R$34,235 at December 31, 2012).

- Other taxes, charges and contributions

Company is involved in disputes related to: (i) Service Tax (ISS) on noncore services; (ii) Municipal Real Estate Tax (IPTU) not subject to exemption; (iii) municipal inspection, operation and publicity charges; (iv) land use fee; (v) social security contributions related to supposed failure to withhold 11% on several invoices, bills and receipts or service providers engaged for workforce assignment; and (vi) Public Price for Numbering Resource Management (PPNUM) by ANATEL.

At December 31, 2013, the consolidated judicial deposits amounted to R$93,941 (R$106,868 at December 31, 2012).

10. PREPAID EXPENSES

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Advertising and publicity	167,873	817	167,873	173,688	172,401
Rent	35,168	20,533	35,168	51,207	43,744
Insurance	29,212	7,875	29,733	14,250	11,984
Financial charges	11,568	-	11,568	7,152	8,743
Software maintenance, taxes and other	35,801	14,105	38,308	33,436	50,322
Total	**279,622**	**43,330**	**282,650**	**279,733**	**287,194**
Current	254,743	26,610	257,286	248,337	255,056
Noncurrent	24,879	16,720	25,364	31,396	32,138

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Years ended December 31, 2013 and 2012

(In thousands of reais)

11. OTHER ASSETS

	Company		Consolidated		
	12.31.13	12.31.12	12.31.13	12.31.12 - Restated	01.01.12
Advances to employees and suppliers	64,101	70,888	64,991	97,152	73,646
Related-party receivables	297,198	130,559	97,748	58,151	60,499
Subsidy on handset sales	55,716	-	55,716	53,756	53,408
Receivables from suppliers (a)	139,563	16,930	139,563	479,283	217,255
Pension plan surplus	17,769	17,595	17,909	48,048	31,210
Other realizable assets	86,492	38,060	92,037	27,235	61,215
Total	**660,839**	**274,032**	**467,964**	**763,625**	**497,233**
Current	533,272	198,445	340,171	671,317	401,184
Noncurrent	127,567	75,587	127,793	92,308	96,049

(a) At December 31, 2013, the consolidated amounts include R$362,774 referring to the disposal of nonstrategic transmission towers, received in 2013.

12. INVESTMENTS

A summary of significant financial data of Company investees is as follows.

The changes in equity interest shown in the following table arise from the corporate reorganization described in Note 1b).

a) *Information on investees - Wholly-owned subsidiaries*

	Subsidiaries								
	At 12.31.13		At 12.31.12						
	TData	Vivo	TData	ATelecom	TSTV	TVA Sul	Lemontree	Comercial Cabo	GTR-T
Assets									
Current	1,090,339	9,877,926	358,299	498,074	40,087	2,178	6	25,435	801
Noncurrent	420,253	13,263,918	140,763	414,985	160,603	41,327	11,835	167,688	1,074
Total assets	**1,510,592**	**23,141,844**	**499,062**	**913,059**	**200,690**	**43,505**	**11,841**	**193,123**	**1,875**
Liabilities									
Current	688,480	8,213,367	174,536	218,126	34,818	9,522	437	117,652	14
Noncurrent	43,823	4,887,981	19,191	54,165	2,744	28,798	-	21,830	-
Equity	778,289	10,040,496	305,335	640,768	163,128	5,185	11,404	53,641	1,861
Total liabilities	**1,510,592**	**23,141,844**	**499,062**	**913,059**	**200,690**	**43,505**	**11,841**	**193,123**	**1,875**
Net income (loss)	258,763	4,173,983	(98,599)	9,336	(51,195)	(5,780)	(12,146)	(33,835)	(1,264)
Equity investment									
At December 31, 2013	100.00%	n/a	100.00%	n/a	n/a	n/a	n/a	n/a	n/a
At December 31, 2012	100.00%	100.00%	100.00%	100.00%	100.00%	79.29%	100.00%	78.48%	100.00%

b) *Information on investees – Jointly-controlled entities*

	At December 31, 2013			At December 31, 2012		
	Cia ACT	Cia AIX	Aliança Atlântica	Cia ACT	Cia AIX	Aliança Atlântica
Current assets	11	10,515	139,414	10	13,414	116,322
Noncurrent assets	-	12,441	-	-	120,024	-
Current liabilities	1	2,950	2,200	-	3,280	2,302
Noncurrent liabilities	-	6,076	-	-	5,792	-
Equity	**10**	**13,930**	**137,214**	**10**	**124,366**	**114,020**

Net income (loss) for the year	**-**	**(110,436)**	**136**	**4**	**(550)**	**1,722**

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Years ended December 31, 2013 and 2012

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c) *Changes in investments*

	Balances at December 31, 2012 - Restated	Additions	Equity pickup	Dividend and interest on equity declared and approved	Other comprehensive income	Merger / split as of July 1, 2013	Balances at December 31, 2013
Equity investments	**11,328,398**	**91,050**	**1,913,508**	**(2,120,289)**	**8,743**	**(10,367,544)**	**853,866**
Wholly-owned subsidiaries	**11,209,200**	**91,050**	**1,968,658**	**(2,120,289)**	**(2,786)**	**(10,367,544)**	**778,289**
A. Telecom	640,768	-	50,927	-	(36)	(691,659)	-
TData	305,335	20,000	258,763	(61,456)	1,731	253,916	778,289
TST	163,128	-	(52,915)	-	-	(110,213)	-
Vivo	10,040,496	-	1,740,186	(2,058,833)	(1,048)	(9,720,801)	-
GTR-T	1,861	-	1,129	-	-	(2,990)	-
Lemontree	11,404	50	(2,957)	-	-	(8,497)	-
CaTV	42,097	68,000	(31,383)	-	(3,078)	(75,636)	-
Sul Paraná	4,111	3,000	4,908	-	(355)	(11,664)	-
Jointly controlled entities	**119,198**		**(55,150)**	**-**	**11,529**	**-**	**75,577**
Aliança	57,010	-	68	-	11,529	-	68,607
AIX	62,183	-	(55,218)	-	-	-	6,965
ACT	5	-	-	-	-	-	5
Goodwill	**10,208,980**	**-**	**-**	**-**	**-**	**16,300**	**10,225,280**
Other investments	**23,683**	**(148)**	**-**	**-**	**(13,465)**	**702**	**10,772**
Other investments (a)	23,683	(148)			(13,465)	702	10,772
	21,561,061	**90,902**	**1,913,508**	**(2,120,289)**	**(4,722)**	**(10,350,542)**	**11,089,918**

Total investments in Company							
Aliança	57,010	-	68	-	11,529	-	68,607
AIX	62,183	-	(55,218)	-	-	-	6,965
ACT	5	-	-	-	-	-	5
Other investments (a)	23,683	(148)	-	-	(13,465)	702	10,772
Total investments in consolidated	**142,881**	**(148)**	**(55,150)**	**-**	**(1,936)**	**702**	**86,349**

	Balance at January 1, 2012	Additions	Equity pickup	Dividend and interest on equity declared and approved	Other comprehensive income	Residual value write-off	Other changes	Balanc Decemb 31, 201 Restat
Equity investments	**10,001,448**	**244,291**	**3,995,228**	**(2,932,200)**	**22,871**	**-**	**(3,240)**	**11,328,3**
Wholly-owned subsidiaries	**9,884,647**	**244,291**	**3,994,640**	**(2,928,743)**	**17,605**	**-**	**(3,240)**	**11,209,2**
A. Telecom	722,857	-	9,336	(91,353)	(72)	-	-	640,7
TData	198,555	210,000	(98,599)		(764)	-	(3,857)	305,3
TST	213,387	-	(51,195)	-	-	-	936	163,1
Vivo	8,685,946	-	4,173,983	(2,837,390)	17,957	-	-	10,040,4
GTR-T	2,073	776	(999)	-	-	-	11	1,8
Lemontree	19,681	2,877	(11,019)	-	-	-	(135)	11,4
CaTV	35,517	28,638	(22,536)	-	720	-	(242)	42,0
Sul Paraná	6,631	2,000	(4,331)	-	(236)	-	47	4,1
Jointly controlled entities	**116,801**		**588**	**(3,457)**	**5,266**	**-**	**-**	**119,1**
Aliança	52,023	-	861	(1,140)	5,266	-	-	57,0
AIX	64,775	-	(275)	(2,317)	-	-	-	62,1
ACT	3	-	2	-	-	-	-	
Goodwill	**10,208,980**	**-**	**-**	**-**	**-**	**-**	**-**	**10,208,9**
Other investments	**35,455**	**-**	**-**	**-**	**(5,068)**	**(6,704)**	**-**&n	