

The Brazilian government has implemented various economic plans and utilized a number of exchange rate policies, including sudden devaluations, periodic mini-devaluations during which the frequency of adjustments ranged from a daily to a monthly basis, floating exchange rate systems, exchange controls and dual exchange rate markets. We cannot predict whether the Central Bank or the Brazilian government will continue to let the *real* float freely or intervene in the exchange rate market by returning to a currency band system or otherwise. The *real* may depreciate or appreciate substantially against the U.S. dollar.

The following tables set forth the exchange rate (rounded to the nearest tenth of a cent), expressed in *reais* per U.S. dollar (R\$/US\$) for the periods indicated, as reported by the Central Bank.

Year ended December 31,	Exchange Rate of R\$ per US\$			
	Low	High	Average(1)	Year-End
2009	1.741	2.378	1.990	1.741
2010	1.655	1.880	1.759	1.665
2011	1.535	1.902	1.671	1.876
2012	1.702	2.112	1.959	2.044
2013	1.953	2.446	2.161	2.343

Source: Central Bank of Brazil, PTAX.

(1)Represents the average of the exchange rates (PTAX) on the last day of each month during the relevant period.

Month ended December 31,	Exchange Rate of R\$ per US\$			
	Low	High	Average(2)	Period-End
September 2013	2.203	2.390	2.270	2.230
October 2013	2.161	2.212	2.189	2.203
November 2013	2.243	2.336	2.295	2.325
December 2013	2.310	2.382	2.345	2.343
January 2014	2.334	2.440	2.382	2.426
February 2014	2.333	2.424	2.384	2.333
March 2014 (through March 18, 2014)	2.309	2.365	2.344	2.352

Source: Central Bank of Brazil, PTAX.

(2)Represents the average of the exchange rates (PTAX) of the lowest and highest rates in the month.

On March 18, 2014, the exchange rate was R\$2.352 to US\$1.00. The *real*/dollar exchange rate fluctuates and, therefore, this exchange rate at 2014 may not be indicative of future exchange rates.

B. Capitalization and Indebtedness

Not applicable.

C. Reasons for the Offer and Use of Proceeds

Not applicable.

D. Risk Factors

This section is intended to be a summary of more detailed discussions contained elsewhere in this annual report. The risks described below are not the only ones we face. Additional risks that we do not presently consider material, or of which we are not currently aware, may also affect us. Our business, results of operations or financial condition could be impacted if any of these risks materializes and, as a result, the market price of our preferred shares and our ADSs could be affected.

Risks Relating to Brazil

The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. This influence, as well as Brazilian political and economic conditions, could adversely affect us and the trading price of our preferred shares and ADSs.

In the past, the Brazilian government has intervened in the Brazilian economy and made changes in policy and regulations. The Brazilian government's actions to control inflation and affect other policies have often involved wage and price controls, currency devaluations, capital controls, and limits on imports, among other things. Our business, financial condition, results of operations and the market price of our preferred shares and ADSs may be adversely affected by changes in government policies, especially those related to our sector, such as changes in telephone fees and competitive conditions, as well as general economic factors, including:

- currency fluctuations;
- exchange control policies;
- internal economic growth;
- inflation;
- energy policy;
- interest rates;
- liquidity of domestic capital and lending markets;
- tax policies; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Uncertainty over the possibility of the Brazilian government implementing changes in policy or regulation affecting these or other factors in the future may contribute to economic uncertainty in Brazil and heightened volatility in the Brazilian securities markets and securities issued abroad by Brazilian companies. In addition, possible political crises may affect the confidence of investors and the public in general, which may result in economic deceleration and affect the trading prices of shares issued by companies listed on the stock exchange, such as us.

Our business may be vulnerable to the current disruptions and volatility in the global financial markets.

The Brazilian economy remains subject to risks and adjustments arising from international financial conditions. The international financial system remains susceptible to unfavorable credit and liquidity conditions. Foreign and national financial institutions, including some of the largest commercial banks, investment banks, mortgage lenders, guarantors and mortgage insurance companies, could experience significant difficulties, including runs on their deposits and inadequate liquidity.

Various governments may continue to intervene in their financial systems, and perform fiscal and monetary adjustments. There is no assurance, however, that these measures will be successful in stabilizing conditions in international financial markets.

Despite the extent of the above-mentioned interventions, the global financial markets could remain volatile and access to credit could still be lacking. The conditions and volatility in the global financial markets may have a material adverse effect on our ability to access the capital markets under appropriate financial conditions, which may adversely affect our operations. Furthermore, an environment of economic downturn may negatively affect the financial stability of our customers, which could result in a general reduction in Brazil's economic activity and the consequent loss of income for us.

Political instability may have an adverse impact on the Brazilian economy and on our business.

Political conditions in Brazil may affect the confidence of investors and the public in general, as well as the development of the economy. It may also have an adverse impact on the Brazilian economy, our business, financial condition, results of operations and the market price of our preferred shares and ADSs.

Inflation and government efforts to curb inflation may contribute to economic uncertainty in Brazil, adversely affecting our business and results of operations.

Brazil has historically experienced high rates of inflation. Inflation and certain government's measures taken in the attempt to curb inflation have had significant negative effects on the Brazilian economy. In 2013, inflation measured by the Consumer Price Index (*Índice de Preços ao Consumidor*), or IPCA, reached 5.8%, below the upper limit established by the CMN, of 6.5%, but above the central inflation target of 4.5%. In 2014, the Brazilian monetary policy will continue to use the IPCA as a reference for the inflation target. The inflation target for 2014 is set at 4.5%, similar to 2013. If inflation rises beyond this target, the basic interest rates may also rise, directly affecting the cost of our debt and indirectly reducing the demand for products and services related to telecommunications. In 2014, factors that may adversely affect consumer inflation are, among others, the international commodities prices, the impact of buoyant domestic economic activity on domestic prices and the indexation of prices and tariffs.

Since 2006, telephone fees for fixed line services have been indexed to the Index of Telecommunication Service, or IST, reduced by a productivity factor. The IST is a basket of national indexes that reflects the industry's operating costs. As a result, this index serves to reduce potential discrepancies between our industry's revenue and costs, and thus reduce the apparent adverse effects of inflation upon our operations.

The fee rate increase authorized by ANATEL, which references the IST, is reduced by a factor of productivity and applied cumulatively after a period of 12 months. This may cause increases in costs and salaries above and below our revenues, with adverse impacts on our profitability. Increases in interest rates may have a material adverse effect on our business.

The Monetary Policy Committee of the Brazilian Central Bank (*Comitê de Política Monetária do Banco Central do Brasil*), or COPOM, sets the target of the basic interest rate for the Brazilian financial system based on an expectation of convergence between the future inflation rate and the central inflation target. On December 31, 2013, the basic interest rate was 10.0% per year, compared to 7.25% per year on December 31, 2012. The basic interest rate has been further adjusted in 2014 and is currently 10.75% per year. Further increases in the basic interest rate may occur throughout 2014 with adverse effects on our business. According to current market consensus, inflation measured by the IPCA will be higher than the established inflation target of 4.50% for 2014. As a result, the Central Bank may increase the SELIC rate (the Central Bank's overnight rate) in 2014 to align inflation with the inflation target, which may adversely affect our business.

Fluctuations in exchange rates may adversely affect our ability to meet liabilities denominated or linked to foreign currencies or reduce our income in foreign currency, and may have a material adverse effect on the market value of our preferred shares and ADSs.

The exchange rate between the U.S. dollar and the Brazilian *real* has experienced significant fluctuations in recent years. The *real* devalued 67% against the U.S. dollar between 2000 and 2003 and appreciated by 40% from 2004 to 2010, considering the annual average exchange rates. From 2011 to 2013, however, the *real* was further devalued, by 29.1%. Between 2001 and 2013, the *real* depreciated by 8.1 % against the U.S. dollar.

As of December 31, 2013, 15.9 % of our R\$ 8.75 billion total financial debt was denominated in U.S. dollars and UMBNDES. As of December 31, 2013, we had currency hedges in place to cover all of our financial foreign currency-denominated bank debt.

Part of the costs relating to our network infrastructure and services provided by outside vendors is payable or linked to payment by us in U.S. dollars. By contrast, our revenue is generated in *reais*, except income derived from hedging transactions, international long-distance interconnection and services to customers outside of Brazil.

To the extent that the value of the *real* decreases relative to the U.S. dollar or the euro, our commitments linked to fluctuations in exchange rates or payable in foreign currencies become more expensive. In return, our accounts receivable denominated in foreign currencies appreciate, which could adversely affect our revenue and expenses.

However, 100% of the net balance of the transactions denominated in foreign currencies is covered by hedge transactions. Since May 2010, the company began using net balance coverage, which is the coverage for net positions in foreign exchange exposures generated by invoices issued or received in foreign currencies, substantially reducing the company's risk to fluctuations in exchange rates. By periodically receiving invoices for the net balance coverage and determining the coverage of exposures, the company's corporate market risk department monitors its foreign exchange exposure and commitments linked to foreign currencies so as not to achieve a significant amount of exposure.

It should be noted that the IST, the current index applicable to telecommunication fees for fixed-line services, does not adequately reflect the true effect of exchange rate fluctuations. Thus, since 2006, telecommunication revenue, when converted to U.S. dollars, does not adequately reflect the true effect of exchange rate fluctuations, so that our results of operations could be adversely affected. See "--A. Selected Financial Data-- Exchange Rates" for more information on exchange rates.

Political, economic and social developments and the perception of risk in other developed and emerging countries may adversely affect the Brazilian economy, our business, and the market price of Brazilian securities, including our preferred shares and ADSs.

The market for securities issued by Brazilian companies may be influenced, to varying degrees, by economic conditions in both developing and developed economies. The reaction of investors to developments in other countries may have an adverse impact on the market value of securities of Brazilian companies. Crises in other emerging countries or the economic policies of other countries may reduce investor demand for securities of Brazilian companies, including our preferred shares. Any of the foregoing developments may adversely affect the market value of our preferred shares and hinder our ability to access the capital markets and finance our operations in the future on acceptable terms and costs, or at all.

Exchange controls and restrictions on remittances abroad may adversely affect holders of our preferred shares and ADSs.

Brazilian law allows that, whenever there is a significant imbalance in Brazil's balance of payments or a significant possibility that such imbalance will exist, the Brazilian government may impose temporary restrictions on capital outflows. Such restrictions could hinder or prevent the holders of our preferred shares or the custodian of our shares in Brazil, Citibank N.A. (acting as the agent for the depositary), from remitting dividends abroad. The Brazilian government imposed restrictions on capital outflows for a six-month period at the end of 1989. If similar restrictions are introduced in the future, they would likely have an adverse effect on the market price of our preferred shares and ADSs.

Risks Relating to the Brazilian Telecommunications Industry and Us

Extensive government regulation of the telecommunications industry and our concession may limit, in some cases, our flexibility in responding to market conditions, competition and changes in our cost structure or impact our fees.

Our business is subject to extensive government regulation, including any changes that may occur during the period of our authorization to provide telecommunication services. ANATEL, which is the main telecommunications industry regulator in Brazil, regulates, among other things:

- industry policies and regulations;
- licensing;
- fees and tariffs;
- competition, including, therefore, our ability to grow by acquiring other telecommunications businesses;

- telecommunications resource allocation;
- service standards;
- technical standards;
- quality standards;
- interconnection and settlement arrangements; and
- universal service obligations.

Brazil's telecommunications regulatory framework is continuously evolving. The interpretation and enforcement of regulations, the assessment of compliance with regulations and the flexibility of regulatory authorities are all marked by uncertainty. We operate under authorization from the Brazilian government, and our ability to retain this authorization is a precondition to our success. However, because of the regulatory framework, we cannot provide assurances that ANATEL will not adversely modify the terms of our authorization. Furthermore, according to the terms of our operating authorizations, we are obligated to meet certain requirements and to maintain minimum quality, coverage and service standards. Failure by us to comply with these requirements may result in the imposition of fines or other government actions, including the termination of our operating authorizations. Any partial or total revocation of any of our operating authorizations would have a material adverse effect on our business, financial condition, revenues, results of operations and prospects. In recent years, ANATEL has also been reviewing and introducing changes in the applicable regulation, especially regarding the interconnection fees among telecommunications service providers in Brazil. Interconnection fees, which are fees charged by telecommunications service providers to each other to interconnect to each other's networks, are an important part of our revenue base. To the extent that changes to the rules governing interconnection fees reduce the amount of interconnection fees we are able to collect, our businesses, financial conditions, revenues, results of operations and prospects could be materially adversely affected.

Therefore, our businesses, results of operations, revenues and financial conditions could be negatively affected by the actions of the Brazilian authorities, including, in particular, the following:

- the introduction of new or stricter operational and/or service requirements;
- the granting of operating licenses in our areas;
- delays in the granting of, or the failure to grant, approvals for rate increases; and
- antitrust limitations imposed by ANATEL and CADE.

Our concession may be terminated by the Brazilian government under certain circumstances.

We operate our business under a concession granted by the Brazilian government offering fixed line services in the State of São Paulo. According to the terms of the concession, we are obligated to meet certain universal service requirements and to maintain minimum quality and service standards. For example, ANATEL requires that we satisfy certain conditions with respect to, among other things, expansion of our network to provide public pay-phone service for all locations with a population over 100 inhabitants, expansion of our network to provide private individual telephone service for all locations with a population over 300 inhabitants, and, with respect to quality of service, targets for the number of call completions. Our ability to satisfy these and other terms and conditions, may be affected by factors beyond our control. Our failure to comply with the requirements of our concession may result in the imposition of fines up to R\$50.0 million or other government actions, including the termination of our concession. Any partial or total revocation of our concession would have a material adverse effect on our financial condition and results of operations. Moreover, the concession agreements establish that all assets owned by the company and which are indispensable to the provision of the services described in such agreements are considered reversible assets and are deemed to be part of the concession assets. The assets will be automatically returned to ANATEL upon expiration of the concession agreements, according to the regulation in force at that time. The last net book value of reversible assets reported to ANATEL is dated December 31, 2013 and estimated at R\$7.3 billion,

which is comprised of switching and transmission equipment and public use terminals, external network equipment, energy equipment and system and operation support equipment.

The expiration date of the original concession agreements was December 31, 2005, but it has since been renewed as of December 22, 2005 for an additional 20-year term. The current concession agreements contain a provision allowing ANATEL to review the concession terms in 2015 and 2020. This provision permits ANATEL to update the renewed concession agreements with respect to network expansion, modernization and quality of service targets in response to changes in technology, competition in the marketplace and domestic and international economic conditions.

Review of our concession agreements may have a materially adverse effect on us.

On December 12, 2013, as part of a review of our concession agreement for fixed telephone line services, ANATEL issued a public consultation, pursuant to the terms of our concession agreement. The public consultation allowed members of the public to comment on certain topics such as service universalization, rates and fees and quality of services, among others. Depending on the comments of the public and decisions made by ANATEL, it may decide to revise our concession agreement and impose obligations on us that may have a materially adverse effect on our financial condition and results of operations.

Important mergers and acquisitions in the market should increase competition in the upcoming years.

Some of the main telecommunication groups in Brazil have been going through a series of mergers and acquisitions since 2012. In December 2011, Sky Brasil (a Brazilian subsidiary of DirecTV), announced the purchase of Acom Comunicações, a Brazilian television and internet company, which was approved by regulators in 2012. Along with the acquisition of Acom, Sky Brasil also acquired grants to operate new 4G spectrum areas in June 2012.

In May 2012, entrepreneur George Soros acquired Sunrise Telecomunicações, a Brazilian paid-TV provider that is now expanding into mobile services. Sunrise Telecomunicações spent US\$9.3 million to acquire two 4G spectrum licenses covering 134 cities in the state of São Paulo.

In October 2013, Oi and Portugal Telecom announced an agreement among Oi, Portugal Telecom, and Telemar Part (CorpCo.) to form a single entity. According to the memorandum of understanding entered into in connection with this operation, Oi will increase its capital stock by approximately R\$14.1 billion, of which a minimum of R\$7.0 billion and a maximum of R\$8.0 billion will be paid in cash and the approximately R\$6.1 billion will be paid in stock of Portugal Telecom. The definitive agreements will provide that Oi's capital increase will be subject to the full subscription of the minimum value of the portion to be paid in cash. In January 2014, CADE, the Brazilian antitrust authority, approved the transactions with no restrictions.

Mergers and acquisitions may change the market dynamic, cause competitive pressure and force small competitors to find partners and may impact our business, in terms of operations, financial condition, marketing strategies and offering of products and promotions.

We face increasing competition from telecom service providers.

Growth in the telecommunication industry in Brazil decelerated in 2013, mainly due to regulatory changes, such as cuts in mobile termination rates and fixed to mobile calls, which directly impact the revenues of telephone operators. However, competition remained strong, despite the weak macroeconomic environment, due to regulation initiatives aimed at stimulating competition, increasing the adoption of services and reinforcing the quality of services. The market has been marked by efforts to stimulate voice and data usage, and to reduce the effects of fixed-mobile substitution. Convergent solutions, which give customers the option to purchase a package of services, are becoming a trend. Furthermore, in 2013 there has also been an increase in competition regulation aimed at stimulating competition, increasing the adoption of new services and reinforcing the quality of services delivered.

Brazilian antitrust regulation is based on Law No. 12,529 of November 30, 2011, which generally prohibits any practice or transactions aimed at restricting free competition, dominating the relevant market of goods or services, arbitrarily increasing profits, or abusively exercising a dominant market position. The new antitrust law has altered several practices in Brazil; particularly, it established a pre-merger notification regime with new turnover thresholds and extended the maximum period for merger review procedures to 330 days from 240 days. We cannot continue to expand our growth through acquisition of other service providers given the antitrust objections of ANATEL along with the fact that we currently already render SMP service all over the country. Consolidation of other competitors in the telecommunications market will increase the competitive pressure on us due to the increase in their economies

of scale and reduction of operational costs, and we may be unable to respond adequately to pricing pressures resulting from consolidation, which would adversely affect our business, financial condition and results of operations.

Our results of operations may be negatively affected by the application of the SMP rules.

Under the SMP regime, our mobile subsidiaries have received payments for the use of their networks in accordance with a network usage payment plan, which includes outbound long-distance calls. Until June 30, 2004, SMP service providers were able to opt to establish a price cap or freely negotiate our interconnection charges. In early 2005, ANATEL began permitting free negotiations for mobile interconnection, or VU-M fees and by July 2005, local-fixed concessionaires and mobile operators had reached a provisional agreement with respect to VU-M fees for local calls, or VC1 (the agreement guaranteed a 4.5% increase in mobile operators' fees). ANATEL approved that provisional agreement and, in March 2006, approved another provisional agreement of a 4.5% increase for VU-M fees for long-distance calls, or VC2, VC3, and international calls, among the same operators that had made the VC1 agreement in July 2005. In July 2007, ANATEL approved a provisional agreement among us and the fixed-line operators Telemar, Brasil Telecom, CTBC Telecom and Sercomtel and the mobile operators for interconnection fees for VC1, VC2 and VC3 calls that provides for an annual adjustment of approximately 1.97% to interconnection fees in Region I (Telemar's Region) and an annual adjustment of approximately 2.25% in Region II (Brasil Telecom's Region) and Region III (Telefônica's Region). The current rule is the free negotiation of fees, subject to ANATEL regulations.

Resolution No. 576/2011 established rules for adjusting the VC fees, with consequent repass for the VU-M (mobile termination rate). It has also determined gradual annual percentages decreases from 2012 to 2014 for these fees. On April 5, 2013, ANATEL published Act 2222 in the Official Gazette, which led to a reduction of 8.77% on the value of our mobile termination rate.

ANATEL also issued Regulation No. 460/2007 regarding Number Portability, implementing and developing fixed and wireless Number Portability in Brazil effective as of March 2009, with most costs being borne by the operators. For SMP, Number Portability is applied for wireless codes of access of the same registration area. As of December 2013, there were 270.5 million cell phones in Brazil. From the period beginning in September 2008, when Number Portability became effective, until December 31, 2013, over 3.6 million users had transferred out of, and another 4 million users had transferred into our mobile services. For fixed service operators, Number Portability is applied for fixed codes of access of the same local area. There can be no assurance that this regulation will not have material adverse effects on the results of our operations.

On July 18, 2012, Vivo was notified by ANATEL that it would be required to present an improvement plan, subject to ANATEL's approval, for the improvement of SMP services provided. The plan is aimed to improve services, in particular: (1) call completions; (2) service interruptions; and (3) user satisfaction. Our competitors were also required to present their own improvement plans to ANATEL. Vivo presented its improvement plan to ANATEL and received approval on September 10, 2012. Beginning in 2013, ANATEL has published measurement results for predefined indicators.

We cannot predict whether the current regulatory regime will remain in place or whether any future regulatory change or requirements will have an adverse effect on our results of operations. We cannot assure you that our service plan will continue to be approved by ANATEL or that the interconnection rates we negotiated will be upheld or that future negotiations will be as favorable as those that were previously set by ANATEL. If the readjustments that we negotiated are cancelled or if freely negotiated interconnection fees in the future are less favorable to us, our business, financial condition, revenues, results of operations and prospects will be adversely affected.

If the inflation adjustment index currently applied to our prices is changed, the new index may not adequately reflect the true effect of inflation on our prices, which could adversely affect our results of operations.

Currently, fixed broadband and mobile service providers use the General Price Index, or IGP-DI (*Índice Geral de Preços - Disponibilidade Interna*) to adjust their prices and TV and cable service providers use the IGP-M (*Índice Geral de Preços ao Mercado*). The IGP-DI and IGP-M are inflation indexes developed by Fundação Getúlio Vargas, an economic private organization. Since 2006, telephone fees for fixed line service have been indexed, as set in regulation, by the Index of Telecommunications Service, or the IST reduced by a productivity factor. The IST is a basket of national indexes that reflect the industry's operational costs. As a result, this index serves to reduce potential discrepancies between our industry's revenue and costs, and thus reduce the apparent adverse effects of inflation upon our operation.

The inflation index for the telecommunication prices adjustment rely exclusively on external factors and we have little control over it. If new inflation adjustment mechanisms, or any other mechanism chosen by the Brazilian government in the future, do not adequately reflect the true effect of inflation on our prices, our results from operations could be adversely affected.

ANATEL's new regulation regarding interconnection and network usage fees could have an adverse effect on our results.

ANATEL issues new regulations every year affecting many of our areas of operations. Such new regulations could have an adverse effect on our operational results because: (1) our interconnection charges could drop significantly, thereby reducing our revenues; (2) ANATEL may allow more favorable prices for economic groups without significant market power; (3) the prices we charge in some regions in which we operate are higher than those in certain other regions, and consolidation of those prices, competitive pressures and other factors would reduce our average prices and thereby reduce our revenues; (4) the granting of new licenses may increase competition in our area from other operators, which could adversely affect our market share, thereby reducing our revenues; (5) the inclusion of revenue received for the usage of the SMP network in the calculation of operational profit, which will increase the cost of renewing licenses; and (6) ANATEL's general plan of updating the telecommunications regulation targets several areas of vital importance for the mobile telecommunications business, such as regulation to improve the quality of services that can cause the rise of operational costs, regulation of the virtual mobile operation, or MVNO which may cause an increase of competitive pressure, regulation against significant market power (*Poder de Mercado Significativo*), or PMS, arising from VU-M fee unification among SMP providers of the same economic group having significant market power, which may cause a decrease on our revenues, and regulation of multimedia communication, or SCM, that can cause an increase in competitive pressure. For a detailed description of the regulations issued by ANATEL and their impact on our business, see "Item 4B. Business Overview-Regulation of the Brazilian Telecommunications Industry."

The industry in which we conduct our business is continually changing and evolving technologically.

The telecommunications industry is subject to rapid and significant technological changes. Our future success depends on our ability to anticipate and adapt in a timely manner to technological changes. We expect that new products and technologies will emerge and that existing products and technologies will be further developed.

The advent of new products and technologies could have a variety of consequences. These new products and technologies may reduce the price of our services by providing lower-cost alternatives, or they may also be superior to, and render obsolete, the products and services we offer and the technologies we use, thus requiring investment in new technology.

We are subject to certain risks related to conditions and obligations imposed by ANATEL for the use of the spectrum needed to the LTE services we offer.

In August 2010, ANATEL established a new policy regulating the 2.5 GHz spectrum, which requires Multichannel Multipoint Distribution Service, or MMDS companies, including Vivo, to return a significant portion of the spectrum we currently own and to offer cable TV on a primary basis, by 2013.

On June 12 and 13, 2012, ANATEL held a public bidding for 273 lots of 4G, on the 2,500 to 2,690MHz frequencies. We acquired the "X" band, with a nationwide coverage, for R\$1.05 billion. Given the rules of the public bidding process, which limited the total spectrum each service provider could hold within this frequency, we agreed to relinquish bands "P," "T" and "U." used for MMDS services within 18 months of obtaining the "X" band. Sky and TIM have preferred rights for the acquisition of the "T" and "U," respectively, and for the "P" bands, in the cities of Curitiba and Rio de Janeiro and Oi have preferred rights for the acquisition of the "P" band in the cities of São Paulo and Porto Alegre.

In order to meet the coverage obligations and the schedule defined by ANATEL, we have made 4G services available to the cities that hosted 2013 FIFA Confederations Cup games and that will host the 2014 FIFA World Cup games. To complete the coverage requirements, we will need to implement the following coverage requirements:

- by May 31, 2014: state capitals, the Federal District and cities with over 500,000 residents;
- by December 31, 2015: cities with over 200,000 residents;
- by December 31, 2016: cities with over 100,000 residents;
- by December 31, 2017: cities with between 30,000 and 100,000 residents; and
- by December 31, 2019: cities with fewer than 30,000.

Tied, ANATEL auctioned a 450 MHz frequency lot that is tied to the 2.5 GHz band, to meet voice and data demand in remote rural areas.

Under band “X,” which we acquired in the bidding process, we will be required to provide infrastructure in rural areas in the states of Alagoas, Ceará, Minas Gerais, Paraíba, Pernambuco, Piauí, Rio Grande do Norte, Sergipe, and countryside of São Paulo, for a total of 2,556 municipalities. The timetable for providing infrastructure in the rural areas requires that 30% of municipalities have infrastructure set up by June 2014, 60% by December 2014 and 100% by December 2015, with a transmission rate of 256Kbps and by December 31, 2017, all of these municipalities will be expected to have 1Mbps.

The targets established by ANATEL associated with a fast paced implementation of networks could impact (1) the ability to obtain municipal licenses for the construction of new sites at the speed necessary to achieve the coverage targets, (2) the capacity of suppliers to deliver the equipment necessary for this expansion, with possible impact on their prices, subject to targets to acquire national technology, and (3) lack of workers to meet the expected implementation pace.

Furthermore, the Ministry of Communications issued ordinance No. 14/2013, which began a debate over the 700 MHz frequency, to align itself with the objectives of the Brazilian National Broadband Plan, or PNBL. After conducting a public consultation, between February 28 and May 5, 2013, and by approving Resolution No. 625/2013, ANATEL has allocated this band to the provision of fixed and mobile telephone and broadband services. However, the completion of the allocation process requires the migration of the TV channels that currently occupy the band as well as the conclusion by ANATEL of studies regarding spectrum interference between mobile and TV services.

Our sales could be suspended as result of issues with the quality of our services.

ANATEL and other judiciary and administrative agencies have the authority to suspend our sales in an attempt to improve the overall quality of telecommunications services. Sales suspensions are generally applied to the services for which there have been complaint by consumers and the consumer protection agencies. When applied, the suspension is temporary and usually lifted once the company presents an improvement action plan. In July 2012 ANATEL suspended mobile service (SMP) sales from three of our main competitors, Oi, Claro and Tim, as result of a considerable increase in consumer complaints. The suspensions lasted about 20 days and ANATEL requested that all telecommunications companies, including Telefonica Brasil, to present an Action and Investment Plan to improve the mobile network. If a similar increase in customer complaints takes place, we may face suspension of one or more of our services until a plan can be produced, which may materially affect our business and results of operations.

Certain of our debt agreements contain financial covenants, and any default under such debt agreements may have a material adverse effect on our financial condition and cash flows.

Certain of our existing debt agreements contain restrictions and covenants and require the maintenance or satisfaction of specified financial ratios and tests. Failure to meet or satisfy any of these covenants, financial ratios or financial tests could result in an event of default under these agreements.

Companies in the telecom industry, including us, may be harmed by restrictions regarding the installation of new antennas for mobile services.

Currently, there are approximately 250 municipal laws that limit the installation of new antennas for mobile service, which has been a barrier to the expansion of mobile networks. Those laws are meant to regulate issues related to urban aspects and the alleged effects of the radiation and radiofrequencies of the antennas. Initiatives for the approval of a federal law that establishes new guidelines to create a consolidated plan for the installation of antennas, have been taken. However as long as the municipal laws remain unchanged, the risk of noncompliance with regulation and of having services of limited quality in certain areas will exist.

Additional antenna installation is also limited as a result of media and other reports, which have suggested that radio frequency emissions from base stations may cause health problems. These concerns could have an adverse effect on the wireless communications industry and, possibly, expose wireless providers, including us, to litigation.

According to the World Health Organization, or WHO, there is no evidence in the latest medical research that shows any relationship between radio frequency emissions of base stations and health concerns. However, expansion of our network may be affected by perceived risks if we experience problems in finding new sites, which in turn may delay expansion and may affect the quality of our services.

On July 2, 2002, ANATEL published Resolution No. 303 that limits emission and exposure for fields with frequencies between 9 kHz and 300 GHz. In addition, the Brazilian government developed specific legislation for the deployment of radio frequency transmission stations that supersedes the existing state and municipal laws. In May 2009, the Brazilian government published Law No. 11934/2009 that limits the exposure for fields with frequencies up to 300 GHz. The new law uses the exposition limits determined by the International Commission on Non-Ionizing Radiation Protection, or ICNIRP and recommended by the WHO.

In May 2011, the specialized body of the WHO for research on cancer (IARC) classified electromagnetic fields of mobile telephony as “possibly carcinogenic,” a classification which also includes products such as coffee and pickled foods. The WHO subsequently indicated, in fact sheet no. 193, published in June 2011, that to date it cannot be confirmed that the use of a mobile telephone has adverse effects on health, although it also announced that an official assessment of this risk will be conducted, taking into account all scientific evidence available.

New laws may create additional transmission regulations, which in turn, could have an adverse effect on our business. Also, health concerns may affect our ability to capture or retain customers, may discourage the use of the mobile telephone and may result in the adoption of new measures by governments or any other regulatory interventions, any of which could materially and adversely affect our business, results of operations and financial condition.

We face risks associated with litigation.

We are party to a number of lawsuits and other proceedings. An adverse outcome in, or any settlement of, these or other lawsuits could result in significant costs to us. In addition, our senior management may be required to devote substantial time to these lawsuits, which they could otherwise devote to our business. See “Item 8. Financial Information–A. Consolidated Statements and Other Financial Information–Legal Matters.”

We may be required to record impairment charges relating to goodwill and long-lived assets in the future.

For IFRS purposes, we are required to test our goodwill for impairment at least annually. The excess of the book value of a company over its market value may indicate that impairment exists. This impairment test is described in Note 3 to our audited consolidated financial statements. The Company has substantial goodwill with a carrying value of R\$10.2 billion as of December 31, 2013. It is possible that we may be required to record impairment charges relating to our goodwill in future periods, and this would have an adverse effect on our results of operations.

In addition, we are required to record impairment charges on long-lived assets, including property, plant and equipment and finite-lived intangible assets (including licenses) if the carrying value of these assets exceeds the recoverable amount expected from their use. This impairment test is also described in Note 3 to our audited consolidated financial statements included in this annual report.

Risks Relating to the Preferred Shares and the ADSs

Holders of our ADSs may face difficulties in serving process on or enforcing judgments against us and other persons.

We are organized under the laws of Brazil, and all of our executive officers and our independent public accountants reside or are based in Brazil. Also, seven of our twelve directors reside or are based in Brazil. Substantially all of our assets and those of these other persons are located in Brazil. As a result, it may not be possible for holders of the ADSs to effect service of process upon us or these other persons within the United States or other jurisdictions outside Brazil or to enforce against us or these other persons judgments obtained in the United States or other jurisdictions outside Brazil. Because judgments of U.S. courts for civil liabilities based upon the U.S. federal securities laws may only be enforced in Brazil if certain conditions are met, holders may face greater difficulties in protecting their interests due to actions by us, our directors or executive officers than would shareholders of a U.S. corporation.

Holders of our Preferred Shares and ADSs generally do not have voting rights.

In accordance with Brazilian Corporate Law and our bylaws, holders of our preferred shares, and therefore of our ADSs, are not entitled to vote at meetings of our shareholders, except in limited circumstances set forth in “Item 10. Additional Information–B. Memorandum and Articles of Association.”

Holders of our Preferred Shares might be unable to exercise preemptive rights with respect to the preferred shares unless there is a current registration statement in effect which covers those rights or unless an exemption from registration applies.

Holders of our preferred shares will not be able to exercise the preemptive rights relating to the preferred shares underlying your ADSs unless a registration statement under the U.S. Securities Act of 1933, as amended, or the Securities Act, is effective with respect to the shares underlying those rights, or an exemption from the registration requirements of the Securities Act is available. We are not obligated to file a registration statement. Unless we file a registration statement or an exemption from registration applies, holders of our preferred shares may receive only the net proceeds from the sale of their preemptive rights by the depositary, or if the preemptive rights cannot be sold, they will lapse and you will not receive any value for them. For more information on the exercise of these rights, see “Item 10. Additional Information–B. Memorandum and Articles of Association–Preemptive Rights.”

An exchange of ADSs for preferred shares risks the loss of certain foreign currency remittance and Brazilian tax advantages.

The ADSs benefit from the certificate of foreign capital registration, which permits Citibank N.A., as depositary, to convert dividends and other distributions with respect to preferred shares into foreign currency, and to remit the proceeds abroad. Holders of ADSs who exchange their ADSs for preferred shares will then be entitled to rely on the depositary’s certificate of foreign capital registration for five business days from the date of exchange. Thereafter, they will not be able to remit non-Brazilian currency abroad unless they obtain their own certificate of foreign capital registration, or unless they qualify under Resolution No. 2,689 of the Central Bank of Brazil, dated January 26, 2000 and issued by BACEN, which entitles certain investors to buy and sell shares on Brazilian stock exchanges without obtaining separate certificates of registration.

If holders of ADSs do not qualify under Resolution No. 2,689, they will generally be subject to less favorable tax treatment with respect to our preferred shares. There can be no assurance that the depositary’s certificate of registration or any certificate of foreign capital registration obtained by holders of ADSs will not be affected by future legislative or regulatory changes, or that additional Brazilian law restrictions applicable to their investment in the ADSs may not be imposed in the future.

Holders of our preferred shares will be subject to, and holders of our ADSs could be subject to, Brazilian income tax on capital gains from sales of preferred shares or ADSs.

Brazilian Law No. 10,833 provides that gains on the disposition of assets located in Brazil by nonresidents of Brazil, whether to other nonresidents or to Brazilian residents, will be subject to Brazilian taxation. The preferred shares are expected to be treated as assets located in Brazil for purposes of the law, and gains on the disposition of preferred shares, even by nonresidents of Brazil, are expected to be subject to Brazilian taxation.

Based on the fact that the ADSs are issued and registered abroad, we believe that gains on the disposition of ADSs made outside of Brazil by nonresidents of Brazil to another non-Brazilian resident would not be subject to Brazilian taxation, since they would not fall within the definition of assets located in Brazil for purposes of Law 10,833. However, considering the general and unclear scope of Law No. 10,833 and the absence of judicial court rulings in respect thereto, we cannot be assured that such an interpretation of this law will prevail in the courts of Brazil. If the income tax is deemed to be due, the gains may be subject to income tax in Brazil at a rate of 15.0% (general taxation) or 25.0% (if the nonresident seller is located in a tax haven, a country which does not impose any income tax, which imposes it at a maximum rate lower than 20.0%, or in which the laws impose restrictions on the disclosure of ownership composition or securities ownership or the identification of the effective beneficiary of income attributed to nonresident holders). See “Item 10. Additional Information–E. Taxation–Brazilian Tax Considerations.”