TELEFONICA BRASIL S.A.
Form 6-K
March 13, 2012

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, 2012

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)

Rua Martiniano de Carvalho, 851 – 21º 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

Financial Statements

Telefônica Brasil S.A. (formerly Telecomunicações de São Paulo S.A. – Telesp)

December 31, 2011 and 2010
With Report of Independent Auditors

(A free translation of the original issued in Portuguese)

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Financial statements

As of and for the years ended December 31, 2011 and 2010.

Contents

Free translation from Portuguese into English of the Individual and Consolidated Financial Statements prepared in accordance with the accounting practices adopted in Brazil and the Consolidated Financial Statements prepared in accordance with the International Financial Reporting Standards (IFRS).

Independent auditors´ report on financial statements

(A free translation of the original report issued in Portuguese)

Shareholders, Management and Board Members

Telefônica Brasil S.A. (formerly Telecomunicações de São Paulo S.A. – TELESP)

São Paulo – SP

We have audited the accompanying individual and consolidated financial statements of Telefônica Brasil S.A. ("Company"), identified as Company and Consolidated, respectively, which comprise the balance sheet as at 31 December, 2011, and the related statements of income, of comprehensive income, of changes in shareholders' equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of the individual financial statements in accordance with accounting practices adopted in Brazil and the consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board – IASB, and in conformity with accounting practices adopted in Brazil, and for such internal control management determines is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with Brazilian and International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of risks of material misstatement of the Company's financial statements, whether due to fraud or error. In this risk assessment, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion on the individual financial statements

In our opinion, the individual financial statements referred to above present fairly, in all material respects, the financial position of Telefônica Brasil S.A. as at December 31, 2011, its financial performance and its cash flows for the year then ended in accordance with accounting practices adopted in Brazil.

Opinion on the consolidated financial statements

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Telefônica Brasil S.A. as at December 31, 2011, its consolidated financial performance and consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRS) issued by the International Accounting Standards Board (IASB), and accounting practices adopted in Brazil.

Emphasis of matter

As mentioned in Note 2, the individual financial statements were prepared in accordance with accounting practices adopted in Brazil. In the case of Telefônica Brasil S.A, these practices differ from the IFRS, applicable to the individual financial statements, solely with respect to the measurement of investments in subsidiaries, affiliates and jointly-owned subsidiary under the equity method, while such investments would be measured at cost or fair value for IFRS purposes. Our opinion is not qualified due to this matter.

Other matters

Statements of value added

We have also audited the individual and consolidated statements of value added for the year ended December 31, 2011, prepared under management responsibility, whose presentation is required by Brazilian corporation law for publicly-held companies, as supplementary information under IFRS, whereby statements of value added presentation is not required. These statements have been subject to the same audit procedures previously described, and, in our opinion, are presented fairly, in all material respects, in relation to the overall financial statements.

São Paulo, February 14, 2012

ERNST & YOUNG TERCO

Auditores Independentes S.S.

CRC-2SP015199/O-6

Alexandre Hoeppers

Accountant CRC-SC021011/O-3-T-PR-S-S

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Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Balance sheets

December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the original issued in Portuguese)

	Note	Company		Consolidated	
Assets		**2011**	**2010**	**2011**	**2010**
Current assets		**4,775,480**	4,374,823	**11,810,118**	5,147,449
Cash and cash equivalents	5 and 36	**826,902**	1,089,089	**2,940,342**	1,556,715
Trade accounts receivable, net	6	**2,286,636**	2,356,013	**5,105,860**	2,546,225
Inventories	7	**31,836**	35,102	**471,721**	77,499
Recoverable taxes	8.1	**1,130,761**	480,691	**2,495,066**	659,357
Escrow deposits	9	**-**	-	**116,421**	-
Derivatives	36	**674**	166	**1,840**	166
Prepaid expenses	10	**37,705**	40,623	**255,056**	41,372
Other	11	**460,966**	373,139	**423,812**	266,115
Noncurrent assets		**50,269,267**	15,226,157	**53,679,855**	14,818,845
Long-term portion of investments pledged as collateral		**-**	-	**99,114**	-
Trade accounts receivable, net	6	**-**	-	**84,855**	67,343
Recoverable taxes	8.1	**787,852**	320,720	**1,014,959**	326,677
Deferred taxes	8.2	**-**	501,354	**1,428,878**	503,679
Escrow deposits	9	**2,815,964**	1,696,417	**3,400,244**	1,710,683
Derivatives	36	**35,142**	-	**225,935**	-
Prepaid expenses	10	**18,290**	24,647	**32,138**	24,647
Other	11	**109,221**	109,698	**148,293**	153,808
Investments	12	**20,245,883**	2,370,573	**37,835**	100,837
Property, plant and equipment, net	13	**9,691,517**	9,575,959	**17,153,920**	10,200,697
Intangible assets, net	14	**16,565,398**	626,789	**30,053,684**	1,730,474
Total Assets		**55,044,747**	19,600,980	**65,489,973**	19,966,294

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	Note	Company		Consolidated	
Liabilities and Shareholders' Equity		**2011**	**2010**	**2011**	**2010**
Current Liabilities		**6,398,178**	5,293,548	**12,740,263**	5,615,310
Payroll and related accruals	15	**244,438**	299,877	**495,624**	307,245
Trade accounts payable	16	**2,396,987**	2,568,077	**6,081,611**	2,832,157
Taxes payable	17	**700,187**	720,143	**1,691,991**	754,993
Loans and financing	18.1	**510,899**	420,412	**988,413**	420,412
Debentures	18.2	**468,624**	-	**468,624**	-
Dividends and interest on shareholders' equity payable	19	**972,986**	450,897	**972,986**	450,897
Provisions	20	**287,137**	240,213	**416,313**	240,213
Derivatives	36	**10,960**	9,502	**51,162**	9,502
Deferred revenue	21	**84,956**	93,518	**761,268**	103,339
Share fractions		**346,396**	112,594	**389,953**	112,594
Other	22	**374,608**	378,315	**422,318**	383,958
Noncurrent Liabilities		**5,320,852**	2,640,318	**9,418,925**	2,683,870
Taxes payable	17	**32,390**	26,786	**459,358**	38,707
Deferred taxes	8.2	**788,954**	-	**788,954**	-
Loans and financing	18.1	**1,277,783**	1,405,314	**3,959,115**	1,405,314
Debentures	18.2	**787,807**	-	**787,807**	-
Provisions	20	**2,336,981**	1,085,633	**3,120,798**	1,118,698
Derivatives	36	**13,382**	18,542	**78,369**	18,542
Deferred revenue	21	**38,616**	35,220	**156,266**	38,400
Other	22	**44,939**	68,823	**68,258**	64,209
Shareholders' equity	23	**43,325,717**	11,667,114	**43,330,785**	11,667,114
Capital		**37,798,110**	6,575,480	**37,798,110**	6,575,480
Capital reserves		**2,719,665**	2,733,562	**2,719,665**	2,733,562
Legal reserve		**877,322**	659,556	**877,322**	659,556
Non-controlling interest acquisition premium		**(29,929)**	-	**(29,929)**	-
Other comprehensive Income		**7,520**	4,417	**7,520**	4,417
Additional proposed dividends		**1,953,029**	1,694,099	**1,953,029**	1,694,099
Non-controlling shareholders		**-**	-	**5,068**	-
Total Liabilities		**55,044,747**	19,600,980	**65,489,973**	19,966,294

The accompanying notes are an integral part of these financial statements.

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statements of income

For the years ended December 31, 2011 and 2010

(In thousands of reais, except earnings per share data)

(A free translation of the original issued in Portuguese)

		Company		**Consolidated**	
	Note	**2011**	**2010**	**2011**	**2010**
Net operating revenue	24	**14,869,327**	14,624,068	**29,128,740**	15,798,251
Cost of goods and services	25	**(8,766,822)**	(7,701,401)	**(14,380,171)**	(8,844,805)
Gross profit		**6,102,505**	6,922,667	**14,748,569**	6,953,446
Operating (expenses) income		**(1,448,017)**	(3,320,796)	**(8,951,203)**	(3,388,110)
Selling	26	**(2,920,471)**	(2,816,885)	**(7,010,125)**	(2,964,632)
General and administrative	27	**(868,954)**	(663,028)	**(2,383,236)**	(738,846)
Equity in earnings (losses) of associates	12	**2,308,650**	(189,047)	**-**	2,889
Other operating income, net	28	**32,758**	348,164	**442,158**	312,479
Operating income before financial expenses, net		**4,654,488**	3,601,871	**5,797,366**	3,565,336
Financial expense, net	29	**(85,063)**	(169,461)	**(139,692)**	(120,738)
Income before income tax and social contribution		**4,569,425**	3,432,410	**5,657,674**	3,444,598
Income tax and social contribution	30	**(214,107)**	(1,033,574)	**(1,295,475)**	(1,045,762)
Net income for the year		**4,355,318**	2,398,836	**4,362,199**	2,398,836
Attributed to:					
Participation of non-controlling shareholders		**-**	-	**6,881**	-
Equity holders of the parent company		**4,355,318**	2,398,836	**4,355,318**	2,398,836
Basic and diluted earnings per share – common		**4.40**	4.45	**4.40**	4.45
Basic and diluted earnings per share – preferred		**4.84**	4.89	**4.84**	4.89

The accompanying notes are an integral part of these financial statements.

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statement of comprehensive income

For the years ended December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the original issued in Portuguese)

	Company	
	2011	**2010**
Net income for the year	**4,355,318**	2,398,83
Gains (Losses) on available for sale securities	**(5,170)**	(117,609
Taxes on earnings (losses) on available for sale securities	**1,758**	39,98
Unrealized actuarial gains (losses) and effect of the limitation of surplus plan assets	**(57,598)**	(54,474
Taxes on unrealized actuarial gains (losses) and effect of the limitation of surplus plan assets	**19,584**	18,52
Gains (losses) on cash flow hedge	**-**	
Taxes on gains (losses) on cash flow hedge	**-**	
Cumulative translation adjustments of foreign currency transactions	**4,520**	(6,778
Participation in comprehensive income of subsidiaries	**(2,988)**	(6,111
Net gains (losses) recognized in equity	**(39,894)**	(126,463
Comprehensive income for the year	**4,315,424**	2,272,37
Attributable to:		
Participation of non-controlling shareholders	**-**	
Equity holders of the parent company	**4,315,424**	2,272,37
Basic and diluted earnings per share – common	4.36	4.2
Basic and diluted earnings per share – preferred	4.80	4.6

The accompanying notes are an integral part of these financial statements.

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statements of changes in shareholders´ equity

For the years ended December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the orginal issued in Portuguese)

	Capital	**Premium paid on acquisition of non-controlling interest**	**Special Goodwill reserve**
Balances as of December 31, 2009	**6,575,480**	**-**	**63,074**
Unclaimed dividends and interest on shareholders' equity, net of taxes	-		-
Net income for the year	-	-	-
Other comprehensive income	-	-	-
Appropriations:		-	
Dividends	-		-
Interest on shareholders' equity	-	-	-
Withholding tax on interest on shareholders' equity	-	-	-
Additional proposed dividend		-	
Balances as of December 31, 2010	**6,575,480**		**63.074**
Unclaimed dividends and interest on shareholders' equity, net of taxes	**-**		**-**
Capital increase due to the acquisiton of Vivo Part. on 04/27/2011	31,222,630	-	-
Withdrawal rights paid to shareholders due to the acquisiton of Vivo Part.	-	-	-
Repurchase of shares	-	-	-
Acquisiton of non-controlling shareholders	-	(29,929)	-
Net income for the year	-	-	-
Other comprehensive income	-	-	-
Appropriations		-	
Dividends	-		-
Interest on shareholders'equity	-	-	-
Withholding tax on interest on shareholders'equity	-	-	-
Legal Reserve	-	-	-
Additional proposed dividend	-	-	-

		-	
Balances as of December 31, 2011	**37,798,110**	**(29,929)**	**63,074**
Outstanding shares (thousand)			
Equity amounts per share			

The accompanying notes are an integral part of these financial statements.

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statements of cash flows

For the years ended December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the original issued in Portuguese)

	Company		Consolidated	
	Dez/2011	**Dez/2010**	**Dez/2011**	**Dez/2010**
Cash flows from operations				
Income before income tax and social contribution	**4,569,426**	3,432,410	**5,657,674**	3,444,598
Items that do not affect cash				
Expenses (revenues) not affecting cash	**394,150**	2,129,647	**5,326,120**	2,270,478
Depreciation and amortization	**2,110,275**	1,653,771	**4,585,994**	1,913,494
Exchange variations from loans	**63,315**	(638)	**89,549**	(638)
Monetary variations	**(33,317)**	31,389	**(30,323)**	34,580
(Gain)/ Loss from equity in earnings of associates	**(2,308,650)**	189,047	**-**	(2,889)
Gain on permanent asset disposals	**(74,304)**	(309,467)	**(482,115)**	(317,486)
Allowance for doubtful accounts	**300,905**	327,302	**506,581**	386,340
Pension and other post-retirement benefits plans	**6,960**	5,187	**(1,163)**	4,504
Tax, civil and labor provisions	**126,652**	6,529	**255,420**	25,578
Interest expense	**192,729**	240,367	**416,426**	240,367
Provision for dismantling costs	**796**	4,120	**(33,138)**	4,332
Provision for loyalty program	**-**	-	**9,861**	-
Others	**8,789**	(17,960)	**9,028**	(17,704)
(Increase) decrease in operating assets	**(246,491)**	(209,966)	**(488,210)**	(208,514)
Trade accounts receivable, net	**(231,527)**	35,558	**(933,558)**	87,501
Inventories	**3,266**	78,463	**(55,669)**	70,937
Other current assets	**168,187**	(76,414)	**601,573**	(61,161)
Other noncurrent assets	**(186,417)**	(247,573)	**(100,556)**	(305,791)
Increase (decrease) in operating liabilities	**(1,335,778)**	(929,004)	**(2,354,209)**	(974,304)
Payroll and related accruals	**(55,439)**	168,256	**(56,908)**	166,994
Accounts payable and accrued expenses	**(53,150)**	(64,178)	**85,694**	(26,355)
Taxes other than income taxes	**(33,153)**	56,332	**130,058**	(8,043)
Other current liabilities	**(338,690)**	52,190	**(521,056)**	43,621

Other noncurrent liabilities	**(44,019)**	(5,699)	**(97,655)**	(3,031)
Interest paid	**(233,255)**	(265,792)	**(496,103)**	(265,792)
Income and social contribution taxes paid	**(578,072)**	(870,113)	**(1,398,239)**	(881,698)
Cash provided by operations	**3,381,307**	4,423,087	**8,141,375**	4,532,258

The accompanying notes are an integral part of these financial statements.

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Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statements of cash flows (Continued)

For the years ended December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the original issued in Portuguese)

	Company		Consolidated	
	Dez/2011	Dez/2010	Dez/2011	Dez/2010
Cash flows generated from (used in) investing activities				
Capital increase in subsidiaries and associates	**(114,000)**	(209,251)	**-**	(3,557)
Ac Aquisition of fixed and intangible assets, net of grants	**(2,231,643)**	(1,948,521)	**(4,653,708)**	(2,126,465)
Cash from sales of fixed assets	**127,817**	292,724	**610,880**	292,858
Cash from sales of investment	**-**	127,185	**-**	178,453
Dividends and interest on shareholders' equity collected	**1,040,211**	-	**-**	-
Cash and cash equivalents for consolidation of companies	**-**	-	**31,095**	-
Cash and cash equivalents from business combination	**698,837**	-	**1,982,898**	-
Cash used in investing activities	**(478,778)**	(1,737,863)	**(2,028,835)**	(1,658,711)
Cash flows generated from (used in) financing activities				
Loans paid	**(1,148,003)**	(1,742,818)	**(1,426,334)**	(1,742,818)
New loans obtained	**2,276,774**	74,275	**2,123,727**	74,275
Net payment on derivatives contracts	**64,712**	(5,399)	**56,765**	(5,399)
Dividends and interest on shareholders' equity paid	**(4,262,729)**	(1,919,906)	**(5,387,601)**	(1,919,906)
Acquisition of non-controlling interest	**(33,850)**	-	**(33,850)**	-
Repurchase of shares	**(61,620)**	-	**(61,620)**	-
Cash used in financing activities	**(3,164,716)**	(3,593,848)	**(4,728,913)**	(3,593,848)
Increase (decrease) in cash and cash equivalents	**(262,187)**	(908,624)	**1,383,627**	(720,301)
Cash and cash equivalents at beginning of year	**1,089,089**	1,997,713	**1,556,715**	2,277,016
Cash and cash equivalents at end of year	**826,902**	1,089,089	**2,940,342**	1,556,715

Changes in cash during the year	**(262,187)**	(908,624)	**1,383,627**	(720,301)

The accompanying notes are an integral part of these financial statements.

Telefônica Brasil S.A.

(formerly Telecomunicações de São Paulo S.A. – Telesp)

Statements of value added

For the years ended December 31, 2011 and 2010

(In thousands of reais)

(A free translation of the original issued in Portuguese)

	Company		**Consolidated**	
	2011	**2010**	**2011**	**2010**
Revenues	**20,470,838**	20,461,874	**40,486,930**	21,838,925
Sale of goods and services	**20,302,208**	20,005,343	**39,755,569**	21,405,355
Other income	**469,535**	783,833	**1,237,942**	819,911
Allowance for doubtful accounts	**(300,905)**	(327,302)	**(506,581)**	(386,341)
Products acquired from third parties	**(9,247,073)**	(8,333,337)	**(15,548,284)**	(9,232,139)
Cost of goods, products and services	**(6,237,109)**	(5,609,807)	**(8,070,174)**	(6,064,202)
Materials, energy, third parties services and others	**(2,851,659)**	(2,425,870)	**(6,666,229)**	(2,826,468)
Loss (Recovery) of assets	**(53,513)**	(137,137)	**(128,765)**	(137,886)
Others	**(104,792)**	(160,523)	**(683,116)**	(203,583)
Gross added value	**11,223,765**	12,128,537	**24,938,646**	12,606,786
Retentions	**(2,110,276)**	(1,653,771)	**(4,585,994)**	(1,913,494)
Depreciation and amortization	**(2,110,276)**	(1,653,771)	**(4,585,994)**	(1,913,494)
Net added value produced	**9,113,489**	10,474,766	**20,352,652**	10,693,292
Added value received upon transfer	**2,858,168**	97,082	**1,103,359**	347,243
Gain (loss) from equity in associates	**2,308,650**	(189,047)	**-**	2,889
Financial income	**549,518**	286,129	**1,103,359**	344,354
Total added value to be distributed	**11,971,657**	10,571,848	**21,456,011**	11,040,535
Distribution of added value	**(11,971,657)**	(10,571,848)	**(21,456,011)**	(11,040,535)
Payroll and related charges	**(702,475)**	(719,309)	**(1,435,014)**	(752,498)
Salary	**(534,423)**	(490,275)	**(1,100,079)**	(514,681)
Benefits	**(116,906)**	(90,529)	**(226,342)**	(95,386)
Payroll tax (FGTS)	**(44,197)**	(40,765)	**(89,131)**	(42,774)
Others	**(6,949)**	(97,740)	**(19,462)**	(99,657)
Taxes, fees and contributions	**(5,593,304)**	(6,473,088)	**(12,679,126)**	(6,601,114)
Federal tax	**(1,324,605)**	(2,123,769)	**(4,471,035)**	(2,213,162)
State tax	**(4,223,367)**	(4,302,080)	**(8,124,977)**	(4,305,339)
Municipal tax	**(45,332)**	(47,239)	**(83,114)**	(82,613)

Interest on third parties capital	**(1,052,410)**	(820,835)	**(2,589,184)**	(1,121,278)
Interest	**(232,248)**	(353,219)	**(490,028)**	(356,337)
Rent and leasing operations	**(420,997)**	(369,384)	**(1,345,329)**	(660,921)
Others	**(399,165)**	(98,232)	**(753,827)**	(104,020)
Dividends and interest on shareholders' equity	**(4,355,318)**	(2,398,836)	**(4,362,199)**	(2,398,836)
Interest on shareholders' equity	**(1,867,000)**	(592,000)	**(1,867,000)**	(592,000)
Dividends	**(2,270,552)**	(1,806,836)	**(2,270,552)**	(1,806,836)
Retained earnings	**(217,766)**	-	**(224,647)**	
Other	**(268,150)**	(159,780)	**(397,369)**	(166,809)
Provisions, net	**(268,150)**	(159,780)	**(397,369)**	(166,809)
Participation of non-controlling shareholders	**-**	-	**6,881**	-

The accompanying notes are an integral part of these Financial Statements.

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Telefônica Brasil S.A.
(formerly Telecomunicações de São Paulo S.A. – Telesp)

Notes to the financial statements
December 31, 2011 and 2010
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1. Operations and background

a) Controlling shareholders

Telefônica Brasil S.A. (formerly Telecomunicações de São Paulo S.A. – Telesp), hereinafter "Telefônica Brasil" or "Company", is headquartered at Rua Martiniano de Carvalho, 851, in the capital of the state of São Paulo, Brazil. Telefônica Brasil belongs to the Telefonica Group, the telecommunications industry leader in Spain which is also present in several European and Latin American countries. The Company is controlled by Telefónica S.A., which as of December 31, 2011, held total direct and indirect interest of 73.81% of which 91.76% are common shares and 64.60% are preferred shares (87.95% in December 31, 2010, of which 85.57% were common shares and 89.13% were preferred shares).

b) Operations

The Company and its subsidiaries' basic business purpose is the rendering of fixed wire telephone services in the state of São Paulo and mobile telephone services nationwide under Fixed Switch Telephone Service Concession Agreement - STFC and authorizations, respectively granted by the National Communications Agency (ANATEL), which is in charge of regulating the telecommunications sector in Brazil under the Law n°9,472 of July 16, 1997 – General Law of Telecommunications modified by Law n° 9,986 of July 18, 2000 (Note 1.b.1 and 1.b.2.). The Company and its subsidiaries have also authorizations from ANATEL to provide other telecommunications services, such as data communication to the business market, broadband internet services (under the Speedy and Ajato brands), mobile telephone services (SMP, through Vivo) and pay TV services (i) by satellite all over the country (Telefonica TV Digital) and (ii) using (MMDS) Multichannel Multipoint Distribution Service technology in the cities of São Paulo, Rio de Janeiro, Curitiba and Porto Alegre. The authorizations for use of 2.5GHz frequency associated with pay TV service by MMDS technology were extended in February 16, 2009 and await a position from ANATEL regarding the payment conditions for renewal.

The Company is registered with the Brazilian Securities and Exchange Commission (CVM) as a publicly-held Company - category A (issuers authorized to negotiate any securities) and its shares are traded in the São Paulo Stock Exchange (Bovespa). The Company is also registered with the U.S. Securities and Exchange Commission (SEC) and its American Depositary Shares (ADSs) – level II, listed only as preferred shares, are traded in the New York Stock Exchange (NYSE).

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b.1. *Fixed Switch Telephone Service Concession Agreement (STFC)*

The Company is the concessionaire of the Fixed Switched Telephone Service (STFC) to render fixed telephony services in the local network and national long distance calls originated in sector 31 of region 3, which comprises the State of São Paulo (except the municipalities that form the sector 33), established in the General Concession Plan (PGO/2008).

The current Concession Agreement dated June 30, 2011, in place since July 1, 2011 awarded as an onerous title, will be valid until December 31, 2025. However, the agreement can be reviewed on December 31, 2015 and December 31, 2020. Such condition allows ANATEL to set up new requirements and goals for universalization and quality of telecommunication services, according to the conditions in place at that moment.

The Concession Agreement establishes that all assets owned by the Company which are indispensable to the provision of the services described on such agreement are considered reversible assets and are deemed to be part of the concession assets. These assets will be automatically returned to ANATEL upon expiration of the concession agreement, according to the regulation in force at that moment. On December 31, 2011, the carrying amount of reversible assets is estimated at R$6,698,899 (R$6,818,075 as of December 31, 2010), comprised of switching and transmission equipment and public use terminals, external network equipment, energy equipment and system and operation support equipment.

In accordance with the Concession Agreement, every two years, during the agreement's new 20-year period, public regime companies will have to pay a fee which will correspond to 2% of its prior-year SFTC revenue, net of taxes and social contributions. In April of 2011, the Company made a payment for this concept of R$186,852, based on the 2010 STFC net revenues.

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b.2. *Commitments and relatives frequencies for mobile services*

The authorizations granted by ANATEL may be renewed just once, for a 15-year period. Biannually, after the first renewal, a payment of rates equivalent to 2% (two percent) of the company's revenue for the preceding year, net of taxes and mandatory social contributions related to the application of the Basic and Alternative Plans of Service.

The subsidiary Vivo S.A. is engaged in cellular mobile telephone services (Personal Mobile Service – SMP), including the activities necessary or useful for the performance of said services, in conformity with the authorities granted to it.

In the auctions held by ANATEL on December 14 and 15, 2010, Vivo S.A. was the winner in 23 lots offered for sale the remaining sub-ranges of 900 MHz and 1800 MHz frequencies, in accordance with the Invitation to Bid n°002/2010/PVCP/SPV-ANATEL.

On April 28, 2011, in its 604th meeting held, ANATEL's Board of Directors, decided in relation to the bidding instructions for H Band surplus (Bidding Instruction No. 002/2010/PVCP/SPV-Anatel) approved Lots 41, 42, 44, 45, 76 to 84, 92, 101, 105, 107, 115, 119, 122, 124, 128 and 163 for Vivo S.A. and other bid-winning operators for lots of that auction.

On May 30, 2011, the decision was published in the Official Gazette (DOU) and the authorization terms were signed with ANATEL. Accordingly, with the ratification of the aforementioned lots, Vivo S.A. increased its overall spectrum and began to operate in the 900 Mhz and 1.800 Mhz frequencies.

On the date of the signature of the Authorization Terms, R$81,175 was paid relating to 10% of the total value and the remaining 90% was paid on December 2011.

The amount of R$811,754, relating to a total of 23 lots, was adjusted in accordance with the remaining license period and recorded as an intangible asset.

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On August 18, 2011, Act No. 7012 was published in the Official Gazette (DOU), which authorized Vivo S.A. to provide Switched Fixed Telephone Services (STFC) to the general public. Vivo S.A. is operating under this authorization nationwide, except in the State of São Paulo, where the Company operates.

Vivo S.A. is engaged in providing the Personal Mobile Service (SMP), including activities necessary or useful for the execution of these services, in accordance with the authorizations granted, as follows:

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c) Subsidiaries

Vivo S. A.:

Wholly-owned subsidiary of the Company, Vivo S.A. is engaged in providing SMP services, including activities necessary or useful for the execution of these services, in accordance with the authorizations granted.

A. Telecom S.A.

A. Telecom S.A. is a wholly-owned subsidiary of the Company, engaged in the following services:

(i) Maintenance of customer internal telephony network, i.e. installation, maintenance, exchange and extension of new points of internal telephony wire in companies and houses;

(ii) iTelefônica, provider of free internet access;

(iii) Speedy Wi-Fi, broadband service for wireless internet access;

(iv) Speedy Corp, broadband provider developed especially for the corporate market;

(v) Integrated IT solution named “Posto Informático” allowing access to Internet, connection of private networks and rental of IT equipment. Since August 2010 the service of internet access has been provided by Telefônica Brasil;

(vi) Product At-home solutions, home automation that is among the consulting services and development of automation design and installation and configuration of the solution;

(vii) Satellite TV services (Direct to Home – DTH) throughout the country and by optical fiber – IPTV (Internal Protocol Television). The DTH is a special type of subscription TV service, which uses satellites for direct distribution of TV and audio signals to subscribers.

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Telefônica Sistema de Televisão S.A.

The corporate purpose of Telefônica Sistema de Televisão S.A. ("TST") is to provide pay-TV services in the form of Multichannel Multipoint Distribution Service (MMDS), as well as telecommunication and internet-based services.

Ajato Telecomunicações Ltda.:

The corporate purpose of Ajato Telecommunications Ltd is to provide telecommunications and IT services, access to telecommunications network, internet and radio, including telemarketing, image and data services, trade lease, import, export, maintenance and repair for those equipments.

Telefônica Data S.A.

The corporate purpose of Telefônica Data S.A. is to provide and operate telecommunications services, as well as to prepare, implement and deploy projects involving integrated corporate solutions, telecommunication advisory services, technical assistance services, sale, lease and maintenance of telecommunication equipment and networks.

Aliança Atlântica Holding B.V.

Company based in Netherlands, Amsterdam, with 50% interest by Telefonica Brasil, holds cash from the sale of Portugal Telecom's shares in June 2010 and a small interest in Zon Multimedia, a company of Portugal Telecom Group which provides pay-TV services, internet, distribution of audiovisual content, cinema and telecommunications services.

Companhia AIX de Participações

This company is engaged in the Refibra consortium, as a leader, as well as in both direct and indirect development of activities related to the construction, conclusion and operation of underground fiber optic networks. Currently, Telesp holds a 50% interest in this company.

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Companhia ACT de Participações

Companhia ACT is engaged in the Refibra consortium, as a leader, as well as in activities related to providing technical assistance for the preparation of the network conclusion project by providing studies to make it more profitable, as well as to inspect the activities in progress related to the project. Currently, Telesp holds a 50% interest in this company.

GTR Participações e Empreendimentos S.A.:

The business purpose of GTR Participações e Empreendimentos S.A. is to hold equity interest in other companies, which are engaged in providing cable and pay-TV services, telecommunications services in general, the production, purchase, licencing, import and distribution of television programs – either its own or third parties', spare parts and equipment, management and exploitation of telecommunications and pay-TV service platforms.

TVA Sul Paraná S.A.:

The business purpose of TVA Sul Paraná S.A. is to provide cable and pay-tv services, telecommunications services in general, produce, purchase, licence, import and distribute television programs – either its own or third parties', spare parts and equipment, manage, update and exploit telecommunications and pay-TV service platforms and publish journals.

Lemontree Participações S.A.:

The business purpose of Lemontree S.A. is to hold equity interest in other companies, which are engaged in providing cable and pay-TV services, telecommunications services in general, the production, purchase, licencing, import and distribution of television programs – either its own or third parties', spare parts and equipments, management, updating and exploitation of telecommunications and pay-TV services plataforms, and data management and trading.

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Comercial Cabo TV São Paulo S.A.:

The business purpose of Comercial Cabo TV São Paulo S.A. is to provide cable and pay-TV services, advisory and consultancy services in telecommunications in general, to produce, purchase, licence, import and distribute television programs – either its own or third parties', spare parts and equipment, manage, update and exploit telecommunications and pay-TV service platforms, and to engage in all types of marketing and advertisement.

The table below shows the list of direct and indirect wholly-owned subsidiaries of the Company as well as the percentage ownership shareholdings:

Subsidiaries	Dec/2011	Dec/2010
Vivo S.A. (1)	100%	-
Telefônica Data S.A.	100%	100%
A.Telecom S.A.	100%	100%
Telefônica Sistema de Televisão S.A.	100%	100%
Ajato Telecomunicações Ltda.	100%	100%
GTR Participações e Empreend. S.A. (2)	66.67%	66.67%
TVA Sul Paraná S.A. (2)	91.50%	91.50%
Lemontree Participações S.A. (2)	83.00%	66.67%
Comercial Cabo TV São Paulo S.A. (2)	93.19%	86.65%
Aliança Atlântica Holding B.V.(3)	50%	50%
Companhia AIX de Participações (3)	50%	50%
Companhia ACT de Participações (3)	50%	50%

(1) fully consolidated as from April 2011 (Notes 1."e" and 4).

(2) fully consolidated as from January 2011.

(3) jointly controlled.

d) Share Trading in Stock Exchanges

d.1. *Shares traded in the São Paulo Stock Exchange (BM&FBovespa)*

On September 21, 1998, the Company started trading its shares in the São Paulo Stock Exchange (BM&FBovespa), under tickers TLPP3 and TLPP4, for common and preferred shares.

The Extraordinary Shareholders' Meetings of Vivo Participações S.A. (Vivo Part.) and Telesp held on October 3, 2011, approved the merger of Vivo Part. into Telesp, which, on the same date, changed its corporate name to Telefônica Brasil S.A. 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 for Telefônica Brasil (see note 4).

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d.2. *Shares traded in the New York Stock Exchange (NYSE)*

On November 16, 1998, the Company started the ADR trading process in the New York Stock Exchange (NYSE), which currently have the following characteristics:

- Type of share: preferred.
- Each ADR represents 1 (one) preferred share.
- The shares are traded in the form of ADRs through code "VIV" on the New York Stock Exchange.
- Foreign depositary bank: The Bank of New York.
- Custodian bank in Brazil: Banco Itaú S.A.

e) Corporate events in 2011

Merger of shares of Vivo Participações S.A. into Telefônica Brasil

In a meeting held on March 24, 2011, ANATEL gave prior consent to the Corporate restructuring operation involving the Company and Vivo Participações S.A., with Act No. 1,970, dated April 1, 2011, published in the Official Gazette on April 11, 2011.

The Company's Extraordinary Shareholders' Meeting held on April 27, 2011, unanimously approved the Protocol of Merger and Instrument of Justification agreed between the Company and Vivo Part., with each share of Vivo Part. exchanged by 1.55 shares of the Company. The Company's common and preferred shareholders and Vivo Part.'s common shareholders had until May 30, 2011 to exercise their right to withdrawal. Shareholders that could evidence shareholding on December 27, 2010, the date of publication of the Notices of Material Fact relating to the transaction, and opted for the right to withdraw were refunded for the shares they had of the respective companies. Amounts refunded to the Company's common and preferred shareholders and to Vivo Part.'s common shareholders were R$23.06 and R$25.30 per share, respectively, calculated based on the net worth value of the shares, as stated in the balance sheet of each of the companies, dated as of December 31, 2010.

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Corporate restructuring – Grouping of SMP Authorizations and Simplification of Corporate Structure

Vivo Part. Board of Director's Meeting held on June 14, 2011 approved a proposal to group the authorizations for the provision of SMP services (by the time held by Vivo Part. in the state of Minas Gerais and by Vivo S.A. in the other states of Brazil), bringing together the operations and the Authorization Terms for SMP services at Vivo S.A.

The means proposed in making this corporate restructuring viable were the transfer, on October 1, 2011, of assets, rights and liabilities related to the operation of SMP services in Minas Gerais from Vivo Part. to Vivo S.A. (mobile operator of the group that had SMP authorizations for the other states in Brazil). When this grouping was completed, Vivo Part became a holding.

In accordance with the provisions of Law No. 6,404/76, a specialized company was engaged to prepare a valuation study for the part of Vivo Part.'s net assets corresponding to SMP operations in the state of Minas Gerais that was transfered to Vivo S.A.'s equity, as well as for the net equity of Vivo Part. that was incorporated into the Company.

Due to the fact that Vivo Part. was a whole owned subsidiary of the Company, since April 27, 2011, which net equity already included the investment of the shares in Vivo S.A., the merger: i) did not result in a capital increase for the Company; ii) there was no exchange of shares held by Vivo Part. non-controlling shareholders for Company's shares; and iii) there was no need to prepare a net equity valuation report to market price for the calculation of the exchange share ratio, as there didn't exist non-controlling shareholders to be protected.

Accordingly, under the terms of article 226, paragraphs I and II of Law No. 6,404/76, shares held by the Company in the net equity value of Vivo Part. were cancelled. On conclusion of the corporate restructuring, Vivo Part. was incorporated by the Company on October 3, 2011 and Vivo S.A. became its full subsidiary, simplifying and rationalizing the cost structure of the companies envolved.

f) Agreement between Telefónica S.A. and Telecom Italia (Act No. 3,804 as of July 07, 2009 and Act No. 68,276 as of October 31, 2007, both from ANATEL's Board

In October 2007, TELCO S.p.A. (in which Telefónica S.A holds an interest of 42.3%), completed the acquisition of 23.6% of Telecom Itália. Telefónica S.A. has the control of the Company, which also has the control of Vivo S.A. Telecom Italia holds an interest in TIM Participações S.A ("TIM"), which is a mobile telephone operator in Brazil. However, the Company does not have any direct involvement in the operations of TIM. Additionally, any transactions between the Company, its subsidiaries and TIM are transactions made in the regular course of business, which are regulated by ANATEL.

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2. Basis of presentation of the financial statements

The consolidated financial statements as of December 31, 2011 and 2010 are presented by the Company in accordance with the International Financial Reporting Standards (IFRS) issued by IASB and the individual and consolidated financial statements are presented in accordance with the accounting practices adopted in Brazil, which comprise the provisions of corporate legislation set forth in Law No. 6,404/76, as amended by Law no. 11,638/07 and by Law no. 11,941/09, and the accounting pronouncements issued by the Brazilian Accounting Pronouncements Board (CPC) and approved by the CVM.

Approval of the issuance of these financial statements occurred in the Board of Directors meeting held on February 15, 2012.

The Company states that the consolidated financial statements are in compliance with International Financial Reporting Standards (IFRS) issued by the IASB and also with the pronouncements, interpretations and guidance issued by CPC in place on December 31, 2011, which include the new pronouncements, interpretations and amendments for the following standards, amendments and interpretations issued by the IASB (*International Accounting Standards Board*) and IFRIC (*International Financial Reporting Interpretations Committee*) which entered into force as from January 1, 2011:

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IAS 24 (Revised) Related Party Disclosures

This revised standard introduces the following changes: (i) provides a partial exemption for government related entities, requiring disclosure of balances and transactions between them only if they are individually or collectively significant; and (ii) provides a new revised definition of a "related party". The adoption of this standard did not impact the Company's financial situation or results.

Changes to IAS 32 Financial Instruments Presentation

This change is intended to clarify that subscription right issues that allow the acquisition of a fixed number of own equity instruments at a fixed price will be classified as equity, irrespective of currency it is denominated and its exercise price, assuming that the issuance is made to all shareholders of a given class of shares or equity proportionate to the number of securities that they hold. The adoption of these changes did not impact the Company's financial situation or results.

Improvements to International Financial Reporting Standards (IFRS) (May 2010)

This text introduces a series of improvements to IFRS in force mainly to eliminate inconsistencies and clarify the wording of some of these standards. These improvements did not impact the Company's financial situation or results.

IFRS 3 Business Combinations

The measurement options available for non-controlling interest (NCI) were amended. Only components of NCI that constitute a present ownership interest that entitles their holder to a proportionate share of the entity's net assets in the event of liquidation should be measured at either fair value or at the present ownership instruments' proportionate share of the acquiree's identifiable net assets. All other components are to be measured at their acquisition date fair value.

The amendments to IFRS 3 are effective for annual periods beginning on or after 1 July 1, 2011.

IFRIC 19 Extinguishing financial liabilities with equity instruments

This interpretation establishes that: (i) when the conditions of a financial obligation are renegotiated with a lender and such lender agrees to accept equity instruments from that company in order to settle that financial liability in full or in part the instruments issued will be considered as part of an installment paid to settle the financial liability; (ii) these instruments will be measured at their fair value, except when these cannot be reliably measured, in which case measurement of new instruments should reflect the fair value of the settled financial liability; and (iii) the difference between the book value of the cancelled financial liability and the initial amount of equity instruments issued is recorded in the income for the period. The adoption of criteria introduced by this new interpretation did not have any impact on the Company's financial situation or results.

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Changes to IFRIC 14 Prepayments of a Minimum Funding Requirement

This change is applied in specific situations when an entity has an obligation to make minimum annual contributions in relation to its post-employment defined benefits plans and makes prepayments to cover these requirements. The change allows an entity to treat the economic benefits of such prepayment as an asset. The adoption of these criteria did not have an impact on the Company's financial situation or results.

New IFRS and Interpretations of the IFRS Interpretations Committee (IFRIC) not yet effective at December 31, 2011.

At the date of these financial statements the following IFRS, amendments and interpretations of the IFRIC have been issued but their application was not mandatory:

Standards and Amendments to Standards		**Application required: fiscal years beginning as from**
Amendments to IAS 1	*Presentation of items of other comprehensive income*	July 1, 2012
Amendments to IAS 12	*Deferred tax: Recovery of underlying assets*	January 1, 2012
IFRS 9	*Financial instruments*	January 1, 2013
IFRS 10	*Consolidated Financial Statements*	January 1, 2013
IFRS 11	*Joint Arrangements*	January 1, 2013
IFRS 12	*Disclosure of Interests in Other Entities*	January 1, 2013
IFRS 13	*Fair Value Measurement*	January 1, 2013
IAS 19 revised	*Employee Benefits*	January 1, 2013
IAS 27 revised	*Consolidated and Separate Financial Statements*	January 1, 2013
IAS 28 revised	*Investments in Associates and jointly controlled companies*	January 1, 2013
Amendments to IFRS 7	*Disclosure – transfers of financial assets*	July 1 , 2011

Amendments to IFRS 7	*Disclosure – offsetting of financial assets and financial liabilities*	January 1, 2013
Amendments to IAS 32	Offsetting Financial Assets and Financial Liabilities	January 1, 2014

The Company is currently analyzing the impact of the application of these standards, amendments and interpretations. Based on preliminary analysis made up to the present date the Company estimates that their application will not have a significant impact on the consolidated financial statements on first time adoption. Notwithstanding, changes introduced by IFRS 9 will affect the presentation of financial assets and transactions with those occurring as from January 1, 2015.

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2.1 Basis of consolidation and main changes in the consolidation environment

In consolidation all assets, liabilities, revenue and expenses resulting from intercompany transactions and equity holding between the Company and its subsidiaries were eliminated.

The main events and changes in the consolidation environment that, due to their significance, should be considered for analysis of the consolidated financial statements for the fiscal year ended December 31, 2011, are presented as follows:

a) Acquisition of Vivo Participações S.A. by the Company

As mentioned in Note 4, the Company incorporated 100% of shares of Vivo Participações S.A. amounting to R$31,222,630 (Note 1."e" and 4). The Company's consolidated financial statements include Vivo Part. (incorporated by the Company on October 3, 2011) and Vivo S.A. results from April 1, 2011. Vivo Participações S.A. and Vivo S.A. were included in the Company's consolidated financial statements through the full consolidation method.

b) Consolidation of TVA companies

As from January 1, 2011, the Company started to include the companies GTR Participações e Empreendimentos S.A., TVA Sul Paraná S.A., Lemontree Participações S.A. and Comercial Cabo TV São Paulo S.A. in its consolidated financial statements by applying the full consolidation method. Up to the prior year these companies were included in the Company's consolidated financial statements through the equity method. The effect of the consolidation of these companies is immaterial in relation to the Company's consolidated financial statements.

c) Acquisition of Lemontree Participações S.A. shares

On September 29, 2011, the Company purchased 68,533,233 common shares representing 49% of the referred class of shares in Lemontree Participações S.A., which is the holder of 80.1% of the common shares of Comercial Cabo TV São Paulo S.A., a company engaged in cable TV services in the State of São Paulo. As a consequence, the Company currently has an interest of 83% in Lemontree Partipações S.A. and 93.19% in Comercial Cabo TV São Paulo S.A. This transaction was considered as a non-controlling shareholders' acquistion for the purpose of disclosure and measurement in these financial statements.

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3. Summary of principal accounting practices

a) Trade accounts receivable, net: are stated at the rendered service value according to the contracted conditions adjusted by the estimated amount of eventual losses. This caption also includes accounts receivable from services rendered but not yet billed at the balance sheet date, as well as the accounts receivable related to the sales of handsets, simcards and accessories. Allowance for doubtful account is recorded in order to cover eventual losses and mainly considers expected losses.

b) Inventories: are stated at average acquisition cost, net of allowance for reduction to net realizable value. This corresponds to items for use, maintenance or resale.

c) Prepaid expenses: are measured at the amounts effectively disbursed related to services paid for but not yet incurred. The prepaid expenses are recognized in the statement of income when the related services and the economic benefits are obtained.

d) Investments: equity interests in subsidiaries and jointly controlled companies are stated by the equity method in the individual financial statements. In the consolidated financial statements, investments in subsidiaries are fully consolidated and investments in jointly controlled subsidiaries are consolidated proportionally.

In consolidation, all assets, liabilities, revenues and expenses resulting from intercompany transactions and equity holdings between the Company and its subsidiaries were eliminated.

The exchange rate variation on the shareholders' equity of the jointly controlled Aliança Atlântica is recognized in the shareholders' equity as cumulative translation adjustments.

e) Property, plant and equipment: this item is measured at acquisition and/or construction cost, less accumulated depreciation and any impairment losses, if applicable. Such cost includes the borrowing costs for long-term construction projects if the recognition criteria are met. Asset costs are capitalized until the asset becomes operational.

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Costs incurred after the asset becomes operational are immediately expensed, under the accrual method of accounting. Expenses that represent asset improvement (expanded installed capacity or useful life) are capitalized.

The estimated costs to be incurred in the dismantling of towers and equipment in rented real property are capitalized with a corresponding provision for dismantling of fixed assets and are depreciated over the useful life of the equipment, which does not exceed the lease term.

An item of property, plant and equipment is derecognized upon disposal or when no future economic benefit is 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 statement of income when the asset is derecognized.

Depreciation is calculated under the straight-line method based on the estimated useful lives of the assets, which is based on technical studies that are regularly reviewed (see Note 13 – Property, plant and equipment, net).

f) Intangible assets (including goodwill): these are stated at acquisition and/or construction cost, less accumulated amortization and any impairment losses, if applicable.

Intangible assets also includes software rights of use acquired from third parties, authorization licenses obtained from ANATEL, customer lists, brands, premium amounts referring to own stores (which are being amortized over the term of the agreements) and other intangible assets.

The useful life of intangible assets is assessed as either finite or indefinite.

Intangible assets with finite lives are amortized under the straight-line method over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for intangible assets with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or in the expected pattern of consumption of future economic benefits embodied in these assets are accounted for by changing the amortization period or method, as appropriate, and treated as changes in accounting estimates. Intangible assets with indefinite useful lives are not amortized, but are tested for impairment annually or when there is an indication that the carrying amount of the assets may not be recoverable. The assessment of indefinite useful life is reviewed annually to determine whether indefinite life continues to be supportable. Otherwise, the change in the useful life from indefinite to finite is made on a prospective basis.

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Gains or 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. Gains and losses are recognized in the statement of income when the asset is derecognized.

Goodwill arising from the acquisition of investments are based on future profits and are treated as intangible assets with indefinite useful lives.

g) Leases: agreements providing for use of specific assets and the right to use an asset are subject to analysis so as to identify the accounting treatment applicable to lease arrangements. Agreements in which the lessor substantially transfers the underlying risks and benefits to the lessee are classified as finance lease.

The Company has agreements classified as finance lease from both the lessor's and lessee's standpoint. As a lessor, subsidiary A.Telecom has equipment lease agreements (Posto Informático), for which it recognizes revenue on the installation date at the present value of the agreement installments, matched against Accounts Receivable. As a lessee in agreements classified as finance lease, the Company records a fixed asset item, classified according to its nature, at the beginning of the lease term, at the present value of the agreement minimum mandatory installments matched against Other Liabilities. The difference between the nominal value of the installments and the accounts receivable/payable recorded is recognized as financial income/expense under the effective interest rate method based on the contract term.

Agreements in which the lessor retains a substantial part of risks and benefits are deemed as operating lease, and their effects are recognized in the income statement for the year throughout the contractual term.

h) Asset recoverability analysis: in compliance with IAS 36/CPC 1 (R1), the Company and its subsidiaries review the net book value of assets, when circumstances indicate it is necessary, in order to assess if there are events or changes in the economic, operating or technological circumstances which may indicate asset impairment or loss in its carrying amount.

If such evidences are identified and the net book value exceeds the recoverable amount, an impairment provision is recorded, adjusting the net book value to the recoverable amount.

The recoverable amount is defined as the higher of the value in use and the fair value less cost to sell.

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In estimating the value in use of an asset, the estimated future cash flows are discounted to their present value using a pre-tax cost of capital - "CAPM - Capital Asset Pricing Model" discount rate, which reflects the weighted average cost of capital and the specific risks of the asset.

The fair value less cost to sell is determined, whenever possible, on firm sale agreement in a transaction on an arm’s length basis, between knowledgeable and willing parties, adjusted by expenses attributable to the sale of the asset, or, when no firm sale agreement exists, based on the market price of an active market, or on the price of the most recent transaction with similar assets.

Losses from continuous operations, including inventory write-off, are recognized in the statement of income in expense accounts compatible with asset purpose.

For assets, excluding goodwill, an analysis is performed on the closing date of each fiscal year, to identify if there is an indication that the impairment previously recognized may no longer exist or may have decreased.

An impairment loss previously recorded is reversed only if there is a change in the assumptions used to determine the asset recoverable value as from the time of recognition of the last impairment.

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

The following criteria are applied to assess the impairment of specific assets:

h.1) *Goodwill*

Goodwill is tested for impairment annually and when circumstances indicate that the carrying amount may be impaired.

When the recoverable amount is lower than its book value, impairment is recognized. Goodwill impairment cannot be reversed in future fiscal years.

h.2) *Intangible assets*

Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash-generating unit level, as appropriate, and when circumstances indicate that the carrying amount may be impaired.

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h.3) *Value in use*

The main assumptions used to estimate the value in use are:

- Revenue: The revenues are estimated considering the growth of the customer base, the evolution of the market income vis-à-vis the GDP – Gross Domestic Product and the Company and its subsidiary's share in this market;

- Operating costs and expenses: The variable costs and expenses were estimated according to the dynamic of the customer base, and the fixed costs and expenses were projected in line with the historical performance of the Company and its subsidiaries, as well as with the historical growth of the revenue; and

- Capex: Capital expenditures are estimated based on the technological infrastructure required to make feasible the offering of services.

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

The impairment tests of the Company and its subsidiaries fixed and intangible assets did not result in the recognition of losses for the years ended December 31, 2011 and 2010, since their estimated market value exceeded their net book value on the assessment date.

i) Business combinations and goodwill**:** Business combinations are accounted for using the acquisition method. The acquisition cost is measured at the fair value of assets, equity instruments and liabilities incurred or assumed at the acquisition date. Identifiable assets acquired and liabilities and contingencies assumed in a business combination are initially measured at fair value on the acquisition date, regardless of the non-controlling shareholders interest (Note 4).

Initially, goodwill represents the excess of the cost of acquisition over the net fair value of the acquired assets, assumed liabilities and identifiable contingent liabilities from an acquired company, on the respective acquisition date. If the acquisition cost is lower than the fair value of the acquired company's net assets, the difference is recognized directly in the income statement

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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 unit that is expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the acquiree are assigned to each unit.

When goodwill forms part of a cash-generating unit and part of the operation within that unit is disposed of, the goodwill associated with the operation disposed of is included in the carrying amount of the operation when determining the gain or loss on disposal. Goodwill disposed of in this circumstance is measured based on the relative values of the operation disposed of and the portion of the cash-generating unit retained.

j) Financial Instruments, cash and cash equivalents

Initial recognition and subsequent measurement

(i) *Cash and cash equivalent*

Includes cash, credit balances in bank accounts and investments redeemable within 90 days of the date of acquisition with immediate liquidity and with insignificant change in market value.

(ii) *Financial Assets*

Initial recognition and measurement

Financial assets are classified as financial assets at fair value through profit or loss, loans and receivables, investments held to maturity, available for sale financial assets or as derivatives, designated as hedging instruments in an effective hedge as appropriate. The Company determines the classification of its financial assets upon their initial recognition, when they become part of the contractual provisions of the instrument.

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

Sales and purchases of financial assets that require delivery of goods within a time frame established by regulation or market convention (regular way trades) are recognized on the transaction date, i.e. the date that the Company commits to buy or sell the asset.

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The Company's financial assets include cash and cash equivalents, trade accounts receivable and other receivables quoted and unquoted financial instruments and derivative financial instruments.

Subsequent measurement

Subsequent measurement of financial assets depends on their classification as follows:

Financial assets at fair value through profit or loss

This category includes derivative financial instruments entered into by the Company that do not meet the hedge accounting criteria as defined by the corresponding standard. Financial assets at fair value through profit or loss are presented in the balance sheet at fair value, with corresponding gains or losses recognized in the income statement.

Receivables

Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. After initial measurement, such assets are carried at amortized cost using the effective interest rate method, less impairment, if and when applicable. Amortized cost is calculated by taking into account any discount or premium in the acquisition and fees or other costs incurred. Amortization under the effective interest method is included in financial income in the income statement. The losses arising from impairment are recognized as financial expense in the income statement, if and when applicable.

Held-to-maturity investments

Non-derivative financial assets with fixed or determinable payments and fixed maturity are classified as held-to-maturity when the Company has the positive intention and financial capacity to hold them to maturity. After initial measurement, held-to-maturity investments are measured at amortized cost using the effective interest rate method, less impairment. Amortized cost is calculated taking into consideration any discount or premium on acquisition and fees or costs incurred. Amortization of effective interest rate is included in financial income in the income statement. Impairment losses are recognized as financial costs in the income statement. The Company did not have any held-to-maturity investments during the years ended December 31, 2011 and 2010.

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Available for sale financial assets

Available for sale financial assets are those non-derivative financial assets that are not classified as (a) loans and receivables, (b) held to maturity investments or (c) financial assets at fair value through profit or loss. These financial assets include equity instruments.

After initial measurement, available for sale financial assets are measured at fair value with unrealized gains or losses recognized directly in the available for sale reserve within the group of other comprehensive income until the investment is derecognized, excepted situation of impairment losses.

When the investment is derecognized or when impairment is detected, the cumulative gains or losses previously recognized in other comprehensive income should be recognized in the statement of income.

The fair value of available for sale financial assets in foreign currency is measured and translated into foreign currency using the spot exchange rate prevailing at the date of the financial statements. The changes in fair value attributable to translation differences are recognized directly in equity.

Derecognition

A financial asset (or, where appropriate, a part of a financial asset or part of a group of similar financial assets) is derecognized when:

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

- The Company transferred its rights to receive cash flows from the asset or has assumed an obligation to pay the cash flows received in full, without significant delay to a third party under a pass-through agreement, and (a) the Company has transferred substantially all risks and rewards of the asset, or (b) the Company has neither transferred nor retained substantially all risks and rewards related to the asset, but has transferred control of the asset.

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