OI S.A.
Form 20-F
April 27, 2012
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As filed with the Securities and Exchange Commission on April 27, 2012

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 20-F

¨ **REGISTRATION STATEMENT PURSUANT TO SECTION 12(b) OR 12(g) OF THE SECURITIES EXCHANGE ACT OF 1934**
OR

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
FOR THE FISCAL YEAR ENDED DECEMBER 31, 2011

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
OR

¨ **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
Commission file number: 001-15256

OI S.A.

(formerly known as Brasil Telecom S.A.)

(Exact Name of Registrant as Specified in Its Charter)

N/A	**The Federative Republic of Brazil**
(Translation of Registrant s Name into English)	**(Jurisdiction of Incorporation or Organization)**

Rua General Polidoro, No. 99, 5th floor/part Botafogo

22280-001 Rio de Janeiro, RJ, Brazil

(Address of Principal Executive Offices)

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(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

Securities registered or to be registered pursuant to section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on which Registered
Common Shares, without par value, each represented by American Depositary Shares	New York Stock Exchange
Preferred Shares, without par value, each represented by American Depositary Shares	New York Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act: None

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: None

The total number of issued shares of each class of stock of Brasil Telecom S.A. as of December 31, 2011 was:

203,423,176 common shares, without par value

399,597,370 preferred shares, without par value

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes x No ¨

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ¨ No x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statements included in this filing:

U.S. GAAP ¨ International Financial Reporting Standards as issued by the International Accounting Standards Board x Other ¨

If Other has been checked in response to the previous question, indicate by check mark which financial statement item the registrant has elected to follow. ¨ Item 17 ¨ Item 18

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

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PRESENTATION OF FINANCIAL AND OTHER INFORMATION

All references herein to *real*, *reais* or R$ are to the Brazilian *real*, the official currency of Brazil. All references to U.S. dollars, dollars or U
are to U.S. dollars.

On April 25, 2012, the exchange rate for *reais* into U.S. dollars was R$1.8807 to US$1.00, based on the selling rate as reported by the Central Bank of Brazil (*Banco Central do Brasil*), or the Central Bank. The selling rate was R$1.876 to US$1.00 at December 31, 2011, R$1.666 to US$1.00 at December 31, 2010, and R$1.741 to US$1.00 at December 31, 2009, in each case, as reported by the Central Bank. The *real*/U.S. dollar exchange rate fluctuates widely, and the selling rate at April 25, 2012 may not be indicative of future exchange rates. See Item 3. Key Information Exchange Rates for information regarding exchange rates for the *real* since January 1, 2007.

Solely for the convenience of the reader, we have translated some amounts included in Item 3. Key Information Selected Financial Information and in this annual report from *reais* into U.S. dollars using the selling rate as reported by the Central Bank at December 31, 2011 of R$1.876 to US$1.00. These translations should not be considered representations that any such amounts have been, could have been or could be converted into U.S. dollars at that or at any other exchange rate.

Financial Statements

We maintain our books and records in *reais*. We prepare our consolidated financial statements in accordance with International Financial Reporting Standards, or IFRS, as issued by the International Accounting Standards Board, or the IASB. Our consolidated financial statements at December 31, 2011 and 2010 and for the three years ended December 31, 2011 have been audited, as stated in the report appearing herein, and are included in this annual report.

Until December 31, 2009, we prepared our consolidated financial statements in accordance with accounting practices adopted in Brazil in effect on and prior to December 31, 2009, or Prior Brazilian GAAP, which were based on:

- Brazilian Law No. 6,404/76, as amended by Brazilian Law No. 9,457/97, Brazilian Law No. 10,303/01, and Brazilian Law No. 11,638/07, which we refer to collectively as the Brazilian Corporation Law;

- the rules and regulations of the Brazilian Securities Commission (*Comissão de Valores Mobiliários*), or the CVM, the accounting standards issued by the Brazilian Institute of Independent Accountants (*Instituto dos Auditores Independentes do Brasil*), or Ibracon, and the Brazilian Federal Accounting Council (*Conselho Federal de Contabilidade*), or CFC; and

- the accounting standards issued by the Brazilian Accounting Standards Committee (*Comitê de Pronunciamentos Contábeis*), or the CPC, and applicable on and prior to December 31, 2009.

In preparing our consolidated financial statements as of and for the two years ended December 31, 2010, the comparative figures in respect of 2009 have been restated to reflect the effects of the transition from Prior Brazilian GAAP to IFRS.

We also prepare individual financial statements in accordance with accounting practices adopted in Brazil, or Brazilian GAAP, which include the pronouncements issued by the CPC applicable to dates and periods ended after December 31, 2009, for certain purposes, including for the calculation of dividends.

Corporate Reorganization

On February 27, 2012, Tele Norte Leste Participações S.A., or TNL, Telemar Norte Leste S.A., a subsidiary of TNL, or Telemar, Coari Participações S.A., a wholly owned subsidiary of Telemar, or Coari, and Brasil Telecom S.A., a subsidiary of Coari, undertook a corporate reorganization in which:

Telemar and Coari engaged in a split-off (*cisão*) and merger of shares (*incorporação de ações*) under Brazilian law in which (1) Telemar transferred the shares of Coari that it owned to Coari, (2) Coari assumed a portion of the liabilities of Telemar, (3) the common and preferred shares of Telemar were exchanged for newly issued common and preferred shares of Coari, and (4) Telemar became a wholly-owned subsidiary of Coari;

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- Coari and Brasil Telecom engaged in a merger (*incorporação*) under Brazilian law in which Coari merged with and into Brasil Telecom;

- TNL and Brasil Telecom engaged in a merger (*incorporação*) under Brazilian law in which TNL merged with and into Brasil Telecom; and

- the corporate name of Brasil Telecom was changed to Oi S.A., or Oi.

We refer to these transactions collectively as the corporate reorganization.

The following chart sets forth the ownership structure of TNL, Telemar and Coari in Brasil Telecom immediately prior to the corporate reorganization. The percentages in bold italics represent the percentage of the voting capital owned by the parent company of each entity, and the percentages not in bold italics represent the percentage of the total share capital owned by the parent company of each entity.

The following chart sets forth the structure of Brasil Telecom and Telemar immediately following the corporate reorganization.

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As a result of the corporate reorganization, we have consolidated the results of TNL into results as from February 28, 2012. The historical financial statements of our company will not be restated to account for the impacts of the corporate reorganization on a retroactive basis. For more details regarding the corporate reorganization, see Item 4. Information on the Company Our History and Development Corporate Reorganization of TNL, Telemar and Our Company.

Information regarding Oi in this annual report is presented giving effect to the corporate reorganization on February 27, 2012. However, financial and other data included in this annual report regarding Oi and its consolidated subsidiaries as of December 31, 2011 and earlier dates and for periods ended on December 31, 2011 and earlier dates is historical in nature and does not give pro forma effect to the corporate reorganization, except as otherwise noted.

In addition, financial and other data included in this annual report regarding TNL and its consolidated subsidiaries as of December 31, 2011 and earlier dates and for periods ended on December 31, 2011 and earlier dates is historical in nature and includes financial and other data regarding Brasil Telecom, a subsidiary of TNL prior to February 27, 2012. The financial statements of TNL as of and for the year ended December 31, 2011 have not been presented elsewhere in this annual report and have not been filed with the SEC.

Unless otherwise indicated or the context otherwise requires:

- all references to our company, we, our, ours, us or similar terms are to Oi S.A. and its consolidated subsidiaries with respect to current information and information as of and for periods ended after February 27, 2012 and to Brasil Telecom S.A. and its consolidated subsidiaries with respect to information as of and for periods ended on or prior to February 27, 2012;
- all references to Oi or Brasil Telecom are to Oi S.A. (formerly known as Brasil Telecom S.A.);
- all references to TmarPart are to Telemar Participações S.A., the direct controlling shareholder of Oi;
- all references to TNL are to Tele Norte Leste Participações S.A., a company that was directly controlled by TmarPart prior to its merger with and into Oi on February 27, 2012 as part of the corporate reorganization;
- all references to Telemar are to Telemar Norte Leste S.A., a company that was directly controlled by TNL prior to the corporate reorganization and which became a wholly-owned subsidiary of Oi on February 27, 2012 as part of the corporate reorganization;
- all references to Coari are to Coari Participações S.A., a company that was wholly-owned by Telemar prior to its merger with and into Oi on February 27, 2012 as part of the corporate reorganization;
- all references to our Common ADSs are to American Depositary Shares, or ADSs, each representing one common share of our company, all references to our Preferred ADSs are to ADSs, each representing three preferred shares of our company, and all references to our ADSs are to our Common ADSs and Preferred ADSs;
- all references to Brazil are to the Federative Republic of Brazil; and
- all references to the Brazilian government are to the federal government of the Federative Republic of Brazil.

Share Split

On April 10, 2007, we authorized the reverse split of all of our issued common shares and preferred shares into one share for each 1,000 issued shares. This reverse share split became effective on May 14, 2007. In connection with this reverse share split, we authorized a change in the ratio of our Preferred ADS. Upon the effectiveness of our reverse share split and the ratio change, the ratio of our preferred shares to our Preferred ADSs, changed from 3,000 preferred shares per Preferred ADS to three preferred shares per Preferred ADS. All references to numbers of shares and dividend amounts in this annual report have been adjusted to give effect to the 1,000-for-one reverse share split.

Market Share and Other Information

We make statements in this annual report about our market share and other information relating to the telecommunications industry in Brazil. We have made these statements on the basis of information obtained from third-party sources and publicly available information that we believe are reliable, such as information and reports from the Brazilian federal telecommunications regulator (*Agência Nacional de Telecomunicações*), or ANATEL, among others. Notwithstanding any investigation that we may have conducted with respect to the market share, market size or similar data provided by third parties or derived from industry or general publications, we assume no responsibility for the accuracy or completeness of any such information.

Rounding

We have made rounding adjustments to reach some of the figures included in this annual report. As a result, numerical figures shown as totals in some tables may not be arithmetic aggregations of the figures that precede them.

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CAUTIONARY STATEMENT WITH RESPECT TO FORWARD-LOOKING STATEMENTS

This annual report contains forward-looking statements. Some of the matters discussed concerning our business operations and financial performance include forward-looking statements within the meaning of the U.S. Securities Act of 1933, as amended, or the Securities Act, or the U.S. Securities Exchange Act of 1934, as amended, or the Exchange Act.

Statements that are predictive in nature, that depend upon or refer to future events or conditions or that include words such as expects, anticipates, intends, plans, believes, estimates and similar expressions are forward-looking statements. Although we believe that these forward-looking statements are based upon reasonable assumptions, these statements are subject to several risks and uncertainties and are made in light of information currently available to us.

Our forward-looking statements may be influenced by factors, including the following:

- competition in the Brazilian telecommunications sector;
- our management s current expectations and estimates concerning our future financial performance, financing plans and programs;
- the Brazilian government s telecommunications policies that affect the telecommunications industry and our business in general, including issues relating to the remuneration for the use of our network, and changes in or developments of ANATEL regulations applicable to us;
- the cost and availability of financing;
- the general level of demand for, and changes in the market prices of, our services;
- our ability to implement our corporate strategies in order to increase our average revenue per user;
- political, regulatory and economic conditions in Brazil and the specific Brazilian states in which we operate;
- inflation and fluctuations in exchange rates;
- legal and administrative proceedings to which we are or become a party; and
- other factors identified or discussed under Item 3. Key Information Risk Factors.

Our forward-looking statements are not guarantees of future performance, and our actual results or other developments may differ materially from the expectations expressed in the forward-looking statements. As for forward-looking statements that relate to future financial results and other projections, actual results will be different due to the inherent uncertainty of estimates, forecasts and projections. Because of these uncertainties, potential investors should not rely on these forward-looking statements.

We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future events or otherwise.

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PART I

ITEM 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3. KEY INFORMATION

Selected Financial Information

The following selected financial data should be read in conjunction with the consolidated financial statements of Oi (including the notes thereto), Item 5. Operating and Financial Review and Prospects and Presentation of Financial and Other Information.

The selected financial data as of December 31, 2011 and 2010 and for the three years ended December 31, 2011 have been derived from the consolidated financial statements of Oi, prepared in accordance with IFRS, and included in this annual report. The selected financial data as of December 31, 2009 have been derived from the consolidated financial statements of Oi, prepared in accordance with IFRS, which is not included in this annual report.

The consolidated financial statements as of and for the years ended December 31, 2010 and 2009 were our first annual consolidated financial statements to be prepared in accordance with IFRS. Therefore, we are only presenting information related to the years ended December 31, 2011, 2010 and 2009.

We have included information with respect to the dividends and/or interest attributable to shareholders equity paid to holders of our common shares and preferred shares since January 1, 2006 in *reais* and in U.S. dollars translated from *reais* at the commercial market selling rate in effect as of the payment date under the caption Item 8. Financial Information Dividends and Dividend Policy Payment of Dividends. We prepare individual financial statements in accordance with Brazilian GAAP for certain purposes, including for the calculation of dividends.

	At and For the Year Ended December 31,			
	2011(1)	**2011**	**2010**	**2009**
	(in millions of US$, except per share amounts)	**(in millions of *reais*, except per share amounts and as otherwise indicated)**		
Income Statement Data:				
Net operating revenue	US$ 4,928	R$ 9,245	R$ 10,263	R$ 10,919
Cost of sales and services	(2,445)	(4,587)	(4,732)	(5,764)
Gross profit	2,483	4,659	5,531	5,155
Operating expenses	(1,648)	(3,091)	(3,072)	(6,232)
Operating income (loss) before financial income (expenses) and taxes	835	1,567	2,459	(1,077)
Financial income	749	1,406	979	630
Financial expenses	(788)	(1,478)	(1,060)	(912)

Financial expenses, net		(38)		(72)		(80)		(281)
Income (loss) before taxes		797		1,495		2,379		(1,358)
Income tax and social contribution		(261)		(490)		(408)		339
Net income (loss)	US$	536	R$	1,006	R$	1,971	R$	(1,019)
Net income (loss) attributable to controlling shareholders	US$	536	R$	1,006	R$	1,971	R$	(1,021)

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	At and For the Year Ended December 31,			
	2011(1)	2011	2010	2009
	(in millions of US$, except per share amounts)	(in millions of *reais*, except per share amounts and as otherwise indicated)		
Net income (loss) attributable to non-controlling shareholders				2
Net income (loss) applicable to each class of shares:				
Common shares	185	347	680	(1,021)
Preferred shares	351	659	1,291	
Net income (loss) per share(2):				
Common shares basic	0.91	1.71	3.34	(1.85)
Common shares diluted	0.91	1.71	3.34	(1.85)
Preferred shares and ADSs basic	0.91	1.71	3.34	
Preferred shares and ADSs diluted	0.91	1.71	3.34	
Weighted average shares outstanding (in thousands):				
Common shares basic		203,423	203,423	245,749
Common shares diluted		203,423	203,423	245,749
Preferred shares basic		386,366	386,366	305,439
Preferred shares diluted		386,388	386,366	305,439
Balance Sheet Data:				
Cash and cash equivalents	US$ 3,201	R$ 6,005	R$ 3,217	R$ 1,717
Cash investments	578	1,084	832	382
Trade accounts receivable, net	1,071	2,010	2,070	1,992
Total current assets	6,528	12,246	8,487	6,127
Property, plant and equipment, net	3,088	5,794	5,317	5,267
Intangible assets, net	579	1,086	1,318	1,572
Total assets	16,878	31,664	26,886	24,564
Short-term loans and financing (including current portion of long-term debt)	610	1,144	1,044	870
Total current liabilities	4,594	8,619	6,691	5,424
Long-term loans and financing	3,711	6,962	3,321	3,573
Share capital	1,989	3,731	3,731	3,731
Total equity	5,645	10,589	11,337	9,906
Shareholders equity attributable to controlling shareholders	5,645	10,589	11,337	9,905
Shareholders equity attributable to non-controlling shareholders				1

(1) Translated for convenience only using the selling rate as reported by the Central Bank at December 31, 2011 for *reais* into U.S. dollars of R$1.876=US$1.00.

(2) Under the Brazilian Corporation Law, preferred shareholders are not obligated to absorb losses, and such losses are exclusively attributed to common shareholders.

Exchange Rates

The Brazilian foreign exchange system allows the purchase and sale of foreign currency and the international transfer of *reais* by any person or legal entity, regardless of the amount, subject to certain regulatory procedures.

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Since 1999, the Central Bank has allowed the U.S. dollar-*real* exchange rate to float freely, and, since then, the U.S. dollar-*real* exchange rate has fluctuated considerably.

In the past, the Central Bank has intervened occasionally to control unstable movements in foreign exchange rates. We cannot predict whether the Central Bank or the Brazilian government will continue to permit the *real* to float freely or will intervene in the exchange rate market through the return of a currency band system or otherwise. The *real* may depreciate or appreciate against the U.S. dollar and/or the euro substantially. Furthermore, Brazilian law provides that, whenever there is a significant imbalance in Brazil s balance of payments or there are serious reasons to foresee a significant imbalance, temporary restrictions may be imposed on remittances of foreign capital abroad. We cannot assure you that such measures will not be taken by the Brazilian government in the future. See Risk Factors Risks Relating to Brazil Restrictions on the movement of capital out of Brazil may impair our ability to service certain debt obligations.

The following table shows the commercial selling rate or selling rate, as applicable, for U.S. dollars for the periods and dates indicated. The information in the Average column represents the average of the exchange rates on the last day of each month during the periods presented.

	***Reais* per U.S. Dollar**			
Year	**High**	**Low**	**Average**	**Period End**
2007	2.156	1.733	1.930	1.771
2008	2.500	1.559	1.834	2.337
2009	2.422	1.702	1.994	1.741
2010	1.881	1.655	1.759	1.666
2011	1.902	1.535	1.671	1.876

	***Reais* per U.S. Dollar**	
Month	**High**	**Low**
October 2011	R$ 1.866	R$ 1.689
November 2011	1.894	1.727
December 2011	1.876	1.783
January 2012	1.868	1.739
February 2012	1.738	1.702
March 2012	1.833	1.715
April 2012 (through April 25)	1.887	1.826

Source: Central Bank

Risk Factors

You should consider the following risks as well as the other information set forth in this annual report when evaluating an investment in our company. In general, investing in the securities of issuers in emerging market countries, such as Brazil, involves a higher degree of risk than investing in the securities of issuers in the United States. Additional risks and uncertainties not currently known to us, or those that we currently deem to be immaterial, may also materially and adversely affect our business, results of operations, financial condition and prospects. Any of the following risks could materially affect us. In such case, you may lose all or part of your original investment.

Risks Relating to the Brazilian Telecommunications Industry and Our Company

Our fixed-line telecommunication services face increased competition from mobile services providers, other fixed-line service providers and cable television service providers, which may adversely affect our revenues and margins.

Our fixed-line telecommunication services in Region I (which consists of 16 Brazil states located in the northeastern and part of the northern and southeastern regions) and Region II (which consists of the Federal District and nine Brazilian states located in the western, central and southern regions) face increasing competition from

mobile services as the prices for mobile services decline and approach those of fixed-line services. Based on information available from ANATEL, from December 31, 2008 to December 31, 2011, the number of fixed lines in service in Brazil increased from 43.0 million to 41.2 million as a result of the increase in the number of fixed lines in service in Region III (which consists of the state of São Paulo) while the number of fixed lines in service in Regions I and II declined. We expect (1) the number of fixed lines in service in Regions I and II to continue to stagnate or decline, as certain customers eliminate their fixed-line services in favor of mobile services, and (2) the use of existing fixed lines to decline as customers substitute calls on mobile phones in place of fixed-line calls as a result of promotional mobile rates (such as free calls within a mobile provider s network). The rate at which the number of fixed lines in service in Brazil may decline depends on many factors beyond our control, such as economic, social, technological and other developments in Brazil. In addition, new fixed lines that we install are expected to be less profitable than existing ones because new fixed-line customers generally have lower average incomes than our existing customers, subscribe to our lower cost service plans and generate fewer chargeable minutes of usage. For the year ended December 31, 2011, our traditional local fixed-line telecommunication services represented 35.6% of our gross operating revenue and the traditional local fixed-line telecommunication services of TNL represented 34.5% of its consolidated gross operating revenue. Because we derive a significant portion of our net operating revenue from our traditional local fixed-line telecommunication services, the reduction in the number of our fixed-lines in service has negatively affected and is likely to continue to negatively affect our net operating revenue and margins.

We also compete in the market for local fixed-line services with other fixed-line service providers, primarily with Empresa Brasileira de Telecomunicações Embratel, or Embratel, and GVT S.A., or GVT. In addition to direct competition for corporate customers in Region I, Embratel competes with us for residential customers in Regions I and II with services that it provides using the cable infrastructure of its subsidiary, Net Serviços de Comunicação S.A., or Net. Net is a cable television company that is our main competitor in the broadband services market. Embratel and Net are affiliates of Teléfonos de México S.A.B. de C.V., or Telmex, one of the leading telecommunication service providers in Latin America. Under an agreement entered into between Embratel and Net in November 2005, Net offers integrated voice, broadband and pay television services to the Brazilian residential market through a single network infrastructure. In addition, we compete in each of these service regions with smaller companies that have been authorized by ANATEL to provide local fixed-line services. Embratel, GVT and Net are each controlled by multinational companies that may have more significant financial and marketing resources, and greater abilities to access capital on a timely basis and on more favorable terms, than our company.

Our loss of a significant number of fixed-line customers would adversely affect our net operating revenue and may adversely affect our results of operations. In addition, because callers in Brazil placing long-distance calls from their fixed-line telephones generally tend to select the long-distance carrier affiliated with the provider of their fixed-line service, our loss of a significant number of fixed-line customers may adversely affect our revenues from long-distance services and our results of operations. For a detailed description of our competition in the local fixed-line services market, see Item 4. Information on the Company Competition Local Fixed-Line Services.

Our mobile services face strong competition from other mobile services providers, which may adversely affect our revenues.

The mobile services market in Brazil is extremely competitive. We face competition from large competitors such as Vivo Participações S.A., or Vivo, Telecom Americas Group, which markets its services under the brand name Claro, and TIM Participações S.A., or TIM. As of December 31, 2011, based on information regarding the total number of subscribers as of that date available from ANATEL:

- we had an estimated 14.2% share of the mobile services market in Region II, while Vivo, Claro and TIM had estimated market shares of 30.8%, 28.6% and 26.3%, respectively;

- TNL had an estimated 23.2% share of the mobile services market in Region I, while Vivo, Claro and TIM had estimated market shares of 27.2%, 22.5% and 26.7%, respectively; and

- TNL had an estimated 14.5% share of the mobile services market in Region III, while Vivo, Claro and TIM had estimated market shares of 33.0%, 26.1% and 26.3%, respectively.

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Vivo, TIM and Telecom Americas Group are each controlled by multinational companies that may have more significant financial and marketing resources, and greater abilities to access capital on a timely basis and on more favorable terms, than our company.

Our ability to generate revenues from our mobile services business depends on our ability to increase and retain our customer base. Each additional customer subscribing to our service entails costs, including sales commissions and marketing costs. Recovering these costs depends on our ability to retain such customers. Therefore, high rates of customer churn could have a material adverse effect on the profitability of our mobile services business. During 2011, our average customer churn rate in the mobile services segment, representing the number of subscribers whose service was disconnected during each month, whether voluntarily or involuntarily, divided by the number of subscribers at the beginning of such month, was 4.9% per month, and TNL s average customer churn rate in the mobile services segment was 3.1% per month in Region I and 4.1% per month in Region III.

We have experienced increased pressure to reduce our rates in response to pricing competition. This pricing competition often takes the form of special promotional packages, which may include, among other things, mobile handset subsidies, traffic usage promotions and incentives for calls made within a mobile services provider s own network. Competing with the service plans and promotions offered by our competitors may cause an increase in our marketing expenses and customer-acquisition costs, which has adversely affected and could continue to adversely affect our results of operations. Our inability to compete effectively with these packages could result in our loss of market share and adversely affect our net operating revenue and profitability. For a detailed description of our competition in the mobile services market, see Item 4. Information on the Company Competition Mobile Services.

Our long-distance services face significant competition, which may adversely affect our revenues.

In Brazil, unlike in the United States and elsewhere, a caller chooses its preferred long-distance carrier for each long-distance call, whether originated from a fixed-line telephone or a mobile handset, by dialing such carrier s long-distance carrier selection code (*Código de Seleção de Prestadora*). The long-distance services market in Brazil is highly competitive. Our principal competitor for long-distance services is TIM, which in 2010 began aggressively promoting its long-distance services with significant discounts. Historically, our principal competitors for long-distance services have been Embratel, Telecomunicações de São Paulo S.A., or Telesp (the parent company of Vivo), which is the incumbent fixed-line service provider in Region III, and TIM. Generally, callers placing long-distance calls in Brazil from their fixed-line telephones tend to select the long-distance carrier affiliated with the provider of their fixed-line service. Similarly, callers placing long-distance calls in Brazil from their mobile handsets tend to select the long-distance carrier affiliated with the provider of their mobile or fixed-line service. However, increased competition from long-distance service providers has resulted in pressure on our long-distance rates and adversely affected our revenue from these services. In addition, aggressive discounting by TIM during 2010 and 2011 has substantially reduced the market share of our company and other service providers in the long-distance market. Competition in the long-distance market may require us to increase our marketing expenses and/or provide services at lower rates than those we currently expect to charge for such services. Competition in the domestic long-distance market has had and could continue to have a material adverse effect on our revenues and margins. See Item 4. Information on the Company Competition Long-Distance Services.

Data transmission services are not subject to significant regulatory restrictions and, as a result, we face an increasing amount of competition in this business.

Competition in data transmission services is not subject to significant regulatory restrictions and, therefore, the market is open to a large number of competitors. Some competitors, such as cable operators, offer telephone and broadband services, which do not require them to use our fixed-line network, thereby allowing them to reach our customers without paying interconnection fees to our company. Increasing competition in data transmission services may lead to rate reductions in this segment, adversely affecting the net operating revenue that we generate from this business. Additionally, increased competition for data transmission customers may require us to increase our marketing expenses and our capital expenditures and may lead to the loss of broadband customers, in each case leading to a decrease in our profitability. For a detailed description of our competition in the data transmission services market, see Item 4. Information on the Company Competition Data Transmission Services.

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The telecommunications industry is subject to frequent changes in technology. Our ability to remain competitive depends on our ability to implement new technology, and it is difficult to predict how new technology will affect our business.

Companies in the telecommunications industry must adapt to rapid and significant technological changes that are usually difficult to anticipate. The mobile telecommunications industry in particular has experienced rapid and significant technological development and frequent improvements in capacity, quality and data-transmission speed. Technological changes may render our equipment, services and technology obsolete or inefficient, which may adversely affect our competitiveness or require us to increase our capital expenditures in order to maintain our competitive position. For example, we and TNL have made significant investments in the last three years in connection with the implementation of our Universal Mobile Telecommunications System services, which we refer to as 3G services. While we have been upgrading our fixed-line networks with technologically advanced fiber optic cable with a microwave overlay for use in our long-distance services, it is possible that alternative technologies may be developed that are more advanced than those we currently provide. Even if we adopt new technologies in a timely manner as they are developed, the cost of such technology may exceed the benefit to us, and we cannot assure you that we will be able to maintain our level of competitiveness.

Our industry is highly regulated. Changes in laws and regulations may adversely impact our business.

Our industry is highly regulated by ANATEL. ANATEL regulates, among other things, rates, quality of service and universal service goals, as well as competition among telecommunication service providers. Changes in laws and regulations, grants of new concessions, authorizations or licenses or the imposition of additional universal service obligations, among other factors, may adversely affect our business, financial condition and results of operations.

In October 2008, ANATEL published items that were on its regulatory agenda, some of which are expected to be adopted in the following years. In furtherance of ANATEL s regulatory agenda:

- ANATEL has proposed a General Plan on Competition Targets (*Plano Geral de Metas de Competição*), which contemplates the creation of three entities to manage information about telecommunications networks, act as an intermediary in contracts between telecommunications providers and supervise the offering of wholesale and retail data traffic services. The proposed General Plan on Competition Targets also addresses a variety of other matters, including criteria for the evaluation of telecommunications providers to determine which providers have significant market power, regulations applicable to the wholesale markets for trunk lines, backhaul, access to internet backbone and interconnection services, and regulations related to partial unbundling and/or full unbundling of the local fixed-line networks of the public regime service providers. The General Plan on Competition Targets was submitted for public consultation in July 2011 and the public consultation period ended on October 23, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012.

- ANATEL has proposed new regulations under which it would modify the Factor X applicable to the determination of rate increases available to public concessionaires providing fixed-line services. These regulations were submitted for public consultation in July 2011 and the public consultation period ended on September 1, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012.

We cannot predict when regulations regarding these matters will be adopted or whether these regulations will be adopted as proposed. Some of these regulations, if adopted, may have adverse effects on our revenues, costs and expenses, results of operations or financial position.

We cannot predict whether ANATEL, the Brazilian Ministry of Communications (*Ministério das Comunicações*) or the Brazilian government will adopt other telecommunications sector policies in the future or the consequences of such policies on our business and the business of our competitors.

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Proposed laws seeking the termination of monthly subscription fees for local fixed-line services may adversely affect our business and financial condition.

Certain legislative bills seeking to terminate monthly subscription fees charged by local fixed-line service providers have been submitted to the Brazilian Congress and remain pending. In March 2008, a special committee was formed in the Brazilian House of Representatives to discuss the various proposed bills on this issue. As of the date of this annual report, no action had been taken by the committee.

During 2011, monthly subscription fees represented 23.4% of our gross operating revenue and 23.2% of TNL s gross operating revenue on a consolidated basis. The enactment of legislation terminating the monthly subscription fees would have a material adverse effect on our results of operations.

Our local fixed-line and domestic long-distance concession agreements are subject to periodic modifications by ANATEL and expire on December 31, 2025. Our bids for new concessions upon the expiration of our existing concessions may not be successful.

We provide fixed-line telecommunication services in Regions I and II pursuant to concession agreements with the Brazilian government. Our concession agreements expire on December 31, 2025, and may be amended by the parties every five years prior to the expiration date. In connection with each five year amendment, ANATEL has the right, following public consultations, to impose new terms and conditions in response to changes in technology, competition in the marketplace and domestic and international economic conditions.

Our obligations under the concession agreements may be subject to revision in connection with each future amendment. We cannot assure you that any future amendments will not impose requirements on our company that will require us to undertake significant capital expenditures or will not modify the rate-setting procedures applicable to us in a manner that will significantly reduce the net operating revenue that we generate from our fixed-line businesses. If the amendments to our concession agreements have these effects, our business, financial condition and results of operations could be materially adversely affected.

Our concession agreements will expire on December 31, 2025. We expect the Brazilian government to offer new concessions in competitive auctions prior to the expiration of our existing concession agreements. We may participate in such auctions, but our existing fixed-line and domestic long-distance concession agreements will not entitle us to preferential treatment in these auctions. If we do not secure concessions for our existing service areas in any future auctions, or if such concessions are on less favorable terms than our current concessions, our business, financial condition and results of operations would be materially adversely affected.

Our local fixed-line and domestic long-distance concession agreements, as well as our authorizations to provide personal mobile services, contain certain obligations, and our failure to comply with these obligations may result in various fines and penalties imposed on us by ANATEL.

Our local fixed-line and domestic long-distance concession agreements contain terms reflecting the General Plan on Universal Service (*Plano Geral de Metas de Universalização*), the General Plan on Quality Goals (*Plano Geral de Metas de Qualidade*) and other regulations adopted by ANATEL, the terms of which could affect our financial condition and results of operations. Our local fixed-line concession agreements also require us to meet certain network expansion, quality of service and modernization obligations in each of the states in Regions I and II. In the event of noncompliance with ANATEL targets in any one of these states, ANATEL can establish a deadline for achieving the targeted level of such service, impose penalties and, in extreme situations, terminate the applicable concession agreement for noncompliance with its quality and universal service obligations. See Item 4. Information on the Company Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services.

On an almost weekly basis, we receive inquiries from ANATEL requiring information from us on our compliance with the various service obligations imposed on us by our concession agreements. If we are unable to respond satisfactorily to those inquiries or comply with our service obligations under our concession agreements, ANATEL may commence administrative proceedings in connection with such noncompliance. We have received numerous notices of the commencement of administrative proceedings from ANATEL, mostly due to our inability to achieve certain targets established in the General Plan on Quality Goals and the General Plan on Universal Service, among others. As of December 31, 2011, we had recorded provisions in the amount of R$278 million in connection with fines sought to be imposed by ANATEL and TNL had recorded provisions in the amount of R$941 million on a consolidated basis. Additional fines from ANATEL or fines in excess of the provisioned amount could adversely impact our financial condition and results of operations. See Item 4. Information on the Company Regulation of the Brazilian Telecommunications Industry and Item 8. Financial Information Legal Proceedings Civil Claims Administrative Proceedings.

In addition, our authorizations to provide personal mobile services contain certain obligations requiring us to meet network scope and quality of service targets. If we fail to meet these obligations, we may be fined by ANATEL until we are in full compliance with our obligations and, in extreme circumstances, our authorizations could be revoked by ANATEL. See Item 4. Information on the Company Regulation of the Brazilian Telecommunications Industry Regulation of Mobile Services Obligations of Personal Mobile Services Providers.

We may be unable to implement our plans to expand and enhance our existing networks in a timely manner or without unanticipated costs, which could hinder or prevent the successful implementation of our business plan and result in revenues and net income being less than expected.

Our ability to achieve our strategic objectives depends in large part on the successful, timely and cost-effective implementation of our plans to expand and enhance our networks. Factors that could affect this implementation include:

- our ability to generate cash flow or to obtain future financing necessary to implement our projects;
- delays in the delivery of telecommunications equipment by our vendors;
- the failure of the telecommunications equipment supplied by our vendors to comply with the expected capabilities; and
- delays resulting from the failure of third-party suppliers or contractors to meet their obligations in a timely and cost-effective manner.

Although we believe that our cost estimates and implementation schedule are reasonable, we cannot assure you that the actual costs or time required to complete the implementation of these projects will not substantially exceed our current estimates. Any significant cost overrun or delay could hinder or prevent the successful implementation of our business plan and result in revenues and net income being less than expected.

We rely on strategic suppliers of equipment, materials and services necessary for our operations and expansion. If these suppliers fail to provide equipment, materials or services to us on a timely basis, we could experience disruptions, which could have an adverse effect on our revenues and results of operations.

We rely on few strategic suppliers of equipment, materials and services, including Nokia Siemens Networks Serviços Ltda., or Nokia Siemens Networks, Alcatel-Lucent Brasil S.A., or Alcatel-Lucent, Telemont Engenharia de Telecomunicações S.A., or Telemont, A.R.M. Engenharia Ltda., or A.R.M. Engenharia, and Huawei do Brasil Telecomunicações Ltda., or Huawei, to provide us with equipment, materials and services that we need in order to expand and to operate our business. There are a limited number of suppliers with the capability of providing the mobile network equipment and fixed-line network platforms that our operations and expansion plans require or the services that we require to maintain our extensive and geographically widespread networks. In addition, because the supply of mobile network equipment and fixed-line network platforms requires detailed supply planning and this equipment is technologically complex, it would be difficult for our company to replace the suppliers of this equipment. Suppliers of cables that we need to extend and maintain our networks may suffer capacity constraints or difficulties in obtaining the raw materials required to manufacture these cables. As a result, we are exposed to risks associated with these suppliers, including restrictions of production capacity for equipment and materials, availability of equipment and materials, delays in delivery of equipment, materials or services, and price increases.

If these suppliers or vendors fail to provide equipment, materials or service to us on a timely basis or otherwise in compliance with the terms of our contracts with these suppliers, we could experience disruptions or declines in the quality of our services, which could have an adverse effect on our revenues and results of operations, and we might be unable to satisfy the requirements contained in our concession and authorization agreements.

Our controlling shareholder, TmarPart, has control over us and TmarPart s interests may not be aligned with your interests.

We are controlled by TmarPart which, as of April 25, 2012 directly and indirectly held 56.4% of our outstanding voting shares. TmarPart s shareholders are parties to four shareholders agreements governing their equity interests in TmarPart. See Item 7. Major Shareholders and Related Party Transactions Major Shareholders TmarPart Shareholders Agreements. TmarPart is entitled to appoint a majority of the members of our board of directors, and it has the power to determine the decisions to be taken at our shareholders meetings on matters of our management that require the prior authorization of our shareholders, including in respect of related party transactions, corporate restructurings and the date of payment of dividends and other capital distributions. The decisions of TmarPart on these matters may be contrary to the expectations or preferences of holders of our securities, including holders of our common shares, preferred shares and ADSs.

In order to expand our business, we may take advantage of the consolidation of the telecommunications industry through the acquisition of other telecommunications companies, which could adversely affect our business, results of operations and financial condition.

We may acquire other companies in the telecommunications industry as part of our growth and convergence strategy. A growth strategy that involves acquisitions may present certain risks to our business, results of operations and financial condition, such as:

- difficulties in capturing synergies in the integration process, causing the anticipated benefits of the acquisition to be more limited than originally expected;
- costs associated with any unforeseen antitrust restrictions;
- failure to identify contingencies during the due diligence process;
- uncertainty in relation to regulatory approval; and
- distractions from our core business to pursue these acquisitions and implement the integration of acquired businesses.

If acquisition transactions cause us to incur unforeseen costs due to the factors described above, we may have to dedicate more resources than we had originally planned and eventually face substantial losses that would adversely affect our business, results of operations and financial condition.

Even if we identify suitable acquisition targets, we may be unable to complete acquisitions or obtain necessary financing to do so on satisfactory terms. Paying for acquisitions could require us to incur or assume debt and/or contingent liabilities, amortize certain identifiable intangible assets and incur acquisition-related expenses. In addition, we may be unable to realize all or any of the anticipated benefits from acquisitions or expansion in other related businesses because of operational factors or difficulties in integrating the acquisitions or such other related businesses with our existing businesses, including disparate information technology systems, database systems and business processes.

We have a substantial amount of existing debt, which could restrict our financing and operating flexibility and have other adverse consequences.

At December 31, 2011, we had total consolidated debt of R$8,105 million and a ratio of debt to equity of 0.8:1, and TNL had total consolidated debt of R$29,768 million and a ratio of debt to equity of 1.2:1.

We are subject to certain financial covenants that limit our ability to incur additional debt. Our existing level of indebtedness and the requirements and limitations imposed by our debt instruments could adversely affect our financial condition or results of operations. In particular, the terms of some of these debt instruments restrict our ability, and the ability of our subsidiaries, to:

- incur additional debt;
- grant liens;
- pledge assets;
- sell or dispose of assets; and
- make certain acquisitions, mergers and consolidations.

Furthermore, some of our debt instruments include financial covenants that require us to maintain certain specified financial ratios. Additionally, the instruments governing a substantial portion of our indebtedness contain cross-default or cross-acceleration clauses and the occurrence of an event of default under one of these instruments could trigger an event of default under other indebtedness or enable the creditors under other indebtedness to accelerate that indebtedness.

If we are unable to incur additional debt, we may be unable to invest in our business and make necessary or advisable capital expenditures, which could reduce future net operating revenue and adversely affect our profitability. In addition, cash required to serve our existing indebtedness reduces the amount available to us to make capital expenditures.

If our growth in net operating revenue slows or declines in a significant manner, for any reason, we may not be able to continue servicing our debt. If we are unable to meet our debt service obligations or comply with our debt covenants, we could be forced to renegotiate or refinance our indebtedness, seek additional equity capital or sell assets. We may be unable to obtain financing or sell assets on satisfactory terms, or at all. For more information regarding the debt instruments of our company and TNL and our indebtedness as of December 31, 2011, see Item 5. Operating and Financial Review and Prospects Liquidity and Capital Resources.

We are subject to numerous legal and administrative proceedings, which could adversely affect our business, results of operations and financial condition.

We are subject to numerous legal and administrative proceedings. It is difficult to quantify the potential impact of these legal and administrative proceedings. We classify our risk of loss from legal and administrative proceedings as probable, possible or remote. We make provisions for probable losses but do not make provisions for possible and remote losses. As of December 31, 2011, we had provisioned R$4,415 million for probable losses relating to various tax, labor and civil legal and administrative proceedings against us, and TNL had provisioned R$6,895 million on a consolidated basis for probable losses relating to various tax, labor and civil legal and administrative proceedings against TNL and its subsidiaries, including our company.

As of December 31, 2011, we had claims against us of R$2,969 million in tax proceedings, R$923 million in labor proceedings and R$648 million in civil proceedings with a risk of loss classified as possible for which we had made no provisions, and TNL had claims against it on a consolidated basis of R$18,252 million in tax proceedings, R$1,262 million in labor proceedings and R$1,262 million in civil proceedings with a risk of loss classified as possible for which TNL had made no provisions.

If we are subject to unfavorable decisions in any legal or administrative proceedings and the losses in those proceedings significantly exceed the amount for which we have provisioned or involve proceedings for which we have made no provision, our results of operations and financial condition may be materially adversely affected. For a more detailed description of these proceedings, see Item 8. Financial Information Legal Proceedings.

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We are subject to potential liabilities relating to our third-party service providers, which could have a material adverse effect on our business, financial condition and results of operations.

We are subject to potential liabilities relating to our third-party service providers. Such potential liabilities may involve claims by employees of third-party service providers directly against us as if we were the direct employer of such employees, as well as claims against us for secondary liability for, among other things, occupational hazards, wage parity or overtime pay, in the event that such third-party service providers fail to meet their obligations to their employees. We have not recorded any provisions for such claims, and significant judgments against us could have a material adverse effect on our business, financial condition and results of operations.

We are subject to delinquencies of our accounts receivables. If we are unable to limit payment delinquencies by our customers, or if delinquent payments by our customers increase, our financial condition and results of operations could be adversely affected.

Our business significantly depends on our customers ability to pay their bills and comply with their obligations to us. During 2011, we recorded provisions for doubtful accounts in the amount of R$333 million and TNL recorded provisions for doubtful accounts in the amount of R$921 million on a consolidated basis, primarily due to subscribers delinquencies. As of December 31, 2011, our provision for doubtful accounts as a percentage of our gross operating revenue was 2.0% and TNL s provision for doubtful accounts as a percentage of its consolidated gross operating revenue was 2.1%.

ANATEL regulations prevent us from implementing certain policies that could have the effect of reducing delinquency, such as service restrictions or limitations on the types of services provided based on a subscriber s credit record. If we are unable to successfully implement policies to limit subscriber delinquencies or otherwise select our customers based on their credit records, persistent subscriber delinquencies and bad debt will continue to adversely affect our operating and financial results.

In addition, if the Brazilian economy declines due to, among other factors, a reduction in the level of economic activity, depreciation of the *real*, an increase in inflation or an increase in domestic interest rates, a greater portion of our customers may not be able to pay their bills on a timely basis, which would increase our provision for doubtful accounts and adversely affect our financial condition and results of operations.

Our operations depend on our ability to maintain, upgrade and operate efficiently our accounting, billing, customer service, information technology and management information systems and to rely on the systems of other carriers under co-billing agreements.

Sophisticated information and processing systems are vital to our growth and our ability to monitor costs, render monthly invoices for services, process customer orders, provide customer service and achieve operating efficiencies. We cannot assure you that we will be able to operate successfully and upgrade our accounting, information and processing systems or that these systems will continue to perform as expected. We have entered into co-billing agreements with each long-distance telecommunication service provider that is interconnected to our networks to include in our invoices the long-distance services rendered by these providers, and they have agreed to include charges owed to us in their invoices. Any failure in our accounting, information and processing systems, or any problems with the execution of invoicing and collection services by other carriers with whom we have co-billing agreements, could impair our ability to collect payments from customers and respond satisfactorily to customer needs, which could adversely affect our business, financial condition and results of operations.

Improper use of our network could adversely affect our costs and results of operations.

We incur costs associated with the unauthorized and fraudulent use of our networks, including administrative and capital costs associated with detecting, monitoring and reducing the incidence of fraud. Fraud also affects interconnection costs and payments to other carriers for non-billable fraudulent roaming. Improper use of our network could also increase our selling expenses if we need to increase our provision for doubtful accounts to reflect amounts we do not believe we can collect for improperly made calls. Any increase in the improper use of our network in the future could materially adversely affect our costs and results of operations.

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Our operations are dependent upon our networks. A system failure could cause delays or interruptions of service, which could cause us to suffer losses.

Damage to our networks and backup mechanisms may result in service delays or interruptions and limit our ability to provide customers with reliable service over our networks. Some of the risks to our networks and infrastructure include (1) physical damage to access lines; (2) power surges or outages; (3) software defects; (4) disruptions beyond our control; (5) breaches of security; and (6) natural disasters. The occurrence of any such event could cause interruptions in service or reduce capacity for customers, either of which could reduce our gross operating revenue or cause us to incur additional expenses. In addition, the occurrence of any such event may subject us to penalties and other sanctions imposed by ANATEL and may adversely affect our business and results of operations.

The mobile telecommunications industry and participants in this industry, including us, may be harmed by reports suggesting that radio frequency emissions cause health problems and interfere with medical devices.

Media and other entities frequently suggest that the electromagnetic emissions from mobile handsets and base stations may cause health problems. If consumers harbor health-related concerns, they may be discouraged from using mobile handsets. These concerns could have an adverse effect on the mobile telecommunications industry and, possibly, expose mobile services providers to litigation. We cannot assure you that further medical research and studies will refute a link between the electromagnetic emissions of mobile handsets and base stations, including on frequency ranges we use to provide mobile services, and these health concerns. Government authorities could increase regulation on electromagnetic emissions of mobile handsets and base stations, which could have an adverse effect on our business, financial condition and results of operations. The expansion of our network may be affected by these perceived risks if we experience problems in finding new sites, which in turn may delay the expansion and may affect the quality of our services. In July 2002, ANATEL enacted regulations that limit emission and exposure for fields with frequencies between 9 kHz and 300 GHz. Although these regulations did not have a material impact on our business, new laws or regulations regarding electromagnetic emissions and exposure may be adopted that could have an adverse effect on our business.

Risks Relating to Brazil

The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. This involvement, as well as Brazilian political and economic conditions, could adversely impact our business, results of operations and financial condition.

All of our operations and customers are located in Brazil, except for minor operations and the customers of these operations provided outside of Brazil. Accordingly, our financial condition and results of operations are substantially dependent on Brazil s economy. The Brazilian government frequently intervenes in the Brazilian economy and occasionally makes significant changes in policy and regulations. The Brazilian government s actions to control inflation and implement macroeconomic policies have often involved increases in interest rates, wage and price controls, currency devaluations, blocking access to bank accounts, imposing capital controls and limits on imports, among other things. We do not have any control over, and are unable to predict, which measures or policies the Brazilian government may adopt in the future. Our business, results of operations and financial condition may be adversely affected by changes in policies or regulations, or by other factors such as:

- political instability;
- devaluations and other currency fluctuations;
- inflation;
- price instability;
- interest rates;

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- liquidity of domestic capital and lending markets;
- energy shortages;
- exchange controls;
- changes to the regulatory framework governing our industry;
- monetary policy;
- tax policy; and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Uncertainty over whether possible changes in policies or rules affecting these or other factors may contribute to economic uncertainties in Brazil and to heightened volatility in the Brazilian securities markets and securities issued abroad by Brazilian issuers. The President of Brazil has considerable power to determine governmental policies and actions that relate to the Brazilian economy and, consequently, affect the operations and financial performance of businesses such as our company. Although we do not believe that Ms. Rousseff will significantly alter current governmental policies, we can offer no assurances that the policies that may be implemented by the Brazilian federal or state governments will not adversely affect our business, results of operations and financial condition.

Instability in the international financial system may adversely affect economic growth in Brazil or limit our access to the financial markets and, therefore, negatively impact our business and financial condition.

The global economic downturn and related instability in the international financial system have had, and may continue to have, a negative effect on economic growth in Brazil. The global economy began to recover from these conditions toward the end of 2009, however, such recovery depends on a number of factors, including a return of job growth and investments in the private sector as well as the timing of the exit from government credit easing policies by central banks globally. In addition, global investor confidence remains cautious and recent downgrades of the sovereign debt of Ireland, Greece, Portugal, Italy, Spain and France have caused renewed volatility in the capital markets. A continued or worsening disruption and volatility in the global financial markets could reduce the availability of liquidity and credit to fund the continuation and expansion of industrial business operations worldwide. A prolonged slowdown in economic activity in Brazil could reduce demand for some of our services, which would adversely affect our results of operations.

As a result of instability in the international financial system, our ability to access the capital markets or the commercial bank lending markets may be severely restricted at a time when we would like, or need, to access such markets, which could have an impact on our flexibility to react to changing economic and business conditions. The instability in the international financial system or a prolonged slowdown in economic activity in Brazil could have an impact on the lenders under our existing credit facilities, on our customers or on the ability of our suppliers to meet scheduled deliveries, causing them to fail to meet their obligations to us. If the instability in the international financial system continues, it could have an adverse effect on the demand for our services and our ability to fund our planned growth.

Depreciation of the real may lead to substantial losses on our liabilities denominated in or indexed to foreign currencies.

During the four decades prior to 1999, the Central Bank periodically devalued the Brazilian currency. Throughout this period, the Brazilian government implemented various economic plans and used various exchange rate policies, including sudden devaluations (such as daily and monthly adjustments), exchange controls, dual exchange rate markets and a floating exchange rate system. Since 1999, exchange rates have been set by the market. The exchange rate between the *real* and the U.S. dollar has varied significantly in recent years. For example, the *real*/U.S. dollar exchange rate increased from R$1.955 per U.S. dollar on December 31, 2000 to R$3.533 on December 31, 2002. The *real* appreciated against the U.S. dollar by 11.8% in 2005, 8.7% in 2006 and 17.1% in

2007. In 2008, primarily as a result of the international financial crisis, the *real* depreciated by 31.9% against the U.S. dollar and prompted foreign investors to remove billions of *reais* from the Brazilian Securities, Commodities and Futures Exchange (*BM&FBOVESPA S.A. - Bolsa de Valores Mercadorias e Futuros*), which we refer to as the BM&FBOVESPA. The *real* appreciated against the U.S. dollar by 25.5% during 2009 and by 4.3% during 2010. The *real* depreciated by 12.6% against the U.S. dollar during 2011.

A significant amount of our financial liabilities are denominated in or indexed to foreign currencies, primarily U.S. dollars, Japanese yen and euros. As of December 31, 2011, R$1 million of our financial indebtedness, was denominated in a foreign currency, and R$8,648 million, or 29.0% of TNL s financial indebtedness on a consolidated basis, was denominated in a foreign currency. When the *real* depreciates against foreign currencies, we incur losses on our liabilities denominated in or indexed to foreign currencies, such as our U.S. dollar-denominated long-term debt and foreign currency loans, and we incur gains on our monetary assets denominated in or indexed to foreign currencies, as the liabilities and assets are translated into *reais*. If significant depreciation of the *real* were to occur when the value of such liabilities significantly exceeds the value of such assets, including any financial instruments entered into for hedging purposes, we could incur significant losses, even if the value of those assets and liabilities has not changed in their original currency. In addition, a significant depreciation in the *real* could adversely affect our ability to meet certain of our payment obligations. A failure to meet certain of our payment obligations could trigger a default under certain financial covenants in our debt instruments, which could have a material adverse effect on our business and results of operations. Additionally, we currently have currency swaps and non-deliverable forwards in place for a portion of our foreign currency debt. If the cost of currency swap instruments increases substantially, we may be unable to maintain our hedge positions, resulting in an increased foreign currency exposure which could in turn lead to substantial foreign exchange losses.

In addition, a portion of our capital expenditures require us to acquire assets at prices denominated in or linked to foreign currencies, some of which are financed by liabilities denominated in foreign currencies, principally the U.S. dollar. We generally do not hedge against risks related to movements of the *real* against foreign currencies. To the extent that the value of the *real* decreases relative to the U.S. dollar, it becomes more costly for us to purchase these assets, which could adversely affect our business and financial performance.

Depreciation of the *real* relative to the U.S. dollar could create additional inflationary pressures in Brazil by increasing the price of imported products and requiring recessionary government policies, including tighter monetary policy. On the other hand, appreciation of the *real* against the U.S. dollar may lead to a deterioration of the country s current account and balance of payments, as well as to a dampening of export-driven growth.

If Brazil experiences substantial inflation in the future, our margins and our ability to access foreign financial markets may be reduced. Government measures to curb inflation may have adverse effects on the Brazilian economy, the Brazilian securities market and our business and results of operations.

Brazil has, in the past, experienced extremely high rates of inflation, with annual rates of inflation reaching as high as 2,708% in 1993 and 1,093% in 1994. Inflation and some of the Brazilian government s measures taken in an attempt to curb inflation have had significant negative effects on the Brazilian economy.

Since the introduction of the *real* in 1994, Brazil s inflation rate has been substantially lower than in previous periods. However, actions taken in an effort to control inflation, coupled with speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities market. More recently, Brazil s rates of inflation, as measured by the General Market Price Index Internal Availability (*Índice Geral de Preços Disponibilidade Interna*), or IGP-DI, published by Fundação Getúlio Vargas, or FGV, were 7.9% in 2007, 9.1% in 2008, (1.4)% in 2009, 11.3% in 2010 and 5.0% in 2011. According to the Broad Consumer Price Index (*Índice Nacional de Preços ao Consumidor Ampliado*), or IPCA, published by the Brazilian Institute for Geography and Statistics (*Instituto Brasileiro de Geografia e Estatística*), or IBGE, the Brazilian consumer price inflation rates were 4.5% in 2007, 5.9% in 2008, 4.3% in 2009, 5.9% in 2010 and 6.5% in 2011.

If Brazil experiences substantial inflation in the future, our costs may increase and our operating and net margins may decrease. Although ANATEL regulations provide for annual price increases for most of our services, such increases are linked to inflation indices, discounted by increases in our productivity. During periods of rapid increases in inflation, the price increases for our services may not be sufficient to cover our additional costs and we may be adversely affected by the lag in time between the incurrence of increased costs and the receipt of revenues resulting from the annual price increases. Inflationary pressures may also curtail our ability to access foreign financial markets and may lead to further government intervention in the economy, including the introduction of government policies that may adversely affect the overall performance of the Brazilian economy.

Fluctuations in interest rates could increase the cost of servicing our debt and negatively affect our overall financial performance.

Our financial expenses are affected by changes in the interest rates that apply to our floating rate debt. As of December 31, 2011, we had, among other debt obligations, R$2,124 million of loans and financing and debentures that were subject to the *Taxa de Juros de Longo Prazo*, or TJLP, a long-term interest rate, R$4,109 million of loans and financing and debentures that were subject to the Interbank Certificate of Deposit (*Certificado de Depósito Interbancário*), or CDI, rate, an interbank rate, and R$535 million of loans and financing that were subject to the IPCA. As of December 31, 2011, TNL had on a consolidated basis, among other debt obligations, R$11,103 million of loans and financing and debentures that were subject to the CDI rate, R$5,937 million of loans and financing and debentures that were subject to the TJLP, R$1,984 million of loans and financing that were subject to the IPCA, and R$3,298 million of loans and financing that were subject to the London Interbank Offered Rate, or LIBOR.

The TJLP includes an inflation factor and is determined quarterly by the National Monetary Council (*Conselho Monetário Nacional*). In particular, the TJLP and the CDI rate have fluctuated significantly in the past in response to the expansion or contraction of the Brazilian economy, inflation, Brazilian government policies and other factors. For example, the CDI from 8.55% per annum as of December 31, 2009 to 10.64% per annum as of December 31, 2010 and increased to 10.87% per annum as of December 31, 2011. A significant increase in any of these interest rates, particularly the CDI rate, could adversely affect our financial expenses and negatively affect our overall financial performance.

The market value of securities issued by Brazilian companies is influenced by the perception of risk in Brazil and other countries, which may have a negative effect on the trading price of our common shares, preferred shares and ADSs and may restrict our access to international capital markets.

Economic and market conditions in other countries, including the United States, the European Union and emerging market countries, may affect to varying degrees the market value of securities of Brazilian issuers. Although economic conditions in these countries may differ significantly from economic conditions in Brazil, investors reactions to developments in these other countries may have an adverse effect on the market value of securities of Brazilian issuers, the availability of credit in Brazil and the amount of foreign investment in Brazil. Crises in the European Union, the United States and emerging market countries may diminish investor interest in securities of Brazilian issuers, including our company. This could materially and adversely affect the market price of our securities, and could also make it more difficult for us to access the capital markets and finance our operations in the future on acceptable terms or at all.

Restrictions on the movement of capital out of Brazil may impair our ability to service certain debt obligations.

Brazilian law provides that whenever there exists, or there is a serious risk of, a material imbalance in Brazil s balance of payments, the Brazilian government may impose restrictions for a limited period of time on the remittance to foreign investors of the proceeds of their investments in Brazil as well as on the conversion of the *real* into foreign currencies. The Brazilian government imposed such a restriction on remittances for approximately six months in 1989 and early 1990. The Brazilian government may in the future restrict companies from paying amounts denominated in foreign currency or require that any such payment be made in *reais*. Many factors could affect the likelihood of the Brazilian government imposing such exchange control restrictions, including the extent of Brazil s foreign currency reserves, the availability of sufficient foreign exchange on the date a payment is due, the size of Brazil s debt service burden relative to the economy as a whole, and political constraints to which Brazil may be subject. There can be no certainty that the Brazilian government will not take such measures in the future.

A more restrictive policy could increase the cost of servicing, and thereby reduce our ability to pay, our foreign currency-denominated debt obligations and other liabilities. As of December 31, 2011, our foreign-currency denominated debt represented was R$1 million, and TNL s foreign-currency denominated debt represented 29.0% of its indebtedness on a consolidated basis. If we fail to make payments under any of these obligations, we will be in default under those obligations, which could reduce our liquidity as well as the market price of our common shares, preferred shares and ADSs.

In addition, a more restrictive policy could hinder or prevent the Brazilian custodian of the common shares and preferred shares underlying our ADSs or holders who have exchanged our ADSs for the underlying common shares or preferred shares from converting dividends, distributions or the proceeds from any sale of such shares into U.S. dollars and remitting such U.S. dollars abroad. In such an event, the Brazilian custodian for our common shares and preferred shares will hold the *reais* that it cannot convert for the account of holders of our ADSs who have not been paid. Neither the custodian nor The Bank of New York Mellon, as depositary of our ADS programs, or the depositary, will be required to invest the *reais* or be liable for any interest.

Risks Relating to Our Common Shares, Preferred Shares and ADSs

Holders of our common shares, preferred shares or ADSs may not receive any dividends or interest on shareholders equity.

According to our by-laws, we must generally pay our shareholders at least 25% of our annual net income as dividends or interest on shareholders equity, as calculated and adjusted under Brazilian GAAP. This adjusted net income may be capitalized, used to absorb losses or otherwise retained as allowed under Brazilian GAAP and may not be available to be paid as dividends or interest on shareholders equity. Holders of our common shares or Common ADSs, may not receive any dividends or interest on shareholders equity in any given year due to the dividend preference of our preferred shares. Additionally, the Brazilian Corporation Law allows a publicly traded company like ours to suspend the mandatory distribution of dividends in any particular year if our board of directors informs our shareholders that such distributions would be inadvisable in view of our financial condition or cash availability. Holders of our preferred shares or Preferred ADSs may not receive any dividends or interest on shareholders equity in any given year if our board of directors makes such a determination or if our operations fail to generate net income.

Our preferred shares and Preferred ADSs have limited voting rights and are not entitled to vote to approve corporate transactions, including mergers or consolidations of our company with other companies, or the declaration of dividends.

Under the Brazilian Corporation Law and our by-laws, holders of our preferred shares and, consequently, our Preferred ADSs, are not entitled to vote at meetings of our shareholders, except in very limited circumstances. These limited circumstances directly relate to key rights of the holders of preferred shares, such as modifying basic terms of our preferred shares or creating a new class of preferred shares with superior rights. Holders of preferred shares without voting rights are entitled to elect one member and his or her respective alternate to our board of directors and our fiscal council. Holders of our preferred shares and Preferred ADSs are not entitled to vote to approve corporate transactions, including mergers or consolidations of our company with other companies, or the declaration of dividends. See Item 10. Additional Information Description of Our Company s By-laws Voting Rights.

Holders of our ADSs may find it difficult to exercise their voting rights at our shareholders meetings.

Under Brazilian law, only shareholders registered as such in our corporate books may attend our shareholders meetings. All common shares and preferred shares underlying our ADSs are registered in the name of the depositary. ADS holders may exercise the voting rights with respect to our common shares and the limited voting rights with respect to our preferred shares represented by our ADSs only in accordance with the deposit agreements relating to our ADSs. There are practical limitations upon the ability of the ADS holders to exercise their voting rights due to the additional steps involved in communicating with ADS holders. For example, we are required to publish a notice of our shareholders meetings in certain newspapers in Brazil. To the extent that holders of our common shares or preferred shares are entitled to vote at a shareholders meeting, they will be able to exercise their voting rights by attending the meeting in person or voting by proxy. By contrast, holders of the ADSs may receive notice of a shareholders meeting by mail from the depositary if notify the depositary of the shareholders meeting and request the depositary to inform ADS holders of the shareholders meeting. To exercise their voting rights, ADS holders must instruct the depositary on a timely basis. This noticed voting process will take longer for ADS holders than for holders of our common shares or preferred shares. If the depositary fails to receive timely voting instructions for all or part of our ADSs, the depositary will assume that the holders of those ADSs are instructing it to give a discretionary proxy to a person designated by us to vote their ADSs, except in limited circumstances.

In the circumstances in which holders of our ADSs have voting rights, they may not receive the voting materials in time to instruct the depositary to vote our common shares or preferred shares underlying their ADSs. In addition, the depositary and its agents are not responsible for failing to carry out voting instructions of the holders of our ADSs or for the manner of carrying out those voting instructions. Accordingly, holders of our ADSs may not be able to exercise voting rights, and they will have no recourse if the common shares or preferred shares underlying their ADSs are not voted as requested.

Holders of our common shares, preferred shares or ADSs in the United States may not be entitled to the same preemptive rights as Brazilian shareholders have, pursuant to Brazilian legislation, in the subscription of shares resulting from capital increases made by us.

Under Brazilian law, if we issue new shares in exchange for cash or assets as part of a capital increase, subject to certain exceptions, we must grant our shareholders preemptive rights at the time of the subscription of shares, corresponding to their respective interest in our share capital, allowing them to maintain their existing shareholding percentage. We may not legally be permitted to allow holders of our common shares, preferred shares or ADSs in the United States to exercise any preemptive rights in any future capital increase unless (1) we file a registration statement for an offering of shares resulting from the capital increase with the U.S. Securities and Exchange Commission, or SEC, or (2) the offering of shares resulting from the capital increase qualifies for an exemption from the registration requirements of the Securities Act. At the time of any future capital increase, we will evaluate the costs and potential liabilities associated with filing a registration statement for an offering of shares with the SEC and any other factors that we consider important in determining whether to file such a registration statement. We cannot assure the holders of our common shares, preferred shares or ADSs in the United States that we will file a registration statement with the SEC to allow them to participate in any of our capital increases. As a result, the equity interest of such holders in our company may be diluted.

If holders of our ADSs exchange them for common shares or preferred shares, they may risk temporarily losing, or being limited in, the ability to remit foreign currency abroad and certain Brazilian tax advantages.

The Brazilian custodian for the common shares and preferred shares underlying our ADSs must obtain an electronic registration number with the Central Bank to allow the depositary to remit U.S. dollars abroad. ADS holders benefit from the electronic certificate of foreign capital registration from the Central Bank obtained by the custodian for the depositary, which permits it to convert dividends and other distributions with respect to the common shares or preferred shares into U.S. dollars and remit the proceeds of such conversion abroad. If holders of our ADSs decide to exchange them for the underlying common shares or preferred shares, they will only be entitled to rely on the custodian s certificate of registration with the Central Bank for five business days after the date of the exchange. Thereafter, they will be unable to remit U.S. dollars abroad unless they obtain a new electronic certificate of foreign capital registration in connection with the common shares or preferred shares, which may result in expenses and may cause delays in receiving distributions. See Item 10. Additional Information Exchange Controls.

Also, if holders of our ADSs that exchange our ADSs for our common shares or preferred shares do not qualify under the foreign investment regulations, they will generally be subject to less favorable tax treatment of dividends and distribution on, and the proceeds from any sale of, our common shares or preferred shares. See Item 10. Additional information Exchange Controls and Item 10. Additional Information Taxation Brazilian Tax Considerations.

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Holders of our ADSs may face difficulties in protecting their interests because, as a Brazilian company, we are subject to different corporate rules and regulations and our shareholders may have fewer and less well-defined rights.

Holders of our ADSs are not direct shareholders of our company and are unable to enforce the rights of shareholders under our by-laws and the Brazilian Corporation Law.

Our corporate affairs are governed by our by-laws and the Brazilian Corporation Law, which differ from the legal principles that would apply if we were incorporated in a jurisdiction in the United States, such as the State of Delaware or New York, or elsewhere outside Brazil. Even if a holder of our ADSs surrenders its ADSs and becomes a direct shareholder, its rights as a holder of our common shares or preferred shares under the Brazilian Corporation Law to protect its interests relative to actions by our board of directors may be fewer and less well-defined than under the laws of those other jurisdictions.

Although insider trading and price manipulation are crimes under Brazilian law, the Brazilian securities markets are not as highly regulated and supervised as the U.S. securities markets or the markets in some other jurisdictions. In addition, rules and policies against self-dealing or for preserving shareholder interests may be less well-defined and enforced in Brazil than in the United States and certain other countries, which may put holders of our common shares, preferred shares and ADSs at a potential disadvantage. Corporate disclosures also may be less complete or informative than those of a public company in the United States or in certain other countries.

We are exempt from some of the corporate governance requirements of the New York Stock Exchange.

We are a foreign private issuer, as defined by the SEC for purposes of the Exchange Act. As a result, for so long as we remain a foreign private issuer, we will be exempt from, and you will not be provided with the benefits of, some of the corporate governance requirements of The New York Stock Exchange, or the NYSE. We are permitted to follow practice in Brazil in lieu of the provisions of the NYSE s corporate governance rules, except that:

- we are required to have an audit committee that satisfies the requirements of Rule 10A-3 under the Exchange Act;
- we are required to disclose any significant ways in which our corporate governance practices differ from those followed by domestic companies under NYSE listing standards;
- our chief executive officer is obligated to promptly notify the NYSE in writing after any of our executive officers becomes aware of any non-compliance with any applicable provisions of the NYSE corporate governance rules; and
- we must submit an executed written affirmation annually to the NYSE. In addition, we must submit an interim written affirmation as and when required by the interim written affirmation form specified by the NYSE.

The standards applicable to us are considerably different than the standards applied to U.S. domestic issuers. Although Rule 10A-3 under the Exchange Act generally requires that a listed company have an audit committee of its board of directors composed solely of independent directors, as a foreign private issuer, we are relying on a general exemption from this requirement that is available to us as a result of the features of Brazilian law applicable to our fiscal council. In addition, we are not required to, among other things:

- have a majority of the board be independent;
- have a compensation committee or a nominating or corporate governance committee of our board of directors;
- have regularly scheduled executive sessions with only non-management directors; or

have at least one executive session of solely independent directors each year.

We intend to rely on some or all of these exemptions. As a result, you will not be provided with the benefits of certain corporate governance requirements of the NYSE.

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 the members of our board of directors, our executive officers and our independent registered public accountants reside or are based in Brazil. The vast majority of our assets and those of these other persons are located in Brazil. As a result, it may not be possible for holders of our 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. In addition, because substantially all of our assets and all of our directors and officers reside outside the United States, any judgment obtained in the United States against us or any of our directors or officers may not be collectible within the United States. 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 in the case of actions by us or our board of directors or executive officers than would shareholders of a U.S. corporation.

Brazilian tax laws may have an adverse impact on the taxes applicable to the disposition of our common shares, preferred shares and ADSs.

According to Law No. 10,833, enacted on December 29, 2003, if a nonresident of Brazil disposes of assets located in Brazil, the transaction will be subject to taxation in Brazil, even if such disposition occurs outside Brazil or if such disposition is made to another nonresident. Dispositions of our ADSs between nonresidents, however, are currently not subject to taxation in Brazil. Nevertheless, in the event that the concept of disposition of assets is interpreted to include the disposition between nonresidents of assets located outside Brazil, this tax law could result in the imposition of withholding taxes in the event of a disposition of our ADSs made between nonresidents of Brazil. Due to the fact that as of the date of this annual report Law No. 10,833/2003 has no judicial guidance as to its application, we are unable to predict whether an interpretation applying such tax laws to dispositions of our ADSs between nonresidents could ultimately prevail in Brazilian courts. See Item 10. Additional Information Taxation Brazilian Tax Considerations.

The relative volatility and illiquidity of the Brazilian securities markets may adversely affect holders of our common shares, preferred shares and ADSs.

The Brazilian securities markets are substantially smaller, less liquid and more volatile than major securities markets in the United States. The BM&FBOVESPA, which is the principal Brazilian stock exchange, had a market capitalization of R$2,294 billion (US$1,223 billion) at December 31, 2011 and an average daily trading volume of R$5.7 billion (US$3.4 billion) for 2011. In comparison, aggregate market capitalization of the companies (including U.S. and non-U.S. companies) listed on the NYSE was US$13.1 trillion at December 31, 2011 and the NYSE recorded an average daily trading volume of US$71.8 billion for 2011. There is also significantly greater concentration in the Brazilian securities markets. The ten largest companies in terms of market capitalization represented approximately 54% of the aggregate market capitalization of the BM&FBOVESPA at December 31, 2011. The ten most widely traded stocks in terms of trading volume accounted for approximately 47% of all shares traded on the BM&FBOVESPA in 2011. These market characteristics may substantially limit the ability of holders of our ADSs to sell the preferred shares underlying our ADSs at a price and at a time when they wish to do so and, as a result, could negatively impact the market price of our ADSs themselves.

The imposition of IOF taxes may indirectly influence the price and volatility of our ADSs, common shares and preferred shares.

Brazilian law imposes the Tax on Foreign Exchange Transactions, or the IOF/Exchange Tax, on the conversion of *reais* into foreign currency and on the conversion of foreign currency into *reais*. Brazilian law also imposes the Tax on Transactions Involving Bonds and Securities, or the IOF/Securities Tax, due on transactions involving bonds and securities, including those carried out on a Brazilian stock exchange.

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In October 2009, the Brazilian government imposed the IOF/Exchange Tax at a rate of 2.0% in connection with inflows of funds related to investments carried out by non-Brazilian investors in the Brazilian financial and capital markets with the objective of slowing the pace of speculative inflows of foreign capital into the Brazilian market and the appreciation of the *real* against the U.S. dollar. The rate of the IOF/Exchange Tax generally applicable to foreign investments in the Brazilian financial and capital markets was later increased to 6.0%. In December 2011, the rate of the IOF/Exchange Tax applicable to several types of investments was reduced back to zero percent, although the general rate of 6.0% still applies. In November 2009, the Brazilian government also established that the rate of the IOF/Securities Tax applicable to the transfer of shares with the specific purpose of enabling the issuance of ADSs would be 1.5% with the objective of correcting an asymmetry created by the imposition of the IOF/Exchange Tax.

The imposition of these taxes may discourage foreign investment in shares of Brazilian companies, including our company, due to higher transaction costs, and may negatively impact the price and volatility of our ADSs, common shares and preferred shares on the NYSE and the BM&FBOVESPA.

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ITEM 4. INFORMATION ON THE COMPANY
Overview

We are one of the largest integrated telecommunication service provider in Brazil, based on information available from ANATEL regarding the total number of fixed-lines in service and mobile subscribers of our company and TNL as of December 31, 2011, and the only telecommunication services provider offering quadruple play services in Brazil. We offer a range of integrated telecommunication services that includes fixed-line and mobile telecommunication services, data transmission services (including broadband access services), ISP services and other services for residential customers, small, medium and large companies, and governmental agencies. We are the largest telecommunications provider in both Region I and Region II in Brazil, based on information available from ANATEL and other publicly available information regarding revenues and customers of our company and TNL as of and for the year ended December 31, 2011. We have also been offering mobile telecommunication services in Region III since October 2008.

According to IBGE:

Region I (which consists of 16 Brazilian states located in the northeastern and part of the northern and southeastern regions) had a population of approximately 101.4 million as of August 1, 2010, representing 54.6% of the total Brazilian population, and represented approximately 39.1% of Brazil s total gross domestic product, or GDP, for 2009 (the most recent period for which such information is currently available).

Region II (which consists of the Federal District and nine Brazilian states located in the western, central and southern regions) had a population of approximately 44.4 million as of August 1, 2010, representing 23.9% of the total Brazilian population, and represented approximately 27.4% of Brazil s total GDP for 2009.

Region III (comprising the state of São Paulo) had a population of approximately 39.9 million as of August 1, 2010, representing 21.5% of the total Brazilian population, and represented approximately 33.5% of Brazil s total GDP for 2009.

Fixed-Line Telecommunications and Data Transmission Services

Our traditional fixed-line telecommunications business in Regions I and II includes local and long-distance services, network usage services (interconnection) and public telephones, in accordance with the concessions and authorizations granted to us by ANATEL. We are one of the largest fixed-line telecommunications companies in South America in terms of total number of lines in service as of December 31, 2011. We are the principal fixed-line telecommunication service provider in Region I and Region II, based on our 12.0 million and 6.8 million fixed lines in service in Region I and Region II, respectively, as of December 31, 2011, with market shares of 72.7% and 66.4%, respectively, of the total fixed lines in service in these regions as of December 31, 2011, based on information available from ANATEL.

We offer a variety of high-speed data transmission services in Regions I and II, including services offered by our subsidiaries BrT Serviços de Internet S.A. and Brasil Telecom Comunicação Multimídia ltda. We also operate a fiber optic cable system that connects the United States, Bermuda, Brazil, Venezuela and Colombia through our subsidiaries Brasil Telecom Cabos Submarinos Ltda., Brasil Telecom Subsea Cable System (Bermuda) Ltd., Brasil Telecom of America Inc. and Brasil Telecom de Venezuela S.A. Our broadband services, primarily utilizing Asymmetric Digital Subscriber Line, or ADSL, technology, are marketed under the brand name *Oi Velox.* As of December 31, 2011, we and TNL had 4.9 million ADSL subscribers in Regions I and II, representing 26.1% of our fixed lines in service at that date. Additionally, we provide voice and data services to corporate clients throughout Brazil.

For the year ended December 31, 2011, our fixed-line and data transmission services segment generated R$8,048 million in net operating revenue and recorded operating income before financial income (expenses) and taxes of R$1,519 million, and TNL s fixed-line segment generated R$20,795 million in net operating revenue on a consolidated basis and recorded operating income before financial income (expenses) and taxes of R$1,197 million on a consolidated basis. As a result of the corporate reorganization, we have consolidated the results of TNL s fixed-line segment into our fixed-line and data transmission services segment as from February 28, 2012.

Mobile Telecommunication Services

We offer mobile telecommunication services throughout Brazil. Based on our 28.3 million, 8.6 million and 8.6 million mobile subscribers in Regions I, II and III, respectively, as of December 31, 2011, we believe that we are one of the principal mobile telecommunication service providers in each service region. Based on information available from ANATEL, as of December 31, 2011 our market share was 23.2% in Region I, 14.2% in Region II and 14.5% in Region III, respectively, of the total number of mobile subscribers in these regions.

For the year ended December 31, 2011, our mobile services generated R$2,006 million in net operating revenue and recorded operating income before financial income (expenses) and taxes of R$48 million, and TNL s mobile services segment generated R$10,731 million in net operating revenue on a consolidated basis and recorded operating income before financial income (expenses) and taxes of R$1,916 million on a consolidated basis. As a result of the corporate reorganization, we have consolidated the results of TNL s mobile services segment into our mobile services segment as from February 28, 2012.

Other Services

We operate an internet portal under the brand name *iG* that was one of the largest internet portals in Brazil in terms of the number of unique visitors in 2011, based on information available from Ibope/NetRatings. We also started a call center business for the sole purpose of providing services to our company and our subsidiaries.

In September 2008, ANATEL authorized TNL to provide subscription television services throughout Brazil, using direct-to-home, or DTH, satellite technology. In 2009, TNL commenced offering DTH subscription television services to the low-income residential market in the states of Rio de Janeiro, Minas Gerais, Rio Grande do Sul, Paraná and Santa Catarina. In 2010, TNL expanded this service to the Distrito Federal and the states of Bahia, Sergipe, Pernambuco, Ceará, Paraíba, Rio Grande do Norte, Alagoas, Espírito Santo and Goiás. In 2011, TNL expanded this service to the remaining states of Regions I and II.

We provide subscription television services and broadband internet access to the residential, commercial and corporate market segments in the cities of Belo Horizonte, Poços de Caldas, Uberlândia and Barbacena in the State of Minas Gerais. We use a hybrid network of fiber optic and bidirectional coaxial cable, or (HFC network, that allows us to offer a broad range of interactive services, such as distance learning, telephony and telemedicine, among others.

Our principal executive office is located at Rua General Polidoro, No. 99, 5th floor/part Botafogo, 22280-001 Rio de Janeiro, RJ, Brazil, and our telephone number at this address is (55-21) 3131-1211.

Our History and Development

Prior to the formation in 1972 of Telebrás, the Brazilian state-owned telecommunications monopoly, there were more than 900 telecommunications companies operating throughout Brazil. Between 1972 and 1975, Telebrás and its operating subsidiaries acquired almost all of the other telecommunications companies in Brazil and thus achieved a monopoly in providing public telecommunication services in almost all areas of the country.

Beginning in 1995, the Brazilian government undertook a comprehensive reform of Brazil s telecommunications regulations. In July 1997, Brazil s Congress adopted the Brazilian General Telecommunications Law (*Lei Geral das Telecomunicações*), which, together with the regulations, decrees, orders and plans on telecommunications issued by Brazil s executive branch, provided for the establishment of a comprehensive regulatory framework introducing competition into the Brazilian telecommunications industry and promoting the privatization of Telebrás and its subsidiaries.

Privatization of Telebrás

In January 1998, in preparation for its restructuring and privatization, Telebrás spun-off its previously integrated mobile telecommunications operations from its fixed-line operations into separate companies. In May 1998, Telebrás was restructured to form 12 new holding companies, or the New Holding Companies, by means of a procedure under Brazilian Corporation Law called *cisão*, or spin-off. Virtually all of the assets and liabilities of Telebrás were allocated to the New Holding Companies, including Telebrás s interest in its operating subsidiaries. The New Holding Companies consisted of:

- eight holding companies each of which controlled one or more mobile services providers, each operating in one of the ten service regions into which Brazil had been divided for mobile telecommunication services and using the frequency range called Band A (other than one mobile services provider that operated in two regions and one region in which the mobile services provider was not part of the Telebrás system);

- three regional holding companies, including Brasil Telecom Participações S.A., or Brasil Telecom Holding, and TNL, each of which controlled the fixed-line service providers that provided local and intraregional long-distance service in one of the three service regions into which Brazil has been divided for fixed-line telecommunications; and

- a holding company, which controlled Embratel, a provider of domestic (including interstate and interregional) and international long-distance service throughout Brazil.

We are the successor to Brasil Telecom Holding and TNL, two of the New Holding Companies in the fixed-line telecommunications business. In the restructuring and privatization of Telebrás, Brasil Telecom Holding was allocated all of the share capital held by Telebrás in the operating subsidiaries that provided fixed-line telecommunication service in Region II, including our company, and TNL was allocated all of the share capital held by Telebrás in the operating subsidiaries that provided fixed-line telecommunication service in Region I, including Telemar.

In August 1998, the Brazilian government privatized Telebrás by selling all of the voting shares that it held in the New Holding Companies, including Brasil Telecom Holding and TNL, to private-sector buyers.

Expansion of Fixed-Line Network in Rio Grande do Sul

In July 2000, we acquired the control of Companhia Riograndense de Telecomunicações, or CRT. CRT was the leading fixed-line telecommunication service company in the State of Rio Grande do Sul. In December 2000, CRT was merged with and into us.

Corporate Reorganization of Brasil Telecom

Following the formation of Brasil Telecom Holding, it provided fixed-line telecommunication services through nine separate operating subsidiaries, including our company, each of which provided telecommunication services in one of the nine states of Region II or the Federal District of Brazil. In February 2000, Brasil Telecom Holding implemented a corporate reorganization, which resulted in each of its other fixed-line operating companies being merged into our company.

Corporate Reorganization of TNL

Following its formation, TNL provided fixed-line telecommunication services through 16 separate operating subsidiaries, each of which provided telecommunication services in one of the 16 states of Region I. In August 2001, TNL implemented a corporate reorganization, which resulted in all of the other fixed-line operating companies being merged into our subsidiary Telecomunicações do Rio de Janeiro S.A., or Telerj. In September 2001, Telerj changed its name to Telemar Norte Leste S.A.

Entry into the Internet Service Provider Business

In October 2001, we formed BrT Serviços de Internet S.A. to provide broadband internet services.

Entry into the Personal Mobile Services Business

In December 2002, we established our wholly-owned subsidiary, 14 Brasil Telecom Celular S.A., which we refer to as Brasil Telecom Mobile, to provide personal mobile services (*Serviço Móvel Pessoal*) in Region II. In December 2002, Brasil Telecom Mobile was granted an authorization by ANATEL to provide personal mobile services in Region II following its successful bid in an auction held for the authorization and the related radio frequency license. Brasil Telecom Mobile commenced operations in September 2004.

Expansion of Our Internet Service Provider Business

In June 2003, we acquired all of the share capital of iBest Holding Corporation that we did not own. Prior to this acquisition, we owned 12.8% of the share capital of iBest Holding Corporation. iBest Holding Corporation controlled (1) iBest S.A., or iBest, a free ISP and the then-largest ISP in Region II, (2) Freelance S.A., and (3) Febraio S.A. In May 2004, iBest and Febraio S.A. merged with and into Freelance S.A.

Acquisition of Submarine Fiber-Optic Cable System

In June 2003, we acquired the submarine fiber-optic cable system of 360 Networks Americas do Brasil Ltda. We refer to this system as GlobeNet. GlobeNet consists of a fiber optic cable system that connects the United States, Bermuda, Brazil, Venezuela and Colombia.

Entry into the Internet Protocol Business

In May 2004, we acquired substantially all of the share capital of Vant Telecomunicações S.A., or Vant, that we did not own. Prior to this acquisition, we owned 19.9% of the share capital of Vant. Vant offered Internet Protocol, or IP, services as well as other services to the corporate market throughout Brazil.

Expansion of Data Transmission Network

In May 2004, we acquired substantially all of the share capital of MetroRED Telecomunicações Ltda., or MetroRED, that we did not own. Prior to this acquisition, we owned 19.9% of the share capital of MetroRED. We have changed the corporate name of MetroRED to Brasil Telecom Comunicação Multimidia Ltda., or Brasil Telecom Multimedia. Brasil Telecom Multimedia is a leading local fiber optic network provider and also has an internet solutions data center in São Paulo which provides internet support to our customers.

Acquisition of iG

In November 2004, we acquired 63.0% of the capital stock of Internet Group (Cayman) Ltd., the parent company of Internet Group do Brasil Ltda., or iG. Prior to this acquisition, Brasil Telecom Holding owned 10.0% of the capital stock of Internet Group (Cayman) Ltd. In July 2005, we acquired an additional 25.6% of the capital stock of Internet Group (Cayman) Ltd. iG is a free internet services provider. iG is the leading dial-up ISP in Brazil and operates in the dial-up and broadband access markets. In addition, iG operates an internet portal under the brand name *iG* and offers value-added internet services to customers in the residential and corporate markets.

Consolidation of Call Centers

In December 2007, our subsidiary Brasil Telecom Call Center S.A. commenced operations, rendering call center services to us and our subsidiaries that demand this type of service. We invested approximately R$50 million in infrastructure and customer service technologies to create call centers in Goiânia, Campo Grande, Florianópolis, Brasília and Curitiba to replace our 30 pre-existing sites.

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Acquisition by Telemar

On January 8, 2009, Copart 1 Participações S.A., or Copart 1, a wholly-owned subsidiary of Coari, itself a wholly-owned subsidiary of Telemar, acquired indirectly all of the outstanding shares of Invitel S.A., or Invitel, and 12,185,836 common shares of Brasil Telecom Holding owned by the shareholders of Invitel. At that time, Invitel owned 100% of the outstanding shares of Solpart Participações S.A., or Solpart, which owned 52.0% of the outstanding voting share capital, representing 19.0% of the outstanding share capital, of Brasil Telecom Holding, which, in turn, owned 67.2% of the outstanding share capital, including 99.1% of the outstanding voting share capital, of our company.

During 2008, Copart 1 had acquired 76,645,842 preferred shares of Brasil Telecom Holding, representing 33.3% of the outstanding preferred shares of Brasil Telecom Holding, and Copart 2 Participações S.A., or Copart 2, a wholly-owned subsidiary of Coari, had acquired 58,956,565 preferred shares of our company, representing 18.9% of our outstanding preferred shares.

As a result of the acquisition of Invitel, Telemar acquired indirect control of Brasil Telecom Holding and Brasil Telecom.

In connection with the approval in October 2010 of Telemar s acquisition of control of our company by the Administrative Council for Economic Defense *(Conselho Administrativo de Defesa Econômica)*, or CADE, the Brazilian antitrust regulator, Telemar entered into a Performance Commitment Term (*Termo de Compromisso de Desempenho)* containing obligations related to the wholesale market, specifically with regard to the provision of interconnection and Industrial Exploitation of Dedicated Lines (*Exploração Industrial de Linha Dedicada*), or EILD. Under this agreement, we must, among other obligations:

- maintain a separate business area exclusively responsible for providing interconnection services, EILD and other wholesale services for a minimum of five years;
- adopt specific procedures and provide specified assistance for our interconnection services and EILD customers; and
- submit reports to CADE periodically and upon CADE s request regarding our activities in these markets.

In addition, in connection with the approval by ANATEL in December 2008 of Telemar s acquisition of control of our company, ANATEL imposed a number of conditions contained in the order granting the approval, some of which have already been fulfilled. The most significant of the remaining conditions require us to:

- extend fiber optic cables to the city of Macapá within six months after the implementation of certain infrastructure connecting the cities of Tucuruí and Macapá by the power companies in this region;
- expand our fiber optic network to 40 new municipalities in Regions I and II in each of 2012 through 2015;
- offer broadband services in 50% of the municipalities covered by our obligations to provide transmission lines connecting the fiber-optic internet backbones of Brasil Telecom and Telemar to municipalities in their concession areas in which they do not provide internet service, which we refer to as backhaul, at rates no greater than Telemar s highest existing rate for broadband services, within five months of completing the backhaul extensions, and 100% of such municipalities within ten months of completing the backhaul extensions; and
- make annual investments in research and development in each of the next ten years in amounts equal to at least 50% of the amounts of Telemar s contributions to the Telecommunications Technology Development Fund (*Fundo para o Desenvolvimento Tecnológico das Telecomunicações*), or the FUNTTEL, which may be increased to 100% at ANATEL s discretion.

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Mandatory Tender Offers by Copart 1 and Copart 2

As a result of the acquisition of control of Brasil Telecom and Brasil Telecom Holding by Telemar on January 8, 2009, under Article 254-A of the Brazilian Corporation Law and CVM Instruction No. 361, of March 5, 2002, as amended, Telemar was required to offer to purchase any and all common shares of Brasil Telecom Holding and Brasil Telecom held by public shareholders.

As a result of these auctions, in June 2009 (1) Copart 1 acquired 40,452,227 common shares of Brasil Telecom Holding, representing 30.5% of the outstanding common shares of Brasil Telecom Holding and 11.2% of the outstanding share capital of Brasil Telecom Holding, and (2) Copart 2 acquired 630,872 common shares of Brasil Telecom, representing 0.3% of the outstanding common shares of Brasil Telecom and 0.1% of the outstanding share capital of Brasil Telecom.

Merger of Copart 1 into Brasil Telecom Holding

On July 31, 2009, (1) Invitel merged with and into Solpart, with Solpart as the surviving company, (2) Solpart merged with and into Copart 1, with Copart 1 as the surviving company, and (3) Copart 1 merged with and into Brasil Telecom Holding, with Brasil Telecom Holding as the surviving company. As a result of these mergers, Coari owned 54.7% of the outstanding share capital, including 91.7% of the outstanding voting share capital, of Brasil Telecom Holding.

Merger of Copart 2 into Brasil Telecom

On July 31, 2009, Copart 2 merged with and into Brasil Telecom, with Brasil Telecom as the surviving company. As a result of this transaction, Coari owned 10.9% of the outstanding share capital, including 0.3% of the outstanding voting share capital, of Brasil Telecom.

Merger of Brasil Telecom Holding into Brasil Telecom

On September 30, 2009, the shareholders of Brasil Telecom and Brasil Telecom Holding approved a merger (*incorporação*) under Brazilian law of Brasil Telecom Holding with and into Brasil Telecom, with Brasil Telecom as the surviving company. In the Brasil Telecom merger:

- each issued and then outstanding common share of Brasil Telecom Holding (other than any common shares held by shareholders that exercised their withdrawal rights) was converted automatically into 1.2190981 common shares of Brasil Telecom;

- each issued and then outstanding preferred share of Brasil Telecom Holding was converted automatically into 0.1720066 common shares of Brasil Telecom and 0.9096173 preferred shares of Brasil Telecom; and

- all issued and then outstanding shares of Brasil Telecom held by Brasil Telecom Holding were cancelled.

As a result of the Brasil Telecom merger, Brasil Telecom Holding ceased to exist and Coari owned 48.2% of the total outstanding share capital of Brasil Telecom, including 79.6% of its outstanding voting share capital.

Corporate Reorganization of TNL, Telemar and Our Company

On February 27, 2012, the shareholders of TNL, Telemar, Coari and Brasil Telecom approved a series of transactions, which we refer to as the corporate reorganization, including:

- a split-off (*cisão*) and merger of shares (*incorporação de ações*) under Brazilian law in which:

  - Telemar transferred its shares of Coari to Coari;

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Coari assumed a portion of the liabilities of Telemar, which became joint and several liabilities of Telemar and Coari or obligations of Coari guaranteed by Telemar;

Coari issued one common share and/or one preferred share to the holders of Telemar common and preferred shares (other than the shares of holders who exercised their withdrawal rights with respect to such shares) in exchange for each of their common and preferred shares of Telemar, respectively; and

Coari retained the Telemar shares exchanged for Coari shares and as a result, Telemar became a wholly-owned subsidiary of Coari;

a merger (*incorporação*) under Brazilian law of Coari with and into our company, with our company as the surviving company, which we refer to as the Coari merger, in which:

each issued and then outstanding share of Brasil Telecom held by Coari and all Coari shares held in treasury were cancelled;

each issued and then outstanding common share of Coari was converted automatically into 5.1149 common shares of Brasil Telecom;

each issued and then outstanding preferred share of Coari was converted automatically into 0.3904 common shares of Brasil Telecom and 4.0034 preferred shares of Brasil Telecom;

Coari ceased to exist; and

Telemar became a wholly-owned subsidiary of Brasil Telecom; and

a merger (*incorporação*) under Brazilian law of TNL with and into our company, with our company as the surviving company, which we refer to as the TNL merger, in which:

each TNL share held in treasury prior to the TNL merger was cancelled, and each issued and then outstanding share of Brasil Telecom held by TNL was cancelled, other than 24,647,867 common shares of Brasil Telecom, which were transferred to the treasury of Brasil Telecom;

each issued and then outstanding common share of TNL (other than common shares held by shareholders who exercised their withdrawal rights with respect to such common shares) was converted automatically into 2.3122 common shares of Brasil Telecom;

each issued and then outstanding preferred share of TNL was converted automatically into 0.1879 common shares of Brasil Telecom and 1.9262 preferred shares of Brasil Telecom; and

TNL ceased to exist.

As a result of these transactions, TmarPart has become our direct controlling shareholder. For additional information about TmarPart, see Item 7. Major Shareholders and Related Party Transactions Major Shareholders.

In addition, on February 27, 2012, our shareholders approved:

- the issuance and distribution of (1) one Class B redeemable preferred share of our company to the holder of each of our common shares, and (2) one Class C redeemable preferred share of our company to the holder of each of our preferred shares;

- the redemption of each Class B redeemable preferred share and Class C redeemable preferred share at a redemption price equal to R$2.543282 per share, or an aggregate of R$1,502 million; and

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the change of our corporate name to Oi S.A.

We will account for the Coari merger and the TNL merger using historical cost, whereby the financial statements of our company will record the historical carrying values of the assets and liabilities of TNL, Telemar, and Coari as from the date of the reorganization. The historical carrying values of Coari reflect the purchase accounting recorded under IFRS in accordance with IFRS 3(R), Business Combinations, under which 100% of the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the subsidiaries of our company were recorded at their fair values on January 8, 2009, the date on which TNL acquired control of our company. The financial statements of TNL as of and for the year ended December 31, 2011 have not been presented elsewhere in this annual report and have not been filed with the SEC. The historical financial statements of our company will not be restated to account for the impacts of the corporate reorganization on a retroactive basis.

Holders of Telemar common shares, class A preferred shares and class B preferred shares and holder of TNL preferred shares as of the close of trading on May 23, 2011, the date prior to the publication of the Relevant Fact that first announced the split-off and share exchange and the TNL merger were entitled to withdrawal rights in connection with the split-off and share exchange and the TNL merger. Shareholders who exercised these withdrawal rights with respect to the Telemar shares were entitled to receive R$74.37 per share and shareholders who exercised these withdrawal rights with respect to the TNL preferred shares were entitled to receive R$28.93 per share. As of March 29, 2012, the expiration of the period for the exercise of these withdrawal rights, holders of 1,020,215 Telemar common shares, 17,856,585 Telemar class A preferred shares, 47,714 Telemar class B preferred shares and 20,446,097 TNL preferred shares had validly exercised their withdrawal rights for an aggregate cost to our company of R$1,999 million.

Corporate Structure

The following chart presents our corporate structure and principal subsidiaries as of April 25, 2012. The percentages in bold italics represent the percentage of the voting capital owned directly and indirectly by the parent company of each entity, and the percentages not in bold italics represent the percentage of the total share capital owned directly and indirectly by the parent company of each entity.

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(1) Ownership represents 53.8% of the share capital of iG owned directly by BrT Serviços de Internet S.A. and 13.6% owned by Oi S.A.

Our Service Areas

Our concessions and authorizations from the Brazilian government allow us to provide:

- fixed-line telecommunication services in Regions I and II;
- long-distance telecommunication services throughout Brazil;
- mobile telecommunication services in Regions I, II and III;
- data transmission services throughout Brazil; and
- direct to home (DTH) satellite television services throughout Brazil.

In addition, we have authorizations to provide fixed-line local telecommunication services in Region III.

Region I consists of 16 Brazilian states located in the northeastern and part of the northern and southeastern regions. Region I covers an area of approximately 5.4 million square kilometers, which represents approximately 64% of the country s total land area and accounted for 39.1% of Brazil s GDP in 2009. The population of Region I was 101.4 million as of August 1, 2010, which represented 54.6% of the total population of Brazil as of that date. In 2009, per capita income in Region I was approximately R$12,118, varying from R$6,051 in the State of Piauí to R$22,103 in the State of Rio de Janeiro.

Region II consists of the Federal District and nine Brazilian states located in the western, central and southern regions. Region II covers an area of approximately 2.9 million square kilometers, which represents approximately 33.5% of the country s total land area and accounted for approximately 27.4% of Brazil s GDP in 2009. The population of Region II was 44.4 million as of August 1, 2010, which represented 23.9% of the total population of Brazil as of that date. In 2009, per capita income in Region II was approximately R$19,418, varying from R$10,687 in the State of Acre to R$50,438 in the Federal District.

Region III consists of the State of São Paulo. Region III covers an area of approximately 200,000 square kilometers, which represents approximately 2.9% of the country s total land area and accounted for approximately 33.5% of Brazil s GDP in 2009. The population of Region III was 39.9 million as of August 1, 2010, which represented 21.5% of the total population of Brazil as of that date. In 2009, per capita income in Region III was approximately R$26,202.

The following table sets forth key economic data, compiled by IBGE, for the Federal District and each of the Brazilian states.

State	Population (in millions) (2010)	Population per Square Kilometer (2010)	% of GDP (2009)	GDP per Capita (in *reais*) (2009)
Region I:				
Rio de Janeiro	15.2	347.4	10.9	22,103
Minas Gerais	19.2	32.7	8.9	14,329

Bahia	13.6	24.1	4.2	9,365
Pernambuco	8.5	86.9	2.4	8,902
Pará	7.4	6.0	1.8	7,859
Amazonas	3.4	2.1	1.5	14,621
Espírito Santo	3.4	73.6	2.1	19,145

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State	Population (in millions) (2010)	Population per Square Kilometer (2010)	% of GDP (2009)	GDP per Capita (in *reais*) (2009)
Ceará	8.2	55.0	2.0	7,687
Paraíba	3.8	66.5	0.9	7,618
Rio Grande do Norte	3.1	59.1	0.9	8,894
Maranhão	6.4	19.4	1.2	6,259
Sergipe	2.0	92.9	0.6	9,787
Alagoas	3.1	111.4	0.7	6,728
Piauí	3.1	12.3	0.6	6,051
Amapá	0.6	4.5	0.2	11,817
Roraima	0.4	1.9	0.2	13,270
Subtotal	101.4		39.1	
Region II:				
Rio Grande do Sul	10.6	37.5	6.7	19,778
Paraná	10.3	51.5	5.9	17,779
Santa Catarina	6.2	64.8	4.0	21,215
Goiás	5.8	17.2	2.6	14,447
Mato Grosso	3.0	3.3	1.8	19,087
Federal District	2.5	425.6	4.1	50,438
Mato Grosso do Sul	2.4	6.7	1.1	15,407
Rondônia	1.5	6.5	0.6	13,456
Tocantins	1.4	4.9	0.4	11,278
Acre	0.7	4.6	0.2	10,687
Subtotal	44.4		27.4	
Region III (State of São Paulo)	39.9	160.8	33.5	26,202
Total	185.7		100.0	

Source: IBGE.

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Set forth below is a map of Brazil showing the areas in Region I, Region II and Region III.

Our business, financial condition, results of operations and prospects depend in part on the performance of the Brazilian economy. See Item 3. Key Information Risk Factors Risks Relating to Brazil.

Our Services

Our telecommunication services consist of:

- local fixed-line services, primarily in Regions I and II, but also in Region III, including installation, monthly subscription, metered services, collect calls and supplemental local services;

- domestic long-distance services and international long-distance services primarily from Regions I and II, placed through fixed-line and mobile telephones using our long-distance carrier selection codes, which are represented by the numbers 31 and 14;

- mobile telecommunication services utilizing 2G and 3G technology;

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- data transmission services, comprised of (1) ADSL services, (2) the lease of dedicated digital and analog lines to other telecommunication services providers, ISPs and corporate customers, (3) IP solutions, and (4) other data transmission services;

- usage of our network (1) to complete calls initiated by customers of other telecommunication services providers (interconnection services) or (2) by service providers that do not have the necessary network;

- traffic transportation services;

- public telephone services;

- value-added services which include voicemail, caller ID, directory assistance and other services;

- advanced voice services to commercial customers, such as 0800 (toll free) services;

- the operation of the iG internet portal; and

- subscription television services, including cable and DTH televisions services.

Local Fixed-Line Services

As of December 31, 2011, we and TNL s other subsidiaries had approximately 12.0 million local fixed-line customers in Region I and approximately 6.8 million local fixed-line customers in Region II. Although we continue to assess our strategic plans with regard to providing such services in Region III, we do not currently plan to offer local fixed-line services to residential customers in Region III due to the size of the investment that would be required.

Local fixed-line services include installation, monthly subscription, metered services, collect calls and supplemental local services. Metered services include local calls that originate and terminate within a single local area. ANATEL has divided Region I into 2,920 local areas and Region II into 1,772 local areas.

Under our concession agreements, we are required to offer two local fixed-line plans to users: the Basic Plan per Minute (*Plano Básico de Minutos*) and the Mandatory Alternative Service Plan (*Plano Alternativo de Serviços de Oferta Obrigatória*), each of which includes installation charges, monthly subscription charges, and charges for local minutes. As of December 31, 2011, 19.8% of the aggregate number of fixed-line customers of our company and TNL s other subsidiaries subscribed to the Basic Plan per Minute or the Mandatory Alternative Service Plan.

In addition to the Basic Plan per Minute and the Mandatory Alternative Service Plan, we offer a variety of alternative fixed-line plans that are designed to meet our customers usage profiles. As of December 31, 2011, 80.2% of the aggregate number of fixed-line customers of our company and TNL s other subsidiaries subscribed to alternative plans. We offer:

- integrated, or bundled plans which permit subscribers to purchase unlimited local calls to other fixed-line customers, a fixed number of minutes per month that may be used for long-distance calls or local calls to fixed-line or mobile subscribers, and broadband services or minutes for use to establish dial-up internet connections, which we market under the brand name *Oi Conta Total* ;

- voice and internet plans which permit subscribers to purchase a fixed number of local minutes per month for calls to fixed-line telephones and for use to establish dial-up internet connections;

voice only plans which permit subscribers to make unlimited local fixed-to-fixed calls and offer our subscribers the option of choosing an increased number of fixed-to-fixed long distance minutes than are available under our other alternative plans at similar prices, which we market under the brand name *Oi Fixo ilimitado* ;

- voice only plans which permit subscribers to purchase a fixed number of local minutes per month for calls to fixed-line telephones; and

- budget plans which permit subscribers to purchase a fixed number of local minutes, either on a pre-paid basis or a monthly basis, but restrict local calls after the purchased minutes have been consumed and require the purchase of a pre-paid card to make long-distance calls or calls to mobile handsets, such as our *Oi Fixo Controle* and *Oi Fixo Economia* plans.

Local fixed-line services also include in-dialing services (direct transmission of external calls to extensions) for corporate clients. For corporate clients in need of a large quantity of lines, we offer digital trunk services, which optimize and increase the speed of the customer s telephone system.

Long-Distance Services

For each long-distance call, whether originated from a fixed-line telephone or a mobile handset, a caller chooses its preferred long-distance carrier by dialing such carrier s long-distance carrier selection code. The caller pays the long-distance service provider for the call and the long-distance service provider pays interconnection fees to the service providers on whose fixed-line or mobile networks the call originated and terminated. Our domestic and international long-distance services consist primarily of calls originated in Region I and Region II.

Fixed Line-to-Fixed Line

Calls from one local area to another local area are domestic long-distance calls, other than calls between separate local areas within specified metropolitan regions which, under ANATEL regulations, are charged as local calls. Calls between locations in Brazil and locations outside Brazil are international long-distance calls.

We provide domestic long-distance services for calls originating from Region I and Region II through our network facilities in São Paulo, Rio de Janeiro and Belo Horizonte and through interconnection agreements, mainly with Telecomunicações de São Paulo S.A., or Telesp, in Region III, that permit us to interconnect directly with their local fixed-line networks. We provide international long-distance services originating from Region I and Region II through agreements to interconnect our network with those of the main telecommunication service providers worldwide.

Mobile Long-Distance

Each mobile subscriber in Brazil is registered in a geographic area (identified by the corresponding area codes, such as 11 (São Paulo) and 21 (Rio de Janeiro)), which we refer to as the subscriber s home registration area, and Brazil is divided into sectors based on the first digit of the area code of a caller s home registration area. A call originated by a mobile subscriber registered in one home registration area to a mobile subscriber registered in another home registration area sharing the same first digit (for example, Rio de Janeiro (area code 21) and Vitória (area code (27)), is referred to as an intrasectorial mobile call. A call originated by a mobile subscriber registered in one home registration area to a mobile subscriber registered in another home registration area that does not share the same first digit (for example, Rio de Janeiro (area code 21) and São Paulo (area code (11)), is referred to as an intersectorial mobile call. Different rates apply to intrasectorial and intersectorial mobile calls.

We provide mobile long-distance services originating from Region I and Region II through network facilities and through interconnection agreements with Telesp in Region III and each of the other principal mobile services providers operating in Brazil that permit us to interconnect directly with their local fixed-line and mobile networks. We provide international long-distance services originating or terminating on our customer s mobile handsets through agreements to interconnect our network with those of the main telecommunication service providers worldwide. We also use our submarine fiber optic network to transport international mobile long-distance calls.

Mobile Telecommunication Services

As of December 31, 2011, we and TNL s other subsidiaries had an aggregate of approximately 28.3 million subscribers located in 1,574 municipalities in Region I, 8.6 million subscribers located in 1,372 municipalities in Region II and 8.6 million subscribers located in 543 municipalities in Region III. As of December 31, 2011, based on the information available from ANATEL regarding the total number of mobile subscribers as of that date, we had a 23.2% share of the mobile services market in Region I, a 14.2% share of the mobile services market in Region II and a 14.5% share of the mobile services market in Region III. As of December 31, 2011, 83.0% of the customers of our company and TNL s other subsidiaries subscribed to pre-paid plans and 17.0% subscribed to post-paid plans.

Pre-Paid Customers

Pre-paid customers activate their cellular numbers through the purchase and installation of a SIM card in their mobile handsets. Our pre-paid customers are able to add credits to their accounts through the purchase of pre-paid cards at prices that vary based on the number of minutes available, or through the purchase of additional credits over the phone that can be charged to the customer s credit card or included on their bill for fixed-line services. These credits are valid for a fixed period of time following activation.

We sell pre-paid cards in minimum denominations of R$1.00 and permit our pre-paid customers to add credits to their account in any amount, including *centavos*, in order to facilitate the continued activation of their mobile handsets, allowing them to continue to receive incoming calls. We regularly launch various packages and promotions designed to incentivize the purchase and use of credits by our pre-paid customers.

We market *Bônus Diário* subscriptions to our pre-paid customers. When a customer that is a subscriber to *Bônus Diário* purchases additional credits, the customer receives bonus credits in that amount on each day during the remainder of the month in which the additional credits were purchased. These bonus credits may be used for (1) local calls to our fixed-line or mobile subscribers, (2) long-distance calls to our fixed-line subscribers, and (3) sending Short Message Service, or SMS, messages to mobile subscribers of any Brazilian mobile service provider. We charge our customers a nominal subscription fee to participate in the *Bônus Diário* program for six-months, and may waive this fee during the first six-month period as part of our marketing activities.

Our customers may also exchange the credits that they purchase for additional services, such as:

- *Bônus Extra* which permits our customers to purchase additional minutes for use on-net at a discount;

- *Pacote de Dados* which permits our customers to purchase a specified data allowance for use on their handsets or for sending SMS messages; and

- *Pacote de SMS* which permits our customers to purchase the ability to send specified number of SMS messages.

In addition, we offer *Crédito Especial* which permits a customer to receive a credit for emergencies for which the customer pays a premium when the customer makes its next purchase of credits.

We have recently launched a promotion called *Oi Fixo + Oi Cartão Ilimitado* under which our fixed-line customers may have a specified number of credits for use on their pre-paid mobile handsets included in their monthly fixed-line bill. A customer that subscribes to this promotion may make unlimited calls to our mobile and fixed-line customers from the customer s mobile handset.

In connection with our strategy of selling pre-paid service packages, we continue to develop new sales channels in order to increase market penetration and reduce sales costs, including selling SIM cards in small retail shops (newsstands, drugstores and supermarkets, among others).

Post-Paid Customers

Post-paid customers pay a monthly subscription fee and are billed on a monthly basis for services provided during the previous month. Post-paid plans include mailbox, caller ID, conference, call forwarding, calls on hold and special services, including Wireless Application Protocol (a protocol which simplifies standard internet codes for the more limited transmission features of a mobile handset), or WAP, General Packet Radio Service, or GPRS, which allows speeds in the range of 115 kilobytes per second (Kbps), Enhanced Data Rates for Global Evolution, or EDGE, which allows speeds in the range of 230 Kbps, and 3G.

The GPRS, EDGE and 3G services we include in our post-paid plans are available to customers with advanced mobile handset models. These services allow mobile access to the internet through mobile telephones, laptops or personal digital assistants. They also enable customers to use simultaneously voice and data services, because the connection to the internet remains active even when the customer is speaking on the phone. This means that the customer can remain continuously online and, at the same time, place or receive calls.

The WAP portal is another service and content channel available to our post-paid plan customers, which provides access to a portfolio of value-added services. Some of its features include sending and receiving e-mails, forming contact groups, accessing banks and buying tickets. The WAP portal can also be used on the internet, for instance, to schedule personal activities and join or initiate contact groups.

We offer a variety of post-paid plans that are designed to meet our customers usage profiles and needs. We offer:

- plans which permit a subscriber to purchase a fixed number of minutes per month for local calls to other fixed-line or mobile subscribers;

- our *Oi a vontade* plans which permit a subscriber to purchase a fixed number of minutes per month for local calls and make unlimited on-net mobile calls and calls to our fixed-line subscribers;

- family plans which permit a subscriber to purchase a fixed number of minutes per month for local calls that may be shared by up to four individuals;

- plans for small and medium commercial enterprises which permit a subscriber to purchase a fixed number of minutes for local calls and on-net mobile calls; and

- data packages that provide data allowances from 50MB to 2 GB and provide data transmission at speeds of 1 Mbps for use by our customers with their smart phones and laptop computers.

We also offer hybrid plans under the brand name *Oi Controle* that permit a subscriber to purchase a fixed number of local and long-distance minutes per month, but restrict outgoing calls after the purchased minutes have been consumed, other than calls made using a pre-paid card. We account of these hybrid plans as post-paid plans as customers selecting these plans pay monthly subscription fees for their fixed allocations of minutes. In general, these plans are attractive to our other post-paid customers that migrate to these plans to place self-imposed limits on their mobile calling habits and to our pre-paid customers who are able to place calls at lower cost than with our pre-paid services.

Roaming

We have roaming agreements with Companhia de Telecomunicações do Brasil Central, or CTBC, and Sercomtel S.A. Telecomunicações, or Sercomtel, providing our customers with automatic access to roaming services when traveling in areas of Brazil outside our coverage area where mobile telecommunication services are available on the GSM standard.

We generate revenues from roaming when one of our mobile subscribers receives a call while at a location outside the sector that includes their home registration area. In addition, we generate revenues when a subscriber of

another mobile services provider places a call from a location that is outside the coverage area of its mobile services provider and the call is originated on our mobile networks. Conversely, when one of our mobile subscribers places a call from outside of Brazil, we pay the applicable roaming rate to the mobile services provider on whose network the call originated.

Data Transmission Services

Broadband Services

We provide high-speed internet access services using ADSL technology, which we refer to as broadband services, to residential customers and businesses in the primary cities in Region I and Region II under the brand name *Oi Velox.* As of December 31, 2011, we and TNL s other subsidiaries offered broadband services in 2,833 municipalities in Region I and 1,848 municipalities in Region II. As of December 31, 2011, we and TNL s other subsidiaries had an aggregate of 4.9 million ADSL customers in Regions I and II.

ADSL technology allows high-speed transmission of voice and data signals on a single copper wire pair for access to the network. Since voice transmission through telephone lines uses only one of many available frequency bands, the remaining frequency bands are available for data transmission. An ADSL modem is installed using the customer s conventional line, which, in turn, is connected to Digital Subscriber Line Access Multiplexer, or DSLAM, equipment at the switching station. As a result, customers can use the telephone line simultaneously with the internet. Customers pay a fixed monthly subscription fee, irrespective of their actual connection time to the internet.

Our network supports ADSL2+, VDSL2, or very-high-bitrate digital subscriber line, and FTTx technologies. ADSL2+ is a data communications technology that allows data transmission at speeds of up to 24 Mbps downstream and 1 Mbps upstream, which is much faster than data transmission through conventional ADSL. ADSL2+ permits us to offer a wider range of services than ADSL, including IP TV. VDSL2 is a DSL technology providing faster data transmission, up to 100 Mbps (downstream and upstream), permitting us to support high bandwidth applications such as HDTV, Voice over Internet Protocol, or VoIP, and broadband internet access, over a single connection. As of December 31, 2011, approximately 85% of our fixed-line network had been updated to support ADSL2+ or VDSL2. FTTx, or Fiber to the x, is a term for broadband network architecture that uses optical fiber to replace all or part of the usual metal local loop used for last mile telecommunications.

Commercial Data Transmission Services

We provide a variety of customized, high-speed data transmission services through various technologies and means of access to other telecommunication services providers, ISPs and corporate customers. Our data transmission services include interconnection between local area networks at data transmission speeds of 34 Mbps, 155 Mbps and 1 Gbps, videoconferencing, video/image transmission and multimedia applications. Our principal commercial data transmission services are:

- Industrial Exploitation of Dedicated Lines (*Exploração Industrial de Linha Dedicada*), or EILD, under which we lease trunk lines to other telecommunication services providers, primarily mobile services providers, which use these trunk lines to link their radio base stations to their switching centers;

- Dedicated Line Services (*Serviços de Linhas Dedicadas*), or SLD, under which we lease dedicated lines to other telecommunication services providers, ISPs and corporate customers for use in private networks that link different corporate websites;

- IP services which consist of dedicated private lines and dial-up internet access which we provide to most of the leading ISPs in Brazil, as well as Virtual Private Network, or VPN, services that enable our customers to operate private intranet and extranet networks; and

- frame relay services which we provide to our corporate customers to allow them to transmit data using protocols based on direct use of our transmission lines, enabling the creation of VPNs.

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We provide these data transmission services using our service network platforms in Regions I and II and our nationwide fiber optic cable network and microwave links.

In order to provide complete solutions to our corporate clients, we have entered into service agreements for the joint supply of international data services with a number of important international data services providers. These commercial relationships with international data services providers are part of our strategy of offering telecommunication services packages to our customers.

In addition, we provide services at our six cyber data centers located in Brasília, São Paulo, Curitiba, Porto Alegre and Fortaleza. We provide hosting, collocation and IT outsourcing at these centers, permitting our customers to outsource their IT structures to us or to use these centers to provide backup for their IT systems.

We also own and operate a submarine fiber optic network, which connects Brazil with the United States, Bermuda, Venezuela and Colombia. Through this network, we offer international data transportation services, primarily leased lines to other telecommunication services providers.

Network Usage Services (Interconnection Service)

All telecommunication services providers in Brazil are required, if technically feasible, to make their networks available for interconnection on a non-discriminatory basis whenever a request is made by another telecommunication services provider. Interconnection permits a call originated on the network of a requesting local fixed-line, mobile or long-distance service provider s network to be terminated on the local fixed-line or mobile services network of the other provider.

Use of Our Local Fixed-Line Network

We are authorized to charge for the use of our local fixed-line network on a per-minute basis for (1) all calls terminated on our local fixed-line networks in Regions I and II that originate on the networks of other local fixed-line, mobile and long-distance service providers, and (2) all long-distance calls originated on our local fixed-line networks in Regions I and II that are carried by other long-distance service providers.

Conversely, other local fixed-line service providers charge us interconnection fees (1) to terminate calls on their local fixed-line networks that are originated on our local fixed-line, mobile or long-distance networks, and (2) for long-distance calls originated on their local fixed-line networks that are carried by our long-distance network.

In addition, we charge network usage fees to long-distance service providers and operators of trunking services that connect switching stations to our local fixed-line networks.

Use of Our Long-Distance Network

We are authorized to charge for the use of our long-distance network on a per-minute basis for all calls that travel through a portion of our long-distance networks for which the caller has not selected us as the long-distance provider. Conversely, other long-distance service providers charge us interconnection fees on a per-minute basis for all calls that travel through a portion of their long-distance networks for which the caller has selected us as the long-distance provider.

Use of Our Mobile Network

We are authorized to charge for the use of our mobile network on a per-minute basis for all calls terminated on our mobile network that originate on the networks of other local fixed-line, mobile and long-distance service providers. Conversely, other mobile services providers charge us interconnection fees to terminate calls on their mobile networks that are originated on our local fixed-line, mobile or long-distance networks.

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Traffic Transportation Services

Long-distance and mobile services providers may avoid paying long-distance network usage charges to us by establishing an interconnection to our local fixed-line networks. In order to retain these customers of our long-distance services, we offer a long-distance usage service, called national transportation, under which we provide discounts to our long-distance network usage fees based on the volume of traffic and geographic distribution of calls generated by a long-distance or mobile services provider.

We also offer international telecommunication service providers the option to terminate their Brazilian inbound traffic through our network, as an alternative to Embratel and Intelig Telecomunicações Ltda., or Intelig. We charge international telecommunication service providers a per-minute rate, based on whether a call terminates on a fixed-line or mobile telephone and the location of the local area in which the call terminates.

Public Telephone Services

We own and operate public telephones throughout Region I and Region II. As of December 31, 2011, we and TNL s other subsidiaries had approximately 771,300 public telephones in service, all of which are operated by pre-paid cards. For a discussion of how we account for the sale of the pre-paid cards, see Item 5. Operating and Financial Review and Prospects Financial Presentation and Accounting Policies Critical Accounting Policies and Estimates Revenue Recognition and Accounts Receivable.

Value-Added Services

Value-added services include voice, text and data applications, including voicemail, caller ID, and other services, such as personalization (video downloads, games, ring tones and wallpaper), SMS subscription services (horoscope, soccer teams and love match), chat, mobile television, location-based services and applications (mobile banking, mobile search, email and instant messaging).

Advanced Voice Services

We provide advanced voice services to our corporate customers, mainly 0800 (toll free) services, as well as voice portals where customers can participate in real-time chats and other interactive voice services.

iG Internet Portal

We operate an internet portal under the brand name *iG* that was one of the largest internet portals in Brazil in terms of the number of unique visitors in 2011 according to Ibope/NetRatings. In 2011, iG was visited by 25 million users on a monthly basis, and as of December 31, 2011, iG had approximately 3.7 million registered subscribers and hosted 7.2 million e-mail accounts. iG offers content channels covering the economy, women s topics, entertainment, education, news, celebrities and sports, among others. We generate revenue through the iG portal from (1) monthly subscription fees that we charge to registered users of this portal, (2) fees charged to place advertisements on this portal, and (3) fees that we receive from fixed-line service providers based on the number of minutes that their subscribers are connected to this portal.

Subscription Television Services

We offer subscription television services and broadband internet access under our *Oi TV* brand using DTH technology throughout Regions I and II and using a hybrid network of fiber optic and bidirectional coaxial cable in the cities of Belo Horizonte, Poços de Caldas, Uberlândia and Barbacena in the State of Minas Gerais.

In 2009, TNL commenced offering DTH subscription television services to the low-income residential market in the states of Rio de Janeiro, Minas Gerais, Rio Grande do Sul, Paraná and Santa Catarina. In 2010, TNL expanded this service to the Distrito Federal and the states of Bahia, Sergipe, Pernambuco, Ceará, Paraíba, Rio Grande do Norte, Alagoas, Espírito Santo and Goiás. In 2011, TNL expanded this service to the remaining states of Regions I and II. As of December 31, 2011, there were approximately 300,000 subscribers to our DTH subscription television services.

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We provide subscription television services and broadband internet access to approximately 50,000 subscribers in the residential, commercial and corporate market segments in the cities of Belo Horizonte, Poços de Caldas, Uberlândia and Barbacena using a coaxial cable network that allows us to offer a broad range of interactive services, such as distance learning, telephony and telemedicine, among others.

We offer basic subscription packages for our *Oi TV* services, as well as a variety of premium packages which allow subscribers to tailor the content that they receive to their individual tastes.

Rates

Our rates for local fixed-line services, domestic long-distance services, mobile services, interconnection, EILD and SLD services are subject to regulation by ANATEL, subject to certain exceptions relating to the rates we charge under alternative fixed-line and mobile plans that we are authorized to offer to our customers. For information on ANATEL regulation of our rates, see Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services Rate Regulation, Regulation of the Brazilian Telecommunications Industry Regulation of Mobile Services Personal Mobile Services Rate Regulation, Regulation of the Brazilian Telecommunications Industry Interconnection Regulations, and Regulation of the Brazilian Telecommunications Industry Regulation of Data Transmission and Internet Services.

Many of the services we provide charge on a per-minute basis. For these services, we charge for calls based on the period of use. The charge unit is a tenth of a minute (six seconds), and rounding is permitted to the next succeeding tenth of a minute. There is a minimum charge period of 30 seconds for every call.

Local Fixed-Line Rates

Local Rates

Our revenues from local fixed-line services consist mainly of monthly subscription charges, charges for local calls and charges for the activation of lines for new subscribers or subscribers that have changed addresses. Monthly subscription charges are based on the plan to which the customer subscribes and whether the customer is a residential, commercial or trunk line customer.

Under our concession agreements, we are required to offer two local fixed-line plans to users: the Basic Plan per Minute and the Mandatory Alternative Service Plan, each of which includes installation charges, monthly subscription charges, and charges for local minutes. As of December 31, 2011, 19.8% of the aggregate number of local fixed-line customers of our company and TNL s other subsidiaries subscribed to the Basic Plan per Minute or the Mandatory Alternative Service Plan.

The monthly subscription fees under the Basic Plan per Minute and the Mandatory Alternative Service Plan vary in accordance with the subscribers profiles, as defined in the applicable ANATEL regulations. The monthly subscription fee for the Basic Plan per Minute includes the use of 200 local minutes per month by residential customers and 150 local minutes per month by commercial customers and trunk line customers. The monthly subscription fee for the Mandatory Alternative Service Plan includes the use of 400 local minutes per month by residential customers and 360 local minutes per month by commercial customers and trunk line customers. We deduct only two local minutes from a Basic Plan per Minute customer s monthly allotment and four minutes from a Mandatory Alternative Service Plan customer s monthly allotment for each local call made, regardless of the duration of the call, during off-peak hours. If the minute limits are exceeded, customers will incur additional metered-minute charges, the prices of which vary depending on whether the customer is a Basic Plan per Minute subscriber or a Mandatory Alternative Service Plan subscriber. If a customer does not use all of the minutes covered by the monthly subscription fee, the minutes cannot be carried over to the next month.

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In addition to the Basic Plan per Minute and the Mandatory Alternative Service Plan, we are permitted to offer non-discriminatory alternative plans to the basic service plans. The rates for applicable services under these plans (e.g., monthly subscription rates and charges for local and long-distance calls) must be submitted for ANATEL approval prior to the offering of those plans to our customers. In general, ANATEL does not raise objections to the terms of these plans. As of December 31, 2011, 80.2% of the aggregate number of local fixed-line customers of our company and TNL s other subsidiaries subscribed to alternative plans.

Under our fixed-line rate plans, we charge for calls on a per-minute basis. There is a minimum charge period of 30 seconds for every call. However, calls of three seconds or less are not charged, except in certain specific instances as provided for in ANATEL regulations.

On an annual basis, ANATEL increases or decreases the maximum rates that we are permitted to charge for our basic service plans. ANATEL increased the rates that we and Telemar may charge by an average of 0.98% as of September 11, 2009, 0.66% as of October 23, 2010 and 1.97% as of December 24, 2011. In addition, we are authorized to adjust the rates applicable to our alternative plans annually by no more than the rate of inflation, as measured by the IST. Discounts from the rates set in basic service plans and alternative service plans may be granted to customers without ANATEL approval.

The following table sets forth selected information regarding service rates under the Basic Plan per Minute of our company and Telemar during the periods indicated.

Monthly subscription rates for Basic Plan per Minute (1)	Year Ended December 31, 2011	2010	2009
		(in *reais*)	
Oi:			
Basic Plan per Minute (residential)	29.22	29.22	28.97
Basic Plan per Minute (commercial)	43.26	43.26	42.89
Basic Plan per Minute (trunk lines)	42.52	42.52	42.50
Telemar:			
Basic Plan per Minute (residential)	28.96	28.96	28.81
Basic Plan per Minute (commercial)	49.91	49.91	48.30
Basic Plan per Minute (trunk lines)	49.78	49.78	48.30

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Local Fixed Line-to-Mobile Rates

When one of our fixed-line customers makes a call to a mobile subscriber of our company or another mobile services provider that terminates in the mobile registration area in which the call was originated, we charge our fixed-line customer per-minute charges for the duration of the call based on rates designated by ANATEL as VC1 rates. In turn, we pay the mobile services provider a per-minute charge based on rates designated by ANATEL as VU-M rates for the use of its mobile network in completing the call. VC1 rates vary depending on the time of the day and day of the week, and are applied on a per-minute basis.

On an annual basis, ANATEL may increase or decrease the maximum VC1 rates that we are permitted to charge. ANATEL authorized our company and Telemar to increase our VC1 rates by an average 0.98% as of February 9, 2010. Discounts from the VC1 rates approved by ANATEL may be granted to customers without ANATEL approval. In November 2011, ANATEL adopted new regulations under which ANATEL was authorized to reduce the then-current VC-1 rates by as much as 18% in 2011, 12% in 2012 and 10% in 2013, after giving effect to an inflation adjustment based on the IST measured from June 2009. In February 2012, ANATEL reduced our VC-1 rates by approximately 10%, although we are appealing the calculation of this rate reduction.

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The following table sets forth the average per-minute VC1 rates that we and Telemar were permitted to charge for fixed-line to mobile calls during the periods indicated.

Per-minute charges for local fixed-line calls made to mobile telephones (1)	Year Ended December 31, 2011	2010	2009
		(in *reais*)	
Oi	0.51	0.51	0.51
Telemar	0.51	0.51	0.51

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Domestic Long-Distance Rates

Fixed Line-to-Fixed-Line

If a caller selects one of our carrier selection codes for a long-distance call that originates and terminates on fixed-line telephones, we receive the revenues from the call and must pay interconnection fees to the service providers that operate the networks on which the call originates and terminates. Rates for these long-distance calls are based on the physical distance separating callers (which are categorized by four distance ranges), time of the day and day of the week, and are applied on a per-minute basis for the duration of the call. Rates on these calls are applied on a per-minute basis.

On an annual basis, ANATEL increases or decreases the maximum domestic fixed line-to-fixed line long-distance rates that we are permitted to charge. ANATEL increased the rates that our company and Telemar may charge by an average of 0.98% as of September 11, 2009, 0.66% as of October 23, 2010 and 1.97% as of December 24, 2011. Discounts from the domestic fixed line-to-fixed line long-distance rates approved by ANATEL may be granted to customers without ANATEL approval.

The following table sets forth selected information on domestic fixed line-to-fixed line long-distance rates that we and Telemar were permitted to charge per minute during peak hours (*i.e.*, between the hours of 9 a.m. and noon and 2 p.m. and 6 p.m. on weekdays) during the periods indicated.

Domestic long-distance rates per minute (1)	Year Ended December 31, 2011	2010	2009
		(in *reais*)	
Oi:			
0 to 50 km	0.13	0.20	0.24
50 to 100 km	0.28	0.35	0.35
100 to 300 km	0.31	0.38	0.36
Over 300 km	0.32	0.39	0.37
Telemar:			
0 to 50 km	0.11	0.17	0.20
50 to 100 km	0.23	0.30	0.32
100 to 300 km	0.32	0.39	0.37
Over 300 km	0.38	0.43	0.41

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Mobile Long-Distance

Rates for long-distance calls that originate or terminate on mobile telephones are based on whether the call is an intrasectorial long-distance call, which is charged at rates designated by ANATEL as VC2 rates, or an intersectorial

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long-distance call, which is charged at rates designated by ANATEL as VC3 rates. If the caller selects one of our carrier selection codes for the call, we receive the revenues from the call and must pay interconnection fees to the service providers that operate the networks on which the call originates and terminates. The applicable VC2 and VC3 rates vary depending on the time of the day and day of the week, and are applied on a per-minute basis.

On an annual basis, ANATEL may increase or decrease the maximum VC2 and VC3 rates we are authorized to charge. ANATEL authorized our company and Telemar to increase our VC2 and VC3 rates by an average of 0.98% as of February 9, 2010. In November 2011, ANATEL adopted new regulations under which ANATEL was authorized to reduce the then-current VC-2 and VC-3 rates by as much as 18% in 2011, 12% in 2012 and 10% in 2013, after giving effect to an inflation adjustment based on the IST measured from June 2009. In February 2012, ANATEL reduced our VC-2 and VC-3 rates by approximately 10%, although we are appealing the calculation of this rate reduction.

The following table sets forth the average per-minute rates that our company and Telemar were permitted to charge for mobile long-distance calls during peak hours (*i.e.*, between the hours of 9 a.m. and noon and 2 p.m. and 6 p.m. on weekdays) during the periods indicated.

	Year Ended December 31,		
Per-minute charges for mobile long-distance calls (1)	**2011**	**2010**	**2009**
		(in *reais*)	
Oi:			
VC2	1.12	1.12	1.11
VC3	1.28	1.28	1.26
Telemar:			
VC2	1.11	1.11	1.09
VC3	1.27	1.27	1.24

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Mobile Rates

Mobile telecommunication service in Brazil, unlike in the United States, is offered on a calling-party-pays basis under which a mobile subscriber pays only for calls that he or she originates (in addition to roaming charges paid on calls made or received outside the subscriber s home registration area). A mobile subscriber receiving a collect call is also required to pay mobile usage charges.

Our revenues from mobile services consist mainly of charges for local and long-distance calls paid by our pre-paid and post-paid mobile subscribers and monthly subscription charges paid by our post-paid plan subscribers. Monthly subscription charges are based on a post-paid subscriber s service plan. If one of our mobile subscribers places or receives a call from a location outside of his or her home registration area, we are permitted to charge that customer the applicable roaming rate.

Under ANATEL regulations, TNL PCS S.A., or TNL PCS, and Brasil Telecom Mobile were each required to submit a basic post-paid service plan and a basic pre-paid service plan to ANATEL for its approval. As of December 31, 2011, fewer than 1% of the aggregate number of mobile customers of our company and TNL s other subsidiaries to our basic post-paid plans or our basic pre-paid plans.

In addition to the basic service plans, we are permitted to offer non-discriminatory alternative plans to the basic service plans. The rates for applicable services under these plans (*e.g.*, monthly subscription rates, charges for local and long-distance calls and roaming charges) must be submitted for ANATEL approval prior to the offering of those plans to our customers. In general, ANATEL does not raise objections to the terms of these plans. As of December 31, 2011, substantially all of the post-paid and pre-paid customers of our company and TNL s other subsidiaries subscribed to these alternative plans.

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Although subscribers of a plan cannot be forced to migrate to new plans, existing plans may be discontinued as long as all subscribers of the discontinued plan receive a notice to that effect and are allowed to migrate to new plans within six months of such notice.

We charge for all mobile calls made by our pre-paid customers, and for mobile calls made by our post-paid customers in excess of their allocated monthly number of minutes, on a per-minute basis.

Rates under our mobile plans may be adjusted annually by no more than the rate of inflation, as measured by the IST. These rate adjustments occur on the anniversary dates of the approval of the specific plans. Discounts from the rates set in basic service plans and alternative service plans may be granted to customers without ANATEL approval. The rate of inflation as measured by the IST was 2.06% in 2009, 5.65% in 2010 and 4.90% in 2011.

Network Usage (Interconnection) Rates

Fixed-Line Networks

Our revenues from the use of our local fixed-line networks consist primarily of payments on a per-minute basis, which are charged at rates designated by ANATEL as TU-RL rates, from:

- long-distance service providers to complete calls terminating on our local fixed-line networks;
- long-distance service providers for the transfer to their networks of calls originating on our local fixed-line networks;
- mobile services providers to complete calls terminating on our local fixed-line networks; and
- other fixed-line service providers for local fixed-line calls that originate on their local fixed-line networks and terminate on our local fixed-line networks.

TU-RL rates vary depending on the time of the day and day of the week, and are applied on a per-minute basis. Charges for the use our local fixed-line networks to terminate local calls originating on the network of another local fixed-line service provider are only billed and due when usage of one of our networks exceeds 55% of the total traffic registered between that network and the network of the other telecommunication service provider.

Since January 1, 2007, the TU-RL rates of our company and Telemar have been equal to 40% of the rate included in their respective Basic Plan per Minute for a local fixed-line call, which is adjusted on an annual basis by ANATEL. As of the date of this annual report, Oi s TU-RL rate during peak hours (*i.e.*, between the hours of 9 a.m. and noon and 2 p.m. and 6 p.m. on weekdays) is R$0.032 per minute, and Telemar s TU-RL rate during peak hours is R$0.029 per minute. ANATEL announced that beginning in 2008, the method used to determine the TU-RL rates would be based on a cost methodology, known as long-run incremental costs. However, in October 2007, ANATEL published an official letter delaying this change until the end of 2010. In September 2010, ANATEL commenced the bidding process to engage an international consultant to assist with the development of the long-run incremental cost methodology. However, ANATEL has not established a definitive timetable for the completion of the project. Therefore, we cannot predict when this new methodology will be proposed.

Our revenues from the use of our long-distance networks consist primarily of payments on a per-minute basis, which are charged at rates designated by ANATEL as TU-RIU rates, from other long-distance carriers that use a portion of our long-distance networks to complete calls initiated by callers that have not selected us as the long-distance provider.

TU-RIU rates vary depending on the time of the day and day of the week, and are applied on a per-minute basis. Since January 1, 2007, the TU-RIU rates of our company and Telemar have been equal to 30% of their respective domestic fixed line-to-fixed line long-distance rates for calls of more than 300 km, which are adjusted on an annual basis by ANATEL. See Local Fixed-Line Rates Domestic Long-Distance Rates Fixed Line-To-Fixed Line. As of the date of this annual report, Oi s TU-RIU rate is R$0.10 per minute and Telemar s TU-RIU rate is R$0.12 per minute.

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The following table sets forth the average per-minute rates our company and Telemar charged for the use of our fixed-line networks during the periods indicated.

Fixed-Line Network Usage Rates (1)	Year Ended December 31, 2011	2010	2009
		(in *reais*)	
Oi:			
TU-RL	0.032	0.031	0.031
TU-RIU	0.097	0.094	0.088
Telemar:			
TU-RL	0.029	0.029	0.028
TU-RIU	0.118	0.108	0.086

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Mobile Networks

Our revenues from the use of our mobile networks consist primarily of payments on a per-minute basis from (1) local fixed-line, long-distance and mobile services providers to complete calls terminating on our mobile networks, and (2) long-distance service providers for the transfer to their networks of calls originating on our mobile networks.

The terms and conditions of interconnection to our mobile networks, including the rates charged to terminate calls on these mobile networks, which are designated by ANATEL as VU-M rates, commercial conditions and technical issues, are freely negotiated between us and other mobile and fixed-line telecommunication service providers, subject to compliance with regulations established by ANATEL relating to traffic capacity and interconnection infrastructure that must be made available to requesting providers, among other things. We must offer the same VU-M rates to all requesting service providers on a nondiscriminatory basis. We apply VU-M charges on a per-minute basis.

If we are not able to establish interconnection rates for use of our mobile networks with other mobile and fixed-line telecommunication service providers, ANATEL is empowered to arbitrate, at its discretion, the interconnection rates that we may charge. In 2005, mobile service providers and fixed-line service providers in Brazil were unsuccessful in negotiating an agreement for new VU-M rates. All mobile service providers and fixed-line service providers in Brazil commenced arbitration proceedings before ANATEL to establish the applicable VU-M rates. The mobile service providers and fixed-line service providers entered into a provisional agreement establishing provisional rates applicable to each mobile service provider, and after the providers entered into this agreement, ANATEL approved the adjusted VC1 rates that the fixed-line service providers were permitted to charge at that time based on the provisional VU-M rates.

We and the other mobile services providers generally negotiate provisional agreements each year to establish rate increases for the VU-M charged by the mobile services providers. No provisional agreement with respect to the VU-M rates was entered into in 2009.

Under the rules established for the auctions of 3G spectrum in December 2007, all mobile services providers were required to establish uniform VU-M rate schedules that would apply in all states of each service region no later than October 30, 2009. This requirement did not affect our company or Telemar because we had already established uniform VU-M rates in each of our service regions. As of October 30, 2009, none of the other mobile services providers had established uniform VU-M rate schedules and we commenced arbitration proceedings before ANATEL with respect to the VU-M rates charged by our competitors. In January 2010, ANATEL set provisional reference rates for each mobile services provider for each region based on the mean VU-M previously charged by that mobile services provider in the applicable service region. In February 2010, ANATEL authorized an increase of 0.67% in the VU-M rates of our company and Telemar, equivalent to 68.5% of the increase in our VC1 rates granted at that time.

In November 2011, ANATEL adopted new regulations that provided procedures under which ANATEL adopted a maximum VU-M rate that is applicable in the event that providers cannot agree upon the VU-M applicable in their interconnection agreements. The maximum VU-M rate established by ANATEL is R$0.35 per minute.

The following table sets forth the average per-minute VU-M rates that we and Telemar charged during the periods indicated.

	Year Ended December 31,		
Per-minute charges for local fixed-line calls made to mobile telephones (1)	**2011**	**2010**	**2009**
		(in *reais*)	
Oi	0.42	0.42	0.41
Telemar	0.41	0.41	0.41

(1) The amounts represent the weighted average of monthly rates, net of taxes.

Data Transmission Rates

Broadband services, IP services and frame relay services are deemed to be value-added services under ANATEL regulations and, therefore, the rates and prices for these services are not subject to regulation and are market-driven. We offer broadband services subscriptions at prices that vary depending on the download speeds available under the purchased subscription.

A significant portion of our revenues from commercial data transmission services are generated by monthly charges for EILD and SLD services, which are based on contractual arrangements for the use of part of our networks. Under ANATEL regulations, because we are deemed to have significant market power in the fixed-line services business, we are required to make publicly available the forms of agreements that we use for EILD and SLD services, including the applicable rates, and are only permitted to offer these services under these forms of agreements. We are allowed to increase these rates on an annual basis by no more than the rate of inflation, as measured by the IST. ANATEL also publishes reference rates for these services and if one of our customers objects to the rates that we charge for these services, that customer is entitled to seek to reduce the applicable rate through arbitration before ANATEL.

Our revenue from IP services is based on the number of data ports to which the customer is granted access. Our revenue from frame relay services consists mainly of charges for access to the data transmission network and metered service charges based on the amount of data transmitted. Such services are offered as pay-per-use or volume-based packages. Our revenue from cyber data center services is generally based on contractual arrangements that are tailored to the specific services provided.

DTH Services Rates

DTH services are deemed to be value-added services under ANATEL regulations and, therefore, the rates and prices for these services are not subject to regulation and are market-driven. We offer DTH subscriptions at prices that vary depending on the content of the subscription package. We offer basic subscription packages for our *Oi TV* services, as well as a variety of premium packages which allow subscribers to tailor the content that they receive to their individual tastes.

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Marketing

In 2011, we incurred R$148 million in marketing expenses and TNL incurred R$559 million in marketing expenses on a consolidated basis, primarily to:

- strengthen the *Oi* brand, reinforcing the image of the convergence of the integrated company;
- promote our *Oi Conta Total* bundled fixed-line plans and additional bundled plans that we have launched to target specific geographic regions as part of our effort to expand our broadband network and customer base;
- promote our mobile telecommunication services through the introduction of new service plans, including post-paid plans offering unlimited calls and pre-paid 3G data services at increased speeds, as well as specific marketing campaigns targeting certain market segments as part of our effort to increase our market share in mobile services;
- promote our broadband services through the introduction of data plans with increased speeds and specific marketing campaigns targeting geographic regions in which we have expanded our broadband network capabilities;
- promote our data transmission services through specific marketing campaigns targeting geographic regions in which we have expanded our data transmission network capabilities; and
- promote our subscription television services through the introduction of new television channels available through *Oi TV*, the launch of *Oi TV* in additional geographic regions, and the implementation of a marketing campaign designed to emphasize the ability of our company to provide quadruple-play services.

Throughout 2011, we and Telemar continued to offer promotions through the integrated packaging of different services, such as mobile communications, ADSL services, fixed-line services and subscription television services. We also continued to reinforce our strategy of selling SIM cards individually, separate from mobile handsets, to acquire new pre-paid customers and retain existing ones.

We advertise through a diverse array of media outlets as part of our strategy to reach all types and classes of customers and potential customers. We use television, radio, billboards, exterior signage, telemarketing, direct mail and internet advertising to market our fixed-line, mobile, long-distance, broadband and subscription television services. We also sponsor sporting events and individual athletes, as well as cultural events, such as fashion shows and popular music concerts. We are the official telecom provider and a sponsor of the 2014 World Cup in Brazil. The goal of our marketing initiatives is to increase brand awareness of our company as a convergent provider capable of meeting all of the telecommunications needs of our customers and expand the use of our distribution channels to increase net operating revenue.

In 2011, we realigned our marketing efforts to target four separate sectors of the telecommunication services market: (1) retail customers, including customers of our mobile services and residential customers of our fixed-line services; (2) customers of our mobile services and residential customers of our fixed-line services that are in upper income categories, which we refer to as high-value residential customers; (3) medium and small commercial customers; and (4) large commercial customers.

Retail Customers

The principal distribution channels that we use to market our fixed-line services to retail customers are:

- our telemarketing sales channel, which consists of approximately 1,200 sales representatives that answer more than seven million calls per month. This channel provides us with the ability to pro-actively reach new customers, thereby increasing our client base and revenues, and also receive calls prompted by offers in numerous types of media.

- door-to-door sales calls made by our sales force and by exclusive agents with approximately 4,100 salespeople trained to sell our services in Region I and Region II in places where customers generally are not reachable by telemarketing.

The principal distribution channels that we use to market our mobile services to retail customers are:

- approximately 7,100 retail stores which sell our SIM cards and pre-paid mobile cards.
- approximately 162,100 pharmacies, supermarkets, newsstands and similar outlets which sell our SIM cards and pre-paid mobile cards.

High-Value Residential Customers

We have established distribution channels that are separate from our retail distribution channels to serve high-value residential customers who are more likely to purchase our higher-value added services, such as post-paid mobile services, fixed-line and mobile broadband services, and our voice, text and data applications. The principal distribution channels that we use to market our services to high-value residential customers are:

- our own network of stores, which we began opening in 2011. As of December 31, 2011, we had opened 62 *Oi* branded stores and expect to open an additional 118 *Oi* branded stores during 2012.
- approximately 520 *Oi* franchised service stores and kiosks located in the largest shopping malls and other high density areas throughout Brazil.
- approximately 370 stores located throughout our service area that primarily sell telecommunications products and services and have entered into exclusivity agreements with us.

Small and Medium-Sized Commercial Customers

We have established separate distribution channels to serve small and medium-sized businesses to whom we market a variety of services, including our core fixed-line and mobile services, but also our higher-value added services, such as broadband services, commercial data transmission services, voice, text and data applications, and advanced voice services. The principal distribution channels that we use to market our services to small and medium-sized commercial customers are:

- our telemarketing sales channel, which consists of approximately 700 sales representatives that are specifically trained to discuss the business needs of our current and prospective commercial customers and promote higher-value and additional services to these customers. Our representatives in this market sector are divided between representatives specifically focused on customer retention and representatives focused on sales of new and/or upgraded services.
- approximately 200 *Oi* franchised service offices with approximately 3,000 sales representatives that are dedicated to understanding and addressing the communications needs of our existing and prospective small and medium-sized commercial customers.

Large Commercial Customers

We market our entire range of services to large commercial customers through our own direct sales force which meets with current and prospective large commercial customers to discuss the business needs of these enterprises and design solutions intended to address their communications needs.

Billing and Collection

Fixed-Line Telephone Services

We send each of our fixed-line customers a monthly bill covering all the services provided during the prior monthly period. Customers are grouped in billing cycles based on the date their bills are issued. Each bill separately itemizes local calls, long-distance calls, calls terminating on a mobile network, toll-free services and other services such as call waiting, voicemail and call forwarding. We have agreements with several banks for the receipt and processing of payments from our customers. A variety of businesses, such as lottery houses, drugstores and grocery stores, accept payments from our customers as agents for these banks.

We are required to include in our monthly bills charges incurred by our customers for long-distance services provided by other long-distance service providers upon the request of these providers. We have billing agreements with each long-distance telecommunication service provider that interconnects with our networks under which we bill our customers for any long-distance calls originated on our network that are carried by another long-distance service provider and transfer the balance to the relevant provider after deducting any access fees due for the use of our network. Payments are due within an average of 15 days after the billing date. We charge late-payment interest at a rate of 1% per month plus a one-time late charge of 2% of the amount outstanding. As of December 31, 2011, 16.4% of all accounts receivable due from our fixed-line customers were outstanding for more than 30 days and 8.9% were outstanding for more than 90 days. As of December 31, 2011, 12.8% of all accounts receivable due from TNL s fixed-line customers, including our customers, were outstanding for more than 30 days and 6.3% were outstanding for more than 90 days.

ANATEL regulations permit us to restrict outgoing calls made by a fixed-line customer when the customer s account is more than 31 days past due, restrict incoming calls received by a fixed-line customer when the customer s account is more than 61 days past due, and disconnect a fixed-line customer when the customer s account is more than 91 days past due, provided in each case that 15-days prior notice has been given to that customer prior to the imposition of each restriction. The disconnection process thus comprises several stages, including customer notification regarding the referral of their delinquency to credit bureaus, before the fixed-line customer may be ultimately disconnected due to non-payment. Notices range from voice messages to active calls for negotiation with the customer. Our collection system enables us to access delinquent subscribers accounts according to their payment profile. This profile takes into consideration, among other things, the length of subscription, the outstanding balance of the account and the longest payment delays.

Mobile Telecommunication Services

We bill our mobile post-paid customers on a monthly basis and itemize charges in the same manner as we bill our fixed-line customers. See Fixed-Line Telephone Services. In addition, the monthly bills also provide details regarding minutes used and roaming charges. Payments are due within an average of 15 days after the billing date. We charge late-payment interest at a rate of 1% per month plus a one-time late charge of 2% of the amount outstanding. As of December 31, 2011, 3.5% of all accounts receivable due from our mobile customers were outstanding for more than 30 days and 2.0% were outstanding for more than 90 days. As of December 31, 2011, 10.2% of all accounts receivable due from TNL s mobile customers, including our mobile customers, were outstanding for more than 30 days and 6.9% were outstanding for more than 90 days.

ANATEL regulations permit us to partially suspend services to a mobile customer when the customer s account is more than 15 days past due, restrict all incoming calls received and outgoing calls made by a mobile customer when the customer s account is more than 45 days past due, and cancel services to a mobile customer when the customer s account is more than 90 days past due, provided in each case that 15-days prior notice has been given to that customer prior to the imposition of each restriction. The cancellation process thus comprises several stages, including customer notification regarding the referral of their delinquency to credit bureaus, before services to the mobile customer may be ultimately cancelled due to non-payment. Notices range from text messages to active calls for negotiation with the customer. Our collection system enables us to access delinquent subscribers accounts according to their payment profile. This profile takes into consideration, among other things, the length of subscription, the outstanding balance of the account and the longest payment delays. We have also implemented an information tool to assist with account management that is designed to warn subscribers of high outstanding amounts due and unpaid.

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Network and Facilities

Our networks are comprised of physical and logical infrastructures through which we provide fully-integrated services, whether fixed-line or mobile, voice, data or image, thereby optimizing available resources. We monitor our networks remotely from our centralized national network operations center in Rio de Janeiro. Network operating and configuration platforms, located at the network operations center, perform failure monitoring, database and configuration management, security management and performance analysis for the each network.

Fixed-Line Network

Our fixed-line networks include (1) networks of access lines connecting customers to digital exchanges, DSLAM or next generation network, or NGN, Multi-service Access Nodes, or MSANs, (2) digital exchanges, NGN controllers, NGN trunk gateways and MSANs, (3) trunk lines connecting digital exchanges, and (4) long-distance transmission equipment. As of December 31, 2011, our access network, including the access network of TNL and its other subsidiaries which we acquired as part of the corporate reorganization, served approximately 17.8 million fixed-line subscribers and approximately 2.9 million ADSL subscribers in Region I, and approximately 10.6 million fixed-line subscribers and approximately 2.1 million ADSL subscribers in Region II. As of December 31, 2011, we provided ADSL services in approximately 4,653 municipalities.

In 2011, we and TNL s other subsidiaries provided fixed-line services at 1,118 new localities, 788 of which were provided with group access (public telephone services) and 331 of which were provided with individual access (residential telephone service), and we visited approximately 3,912 localities to confirm data on our record of localities. As of December 31, 2011, we and TNL s other subsidiaries offered fixed-line services either with individual or group access in approximately 34,661 localities.

The following table sets forth selected information about our fixed-line networks as of the dates and for the periods indicated.

	As of and For Year Ended December 31,		
	2011	**2010**	**2009**
Region I:			
Installed access lines (in millions)	17.8	18.0	17.8
Access lines in service (in millions)	10.6	12.8	13.6
Public telephones in service (in thousands)	504.3	560.8	573.6
Broadband access lines in service (in millions)	2.9	2.4	2.2
Region II:			
Installed access lines (in millions)	10.4	10.4	10.4
Access lines in service (in millions)	6.8	7.2	7.7
Public telephones in service (in thousands)	265.0	266.1	277.9
Broadband access lines in service (in millions)	2.1	1.9	1.9

Our fixed-line networks are fully digitalized and we have been introducing NGN technology in selected areas. Our long-distance network consists of optical fiber cable networks supporting high capacity Dense Wavelength Division Multiplex systems that can operate with up to 80 channels at 10 and 40 Gbps and microwave links that we use to complement the optical network in Region I and Region II. We have a nationwide long-distance backbone, consisting of an optical fiber network that connects the Federal District and the state capitals in Region I and Region II, other than Macapá (located in the State of Amapá) and is complimented by our satellite system. Most of the large urban areas of Regions I and II are also connected by our fiber optic cable networks. Our transmission infrastructure connects these digital switches to four international gateway switches: two in Rio de Janeiro, one in Curitiba and one in Brasília. Additionally, our network supports advanced services, including pre-paid and toll-free services, and permits local number portability.

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Our long-distance backbone employs the most recent optical technologies available in the telecommunications industry. Currently we are in the process of quadrupling the capacity of our backbone as a result of the deployment of 40 Gbps optical technology. We employ automatic traffic protection to improve the reliability of our network and increase its traffic capacity. The network is fully supervised and operated by management systems that allow rapid response to customer service requests and reduce the recovery time in case of failures.

Satellite Network

We have deployed an expanded range of satellite-based services to comply with our public service obligations to the rural and remote areas of Brazil, including the Amazon rainforest region. These satellite services include internet access and access to corporate data applications. As of December 31, 2011, our satellite network covered approximately 4,500 localities in 24 states and the Federal District and provided voice and data services to approximately 6.8 million customers.

In 2000, we and TNL began the implementation of the land-based segment of our respective satellite networks in order to extend transmission to remote areas in the states of Acre, Paraná, Rondônia, Rio Grande do Sul, Santa Catarina, Pará, Amazonas, Amapá and Roraima, as well as to other areas with limited access to telecommunication services due to geographical conditions, such as Mato Grosso, Mato Grosso do Sul, Goiás and Tocantins. The satellite network comprises satellite earth stations located in less-populated rural areas, as well as hub stations in the cities of Brasília, Manaus, Boa Vista, Macapá, Belém, Santarém, Marabá, Rio de Janeiro, Curitiba, Porto Alegre, Florianópolis, Cuiabá, Porto Velho and Goiânia. These satellite networks use digital technology and began operating in August 2000. The fiber optic and satellite backbones are interconnected in Brasília, Belém, Fortaleza, Rio de Janeiro, Curitiba, Porto Alegre, Florianópolis, Cuiabá, Porto Velho and Goiânia. The integration of the land-based segment of our satellite network allows us to service our subscribers in any location in Regions I and II.

Hispamar Satellite S.A., or Hispamar, a Spanish-Brazilian consortium created in November 1999 by Hispasat (the leading satellite telecommunications provider in the Iberian Peninsula), and TNL operate the Amazonas 1 satellite, which was manufactured by Astrium (EADS Space Company). In December 2002, TNL entered into an agreement with Hispasat that granted and transferred to Hispamar the rights to exploit geostationary orbital position 61 degrees west, and TNL acquired a minority equity stake in Hispamar. The Amazonas 1 satellite was launched into geostationary orbit over the Americas and started to operate in November 2004. The Amazonas 1 satellite provides both C and Ku band transponders and on-board switching. The Amazonas 1 satellite is owned by a subsidiary of Hispasat and Hispamar has been granted the right to operate and lease all of the transponder space on this satellite.

In 2009, the Amazonas 2 satellite was launched and this satellite commenced commercial operations in early 2010. The Amazonas 2 satellite was manufactured by Astrium and launched into geostationary orbit of 61 degrees West. This satellite provides both C and Ku band transponders and on-board switching, with an expected lifetime of 15 years. The Amazonas 2 satellite is owned by a subsidiary of Hispasat and Hispamar has been granted the right to operate and lease all of the transponder space on this satellite.

We lease transponders from:

- Hispamar with 754 MHz of capacity in the C band on the Amazonas 1 satellite and 540 MHz of capacity in the C band on the Amazonas 2 satellite to provide voice and data services through 653 remote switches covering 390 municipalities;

- Hispamar with 98.3 Mhz of capacity in the Ku band on the Amazonas 1 satellite and 576 Mhz of capacity in the Ku band on the Amazonas 2 satellite to provide voice and data services to approximately 3,028 localities;

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Intelsat Satellite with 205.8 MHz of capacity in the C band on the IA-8 satellite to provide voice and data services between five existing gateway switches;

Intelsat Satellite with 122 MHz of capacity in the C band on the IS-805 satellite and 648 MHz of capacity in the C band on the IS 10-02 satellite to transport voice and data signals from Manaus to Rio de Janeiro; and

Intelsat Satellite with 103 MHz of capacity in the C band on the IS-905 satellite to transport voice and data signals from Macapá to Rio de Janeiro and Boa Vista to Rio de Janeiro.

In 2005, we and TNL started to operate satellite platforms operating in the Ku band that are comprised of a satellite transport solution with Digital Video Broadcast Return Channel Satellite, or DVB-RCS, technology and an NGN control solution.

Mobile Network

Our mobile networks operate on frequencies of 900 MHz/1800 MHz for GSM and 2100 MHz for UMTS. We offer mobile data applications based on GPRS/EDGE technology for our GSM network and on high speed packet access, or HSPA, technology for our UMTS network. We offer voice applications using our GSM and UMTS networks.

As of December 31, 2011, the 2G mobile networks of our company and TNL s other subsidiaries, consisting of 12,688 active radio base stations, covered 1,468 municipalities in Region I, or 88.0% of the urban population in Region I, 1,287 municipalities in Region II, or 96.0% of the urban population in Region II, and 544 municipalities in Region III, or 99.0% of the urban population in Region III. We have GPRS coverage in 100% of the localities covered and EDGE coverage in all state capitals.

As of December 31, 2011, the 3G mobile networks of our company and TNL s other subsidiaries, consisting of 5.833 active radio base stations, covered 92 municipalities in Region I, or 47.0% of the urban population in Region I, 85 municipalities in Region II, or 53.0% of the urban population in Region II, and 95 municipalities in Region III, or 71.0% of the urban population in Region III. We have 3G coverage in all state capitals.

Our mobile networks have unique data core that are fully integrated with our fixed-line data networks. Our mobile networks are directly interconnected to the national and international long-distance networks of all long-distance service providers operating in Regions I, II and III and all mobile services providers in Regions I, II and III.

Data Transmission Network

Broadband Services

We use ADSL, ADSL2+ and VDSL2 as a broadband access technology using our existing fixed-line networks which are capable of speeds of up to 100 Mbps (download) and 1 Mbps (upload). We have implemented an address control and name resolution system for our IP networks with the objective of optimizing resources and improving the availability of internet access services.

We have deployed a Metro Ethernet network, which is a network that covers a metropolitan area to connect our subscribers to the internet, in several major metropolitan areas. We are currently expanding our Metro Ethernet network to other cities due to new customer demand. We have also deployed optical fiber networks based on gigabit passive optical network, or GPON, technology together with VDSL2 to provide fiber to the building and GPON providing fiber to the home. As a result of the implementation of this technology we are now able to provide broadband with speeds up to 100 Mbps to residential customers and up to 1 Gbps to commercial customers.

Our dial-up IP platform supports dial-up access from the fixed-line networks. We operate an internet backbone network and a fully IP-routed network, which provides a backbone for all internet dedicated and dial-up services and VPN offerings. Our internet backbone connects to the public internet via international links that we maintain abroad. With these international links, we do not need to rely on other companies to connect our outbound internet traffic with the internet backbones of international ISPs.

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Commercial Data Transmission Services

Our Asynchronous Transfer Mode, or ATM, network, with its fully-integrated management system, provides:

- Frame relay data services (a data transmission service using fast protocols based on direct use of transmission lines) from 64 Kbps up to 2 Mbps;
- ATM data services supporting access rates from 2 Mbps to 622 Mbps; and
- Aggregation network services for ADSL2+ platforms.

These features allow our integrated ATM network to service each of the different types of data applications used by our customers. ATM is a technology that converts existing twisted-pair telephone lines into access paths for high-speed communications. In response to changing customer needs, we are systematically replacing our ATM network with Ethernet and IP technologies.

Our Metro Ethernet network is fully-integrated management system and also provides:

- Ethernet data services from 4Mbps up to 500Mbps for point-to-point and multipoint dedicated access;
- Ethernet access services from 4Mbps up to 500Mbps for IP access and Multiprotocol Label Switching/VPN access;
- Aggregation network services for ADSL2+ and VDSL2 platforms; and
- Aggregation network services for GPON platforms.

We have a fully integrated and managed network providing access for IP and ATM networks over legacy copper wire through which are able to provide:

- Symmetric and transparent access to Frame Relay services at speeds from 64 kbps to 1.5 Mbps;
- Symmetrical access with PPP (Point to Point) for the Internet connection services at speeds from 64 kbps to 1.5 Mbps; and
- Symmetrical access with PPP (Point to Point) to provide connection services for VPN over Multiprotocol Label Switching at speeds from 64 kbps to 1.5 Mbps.

DTH Network

We provide our DTH services through a satellite uplink located in Lurin, Peru which receives, encodes and transmits the television signals to satellite transponders. We lease these facilities and license the related technology from Telefónica.

We lease transponders for the delivery of the television signals to our subscribers from Telefónica. We have leased 216 Mhz of capacity in the Ku band on the Amazonas 1 satellite and 36 Mhz of capacity in the Ku band on the Amazonas 2 satellite to provide DTH services.

Our customers lease satellite dishes and set-top boxes from us as part of their subscriptions to our *Oi TV* services.

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Television Cable Network

We provide subscription analog and digital television services and broadband internet access to the residential and commercial market segments in the cities of Belo Horizonte, Poços de Caldas, Uberlândia and Barbacena using a HFC network. The analog television signal is distributed from integrated headend equipment owned by Cemig Telecom that is located in these cities. The digital television signal is distributed to the HFC network in Belo Horizonte from our integrated headend equipment located in Alvorada in the city of Rio de Janeiro.

Network Maintenance

Most of our maintenance, installation and network servicing are performed by third-party service providers. For example, we have contracts with some well-known providers such as A.R.M. Engenharia for the maintenance of our external plant and equipment, and Alcatel-Lucent and Nokia Siemens Networks and Telemont for the maintenance of our internal plant and equipment. We also perform some of our ordinary course maintenance with our own team of maintenance technicians, which also coordinate the planning and execution of maintenance services performed by third parties.

In June 2007, Telemar entered into a services agreement with Nokia Siemens Networks for installation, operation, and corrective and preventive maintenance in connection with their external plant and associated equipment, public telephones, and fiber optic and data communication networks (including broadband access services) in the States of Rio de Janeiro and São Paulo. The total estimated payments under this contract are R$1.3 billion during the five-year term of this contract.

In July 2007, Telemar entered into a services agreement with Serede Serviços de Rede S/A for installation, operation, and corrective and preventive maintenance in connection with their external plant and associated equipment, public telephones and fiber optic in the State of Rio de Janeiro. The total estimated payments under this contract are R$385.9 million during the five-year term of this contract.

In July 2009, Telemar and Oi, entered into a services agreement with Nokia Siemens Networks for installation, operation, and corrective and preventive maintenance in connection with their fixed-line telecommunication services, mobile telecommunication services, data transmission services (including broadband access services), satellite services, buildings, access ways, and towers, in the States of Rio de Janeiro, Minas Gerais, Espírito Santo, São Paulo, Bahia, Sergipe, Pernambuco, Alagoas, Paraíba, Rio Grande do Norte, Ceará, Piauí, Maranhão, Pará, Amapá, Amazonas and Roraima. The total estimated payments under this contract are R$2.5 billion during the five-year term of this contract.

In November 2009, Telemar and Oi entered into a services agreement with Alcatel-Lucent to perform the same services in the States of Rio Grande do Sul, Santa Catarina, Paraná, Mato Grosso do Sul, Mato Grosso, Goiás, Tocantins, Acre, Rondônia and the Federal District, as well as Pegasus data transmission network equipment in the States of Paraná, Santa Catarina, Rio Grande do Sul, Goiás and the Federal District. The total estimated payments under this contract are R$1.2 billion during the five-year term of this contract.

In March 2010, Telemar and Oi entered into a services agreement with Telemont for installation, operation, and corrective and preventive maintenance in connection with their external plant and associated equipment, public telephones, and fiber optic and data communication networks (including broadband access services) in the States of Minas Gerais, Espirito Santo, a portion of Rio de Janeiro, the Federal District, Mato Grosso, Mato Grosso do Sul, Tocantins, Acre, Rondônia and Goias. The total estimated payments under this contract are expected to be R$2.8 billion during the five-year term of this contract.

In July 2010, Telemar and Oi entered into a services agreement, which was effective as of March 1, 2010, with A.R.M. Engenharia for installation, operation, and corrective and preventive maintenance in connection with their external plant and associated equipment, public telephones, and fiber optic and data communication networks (including broadband access services) in the States of Maranhão, Piauí, Ceará, Rio Grande do Norte, Paraíba, Pernambuco, Alagoas, Sergipe, Bahia, Amazonas, Roraima, Pará, Amapá, Paraná, Santa Catarina and Rio Grande do Sul. The total estimated payments under this contract are R$3.2 billion during the five-year term of this contract.

Call Centers

In 2007, we consolidated our call center structure by merging our 30 pre-existing sites into five sites (Goiânia, Campo Grande, Florianópolis, Brasília and Curitiba). We improved our customer relationship management system which integrates our systems and provides a database of information for each customer in order to provide better service and identify sales opportunities during each contact we have with our customers.

In 2009, Telemar revised its call center arrangements with Contax Participações S.A., or Contax, relocating several of its call centers and reducing the number of call centers from 12 to nine. As part of this revision, Telemar invested in automated platforms that permit its prepaid customers to add pre-paid minutes to their subscriptions through an automated process.

Competition

Our industry is highly competitive. The competitive environment is significantly affected by key trends, including technological and service convergence, market consolidation and combined service offerings by service providers. See Item 5. Operating and Financial Review and Prospects Principal Factors Affecting Our Financial Condition and Results of Operations Effects of Competition on the Rates that We Realize and the Discounts We Record.

Local Fixed-Line Services

In the local fixed-line telecommunication services market, competition has historically been focused on corporate customers, however, recently our competitors have begun compete in the consumer market with bundles or services targeted to the needs of lower income customers. In addition, competition from other telecommunication services has been increasing, particularly from mobile telecommunication services, which has led to traffic migration from fixed-line traffic to mobile traffic and the substitution of mobile services in place of fixed-line services, encouraged by offers of aggressively-priced packages from some mobile telecommunication service providers. Finally, the decrease in interconnection rates has discouraged the construction of new fixed-line networks and has led to decreases in market prices for telecommunication services by enabling telecommunication service providers that use the local fixed-line networks of incumbent fixed-line providers to offer lower prices to their customers.

We are the leading provider of local fixed-line services in Region I with 12.0 million fixed lines in service as of December 31, 2011 and an estimated market share of 72.7% of the total fixed lines in service in this region as of December 31, 2011, based on information available from ANATEL. Our principal competitor in Region I for fixed-line services are (1) Embratel (an affiliate of Telecom Americas Group, which is a subsidiary of América Móvil, an affiliate of Telmex), which had an estimated market share of 17.4% of the total fixed lines in service in this region as of December 31, 2011, and (2) GVT (an affiliate of Vivendi S.A.), which had an estimated market share of 5.0% of the total fixed lines in service in this region as of December 31, 2011, in each case based on information available from ANATEL. During 2011, GVT increased its competitive activities in Region I, expanding its fiber optic network in high-income residential areas and increasing its services to low- and medium-size businesses.

We are the leading provider of local fixed-line services in Region II with 6.8 million fixed lines in service as of December 31, 2011 and an estimated market share of 66.4% of the total fixed lines in service in this region as of December 31, 2011, based on information available from ANATEL. Our principal competitors in Region II for fixed-line services are (1) GVT, which had an estimated market share of 18.5% of the total fixed lines in service in this region as of December 31, 2011, and (2) Embratel, which has an estimated market share of 11.0% of the total fixed lines in service in this region as of December 31, 2011, in each case based on information available from ANATEL.

Embratel provides local fixed-line services to residential customers through the cable network owned by its subsidiary Net in the portions of Regions I and II where Net provides cable television service. As a result, Net is able to offer cable television, broadband and telephone services as a bundle at a very competitive price. Net has engaged in efforts to promote Embratel s fixed-line service by offering free local fixed-line service to its customers for a period of one year. We expect competition from Embratel to increase as the cable network of Net expands through internal growth and as a result of acquisitions.

We also expect competition from Embratel and GVT to increase in certain large cities, such as Rio de Janeiro, Belo Horizonte and Salvador, where they continue to expand their respective local fixed-line network. GVT has also begun to expand in some medium size cities with population in the range of 350,000 to 1,000,000.

TIM and Vivo have entered the local fixed-line services market by offering fixed-line wireless services which, unlike traditional mobile services, only permit a subscriber to place and receive calls when in proximity to a single specified radio base station. These services allow TIM and Vivo to offer fixed-line service without installing a network of fixed lines directly to the homes or businesses of their fixed-line customers. As of December 31, 2011, TIM has a market share of 1.2% in the Brazilian local fixed-line services market.

We expect to continue to face competition from mobile services providers, which represent the main source of competition in the local fixed-line service market. As of December 31, 2011, there were 122 million mobile subscribers (including our mobile customers) in Region I, a 18.0% increase over December 31, 2010, there were 61 million mobile subscribers (including our mobile customers) in Region II, a 14.0% increase over December 31, 2010, and there were 60 million mobile subscribers (including our mobile customers) in Region III, a 16.0% increase over December 31, 2010, based on information available from ANATEL. The increase in the number of mobile users, in addition to reduced mobile services rates, is expected to continue to adversely affect the number of fixed-line subscribers and the volume of local fixed-line traffic. In addition, because mobile providers offer promotions and service plans that permit subscribers to make calls within the mobile provider s network at rates that are less than those charged for calls from a fixed-line telephone to a mobile telephone, we believe that we may be vulnerable to traffic migration as customers with both fixed-line and mobile telephones use their mobile devices to make calls to other mobile subscribers.

We believe that major technological innovations, such as instant messaging services and VoIP, may impact local fixed-line traffic in the future. In Brazil, those services have been increasing in popularity, which could put further pressure on the local fixed-line telecommunications market.

Long-Distance Services

The long-distance services market is highly competitive. For the year ended December 31, 2011, based on information available from ANATEL, (1) of the total number of long-distance minutes originated in Region I, we had a market share of 9.1%, ranking behind TIM with 57.4% and Embratel with 29.8%, (2) of the total number of long-distance minutes originated in Region II, we had a market share of 17.4%, ranking behind TIM with 48.0% and ahead of Embratel with 26.1%, and (3) of the total number of long-distance minutes originated in Region III, we had a market share of 10.8%, ranking behind TIM with 34.5%, Telesp with 20.3% and Embratel with 29.0%.

Our principal competitor for long-distance services is TIM, which in 2010 began aggressively promoting its long-distance services with significant discounts. Historically, our principal competitor for long-distance services has been Embratel. As a result of our commencement of mobile services in Region III, we have also begun to compete with Telesp (a subsidiary of Telefónica), which is the incumbent fixed-line service provider in Region III.

Generally, callers placing fixed-line long-distance calls in Brazil tend to select the long-distance carrier affiliated with the provider of their fixed-line service. Similarly, callers placing mobile long-distance calls in Brazil tend to select the long-distance carrier affiliated with the provider of their mobile or fixed-line service. However, increased competition from long-distance service providers has resulted in pressure on our long-distance rates and adversely affected our revenue from these services.

In addition, the offering of plans by other mobile services providers that include free minutes for calls to other subscribers of those mobile services providers may adversely impact our revenues from mobile long-distance calls if our mobile customers migrate to our competitors to remain within the network of the people to whom they plan to place long-distance calls. However, as a result of the increased use of SIM card only strategies by other mobile service providers, there is a trend among Brazilian pre-paid customers to purchase SIM cards from multiple mobile service providers to maximize the number of calls that they can make which are covered by these promotional offers.

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New technologies that serve as an alternative to traditional long-distance telephone calls, such as VoIP, may start to capture part of Brazil s long-distance traffic. However, in contrast to what has occurred in other countries, such as the United States, we do not expect intense competition from VoIP providers in the near term due to (1) the low level of broadband penetration in Brazil due to the population s relatively low per capita income, and (2) the expected adverse effect of the success of this technology on the long-distance call margins of Embratel, which is an affiliate of Net, the main service provider with the ability to offer alternatives through VoIP.

Mobile Services

The mobile telecommunication services market in Brazil is characterized by intense competition among providers of mobile telecommunication services. We compete primarily with the following mobile services providers, each of which provides services throughout Brazil:

Vivo, which is controlled by Telefónica S.A, and which markets its services under the brand name Vivo ;

TIM, which is a subsidiary of Telecom Italia S.p.A. and markets its services under the brand name TIM ; and

Telecom Americas Group, which markets its services under the brand name Claro.

In December 2010, Nextel Brazil acquired licenses to provide 3G services throughout Brazil. Nextel has announced that if expects to launch commercial services on its 3G network in certain markets between June and December 2012. We expect that Nextel s entrance in the market will increase competition for mobile services.

As of December 31, 2011, based on information available from ANATEL, we had a market share of 23.2% of the total number of subscribers in Region I, ranking behind Vivo with 27.2% and TIM with 26.7%, and ahead of Claro with 22.5%, and we captured 19.9% of all net additions of mobile subscribers in Region I (calculated based on the number of mobile subscribers at the end of a period less the number of mobile subscribers at the beginning of that period) during 2011.

As of December 31, 2011, based on information available from ANATEL, we had a market share of 14.2% of the total number of subscribers in Region II, ranking behind Vivo with 30.8%, Claro with 28.6% and TIM with 26.3%, and we captured 9.0% of all net additions of mobile subscribers in Region II during 2011.

As of December 31, 2011, we had a market share of 14.5% of the total number of subscribers in Region III, ranking behind Vivo with 33.0%, Claro with 26.1% and TIM with 26.3%. Based on information available from ANATEL, we captured 16.4% of all net additions of mobile subscribers in Region III during 2011.

Competitive efforts in the Brazilian mobile telecommunication services market generally take the form of handset subsidies in the post-paid market and traffic subsidies in both the pre-paid and post-paid market. The aggressiveness of promotions is generally driven by the desire of the provider offering the promotion to increase market share; however, these promotions generally are for a short duration as the pricing terms offered are not sustainable over the long term.

Competitive efforts in the Brazilian mobile telecommunication services market generally take the form of handset subsidies in the post-paid market and traffic subsidies in both the pre-paid and post-paid market. The aggressiveness of promotions is generally driven by the desire of the provider offering the promotion to increase market share; however, these promotions generally are for a short duration as the pricing terms offered are not sustainable over the long term.

Data Transmission Services

Cable television providers that offer broadband services, particularly Net, represent our principal competition in the broadband market. We face competition from these providers that offer integrated packages, consisting of subscription television, broadband and voice telephone services to cable television subscribers who, in general, have more purchasing power than other consumers.

Our principal competitors in the commercial data transmission services market are Embratel, GVT and Intelig. Because the commercial data transmission services market is significantly less regulated than the fixed-line, long-distance and mobile services markets and, therefore, presents fewer barriers to entry, this market is subject to competition from a large number of competitors, including fixed-line telecommunication service providers and specialized services companies competing in this high-growth market and focused on large- and medium-sized business customers. Along with growth in traffic volume and increasing demand for broadband capacity, we expect significant price reductions in data transmission services as competitors expand their networks. We also anticipate a shift in competition towards value-added services provided over IP platforms.

DTH Services

In Brazil, the high quality programming of television broadcasters has resulted in aggregate ratings for these broadcasters of approximately 90% of viewers and has limited the perceived value of subscription television. As a result, the subscription television market in Brazil has a low penetration compared to developed countries and even to other South American countries such as Argentina, Chile and Mexico. Penetration rates by subscription television have grown from 8.0% of Brazilian households in 2005 to 21.2% in 2011. According to information available from ANATEL, the Brazilian subscription television market grew by more than 30.7% in 2011.

The primary providers of subscription television services in Regions I and II in Brazil are Embratel, which provides DTH service under the Claro TV brand, SKY, which provides DTH services, and Net, which provides subscription television services using coaxial cable. We commenced offering DTH subscription television services to the low-income residential market in the states of Rio de Janeiro, Minas Gerais, Rio Grande do Sul, Paraná and Santa Catarina. In 2010, we expanded this service to the Distrito Federal and the states of Bahia, Sergipe, Pernambuco, Ceará, Paraíba, Rio Grande do Norte, Alagoas, Espírito Santo and Goiás. In 2011, we expanded this service to the remaining states of Regions I and II.

Concessions, Authorizations and Licenses

Under the General Telecommunications Law and ANATEL regulations, the right to provide telecommunication services is granted either through a concession under the public regime or an authorization under the private regime. For additional details regarding the rights and obligations of service providers operating under the public regime and the private regime, see Regulation of the Brazilian Telecommunications Industry Concessions and Authorizations. We operate under:

- a concession to provide local fixed-line services in Region I (other than the 57 municipalities in the State of Minas Gerais that are excluded from the concession area of Region I) and a concession to provide local fixed-line services in Region II (other than the nine municipalities in the States of Goiás, Mato Grosso do Sul and Paraná that are excluded from the concession area of Region II);

- a concession to provide domestic long-distance services in Region I (other than the 57 municipalities in the State of Minas Gerais that are excluded from the concession area of Region I) and a concession to provide domestic long-distance services in Region II (other than the nine municipalities in the States of Goiás, Mato Grosso do Sul and Paraná that are excluded from the concession area of Region II);

- authorizations to provide personal mobile services in Regions I, II and III;

- radio frequency licenses to provide 3G mobile services in Regions I, II and III (other than 23 municipalities in the interior of the State of São Paulo that include the city of Franca and surrounding areas);

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- authorizations to provide local fixed-line services and domestic long-distance services in (1) the 57 municipalities in the State of Minas Gerais that are excluded from the concession area of Region I, (2) the nine municipalities in the States of Goiás, Mato Grosso do Sul and Paraná that are excluded from the concession area of Region II, and (3) Region III;
- authorizations to provide international long-distance services originating anywhere in Brazil;
- authorizations to provide Multimedia Communication Services (*Serviço de Comunicação Multimídia*) throughout Brazil; and
- an authorization to provide DTH satellite television services throughout Brazil.

These concessions and authorizations allow us to provide specific services in designated geographic areas and set forth certain obligations with which we must comply.

Fixed-Line Services Concession Agreements

We have entered into concession agreements with ANATEL that govern our concessions to provide fixed-line services in the Federal District and each of the states of Regions I and II. Each of our concession agreements:

- expires on December 31, 2025;
- sets forth the parameters that govern adjustments to our rates for fixed-line services;
- requires us to comply with the network expansion obligations set forth in the General Plan on Universal Service;
- requires us to comply with certain quality of service obligations set forth in these concession agreements as well as the quality of service obligations set forth in the General Plan on Quality Goals; and
- requires payment of biannual fees equal to 2.0% of our net operating revenue that is derived from the provision of local fixed-line services (excluding taxes and social contributions) during the immediately preceding year.

For more information regarding the adjustment of our rates for fixed-line services, the General Plan on Universal Service and the General Plan on Quality Goals, see Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services.

These concession agreements required us to render services in public telecommunications offices that serve as business centers for low-income populations. In April 2008, these concession agreements were amended to remove the obligation to construct new public telecommunications offices and replace this obligation with obligations to provide transmission lines connecting our fiber-optic internet backbones to municipalities in our concession areas in which we did not provide internet service, which we refer to as backhaul. Under these amendments, we were obligated to set up backhaul in 3,252 municipalities in Regions I and II. The facilities that we constructed to meet these obligations are considered to be property that is part of our concessions and will therefore revert to the Brazilian government on January 1, 2026.

On June 30, 2011, these concession agreements were amended, and we consolidated our previously existing concession agreements for the Federal District and each of the states of Region II in a single concession agreement and our previously existing concession agreements for each of the states of Region I in a single concession agreement. In addition to the terms of our existing obligations under our previously existing local fixed-line concession agreements, the new concession agreements:

remove the restrictions that had been in our local fixed-line concession agreements which had prohibited us from offering subscription television services, such as IP TV, over our fixed-line networks;

- expand the scope of revenue generating activities that we must use to calculate the biannual fees we owed in connection with their concession agreements, while allowing us to apply the amount of such fees to finance the expanded service obligations created by the amended General Plan on Universal Service in lieu of making payment to ANATEL;

- requires us to implement electronic billing systems;

- establishes new conditions under which ANATEL may access information from us;

- removes the grace period during which we could repair systemic service interruptions without incurring fines; and

- requires us to rescind our contracts if ANATEL determines they are contrary to any rules or regulations, economic order or public interest.

These concession agreements provide that ANATEL may further modify their terms in 2015 and 2020 and may revoke them prior to expiration under the circumstances described under Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services Termination of a Concession. The modification right permits ANATEL to impose new terms and conditions in response to changes in technology, competition in the marketplace and domestic and international economic conditions. ANATEL is obligated to engage in public consultation in connection with each of these potential modifications.

Domestic Long-Distance Services Concession Agreements

We have entered into concession agreements with ANATEL that govern our concessions to provide domestic long-distance services originating from the Federal District and each of the states of Regions I and II. Each of our concession agreements:

- expires on December 31, 2025;

- sets forth the parameters that govern adjustments to our rates for domestic long-distance services;

- requires us to comply with certain quality of service obligations set forth in these concession agreements as well as the quality of service obligations set forth in the General Plan on Quality Goals; and

- requires payment of biannual fees equal to 2.0% of our net operating revenue that is derived from the provision of domestic long-distance services (excluding taxes and social contributions) during the immediately preceding year.

For more information regarding the adjustment of our rates for fixed-line services, the General Plan on Universal Service and the General Plan on Quality Goals, see Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services.

On June 30, 2011, these concession agreements were amended, and we consolidated our previously existing concession agreements for the Federal District and each of the states of Region II in a single concession agreement and our previously existing concession agreements for each of the states of Region I in a single concession agreement. In addition to the terms of our existing obligations under our previously existing domestic long-distance concession agreements, the new concession agreements:

- expand the scope of revenue generating activities that we must use to calculate the biannual fees we owe in connection with our concession agreements;

requires us to implement an electronic billing systems;

establishes new conditions under which ANATEL may access information from us;

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removes the grace period during which we can repair systemic service interruptions without incurring fines; and

requires us to rescind our contracts if ANATEL determines they are contrary to any rules or regulations, economic order or public interest.

These concession agreements provide that ANATEL may further modify their terms in 2015 and 2020 and may revoke them prior to expiration under the circumstances described under Regulation of the Brazilian Telecommunications Industry Regulation of Fixed-Line Services Termination of a Concession. The modification right permits ANATEL to impose new terms and conditions in response to changes in technology, competition in the marketplace and domestic and international economic conditions. ANATEL is obligated to engage in public consultation in connection with each of these potential modifications.

Personal Mobile Services Authorization Agreements and Radio Frequency Spectrum Licenses

We have entered into authorization agreements with ANATEL that govern our authorizations to provide personal mobile services in Regions I, II and III. These authorizations permit us to provide personal mobile services for an indeterminate period of time, but do not provide us with the right to use specific radio frequency spectrum.

We hold nine licenses to use radio frequency spectrum to provide 2G services in specific geographic regions of Region II. These licenses grant us permission to use the applicable radio spectrum for 15 years from the date of the authorization agreement under which they are granted and are renewable for additional 15-year terms. Upon renewal of any of these licenses and on every second anniversary of such renewal, we will be required to pay an amount equal to 2.0% of our prior year s net operating revenue from personal mobile services. The initial terms of our radio frequency spectrum licenses expire between 2016 and 2022.

Our authorization agreements are subject to network scope and service performance obligations set forth in these authorization agreements. Under these obligations we are required to (1) service all municipalities in Regions I and II with a population in excess of 100,000, and (2) service all municipalities in Region III with a population in excess of 200,000. In addition, by the fifth anniversary of the date of the authorization agreement for Region III, we will be required to service all municipalities in Region III with a population in excess of 100,000. A municipality is considered serviced when the covered service area contains at least 80% of the urban area in the municipality. Our failure to meet these targets may result in the imposition of penalties established in ANATEL regulations and, in extreme circumstances, in termination of our personal mobile services authorizations by ANATEL. As of the date of this annual report, we have satisfied the network scope and service performance obligations set forth in these authorization agreements.

In August 2007, ANATEL adopted a revision of the personal mobile services regulations that became effective in February 2008. These revised regulations imposed additional obligations on personal mobile services providers, in particular in connection with customers rights. For a discussion of these additional obligations, see Regulation of the Brazilian Telecommunications Industry Regulation of Mobile Services Additional Obligations.

3G Radio Frequency Licenses

We hold five licenses to use radio frequency spectrum to provide 3G services in Regions I, II and III. Each of these licenses grants us permission to use the applicable radio spectrum for 15 years from the date of grant and is renewable for additional 15-year terms. We will be required to pay an amount equal to 2.0% of our prior year s net operating revenue from personal mobile services upon renewal of the license and on every second anniversary of the renewal. The initial terms of these licenses expire in 2023.

These radio frequency licenses include network scope obligations. Under these obligations, we are currently required to (1) provide service to 168 municipalities in Region II that did not have mobile services at the time these licenses were granted with either 2G or 3G mobile telecommunication services, and (2) provide 3G service to all state capitals in Region II, the Federal District and all municipalities with a population in excess of 500,000 inhabitants. In addition, we will be required to:

provide 3G service to all of municipalities covered by these licenses with a population in excess of 200,000 by the fourth anniversary of the date of these licenses;

- provide 3G service to all of the municipalities covered by these licenses with a population in excess of 100,000 by the fifth anniversary of the date of these licenses;

- provide 3G service to 50% of all of the municipalities with a population between 30,000 and 100,000 by the fifth anniversary of the date of these licenses; and

- provide 3G service to 60% of the municipalities, including 242 specified municipalities, covered by these licenses with a population less than 30,000 by the eighth anniversary of the date of these licenses.

A municipality is considered serviced when the covered service area contains at least 80% of the urban area in the municipality. Our failure to meet these targets may result in the imposition of penalties established in ANATEL regulations and, in extreme circumstances, in termination of our 3G frequency licenses by ANATEL. As of the date of this annual report, we have satisfied the network scope and service performance obligations set forth in these licenses.

Fixed-Line Services Authorization Agreements

We have entered into authorization agreements with ANATEL that govern our authorizations to provide local fixed-line services in and domestic long-distance services originating from (1) the 57 municipalities in the State of Minas Gerais that are excluded from the concession area of Region I, (2) the nine municipalities in the States of Goiás, Mato Grosso do Sul and Paraná that are excluded from the concession area of Region II, and (3) Region III. These authorizations do not have termination dates and require us to comply with certain quality of service obligations set forth in the General Plan on Quality Goals.

We have also entered into authorization agreements with ANATEL that govern our authorizations to provide international long-distance services originating from anywhere in Brazil. These authorizations do not have termination dates and require us to comply with quality of service obligations set forth in the General Plan on Quality Goals.

Multimedia Communication Services Authorization Agreements

We have a Multimedia Communication Services authorizations, which superseded our prior Telecommunications Network Transportation Services (*Serviço de Rede de Transporte de Telecomunicações*) authorizations, permitting us to provide high speed data service.

The Multimedia Communication Services authorizations became effective in May 2003 and cover the same geographical areas as our concession agreements. In April 2008, in connection with the amendments to our fixed-line services concessions, we agreed to provide internet service free of charge until December 31, 2025 to all urban schools in the areas of our concession agreements.

Term of Commitment to Adhere to National Broadband Plan

On June 30, 2011, we entered into a Term of Commitment (*Termo de Compromisso*) with ANATEL and the Ministry of Communications to formalize our voluntary commitment to adhere to the terms of the National Broadband Plan, created in May 2010 by Executive Decree No. 7,175/10 with the goal to make broadband access available at low cost, regardless of technology, throughout Brazil. Pursuant to the Term of Commitment, we are required to offer (1) broadband services with minimum upload and download capabilities to retail customers in certain sectors of Region I and II for a maximum price of R$35 per month (or R$29.90 in ICMS-exempt states), plus fees, and (2) access to our broadband infrastructure to certain wholesale customers, including small businesses and

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municipalities, in certain sectors of Region I and II for a maximum price of R$1,253 per 2 Mbps per month and a one-time installation fee, while observing all quality standards under ANATEL regulations. Both retail and wholesale services are subject to certain network capacity limits and need only be provided at the demand of the customer. The services provided under the Term of Commitment may be implemented gradually, beginning in November 2011, although we are obligated to make services available to 100% of eligible retail and wholesale customers by December 31, 2014 and June 30, 2013, respectively. The Term of Commitment also requires that we:

- provide one public internet access point for the first 20,000 inhabitants and one additional access point for each subsequent 10,000 inhabitants, with a limit of six access points, at a speed of 2 Mbps, in each municipality that has only satellite service, free of charge and upon demand of such municipality;

- adequately advertise the services contemplated by the Term of Commitment and present to the Ministry of Communications semi-annual reports detailing our marketing efforts; and

- make our best efforts to offer broadband services to retail customers at speeds of up to 5 Mbps, reaching the largest possible number of municipalities by 2015.

The Term of Commitment will expire on December 31, 2016.

DTH Authorization Agreement

In November 2008, we entered into an authorization agreement with ANATEL that governs our use of satellite technology to provide DTH satellite television services throughout Brazil. The authorization agreement permits us to provide DTH satellite television services for 15-years and is renewable for an additional 15 year term in exchange for a fee to be agreed upon between us and ANATEL.

Under this authorization, we are required to furnish equipment to certain public institutions, to make channels available for broadcasting by specified public institutions, and to comply with quality of service obligations set forth in applicable ANATEL regulations.

Capital Expenditures

Our capital expenditures on property, plant and equipment and intangible assets were R$1,297 million in 2011, R$889 million in 2010 and R$1,090 million in 2009. The following table sets forth our capital expenditures on plant expansion and modernization for the periods indicated.

	Year Ended December 31, (in millions of *reais*)		
	2011	2010	2009
Mobile network and systems	R$ 96	R$ 150	R$ 444
Data transmission equipment	443	146	170
Voice transmission	212	260	174
Telecommunication services infrastructure	58	43	15
Information technology services	60	55	63
Backbone transmission	25	21	66
Network management system equipment	13	45	3
Buildings, improvements and furniture	6	3	9
Submarine cables	15	52	69
Internet services equipment	12	33	17
Other	357	81	60
Total capital expenditures	1,297	889	1,090
(Unpaid) amount and cash outflow to settle previously recorded liabilities	(413)	(134)	307

Total capital expenditures according to the cash flow statement	R$ 884	R$ 755	R$ 1,397

TNL s capital expenditures on property, plant and equipment and intangible assets on a consolidated basis were R$4,959 million in 2011, R$2,947 million in 2010 and R$4,859 million in 2009. The following table sets forth TNL s capital expenditures on plant expansion and modernization for the periods indicated.

	Year Ended December 31,		
	2011	2010	2009
	(in millions of *reais*)		
Mobile network and systems	R$ 952	R$ 703	R$ 2,447
Data transmission equipment	1,497	500	698
Voice transmission	870	740	1,120
Telecommunication services infrastructure	571	296	304
Information technology services	286	221	157
Other	783	487	133
Total capital expenditures	4,959	2,947	4,859
Amount paid and cash outflow to settle previously recorded liabilities	150	625	882
Total capital expenditures according to the cash flow statement	R$ 5,109	R$ 3,572	R$ 5,741

Number Portability

We implemented the systems necessary for us to comply with ANATEL s number portability requirements. This project was commenced in September 2008 and was completed in March 2009. The total cost of this was R$163 million.

Upgrade of Our Core Mobile Network

In February 2010, we completed a project to upgrade our core mobile network, with the primary goal of fully integrating our mobile network into the mobile network of Telemar. We engaged Nokia Siemens Networks to replace our existing core mobile network, which relied on technology from Ericsson, with a new core mobile network that uses the same Nokia Siemens Networks technology employed in Telemar s existing core mobile network to facilitate the integration of our networks. The total cost of this project was R$131 million.

Ongoing Capital Expenditures

Our principal capital expenditures relate to a variety of projects designed to expand and upgrade our mobile telephone networks, our voice transmission networks, our data transmission networks, our subscription television services, and our telecommunications infrastructure and information technology equipment.

Mobile Services Network

We have undertaken a project to upgrade a portion of our mobile networks to enable us to increase the capacity of our mobile network by approximately 10 million subscribers. We plan to support the growth of our subscriber base by constructing 205 new radio base stations and expanding the capacity at many of our existing radio base stations. In addition, we have undertaken a project to replace approximately 2,265 of our radio base stations, all of which previously employed Alcatel-Lucent technology, with Huawei base stations. We expect to complete the replacement of these radio base stations by December 2012. Our total investment in these projects was R$498 million in 2009, R$151 million in 2010 and R$100 million in 2011.

We plan to deploy new base stations and transceivers to improve our 3G coverage and quality in areas which we already serve, reducing the level of signal congestion in these areas, and to expand our 3G service to municipalities in Regions I, II and III where we currently do not provide 3G service. We are also investing in equipment to support the introduction of wireless local loop technology which will provide service to our customers through our GSM network in areas not supported by our fixed-line network. We are continuing to upgrade portions of our mobile networks to support greater data rates through the HSPA+ standard. We are in the final phases of testing of Long Term Evolution technology as a solution for the evolution of our mobile network.

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Voice Transmission Network

We are investing in new equipment for our switching station to support next-generation networks to support offerings of new value-added services to our fixed-line customers. We believe that our investment in next-generation networks will (1) assist us in meeting the increased demand for long distance traffic, both domestic and international, through the use of VoIP, (2) will permit us to offer differentiated services, such voice over broadband, and (3) significantly promote fixed-mobile convergence. In addition, we are undertaking a program of removing and replacing smaller switching stations and integrating these operations with other switching stations to promote efficiency in our operations. In addition, we monitor the anticipated demands of new residential developments and the service demand growth of existing residential areas to ensure that we adequate network equipment is available to service the demands of these areas.

Data Transmission Network

We are investing in the acquisition and installation of data communications equipment to replace our ATM network with Ethernet and IP technologies. During 2012, we expect to deploy IP routers and multi-protocol label switching nodes along the main ATM core in each of our service regions. Following this deployment, we expect to begin migrating our customers to the new routers.

In addition, we are investing in our ultra broadband project, through which we expect to increase the availability of high-speed internet access services as part of Brazil s National Broadband Plan.

Telecommunications Infrastructure and Information Technology Equipment

We are investing in the expansion of the network operating platform supporting our network operations center to assist us in monitoring transmission failures in real time and assist us in correlating and integrating data related to these transmission failures to their root causes with the aim of reducing the frequency of these events.

We are investing in the expansion of our transport networks in an effort to ensure that our networks continue to have the capacity to serve our existing customers and to support our plans to expand our services. Among other investments, we are investing in the expansion of our national backbone to support the expansion of 3G services and new services, the expansion of our satellite network, taking measures to improve our network synchronization and signaling links, taking measures to improve our interconnection traffic, investing in projects to improve route optimization.

We are also investing in projects to improve our networks by increasing the redundancy of our wire and fiber optic cable routes and establishing new linear and ring routes. We also perform preventive maintenance on sections of our network that have unusually high failure rates, and have a program to replace network elements in these sections.

We are investing in the expansion of capacity of our servers dedicated to our corporate customers with a view to increasing the efficiency of the services that we provide to these customers.

We are investing in the standardization of our facilities to deter fraud and improve the quality of our services, including the replacement of some of our public telephones.

2012 Capital Expenditure Budget

Our 2012 capital expenditure budget totals approximately R$6.0 billion. We plan to finance such expenditures through operating cash flows and long-term financings. From this total, we have budgeted 16% of our 2012 capital expenditure budget for the mobile telephone services business, 16% for voice transmission, including capital expenditures necessary to meet our regulatory targets, 29% for data transmission equipment, including equipment for broadband services, 10% for telecommunications services infrastructure, 7% for information technology services, and 2% for the IPTV business, including capital expenditures for fiber-to-the-home infrastructure, broadband and VOIP services.

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Research and Development

We conduct independent innovation, research and development in areas of telecommunication services but historically we have not independently developed new telecommunications technologies. We depend primarily on suppliers of telecommunications equipment for the development of new technology.

As a condition to ANATEL s approval of Telemar s acquisition of control of our company in January 2009, Telemar agreed to make annual investments in innovation, research and development through 2018 in amounts equal to at least 50% of the amounts of its contributions to the Telecommunications Technology Development Fund (*Fundo para o Desenvolvimento Tecnológico das Telecomunicações*), or the FUNTTEL. To fulfill this obligation, as well as to centralize our innovation, research and development activities and programs, in 2009, we have created a division to manage innovation, research and development with the mission of coordinating and promoting efforts and projects that it develops.

Our technology laboratory performs a variety of functions, such as operation support systems, business support systems and information security. We conduct trials of technologies from different vendors in this laboratory to evaluate these technologies for deployment.

Since 2009, we has executed cooperation agreements with the following national research centers: CERTI Foundation, C.E.S.A.R., Technological Projects, Research and Studies Coordination Foundation (*Fundação Coordenação de Projetos, Pesquisas e Estudos Tecnológicos COPPETEC*), Telecommunications Research and Development Foundation (*Fundação Centro de Pesquisa e Desenvolvimento em Telecomunicações - CPqD*), Technological Innovation Foundation (*Fundação Para Inovações Tecnológicas FITEC*), National Institute for Telecommunications Foundation (*Fundação Instituto Nacional de Telecomunicações Inatel*) and PUC-RJ. We have also executed cooperation agreements with Brazilian national telecommunication suppliers which develop technology in Brazil, such as AsGa S.A., Digitel S.A. Indústria Eletrônica and Padtec S.A.

In order to achieve our goals on innovation investments, in 2011, we intensified the process for the exploration of innovative services and activities concerning innovation, research and development to promote our innovation ecosystem and in October 2011 launched the first call for Innovative Mobile Applications for Major Events through the Oi Innovation Program (*Programa Oi Inovação*).

Our investments in innovation, research and development totaled R$0.4 million in 2009, R$2 million in 2010, and R$23 million in 2011, and the investment of TNL in innovation, research and development on a consolidated basis totaled R$83 million in 2009, R$99 million in 2010 and R$122 million in 2011.

Property, Plant and Equipment

Our principal properties, owned and leased, are located in Regions I and II. At December 31, 2011, the net book value of our property, plant and equipment was R$5,793 million and the net book value of TNL s property, plant and equipment on a consolidated basis was R$23,294 million. Our main equipment consists of transmission equipment, trunking and switching stations (including local, tandem and transit telephone exchanges), metallic and fiber-optic cable networks and lines, underground ducts, posts and towers, data communication equipment, network systems and infrastructure (including alternating and direct current supply equipment) and motor-generator groups.

As of December 31, 2011, of the net book value of our property, plant and equipment transmission equipment represented 47.6%; construction in progress represented 17.3%; infrastructure, primarily underground ducts, post and towers, cables and lines represented 16.9%; buildings represented 6.8%, plant and equipment related to switching stations represented 5.8%; and other fixed assets represented 5.6%.

As of December 31, 2011, of the net book value of TNL s property, plant and equipment on a consolidated basis transmission equipment represented 42.3%; infrastructure, primarily underground ducts, post and towers, cables and lines represented 21.8%; construction in progress represented 15.1%; plant and equipment related to switching stations represented 9.5%; buildings represented 6.5%; and other fixed assets represented 4.9%.

All property, plant and equipment that are essential in providing the services described in our concession agreements are considered reversible assets, which means that, should our concession agreements expire or terminate without being renewed, these assets will automatically revert to ANATEL. There are no other encumbrances that may affect the utilization of our property, plant and equipment. For more details, see note 17 to our consolidated financial statements.

Intellectual Property

We believe the trademarks that identify us and our businesses are important for us, and as a result, we have taken steps to protect them. At December 31, 2011, we had 171 trademarks registered with the National Institute of Industrial Property (*Instituto Nacional de Propriedade Industrial*), or INPI, and 273 pending trademark applications, and TNL and its subsidiaries, including our company, had 803 trademarks registered with the INPI and 667 pending trademark applications. Our main trademark, *Oi*, is registered with the INPI in several classes, which allows us to use this trademark in a variety of markets in which we operate, including in connection with our fixed-line, mobile and broadband services. Among the various trademarks we have registered with the INPI, two are being contested by third parties, and 12 of the trademarks TNL and its subsidiaries, including our company, has registered with the INPI are being contested by third parties. In addition, of our 273 pending trademark applications, six have been challenged by third parties, and of the 667 pending trademark applications of TNL and its subsidiaries, including our company, 83 have been challenged by third parties.

As of December 31, 2011, we had 837 domain names and TNL and its subsidiaries, including our company, had 1,034 domain names registered with the Center of Information and Coordination of Dot Br NIC. Br, an agency responsible for registering domain names in Brazil. The information included on our websites or that might be accessed through our websites is not included in this annual report and is not incorporated into this annual report by reference.

As of December 31, 2011, we the INPI had granted one patent to our company. We had also filed eight patent applications, which are pending with the INPI. Requests for technical examination have been submitted to the INPI for all of these pending patent applications. Once examination is concluded, a decision accepting or rejecting the application will be issued. If granted, the patent will have a term of 20 years from the date of filing and no less than ten years from the date the application is granted.

Insurance

Pursuant to requirements in our concession agreements, we maintain the following insurance policies: (1) all risk property insurance covering all insurable assets pertaining to the concessions; (2) loss of profit insurance covering lost profits deriving from property damage and business interruption; and (3) performance bond insurance to assure compliance with our obligations related to quality of service and universal service targets set forth in our concession agreements.

In addition to the above policies, we maintain civil liability insurance. Our assets that are of material value and/or exposed to high degrees of risks are also insured. All of our insurance coverage was purchased from established insurance companies in Brazil, such as Bradesco and Itaú Seguros.

We believe that our current insurance coverage is suitable to our operations.

Social Responsibility

Oi Futuro is a non-profit institution that organizes our social responsibility activities, including social projects that foster education, the environment, sports and culture. The aim of *Oi Futuro* is to democratize access to knowledge, in order to accelerate and promote human development.

During the ten years since its inception, *Oi Futuro* has aided more than four million people through programs such as *Oi Tonomundo*, which provides broadband internet access to computer laboratories in public schools, *NAVE* Advanced Education Nucleus, *Oi Kabum!* Schools of Arts and Technology, *Oi Novos Brasils* (new Brazils), which lends support to social projects developed by nonprofit organizations, the Cultural Sponsorships Program, the Incentivized Sports Sponsorship and the Oi Environmental Projects Program. We also maintain, in partnership with the Brazilian government, the Broadband Program in Schools, which as of December 2011, provided high speed internet access to more than 49,800 urban public schools.

We contributed R$31 million to *Oi Futuro* in 2011, R$28 million in 2010 and R$28 million in 2009.

Regulation of the Brazilian Telecommunications Industry

Overview

Our business, including the nature of the services we provide and the rates we charge, is subject to comprehensive regulation under the General Telecommunications Law and a comprehensive regulatory framework for the provision of telecommunication services promulgated by ANATEL. We provide fixed-line, domestic and international long-distance and mobile telecommunication services under concessions, authorizations and licenses that were granted by ANATEL and allow us to provide specified services in designated geographic areas, as well as set forth certain obligations with which we must comply. See Concessions, Authorizations and Licenses.

ANATEL is a regulatory agency that was established in July 1997 pursuant to the General Telecommunications Law and the *Regulamento da Agência Nacional de Telecomunicações*. ANATEL oversees our activities and enforces the General Telecommunications Law and the regulations promulgated thereunder. ANATEL is administratively independent and is financially autonomous. ANATEL is required to report on its activities to the Brazilian Ministry of Communications. ANATEL has authority to propose and to issue regulations that are legally binding on telecommunication service providers. ANATEL also has the authority to grant concessions and licenses for all telecommunication services, other than broadcasting services. Any regulation or action proposed by ANATEL is subject to a period of public comment, which may include public hearings, and ANATEL s decisions may be challenged administratively before the agency itself or through the Brazilian judicial system.

Concessions and Authorizations

Under the General Telecommunications Law and ANATEL regulations, the right to provide telecommunication services is granted either through a concession under the public regime (as discussed below) or an authorization under the private regime (as discussed below). A concession is granted for a fixed period of time following a public auction and is generally renewable only once. An authorization is granted for an indeterminate period of time and public auctions are held for some authorizations. These concessions and authorizations allow service providers to provide specific services in designated geographic areas, set forth certain obligations with which the service providers must comply and require equal treatment of customers by the service providers.

The four principal providers of fixed-line telecommunication services in Brazil, Telemar, Oi, Telesp and Embratel, provide these services under the public regime. In addition, CTBC and Sercomtel, which are secondary local fixed-line telecommunication service providers, operate under the public regime. All of the other providers of fixed-line telecommunication services and all providers of personal mobile services and data transmission services in Brazil operate under the private regime.

Providers of public regime services are subject to more obligations and restrictions than providers of private regime services. Under Brazilian law, providers of public regime services are subject to certain requirements with respect to services such as quality of service, continuity and universality of service, network expansion and network modernization. Additionally, the rates that public regime service providers may charge customers are subject to ANATEL supervision.

Providers of private regime services, although not generally subject to the requirements concerning continuity and universality of service and network modernization, are subject to certain network expansion and quality of service obligations set forth in their respective authorizations.

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Regulation of Fixed-Line Services

General Policies for the Regulation of the Fixed-Line Telecommunications Sector

In June 2003, Brazil s president issued Decree No. 4,733, outlining a number of new rules and guidelines which were intended to consolidate several changes in the regulation of Brazil s fixed-line telecommunications sector. This decree sets forth general declarations of policy regarding, among other things:

- universal access to telecommunication services;
- stimulation of employment and development of the Brazilian telecommunications sector;
- promotion of competition and adoption of rate readjustment policies that take into account Brazilian socioeconomic considerations; and
- the financial equilibrium of existing concession agreements.

This decree also defined certain changes that are reflected in the concession agreements entered into by providers of public regime services that became effective on January 1, 2006.

A number of bills affecting telecommunications policy have been submitted to the Brazilian Congress with an aim to make telecommunication services more accessible to Brazil s low-income population. These bills have proposed to (1) eliminate the monthly subscription fee *(assinatura mensal)* that compensates telecommunication companies for extending and maintaining fixed-line telecommunication services for their customers, and (2) impose inexpensive fixed-line telephone plans *(telefone social)* that telecommunications companies would be required to provide to certain eligible low-income residential customers. If approved, we expect that these types of proposals will adversely affect the overall margin of telecommunications providers, including us. For a discussion of the legal and regulatory risks associated with our business, see Item 3. Key Information Risk Factors Risks Relating to Our Company and the Brazilian Telecommunications Industry Our industry is highly regulated. Changes in laws and regulations may adversely impact our business.

Private Regime Authorizations

With the goal of introducing competition in fixed-line telephone services in Brazil, the federal government granted four private-regime authorizations in 1999 to permit fixed-line service providers to compete with the incumbent fixed-line concessionaires. Since 2002, the number of authorizations to provide fixed-line services that the federal government may issue is unlimited.

Public Regime Concessions

Each of the public regime service providers operates under concession agreements that expire in December 2025. Under these concession agreements, each of the public regime service providers is required to comply with the provisions of (1) the General Plan on Universal Service that was adopted by ANATEL in June 2003, (2) the General Plan on Quality Goals that was adopted by ANATEL in June 2003, and (3) the General Plan on Competition Targets, which, as of the date of this annual report, has not yet been adopted by ANATEL. The General Plan on Competition Targets was submitted for public consultation in July 2011 and the public consultation period ended on October 23, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012. For more information on the proposed General Plan on Competition Targets, see General Plan on Competition Targets.

The concession agreements provide that ANATEL may modify their terms in 2015 and 2020 and may revoke them prior to expiration under the circumstances described below under Termination of a Concession. The modification right permits ANATEL to impose new terms and conditions in response to changes in technology, competition in the marketplace and domestic and international economic conditions. ANATEL is obligated to engage in public consultation in connection with each of these potential modifications.

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Rate Regulation

Public regime service providers must offer a basic service plan comprised of the following basic services: (1) installation; (2) monthly subscription; and (3) switched local minutes. Modifications of the rates charged for these basic services are determined by reference to a local rate basket that represents the weighted average of the rates for monthly subscriptions and switched local minutes. Rates for long-distance services originated and terminated on fixed lines vary in accordance with three basic criteria: (1) physical distance separating callers; (2) time of the day; and (3) day of the week on which the call is placed. Modifications of the rates charged for these long-distance services are determined by reference to a long-distance rate basket that represents the weighted average of the rates for long-distance calls. The rates for the provision of services through payphones and installation rates are treated separately. The rates for international long-distance services provided by Embratel, the incumbent international long-distance concessionaire, are regulated by ANATEL. However, the rates for international long-distance services charged by other long-distance service providers, all of whom provide these services under authorizations rather than concessions, are not subject to ANATEL regulation.

The concession agreements establish a price-cap mechanism for annual rate adjustments for basic service plans and domestic long-distance rates based on formulas set forth in each provider s concession agreement. The formula provides for two adjustments to the price cap based on the local rate basket, the long-distance rate basket and the use of a price index. The price cap is first revised upward to reflect increases in inflation, as measured by an index, then ANATEL applies a productivity discount factor, or Factor X, which reduces the impact of the rate readjustment provided by the index.

Prior to 2008, Factor X, which was discounted from the IST, was equal to 50% of the increase in a public regime provider s productivity. Beginning in 2008, ANATEL has calculated the sector s weighted average productivity rate. As of the date of this annual report, Factor X is equal to (1) 50% of the increase in the weighted average productivity rate of public regime providers, plus (2) a factor calculated by ANATEL that is designed to reflect cost optimization targets for the telecommunications industry as a whole. If the weighted average productivity rate is negative, ANATEL will not allow an annual adjustment in excess of the IST.

ANATEL has proposed new regulations under which it would modify the Factor X applicable to the determination of rate increases available to public concessionaires providing fixed-line services. These regulations were submitted for public consultation in July 2011 and the public consultation period ended on September 1, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012.

A provider may increase rates for individual services within the local rate basket or the long-distance rate basket by up to 5% more than the IST so long as the rates for other services in that rate basket are reduced to the extent necessary to ensure that the weighted average increase for the entire rate basket does not exceed the permitted annual rate adjustment.

A provider may also offer alternative plans in addition to the basic service plan. Alternative plans must be submitted for ANATEL s approval. The rates offered under the alternative plans may be adjusted annually based on the IST.

For information on our rates and service plans, see Rates.

General Plan on Universal Service

The General Plan on Universal Service was approved by ANATEL in June 2003 and became effective in January 2006. The General Plan on Universal Service sets forth the principal network expansion and modernization obligations of the public regime providers, such as providing public telephones in localities with a population in excess of 100, and installing residential fixed lines within seven days of a request in localities with a population in excess of 300. In addition, public regime providers must comply with the Special Individual Access Class (*Acesso Individual Classe Especial*) rules, which are designed to require service for economically disadvantaged people. Under the Special Individual Access Class rules, a qualifying customer may subscribe to a service plan, limited to one fixed-line per household, and pay a lower monthly fee for service than under the basic service plans.

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Public regime providers are also subject to network expansion requirements under the General Plan on Universal Service, which are revised by ANATEL from time to time. No subsidies or other supplemental financings are anticipated to finance our network expansion obligations. Our failure to meet the network expansion and modernization obligations established by the General Plan on Universal Service or in our concession agreements may result in fines and penalties of up to R$50 million, as well as potential revocation of our concessions.

On June 30, 2011, the General Plan on Universal Service was amended. Among other things, these amendments:

- expanded the obligations of local fixed-line service providers to provide individual access to fixed-line voice services to economically disadvantaged segments of the Brazilian population within their service areas, through programs to be established and regulated by ANATEL;

- reduced the density requirements applicable to the obligations of local fixed-line service providers to provide public telephones in urban areas within their service areas; and

- expanded the obligations to provide universal service in rural and remote areas of local and long-distance fixed-line providers that obtain authorizations to use radio spectrum in the 450 Mhz band, including increased obligations to provide individual and group access to fixed-line voice services.

Unbundling of Local Fixed-Line Networks

On May 2004, ANATEL issued an order establishing rules for partial unbundling of the local fixed-line networks of the public regime service providers, which we refer to as line sharing, and requiring the eventual full unbundling of local fixed-line networks, which will entail these providers making their entire networks available to other telecommunication service providers. This order (1) establishes a time by which service providers must comply with the order to provide such access, (2) limits the rates service providers can charge for line sharing, and (3) addresses related matters such as co-location space requirements. Co-location means that a service provider requesting unbundling may place its switching equipment in or near the local exchange of the service provider whose network the requesting service provider wishes to use and may connect to the network at this local exchange.

This regulation was designed to increase competition in the local fixed-line and broadband internet access markets by making it easier for new telecommunication service providers operating under either the public or private regime to enter these markets and for existing service providers to provide new services or enter new regions.

As of the date of this annual report, ANATEL has not yet adopted final unbundling rules or rates for full unbundling, although ANATEL has proposed a General Plan on Competition Targets, which addresses a variety of matters, including regulations related to partial unbundling and/or full unbundling of the local fixed-line networks of the public regime service providers. The General Plan on Competition Targets was submitted for public consultation in July 2011 and the public consultation period ended on October 23, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012. We expect that the rates that we would receive from other telecommunication services providers accessing our fixed-line networks under these regulations, if adopted, will be lower than the rates we currently charge our customers for providing fixed-line and broadband internet services.

Service Restrictions

Pursuant to regulations in effect as of the date of this annual report, public regime providers are subject to certain restrictions on alliances, joint ventures and mergers and acquisitions with other public regime providers, including:

- a prohibition on holding more than 20% of the voting shares of more than one other provider of public regime services; and

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- a restriction on mergers between regional fixed-line service providers.

In December 2010, ANATEL adopted new regulations eliminating the limitation on the number of authorizations to provide subscription television services. In September 2011, the Brazilian congress passed Law No. 12,485, which was signed into law by the President of Brazil in September 2011. Law No. 12,485 creates a new legal framework for subscription television services in Brazil, replacing and unifying the previously existing regulatory provisions that governed various forms of subscription television services, such as cable television, Multichannel Multipoint Distribution Service, or MMDS, and DTH. The principal provisions of Law No. 12,485:

- allow fixed-line telephone concessionaires, such as us, who previously were allowed to provide subscription television services using only MMDS and DTH technologies, to enter the cable television market in Brazil;
- remove existing restrictions on foreign capital investments in cable television providers;
- establish minimum quotas for domestic content programming on every television channel;
- limit the total and voting capital held by broadcast concessionaires and authorized providers, and in television programmers and producers, with headquarters in Brazil to 30%; and
- prohibit telecommunications service providers with collective interests from acquiring rights to disseminate images of events of national interest and from hiring domestic artistic talent.

The framework established by Law No. 12,485 is expected to increase the availability and lower the price of subscription television services in Brazil, through increased competition among providers, and improve the quality, speed and availability of broadband internet services as a result of the expected proliferation of fiber optic cables used to transmit cable television.

In March 2012, ANATEL adopted new regulations under which the authorizations to provide various existing subscription television services have been consolidated into authorizations to provide a newly-defined service called Conditional Access Service. Under these regulations, authorizations to provide Conditional Access Service will apply to private telecommunications services, the receipt of which are conditioned on payment by subscribers, for the distribution of audiovisual contents in the form of packages, individual channels and channels with required programming, by means of any communications technology, processes, electronic means or protocols. An authorization granted by ANATEL to provide Conditional Access Service will be valid for the entire Brazilian territory, however, the provider must indicate in its application for an authorization the localities that it will service.

Termination of a Concession

ANATEL may terminate the concession of any public regime telecommunication service provider upon the occurrence of any of the following:

- an extraordinary situation jeopardizing the public interest, in which case the Brazilian government is authorized to start rendering the services set forth under the concession in lieu of the concessionaire, subject to congressional authorization and payment of adequate indemnification to the owner of the terminated concession;
- termination by the provider (through an agreement with ANATEL or pursuant to legal proceedings) as a consequence of an act or omission of the Brazilian government that makes the rendering of the services excessively burdensome to the provider;
- annulment of the concession due to a contractual term, which is deemed by subsequent law to be illegal;

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material failure to comply with the provider s universalization targets;

failure to meet insurance requirements set forth in the concession agreement;

a split-up, spin-off, amalgamation, merger, capital reduction or transfer of the provider s control without ANATEL s authorization;

the transfer of the concession without ANATEL s authorization;

the dissolution or bankruptcy of the provider; or

an extraordinary situation in which Brazilian government intervention, although legally permissible, is not undertaken, as such intervention would prove to be inconvenient, unnecessary or would result in an unfair benefit to the provider.

In the event a concession is terminated, ANATEL is authorized to administer the provider s properties and its employees in order to continue rendering services.

General Plan on Quality Goals

The General Plan on Quality Goals was approved by ANATEL in June 2003 and became effective in January 2006. Each fixed-line service provider operating under the public regime or the private regime must comply with the provisions of the General Plan on Quality Goals. All costs related to compliance with the quality goals established by the General Plan on Quality Goals must be borne exclusively by the service provider. The General Plan on Quality Goals establishes minimum quality standards with regard to:

modernization of the network;

responses to repair requests;

responses to change of address requests;

rate of call completion;

operator availability;

availability of services to customers;

personal services to customers;

issuance of bills;

- responses to mail received from customers; and

- quality of public telephones.

These quality standards are measured according to the definitions and quality indicators established by ANATEL. Every month, fixed-line service providers are required to report their compliance with quality goals to ANATEL. Additionally, they are obligated to provide ANATEL with an in-depth report and analysis on each quality goal that is not satisfied. ANATEL may also collect such data from fixed-line service providers at any time without prior notice. Fixed-line service providers that fail to meet quality goals established by ANATEL may be subject to warnings, fines, intervention by ANATEL, temporary suspensions of service or cancellation of their concessions and authorizations.

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ANATEL measures the performance of fixed-line service providers in each individual state in which they operate. As a result, the performance of fixed-line service providers in any particular state may not meet one or more quality performance targets even if such service provider s overall performance is satisfactory. Therefore, fixed-line service providers, including us, could be subject to fines or penalties as a result of the failure to meet the quality performance targets in one or more particular states.

Our failure to meet the quality of service obligations established by the General Plan on Quality Goals or in our concession agreements may result in fines and penalties of up to R$40 million.

General Plan on Competition Targets

ANATEL has proposed a General Plan on Competition Targets, which contemplates the creation of three entities to manage information about telecommunications networks, act as an intermediary in contracts between telecommunications providers and supervise the offering of wholesale and retail data traffic services. The proposed General Plan on Competition Targets also addresses a variety of other matters, including criteria for the evaluation of telecommunications providers to determine which providers have significant market power, regulations applicable to the wholesale markets for trunk lines, backhaul, access to internet backbone and interconnection services, and regulations related to partial unbundling and/or full unbundling of the local fixed-line networks of the public regime service providers. The General Plan on Competition Targets was submitted for public consultation in July 2011 and the public consultation period ended on October 23, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012.

Regulation of Mobile Services

In September 2000, ANATEL adopted regulations that established operating rules for providers under the personal mobile service (*Serviço Móvel Pessoal*) regime. The regulations permitted ANATEL to grant authorizations to provide mobile telecommunication services under the personal mobile service regime. For purposes of the personal mobile service regulations, Brazil is divided into three service regions covering the same geographic areas as the concessions for fixed-line telecommunication services.

Under the personal mobile service regulations:

- Band A and Band B service providers can apply for an additional frequency range;
- each service provider may apply to provide domestic and international long-distance services originating from its service region;
- existing service providers, as well as new entrants into the Brazilian telecommunications market, may bid for new licenses in all frequency bands, other than Band A and Band B;
- personal mobile services providers are required to offer a basic service plan to their customers containing certain prescribed features;
- personal mobile services providers are required to establish interconnection rates for the use of one provider s network by another provider;
- the number of regions in which a personal mobile services provider may offer services is not limited; and
- a personal mobile services provider, or its controlling shareholders, may not hold more than one personal mobile services authorization covering any specific region.

Auction of Personal Mobile Services Spectrum

Prior to the establishment of the personal mobile services regime, ANATEL had granted licenses to mobile services providers to operate in each region of Brazil using Bands A and B. In 2001 and 2002, ANATEL successfully auctioned authorizations and licenses to operators in Band D and Band E in each region. TNL was granted its initial authorization to provide personal mobile services in Region I and a license to operate in Band D in March 2001. We were granted our initial authorization to provide personal mobile services in Region II and a license to operate in Band E in December 2002.

ANATEL conducted additional auctions of radio frequency licenses in 2004 and 2006. In April 2004, we acquired an additional license to operate in Region II.

In December 2007, ANATEL auctioned the remaining spectrum of Bands A, B, C, D and E to existing service providers as extension blocks and auctioned additional spectrum in Band M (1.8 GHz) and Band L (1.9 GHz). In these auctions, TNL acquired (1) an authorization to provide personal mobile services in the State of São Paulo and licenses to operate using Band M throughout the State of São Paulo and Band E outside of the city of São Paulo and (2) licenses to use additional spectrum in 12 states in Region I.

Auction of 3G Spectrum

In preparation for auctions of spectrum in Bands F, G, I and J (2.1 GHz), the use of which allows personal mobile services providers to offer 3G services to their customers, ANATEL issued regulations that divide the Brazilian territory into nine regions for purposes of operations using these frequency bands. In December 2007, ANATEL auctioned radio frequency licenses to operate on each of these frequency bands in each of the nine regions and the related licenses to use these frequency bands. In this auction, we acquired the radio frequency licenses necessary to offer 3G services in two of the nine regions delineated by ANATEL for 3G services (corresponding to Regions II under the personal mobile services regime) and TNL acquired radio frequency licenses necessary to offer 3G services in six of the nine regions delineated by ANATEL for 3G services (corresponding to Regions I and III under the personal mobile services regime, other than an area that consists of 23 municipalities in the interior of the State of São Paulo that includes the city of Franca and surrounding areas).

Authorizations to Use 450MHz Band and 2.5 GHz Band

Under Executive Decree 7,512, dated June 30, 2011, or Executive Decree 7,512, ANATEL is required to grant authorizations to telecommunications providers to use radio spectrum in the 450 Mhz band radio spectrum and the 2.5 GHz radio spectrum in the second quarter of 2012. Among other obligations, licensees of radio frequencies in the 450 Mhz band radio spectrum must agree to provide individual and collective voice and data services in rural and remote areas, in accordance with the provisions of Executive Decree 7,512 and the General Plan on Universal Service. The rules of the auctions for radio frequency spectrum in the 450 Mhz band and 2.5 GHz band and the terms of the related authorizations were submitted for public consultation and the public consultation period ended on March 5, 2012. ANATEL is expected to announce the terms of the auctions for radio frequency spectrum in the 450 Mhz band and 2.5 GHz band on April 27, 2012. We intend to evaluate our participation in these auctions following the announcement of the terms of these auctions.

Personal Mobile Services Rate Regulation

Rates for personal mobile services are regulated by ANATEL. Personal mobile services providers are required to offer a basic service plan that consists of a monthly subscription, local calls and roaming. Basic service plans were approved by ANATEL for each of the personal mobile services providers following the grant of personal mobile services authorizations to each of these providers.

Following the effectiveness of the basic service plans, annual adjustments of the rates under these plans have been subject to a price cap mechanism. Through 2005, rates were adjusted annually by no more than the rate of inflation, as measured by the IGP-DI. In 2006, ANATEL replaced the IGP-DI with the IST to calculate annual rate adjustments.

Personal mobile services providers are permitted to offer non-discriminatory alternative plans to the basic service plan. The rates charged under these plans (e.g., monthly subscription rates, charges for local calls and roaming charges) are subject to ANATEL approval prior to the time that these plans are first offered to mobile customers. Following the approval of these plans, the rates under these plans may be increased up to an annual adjustment that is approved by ANATEL and is no more than the rate of inflation, as measured by the IST.

Although subscribers of a plan cannot be forced to migrate to new plans, existing plans may be discontinued as long as all subscribers receive a notice to that effect and are allowed to migrate to new plans within six months of such notice. Discounts from the rates set in basic service plans and alternative service plans may be granted to customers without ANATEL approval.

Obligations of Personal Mobile Services Providers

As a telecommunication service provider, we are subject to requirements concerning network expansion and quality of service, as established in applicable regulations and in our personal mobile services authorizations. If we fail to meet these obligations, we may be fined, subject to a maximum penalty of R$50 million, until we are in full compliance with our obligations. While it is possible for an authorization to be revoked for non-compliance with these obligations, there are no precedents for such a revocation.

Network Expansion Obligations

The personal mobile services authorizations set forth certain obligations and targets that must be met by a personal mobile services provider. For a description of the obligations and targets that must be met by our company, see Concessions, Authorizations and Licenses Personal Mobile Services Authorization Agreements and Radio Frequency Spectrum Licenses and Concessions, Authorizations and Licenses 3G Radio Frequency Licenses.

Quality of Service Obligations

Our personal mobile services authorizations impose obligations on us to meet quality of service standards relating to our network s ability to make and receive calls, call failure rates, capacity to handle peak periods, failed interconnection of calls and customer complaints. ANATEL defines these quality of service standards, and we must report information in connection with such standards to ANATEL.

Additional Obligations

In August 2007, ANATEL adopted revisions to the personal mobile services regulations that became effective in February 2008. These revised regulations imposed additional obligations on personal mobile services providers, particularly in connection with customers rights. These obligations require personal mobile services providers to:

- establish at least one customer service center in each registration area served that has more than 100,000 inhabitants;
- upgrade customer service centers to improve access by people with hearing disabilities;
- increase the term applicable to pre-paid cards from 90 days to 180 days or more;
- deliver to pre-paid customers a detailed report of service use upon request;
- reimburse unused pre-paid credits;
- limit the duration of contracts with pre-paid customers to 12 months;
- permit customers to change service plans without penalties; and

unblock mobile handsets, allowing a customer who purchased a mobile handset from any personal mobile services provider to use it on the network of another personal mobile services provider.

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Interconnection Regulations

Under the General Telecommunications Law, all telecommunication service providers are required, if technically feasible, to make their networks available for interconnection on a non-discriminatory basis whenever a request is made by another telecommunication service provider. Interconnection permits a call originated on the network of a requesting fixed-line or personal mobile services provider s network to be terminated on the fixed-line or personal mobile services network of the other provider. ANATEL initially adopted General Rules on Interconnection (*Regulamento Geral de Interconexão*) in 1998, which were amended and restated in July 2005.

Interconnection Regulations Applicable to Fixed-Line Providers

Interconnection fees are charged at a flat rate per minute of use of a fixed-line provider s network. Interconnection rates charged by a fixed-line provider to terminate a call on its local network (the TU-RL rate) or intercity network (the TU-RIU rate) are subject to a price cap established by ANATEL. The price cap for interconnection rates varies from service provider to service provider based on the underlying cost characteristics of such service provider s network and whether such service provider has significant market power.

Fixed-line service providers must offer the same TU-RL and TU-RIU rates to all requesting providers on a nondiscriminatory basis. The price caps on interconnection rates are adjusted annually by ANATEL at the same time that rates for local and long-distance rates are adjusted.

Fixed-line service providers are only required to pay interconnection fees to another fixed-line service provider for traffic in the same local area in the event that the ratio of the outbound traffic generated by that provider (measured in minutes) to the inbound traffic terminated by that provider (measured in minutes) exceeds 55% or was less than 45%. This system is designated the bill-and-keep system.

In 2006, the TU-RL rates that fixed-line service providers could charge each other to terminate a call on their respective networks were reduced to 50% of the rate included in their Basic Plan per Minute for a local fixed-line call. In 2007, the TU-RL rates of the fixed-line service providers were reduced to 40% of the rate included in their Basic Plan per Minute for a local fixed-line call. ANATEL announced that beginning in 2008, the method used to determine the TU-RL rates would be based on a cost methodology, known as long-run incremental costs. However, in October 2007, ANATEL published an official letter delaying this change until the end of 2010. In September 2010, ANATEL commenced the bidding process to engage an international consultant to assist with the development of the long-run incremental cost methodology. However, ANATEL has not established a definitive timetable for the completion of the project. Therefore, we cannot predict when this new methodology will be proposed.

In 2006, the TU-RIU rates that fixed-line service providers could charge each other to use a portion of their long-distance networks to complete long-distance calls were reduced to 30% of the applicable domestic fixed line-to-fixed line long-distance rates for calls of more than 300 km.

Interconnection Regulations Applicable to Personal Mobile Services Providers

Interconnection fees are charged at a flat rate per minute of use of a personal mobile services provider s network. The terms and conditions of interconnection agreements of all personal mobile services providers, including the rates charged by the operator of the network to terminate a call on its mobile network (the VU-M rate), commercial conditions and technical issues, are freely negotiated between mobile and fixed-line telecommunication service providers, subject to compliance with regulations established by ANATEL relating to traffic capacity and interconnection infrastructure that must be made available to requesting providers, among other things.

Personal mobile services providers must offer the same VU-M rate to all requesting providers on a nondiscriminatory basis. Interconnection agreements must be approved by ANATEL before they become effective and they may be rejected if they are contrary to the principles of free competition and the applicable regulations. If the providers cannot agree upon the terms and conditions of interconnection agreements, ANATEL may determine terms and conditions by arbitration. Since no agreement with fixed-line service providers could be reached regarding VU-M rates when we began offering personal mobile services, ANATEL set the initial VU-M rates.

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Personal mobile services providers negotiate annual rate increases for their VU-M charges with the fixed-line telecommunications providers. If the providers cannot agree upon the terms and conditions of annual rate increases, ANATEL may determine the annual rate increases by arbitration.

In November 2011, ANATEL adopted new regulations under which ANATEL was authorized to reduce the then-current VC-1, VC-2 and VC-3 rates by as much as 18% in 2011, 12% in 2012 and 10% in 2013, after giving effect to an inflation adjustment based on the IST measured from June 2009. In February 2012, ANATEL reduced our VC-1, VC-2 and VC-3 rates by approximately 10%, although we are appealing the calculation of this rate reduction. These regulations also provided procedures under which ANATEL adopted a maximum VU-M rate that is applicable in the event that providers cannot agree upon the VU-M applicable in their interconnection agreements.

Full Billing System

In July 2006, ANATEL adopted regulations under which personal mobile services providers recognize interconnection revenues (and costs) for traffic in the same registration area on a gross basis based on the total traffic between personal mobile services providers networks. This system is designated the full billing system. These regulations also:

- require that personal mobile services providers adopt discounts to the VU-M rates for off-peak calls that correspond to the discounts required to be offered by fixed-line service providers; and

- provide that more stringent regulations applicable to interconnection between personal mobile services providers that are members of economic groups with significant market power will be adopted in order to ensure market competition.

Regulation of Interconnection Rates Charged by Providers with Significant Market Power

In 2005, ANATEL issued regulations defining a series of cost-based methods, including the fully allocated cost methodology, for determining interconnection fees charged by telecommunication service providers belonging to economic groups with significant market power based on their fixed-line or personal mobile services interconnection networks. All incumbent fixed-line service providers and all personal mobile services providers are deemed by ANATEL to belong to economic groups with significant market power in their respective service areas until ANATEL finalizes its evaluation of each provider under published criteria to determine significant market power.

In July 2006, ANATEL issued regulations regarding the fees that may be charged for the use of mobile networks by personal mobile services providers with significant market power in the mobile interconnection market. The date on which these regulations will become effective has not yet been established by ANATEL. Under these regulations, ANATEL will determine, based on a fully allocated cost model, a reference value for VU-M rates of providers that are deemed to hold significant market power. This reference value will be reassessed every three years. In order to determine whether a provider has significant market power, ANATEL will establish criteria that consider:

- that provider s market share in the mobile interconnection market and in the personal mobile services market;

- the economies of scope and scale available to that provider;

- that provider s dominance over infrastructure that is not economically viable to duplicate;

- the existence of that provider s power to negotiate the acquisition of equipment and services;

the existence of vertical integration in that provider s operations;

the existence of barriers to entry in the mobile interconnection market and the personal mobile services market served by that provider; and

that provider s access to financing sources.

ANATEL has proposed a General Plan on Competition Targets, which addresses a variety of matters, including criteria for the evaluation of telecommunications providers to determine which providers have significant market power. The General Plan on Competition Targets was submitted for public consultation in July 2011 and the public consultation period ended on October 23, 2011. We expect these new regulations, as they may be modified as a result of ANATEL s further analysis, to be adopted in 2012.

Number Portability Regulations

Number portability is the ability of a customer to move to a new home or office or switch service providers while retaining the same fixed-line or mobile telephone number. In March 2007, ANATEL adopted the General Regulation of Portability (*Regulamento Geral de Portabilidade*), establishing general rules regarding portability of fixed-line and mobile telephone numbers. These regulations permit fixed-line customers to retain their telephone numbers if they become customers of a different fixed-line service provider in the same municipality or if they move to a new home or office in the same municipality. Personal mobile services customers are permitted to retain their telephone numbers if they change their service plan or if they become customers of a different personal mobile services provider within the same registration area. Each telecommunications provider has been required to contract a third-party management entity to manage all procedures relating to number portability. Service providers are permitted to charge a migrating customer that elects to retain its telephone number a one-time fee of no more than R$4.00. This amount is intended to compensate the customer s current provider for the costs associated with managing the portability process. The new provider may elect to absorb this fee on behalf of the customer.

Regulation of Data Transmission and Internet Services

Under Brazilian regulation, ISPs are deemed to be suppliers of value-added services and not telecommunication service providers. Value-added services are considered an activity that adds features to a telecommunication service supported by such value-added services. Telecommunication service providers are permitted to render value-added services through their own networks. In addition, ANATEL regulations require all telecommunication service providers and cable television operators to grant network access to any party interested in providing value-added services, including internet access, on a non-discriminatory basis, unless not technically feasible.

ANATEL has adopted regulations applicable to fixed-line service providers with significant market power. Under these regulations, these providers are required to make the forms of agreements that they use for EILD and SLD services publicly available, including the applicable rates, and are only permitted to offer these services under these forms of agreement. Following publication of these forms of agreement, the rates under these agreements may be increased on an annual basis by no more than the rate of inflation, as measured by the IST. ANATEL also publishes reference rates for these services, and if a customer of one of these providers objects to the rates which that provider charges for these services, the customer is entitled to seek to reduce the applicable rate through arbitration before ANATEL.

Multimedia Communications Service Quality Management Regulations

In June 2011, the President of Brazil issued Executive Decree No. 7,512/11, which mandated ANATEL to take the necessary regulatory measures to establish quality standards for broadband internet services. In compliance with such decree, on October 31, 2011, ANATEL published a resolution approving the Multimedia Communications Service Quality Management Regulations (*Regulamentação de Gestão da Qualidade do Serviço de Comunicação Multimídia*), or the Regulations, which identify network quality indicators and establish performance goals for multimedia communications service providers, including broadband internet service providers, with more than 50,000 subscribers. Such providers will be required to collect representative data using dedicated equipment installed at the site of each network connection and be subject to periodic measurements to ensure their compliance with the Regulations, including:

individual upload and download speeds of at least 20%, 30% and 40% of contracted speeds per measurement for at least 95% of all measurements, during the first year, second year and thereafter, respectively, following implementation of the Regulations;

- average upload and download speeds of at least 60%, 70% and 80% of contracted speeds for all measurements during the first year, second year and thereafter, respectively, following implementation of the Regulations; and

- individual round-trip latencies for fixed-line connections of up to 80 milliseconds per measurement for at least 95% of the measurements.

To increase transparency, customers must be provided with specialized software at no cost to measure their own network quality, although such customer-generated measurements will not be included in official calculations. In addition to ensuring network quality standards, service providers must hire specialized companies to measure customer service and customer satisfaction indicators, including complaint resolution, customer service personnel competence, customer perceptions relating to billing and quality of technical support staff. Service providers must comply with the above-mentioned quality standards beginning on the thirteenth month following implementation of the Regulations. Failure to meet such standards will subject non-compliant service providers to sanctions.

National Broadband Plan

On June 30, 2011, we entered into a Term of Commitment (*Termo de Compromisso*) with ANATEL and the Ministry of Communications to formalize our voluntary commitment to adhere to the terms of the National Broadband Plan, created in May 2010 by Executive Decree No. 7,175/10 with the goal to make broadband access available at low cost, regardless of technology, throughout Brazil. Pursuant to the Term of Commitment, we are required to offer (1) broadband services with minimum upload and download capabilities to retail customers in certain sectors of Region I and II for a maximum price of R$35 per month (or R$29.90 in ICMS-exempt states), plus fees, and (2) access to our broadband infrastructure to certain wholesale customers, including small businesses and municipalities, in certain sectors of Region I and II for a maximum price of R$1,253 per 2 Mbps per month and a one-time installation fee, while observing all quality standards under ANATEL regulations. Both retail and wholesale services are subject to certain network capacity limits and need only be provided at the demand of the customer. The services provided under the Term of Commitment may be implemented gradually, beginning in November 2011, although we are obligated to make services available to 100% of eligible retail and wholesale customers by December 31, 2014 and June 30, 2013, respectively. The Term of Commitment also requires that we:

- provide one public internet access point for the first 20,000 inhabitants and one additional access point for each subsequent 10,000 inhabitants, with a limit of six access points, at a speed of 2 Mbps, in each municipality that has only satellite service, free of charge and upon demand of such municipality;

- adequately advertise the services contemplated by the Term of Commitment and present to the Ministry of Communications semi-annual reports detailing our marketing efforts; and

- make our best efforts to offer broadband services to retail customers at speeds of up to 5 Mbps, reaching the largest possible number of municipalities by 2015.

The Term of Commitment will expire on December 31, 2016.

Environmental and Other Regulatory Matters

As part of our day-to-day operations, we regularly install ducts for wires and cables and erect towers for transmission antennae. We may be subject to federal, state and/or municipal environmental licensing requirements due to the installation of cables along highways and railroads, over bridges, rivers and marshes and through farms, conservation units and environmental preservation areas, among other places. As of the date of this annual report, we have been required to obtain environmental licenses for the installation of transmission towers and antennae in several municipalities with no material impact on our operations. However, there can be no assurances that other state and municipal environmental agencies will not require us to obtain environmental licenses for the installation of transmission towers and antennae in the future and that such a requirement would not have a material adverse effect on the installation costs of our network or on the speed with which we can expand and modernize our network.

We must also comply with environmental legislation regarding the management of solid waste. According to resolutions adopted by the National Environmental Council (*Conselho Nacional do Meio Ambiente*), companies responsible for the treatment and final disposal of solid industrial waste, special waste and solid urban waste are subject to environmental licensing. Should the waste not be disposed of in accordance with standards established by environmental legislation, the company generating such waste may be held jointly and severally liable with the company responsible for waste treatment for any damage caused. Also, in all states where we operate, we have implemented management procedures promoting the recycling of batteries, transformers and fluorescent lamps.

In addition, we are subject to ANATEL regulations that impose limits on the levels and frequency of the electromagnetic fields originating from our telecommunications transmissions stations.

We believe that we are in compliance with ANATEL standards as well as with all applicable environmental legislation and regulations. We are currently not involved in any administrative or judicial proceeding involving material liability for environmental damage.

ITEM 4A. UNRESOLVED STAFF COMMENTS

Not applicable.

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ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion of our financial condition and results of operations should be read in conjunction with our consolidated financial statements as of December 31, 2011 and 2010 and for the three years ended December 31, 2011, which are included in this annual report, as well as with the information presented under the sections entitled Presentation of Financial and Other Information and Item 3. Key Information Selected Financial Information.

The following discussion contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those discussed in the forward-looking statements as a result of various factors, including those set forth in Forward-Looking Statements and Item 3. Key Information Risk Factors.

The following discussion and analysis of our financial condition and results of operations presents the following:

- a brief overview of our company and the principal factors that influence our results of operations, financial condition and liquidity;
- a discussion of the corporate reorganization of our company, TNL, Telemar and Coari that was completed on February 27, 2012;
- a review of our financial presentation and accounting policies, including our critical accounting policies;
- a discussion of the principal factors that influence our results of operations;
- a discussion of developments since the end of 2011 that may materially affect our results of operations, financial condition and liquidity;
- a discussion of our results of operations for the years ended December 31, 2011, 2010 and 2009;
- a discussion of our liquidity and capital resources, including our working capital at December 31, 2011
- a discussion of our cash flows for the years ended December 31, 2011, 2010 and 2009;
- a discussion of our material short-term and long-term indebtedness at December 31, 2011;
- a discussion of our contractual commitments; and
- supplemental information regarding (1) the results of operations of TNL for the years ended December 31, 2011 and 2010, (2) the cash flows of TNL for the year ended December 31, 2011, (3) the material short-term and long-term indebtedness at December 31, 2011 of TNL, and (4) the contractual commitments of TNL as of December 31, 2011.

Overview

We are the largest telecommunications service provider in Region II in Brazil, based on our aggregate number of fixed-lines in service and mobile subscribers as of December 31, 2011 and information available from ANATEL. We offer a range of integrated telecommunication services that includes fixed-line and mobile telecommunications services, data transmission services (including broadband access services), ISP services and other services, for residential customers, small, medium and large companies, and governmental agencies. We operate under the brand name Oi. In 2011, we recorded net operating revenue of R$9,245 million and net income of R$1,006 million.

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Our results of operations and financial condition will be significantly influenced in future periods by the corporate reorganization of our company, TNL, Telemar and Coari described under Corporate Reorganization. In addition, our results of operations for the years ended December 31, 2011, 2010 and 2009 have been influenced, and our future results of operations will continue to be influenced, by a variety of factors, including:

- the acquisition of our company and Brasil Telecom Holding by Telemar and the subsequent corporate reorganization of the entities in that directly and indirectly controlled our company, which have resulted in (1) our incurring increased selling, general and administrative expenses relating to the integration of our operations into those of Telemar and the implementation of new mobile services plans as required by ANATEL, and (2) our incurring increased capital expenditures and the corresponding depreciation and amortization expenses as a result of the upgrading and integration of our infrastructure with that of Telemar;

- the rate of growth of Brazilian GDP, which grew by an estimated 2.7% in 2011 and grew by 7.5% in 2010 following a contraction of 0.2% in 2009, which we believe affects demand for our services and, consequently, our net operating revenue;

- the number of our fixed lines in service, which declined to 6.8 million as of December 31, 2011 from 7.2 million as of December 31, 2010, and the percentage of our fixed-line customers that subscribe to our alternative plans which increased to 75.8% as of December 31, 2011 from 74.5% as of December 31, 2010;

- the number of our mobile customers, which increased by 10.4% to 8.6 million as of December 31, 2011 from 7.8 million at December 31, 2010;

- the number of our fixed-line customers that subscribe to our broadband services, which increased by 5.3% to 2.0 million as of December 31, 2011 from 1.9 million as of December 31, 2010;

- the increased competition in the Brazilian market for telecommunications services, which affects the amount of the discounts that we offer on our service rates and the quantity of services that we offer at promotional rates, and resulted in a 3.2% increase in the amount that we recorded as discounts and returns against our gross operating revenue to R$3,830 million in 2011 from R$3,710 million in 2010;

- inflation rates in Brazil, which were 4.90% in 2011 and 5.65% in 2010, as measured by the IST, and the resulting adjustments to our regulated rates, as well as the effects of inflation on our *real*-denominated debt that is indexed to take into account the effects of inflation or bears interest at rates that are partially adjusted for inflation;

- changes in regulatory requirements that result in our incurrence of additional capital expenditures, changes in the revenues we generate, or changes in the costs that we incur;

- our compliance with our quality of service obligations under the General Plan on Quality Goals and our network expansion and modernization obligations under the General Plan on Universal Service and our concession agreements, the amount of the fines assessed against us by ANATEL for alleged failures to meet these obligations and our success in challenging fines that we believe are assessed in error;

- changes in the *real*/U.S. dollar exchange rate, including the 12.2% depreciation of the *real* against the U.S. dollar in 2011 and the 4.3% appreciation of the *real* against the U.S. dollar in 2010, which has affected the cost in *reais* of a substantial portion of the network equipment that we purchase for our capital expenditure projects, the prices of which are denominated in U.S. dollars or are U.S. dollar-linked; and

the level of our outstanding indebtedness, fluctuations in benchmark interest rates in Brazil, principally the CDI rate and the TJLP rate, which affects our interest expenses on our *real*-denominated floating rate debt.

Our financial condition and liquidity is influenced by a variety of factors, including:

- our ability to generate cash flows from our operations;
- prevailing Brazilian and international interest rates, which affect our debt service requirements;
- our ability to borrow funds from Brazilian and international financial institutions and to sell our debt securities in the Brazilian securities markets, which is influenced by a number of factors discussed below;
- our capital expenditure requirements, primarily consisting of (1) investments in infrastructure to expand our mobile telecommunications services, including the expansion of our 3G networks, and (2) investments in fixed-line telecommunications network equipment, primarily to enhance the technical capabilities of our network in order to enable us to provide value-added services, such as broadband and IP TV services, and to comply with our universal service obligations; and
- the requirement under Brazilian corporate law and our by-laws that we pay dividends on an annual basis in an amount equal to at least 25% of our adjusted net income, unless our board of directors deems it inconsistent with our financial position.

Corporate Reorganization

On February 27, 2012, the shareholders of TNL, Telemar, Coari and Brasil Telecom approved a series of transactions including:

- a split-off (*cisão*) and merger of shares (*incorporação de ações*) under Brazilian law in which:
  - Telemar transferred its shares of Coari to Coari;
  - Coari assumed a portion of the liabilities of Telemar, which became joint and several liabilities of Telemar and Coari or obligations of Coari guaranteed by Telemar;
  - Coari issued one common share and/or one preferred share to the holders of Telemar common and preferred shares (other than the shares of holders who exercised their withdrawal rights with respect to such shares) in exchange for each of their common and preferred shares of Telemar, respectively; and
  - Coari retained the Telemar shares exchanged for Coari shares and as a result, Telemar became a wholly-owned subsidiary of Coari;
- a merger (*incorporação*) under Brazilian law of Coari with and into our company, with our company as the surviving company, which we refer to as the Coari merger, in which:

each issued and then outstanding share of Brasil Telecom held by Coari and all Coari shares held in treasury were cancelled;

each issued and then outstanding common share of Coari was converted automatically into 5.1149 common shares of Brasil Telecom;

each issued and then outstanding preferred share of Coari was converted automatically into 0.3904 common shares of Brasil Telecom and 4.0034 preferred shares of Brasil Telecom;

Coari ceased to exist; and

Telemar became a wholly-owned subsidiary of Brasil Telecom; and a merger (*incorporação*) under Brazilian law of TNL with and into our company, with our company as the surviving company, which we refer to as the TNL merger, in which:

each TNL share held in treasury prior to the TNL merger was cancelled, and each issued and then outstanding share of Brasil Telecom held by TNL was cancelled, other than 24,647,867 common shares of Brasil Telecom, which were transferred to the treasury of Brasil Telecom;

each issued and then outstanding common share of TNL (other than common shares held by shareholders who exercised their withdrawal rights with respect to such common shares) was converted automatically into 2.3122 common shares of Brasil Telecom;

each issued and then outstanding preferred share of TNL was converted automatically into 0.1879 common shares of Brasil Telecom and 1.9262 preferred shares of Brasil Telecom; and

TNL ceased to exist.

In addition, on February 27, 2012, our shareholders approved:

the issuance and distribution of (1) one Class B redeemable preferred share of our company to the holder of each of our common shares, and (2) one Class C redeemable preferred share of our company to the holder of each of our preferred shares; and

the redemption of each Class B redeemable preferred share and Class C redeemable preferred share at a redemption price equal to R$2.543282 per share, or an aggregate of R$1,502 million.

We will account for the Coari merger and the TNL merger using historical cost, whereby the financial statements of our company will record the historical carrying values of the assets and liabilities of TNL, Telemar, and Coari as from the date of the reorganization. The historical carrying values of Coari reflect the purchase accounting recorded under IFRS in accordance with IFRS 3(R), Business Combinations, under which 100% of the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the subsidiaries of our company were recorded at their fair values on January 8, 2009, the date on which TNL acquired control of our company. The historical financial statements of our company will not be restated to account for the impacts of the corporate reorganization on a retroactive basis. As a result, for dates after the completion of the corporate reorganization, our balance sheet will reflect a significant increase in non-current intangible assets and property, plant and equipment, a significant increase in liabilities, particularly loans, financings and debentures, and a significant increase in total equity. In addition, for periods ended after the completion of the corporate reorganization, we will record an increase in depreciation and amortization expenses reflecting this step-up in the carrying value of our intangible assets and property, plant and equipment, and an increase in financial expenses reflecting the increase in our loans, financings and debentures, with a consequent negative effect on our gross profit, operating income and net income.

In order to assist investors in evaluating our company following the corporate reorganization, we have included in this Item 5. Operating and Financial Review and Prospects :

supplemental information regarding the results of operations of TNL for the years ended December 31, 2011 and 2010;

supplemental information regarding the cash flows of TNL for the years ended December 31, 2011; and

supplemental information regarding the material short-term and long-term indebtedness at December 31, 2011 of TNL.

The financial statements of TNL as of and for the year ended December 31, 2011 have not been presented elsewhere in this annual report and have not been filed with the SEC.

Holders of Telemar common shares, class A preferred shares and class B preferred shares and holders of TNL preferred shares as of the close of trading on May 23, 2011, the date prior to the publication of the Relevant Fact that first announced the split-off and share exchange and the TNL merger were entitled to withdrawal rights in connection with the split-off and share exchange and the TNL merger. Shareholders who exercised these withdrawal rights with respect to the Telemar shares were entitled to receive R$74.37 per share and shareholders who exercised these withdrawal rights with respect to the TNL preferred shares were entitled to receive R$28.93 per share. As of March 29, 2012, the expiration of the period for the exercise of these withdrawal rights, holders of 1,020,215 Telemar common shares, 17,856,585 Telemar class A preferred shares, 47,714 Telemar class B preferred shares and 20,446,097 TNL preferred shares had validly exercised their withdrawal rights for an aggregate cost to our company of R$1,999 million.

Financial Presentation and Accounting Policies

Presentation of Financial Statements

We have prepared our consolidated financial statements as of December 31, 2011 and 2010 and for the years ended December 31, 2011, 2010 and 2009 in accordance with IFRS as issued by the IASB.

Effects of the Acquisition of our Company and Brasil Telecom Holding by Telemar and the Subsequent Corporate Reorganization

On January 8, 2009, Copart 1, an indirect wholly-owned subsidiary of Telemar, acquired all of the outstanding shares of Invitel and 12,185,836 common shares of Brasil Telecom Holding owned by the shareholders of Invitel. As of January 8, 2009, Invitel owned all of the outstanding shares of Solpart, Solpart owned 19.0% of the outstanding share capital, including 52.0% of the voting share capital, of Brasil Telecom Holding, which, in turn, owned 67.2% of the outstanding share capital, including 99.1% of the voting share capital, of Brasil Telecom.

Prior to this acquisition Copart 1 owned 21.1% of the outstanding share capital of Brasil Telecom Holding and Copart 2, an indirect wholly-owned subsidiary of Telemar, owned 10.7% of the outstanding share capital of our company. In connection with this acquisition, on June 23, 2009:

- Copart 1 acquired 40,452,227 common shares of Brasil Telecom Holding, representing 30.5% of the outstanding common shares of Brasil Telecom Holding and 11.2% of the outstanding share capital of Brasil Telecom Holding, through a public tender offer; and

- Copart 2 acquired 630,872 of our common shares, representing 0.3% of our outstanding common shares and 0.1% of our outstanding share capital, through a public tender offer.

In anticipation of its corporate reorganization, on July 31, 2009, Telemar undertook the transactions described below, which we refer to collectively as the Intermediate Mergers, to eliminate the intermediate holding companies in the structure of its ownership of Brasil Telecom Holding and our company:

- Invitel merged with and into Solpart, with Solpart as the surviving company;

- Solpart merged with and into Copart 1, with Copart 1 as the surviving company;

- Copart 1 merged with and into Brasil Telecom Holding, with Brasil Telecom Holding as the surviving company; and

- Copart 2 merged with and into Brasil Telecom, with Brasil Telecom as the surviving company.

As a result of these transactions, Coari directly owned (1) 54.7% of the outstanding share capital, including 91.7% of the outstanding voting share capital, of Brasil Telecom Holding, and (2) 10.9% of the outstanding share capital, including 0.3% of the outstanding voting share capital, of our company.

On September 30, 2009, Brasil Telecom Holding merged with and into Brasil Telecom. As a result of these transactions, at December 31, 2009, Coari owned 49.3% of the outstanding share capital, including 79.6% of the voting share capital, of Brasil Telecom.

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Under IFRS, we accounted for the merger of Brasil Telecom Holding into our company by recording the tax benefit of the controlling interest on assets acquired in connection with the Brasil Telecom Acquisition as a capital contribution based on the amount of tax benefit realizable on the date of the merger of Brasil Telecom Holding into our company in accordance with IFRS and specific CVM requirements. The historical financial statements of our company were not restated to account for the impacts of the merger on a retroactive basis.

Business Segments and Presentation of Segment Financial Data

We have implemented an organizational structure that we believe reflects our business activities and corresponds to the principal services that we provide. We report our results in three segments to reflect this organizational structure:

- *Fixed-Line and Data Transmission Services* This segment includes our local fixed-line services (including public telephones), our long-distance services, our fixed-line data transmission services and interconnections to our fixed-line network.

- *Mobile Services* This segment includes our mobile services, including voice, mobile data communications and other value added services, and interconnections to our mobile network.

- *Other Services* This segment includes the operations of our internet portal, ISP services and call center.

We evaluate and manage business segment performance based on information prepared in accordance with IFRS, and, accordingly, the segment data included in this annual report is presented under IFRS. We have included a reconciliation of the operating results of our segments to our consolidated results under Results of Operations below.

Critical Accounting Policies and Estimates

Our critical accounting policies and estimates described in note 2(c) to our consolidated financial statements. In preparing our consolidated financial statements, we relied on estimates and assumptions derived from historical experience and various other factors that we deemed reasonable and relevant. Critical accounting policies are those that are important to the portrayal of our consolidated financial position and results of operations and require management s subjective and complex judgments, estimates and assumptions. The application of these critical accounting policies often requires judgments made by management regarding the effects of matters that are inherently uncertain with respect to our results of operations and the carrying value of our assets and liabilities. Our results of operations and financial position may differ from those set forth in our consolidated financial statements, if our actual experience differs from management s assumptions and estimates. In order to provide an understanding of our critical accounting policies, including some of the variables and assumptions underlying the estimates, and the sensitivity of those assumptions and estimates to different parameters and conditions, we set forth below a discussion of our critical accounting policies relating to:

- revenue recognition and trade receivables;

- provision for doubtful accounts;

- depreciation of property, plant and equipment;

- impairment of long-lived assets;

- provisions;

derivative instruments;

deferred income taxes and social contribution;

employee benefits; and

amortization of intangible assets.

Revenue Recognition and Trade Receivables

Our revenue recognition policy is significant because our revenue is a material component of our results of operations. Management s determination of price, collectability and the rights to receive certain revenues for the use of our network are based on judgments regarding the nature of the fee charged for services rendered, the price for certain services delivered and the collectability of those revenues. Should changes in conditions cause management to conclude that these criteria are not met for certain transactions, the amount of accounts receivable could be adversely affected. In addition, for certain categories of revenue we rely upon revenue recognition measurement guidelines set by ANATEL.

Revenues are generally recognized on an accrual basis. Revenues from local fixed-line, long-distance and post-paid mobile calls and data transmission services are recognized when services are provided. Services provided and not billed at the end of each month are estimated and recorded on an accrual basis. Late-payment interest is recognized upon the issuance of the first bill following the payment of the overdue bill.

Revenues from pre-paid mobile cards are recognized based on the use of the respective credits. Revenue from the sale of public telephone cards is recognized when the credits are effectively consumed by customers. Revenues related to the sale of mobile handsets and accessories are accounted for when the goods are delivered and accepted by the customer.

Revenues from the usage of our network by other telecommunications service providers are recorded based on a formal document of declared traffic and services rendered, the Traffic Exchange Declaration (*Documento de Declaração de Tráfego e Prestação de Serviço*), or DETRAF, issued by an independent, outsourced clearinghouse.

We consider revenue recognition to be a critical accounting policy, because of the uncertainties caused by different factors such as the complex information technology required, high volume of transactions, fraud and piracy, accounting regulations, management s determination of collectability and uncertainties regarding our right to receive certain revenues (mainly revenues for use of our network). Significant changes in these factors could cause us to fail to recognize revenues or to recognize revenues that we may not be able to realize in the future, despite our internal controls and procedures. We have not identified any significant need to change our revenue recognition policy.

Provision for Doubtful Accounts

Our allowance for doubtful accounts is established in order to recognize probable losses on accounts receivable and takes into account limitations we impose to restrict the provision of services to customers with past-due accounts and actions we take to collect delinquent accounts. We include government entities, corporate customers and other telecommunications service providers in the basis for our calculation of the allowance for doubtful accounts. For additional information regarding our allowance for doubtful accounts, see note 2(b) to our consolidated financial statements.

We have entered into agreements with certain customers to collect past-due accounts receivable, including agreements allowing customers to settle their delinquent accounts in installments. The amounts that we actually fail to collect in respect of these accounts may differ from the amount of the allowance established, and additional allowances may be required.

Following Telemar s acquisition of control of our company on January 8, 2009, we have adopted the same accounting estimate method with respect to our allowance for doubtful accounts as that adopted by Telemar. As a result of this change in accounting estimate method, we recorded a change in accounting estimate in the amount of R$38 million, net of income taxes, during the year ending December 31, 2009.

Depreciation of Property, Plant and Equipment

We depreciate property, plant and equipment using the straight-line method at rates we judge compatible with the useful lives of the underlying assets. The depreciation rates of our most significant assets are described in note 17 to our consolidated financial statements. The useful lives of assets in certain categories may vary based on whether they are used primarily to provide fixed-line or mobile services. We review the estimated useful lives of the assets taking into consideration technical obsolescence and a valuation by outside experts.

We modified our estimate of the useful life of our property, plant and equipment as from September 30, 2009. These modifications increased the estimated useful lives of many of our assets, which have been reflected for periods ended after September 30, 2009, resulting in a reduction of our depreciation expenses of R$350 million for 2010 compared to 2009.

Given the complex nature of our property, plant and equipment, the estimates of useful lives require considerable judgment and are inherently uncertain, due to rapidly changing technology and industry practices, which could cause early obsolescence of our property, plant and equipment. If we materially change our assumptions of useful lives and if external market conditions require us to determine the possible obsolescence of our property, plant and equipment, our depreciation expense, obsolescence write-off and consequently net book value of our property, plant and equipment could be materially different.

Impairment of Long-Lived Assets

We test property, plant and equipment items and intangible assets for impairment whenever (1) we decide to discontinue activities in which such assets are used, or (2) there is evidence that future operating results will not be sufficient to ensure their realization.

Assets with finite useful lives are tested for impairment whenever events or changes in circumstances indicate that the asset might be impaired. We test asset with indefinite useful lives (goodwill) for impairment at least annually.

Impairment losses, if any, are recognized in an amount by which the carrying amount of an asset exceeds its recoverable value. Recoverable value is the higher of fair value less cost to sell and the value in use. These calculations require the use of judgments and assumptions. The determination of fair values and discounted future operating cash flows requires that we make certain assumptions and estimates with respect to projected cash inflows and cash outflows related to future revenue, costs and expenses. These assumptions and estimates may be influenced by different external and internal factors, such as economic trends, industry trends and interest rates, changes in business strategies, and changes in the type of services and products sold by our company. The use of different assumptions and estimates could significantly change our consolidated financial statements.

We have not recorded any impairment during the three years ended December 31, 2011.

Provisions

We recognize provisions for losses in labor, tax and civil proceedings, as well as administrative proceedings. The recognition of a provision is based on the assessment of the risk of loss made for each proceeding, which includes assessing available evidence and recent decisions.

We classify our risk of loss in legal proceedings as remote, possible or probable. Provisions recorded in our consolidated financial statements in connection with these proceedings reflect reasonably estimated losses at the relevant date as determined by our management after consultation with our general counsel and the outside legal counsel. As discussed in note 23 to our consolidated financial statements, we record as a liability our estimate of the costs of resolution of such claims, when we consider our losses probable. We continually evaluate the provisions based on changes in relevant facts, circumstances and events, such as judicial decisions, that may impact the estimates, which could have a material impact on our results of operations and shareholders equity. While management believes that the current provision is adequate, it is possible that our assumptions used to estimate the provision and, therefore, our estimates of loss in respect of any given contingency will change in the future based on changes in the relevant situation. This may therefore result in changes in future provisioning for legal claims. For more information regarding material pending claims against our company, see Item 8. Financial Information Legal Proceedings and note 23 to our consolidated financial statements.

As the result of Telemar s acquisition of control of our company in January 2009, we have changed our criteria for estimating probable losses in connection with labor proceedings and the recognition of Tax on the Circulation of Merchandise and Services (*Imposto Sobre a Circulação de Mercadorias e Serviços*), or ICMS (a state value-added tax on sales and services), tax credits in order to align our policies with those of Telemar. As a result, we recorded additional provisions for labor proceedings and tax proceedings in 2009 in the amount of R$334 million and R$387 million, respectively.

In addition, as the result of certain judicial decisions in 2009, we have reclassified the probability of loss in certain civil proceedings involving CRT, the leading fixed-line telecommunications service company in the State of Rio Grande do Sul that we acquired in July 2000, from possible to probable. With the assistance of our internal and external legal advisors, we revised our estimate of the amount of provisions for civil contingencies in connection with the financial participation agreements entered into in connection to the expansion plans of CRT, considering aspects of the process we use to estimate the amount of provisions for civil contingencies related to the dates and discussions that guided the final decisions of the proceedings, as well as the use of statistical criteria to estimate the amount of the provisions. As a result, the provision for civil contingencies in connection with the financial participation agreements entered into in connection to the expansion plans of CRT was increased by R$2,325 million. For additional information regarding these suits, see Item 8. Financial Information Legal Proceedings Civil Claims.

Derivative Instruments

We recognize derivative financial instruments at fair value based on future cash flow estimates associated with each instrument contracted. Our estimates of future cash flows may not necessarily be indicative of the amounts that could be obtained in the current market. The use of different assumptions to measure the fair value could have a material effect on the amounts obtained and not necessarily be indicative of the cash amounts that we would receive or pay to settle such transactions.

Deferred Income Taxes and Social Contribution

Income taxes in Brazil are calculated and paid on a legal entity basis, and there are no consolidated tax returns. Accordingly, we only recognize deferred tax assets, related to tax loss carryforwards and temporary differences, if it is likely that they will be realized on a legal entity basis.

We recognize and settle taxes on income based on the results of operations determined in accordance with the Brazilian Corporation Law, taking into consideration the provisions of Brazilian tax law, which are materially different from the amounts calculated for IFRS purposes. Under IFRS, we recognize deferred tax assets and liabilities based on the differences between the carrying amounts and the taxable bases of the assets and liabilities.

We regularly test deferred tax assets for impairment and recognize a provision for impairment losses when it is probable that these assets may not be realized, based on the history of taxable income, the projection of future taxable income, and the time estimated for the reversal of existing temporary differences. These projections require the use of estimates and assumptions. In order to project future taxable income, we need to estimate future taxable revenues and deductible expenses, which are subject to a variety of external and internal factors, such as economic trends, industry trends and interest rates, changes in business strategies, and changes in the type of services and products sold by our company. The use of different estimates and assumptions could result in the recognition of a provision for impairment losses for the entire or a significant portion of the deferred tax assets.

Employee Benefits

We record liabilities for employee benefits based on actuarial valuations which are calculated based on assumptions and estimates regarding discount rates, investment returns, inflation rates for future periods, mortality indices and projected employment levels relating to pension fund benefit liabilities. The accuracy of these assumptions and estimates will determine whether we have created sufficient reserves for the costs of accumulated pensions and healthcare plans, and the amount we are required to disburse each year to fund pension benefits. These assumptions and estimates are subject to significant fluctuations due to different external and internal factors, such as economic trends, social indicators, our capacity to create new jobs and our ability to retain our employees. All of these assumptions are reviewed at the end of each reporting period. If these assumptions and estimates are not accurate, we may be required to revise our reserves for pension benefits, which could materially impact our results of operations.

Amortization of Intangible Assets

Intangible assets consist primarily of authorizations to provide personal mobile services and radio frequency licenses, licenses to use software and goodwill on the acquisition of investments, which is calculated based on expected future economic benefits.

Amortization of intangible assets, other than goodwill, is calculated under the straight-line method over (1) the effective term of the authorization to provide personal mobile services or of the radio frequency license, or (2) over a maximum period of five years in the case of software licenses.

We do not amortize goodwill in our consolidated statements of income and we are required to test goodwill for impairment at least on an annual basis.

Principal Factors Affecting Our Financial Condition and Results of Operations

Rate of Growth of Brazil s Gross Domestic Product and Demand for Telecommunications Services

As a Brazilian company with substantially all of our operations in Brazil, we are affected by economic conditions in Brazil. Brazilian GDP grew by an estimated 2.7% in 2011 and grew by 7.5% in 2010 following a contraction of 0.2% in 2009. While we believe that growth in Brazil s GDP stimulates demand for telecommunications services, we believe that demand for telecommunications services is relatively inelastic in periods of economic stagnation and that the effect on our revenues of low growth or a recession in Brazil would not be material under foreseeable scenarios. However, a substantial and prolonged deterioration of economic conditions in Brazil could have a material adverse effect on the number of subscribers to our services and the volume of usage of our services by our subscribers and, as a result, our net operating revenue.

Based on information available from ANATEL, the number of fixed lines in service in Brazil increased from 34.7 million as of December 31, 2000 to 43.0 million as of December 31, 2011, and the number of mobile subscribers in Brazil increased from 28.8 million as of December 31, 2000 to 242.0 million as of December 31, 2011. Although the demand for telecommunications services has increased substantially during the past ten years, the tastes and preferences of Brazilian consumers of these services have shifted.

During the three years ended December 31, 2011, the number of mobile subscribers in Brazil has grown at an average rate of 20.3% per year while the number of fixed lines in service in Brazil has increased by an average rate of 1.5% per year. As the incumbent provider of fixed-line services and a provider of mobile services in Region I and Region II, we are both a principal target and a beneficiary of this trend. During the three years ended December 31, 2011, the number of our mobile subscribers in Region II has grown at an average rate of 17.7% per year from 5.6 million at December 31, 2008 to 8.6 million at December 31, 2011 and the number of TNL s mobile subscribers in Region I has grown at an average rate of 17.1% per year from 24.4 million as of December 31, 2008 to 28.3 million at December 31, 2011, while the number of our fixed lines in service in Region II has declined by an average rate of 5.3% per year from 8.0 million at December 31, 2008 to 6.8 million at December 31, 2011 and the number of TNL s fixed lines in service in Region I has decreased by an average rate of 4.5% per year from 13.9 million at December 31, 2008 to 12.0 million at December 31, 2011.

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Demand for Our Telecommunications Services

Demand for Our Local Fixed-Line Services

Brazil s fixed-line penetration level is now similar to that of other countries with similar per capita income, and, as has happened in such other countries, the fixed-line telecommunications customer base has remained stable. Demand for local fixed-line services of our company and TNL has reached a plateau in recent years. Because the number of customers of TNL and our company terminating their fixed-line services has exceeded new activations during this period, the number of our fixed lines in service in Region II declined by 1.2 million between December 31, 2008 and December 31, 2011 and the number of TNL s fixed lines in service in Region I declined by 1.8 million. In addition, the new fixed lines that we and TNL have activated between December 31, 2008 and December 31, 2011 generally represent customers that have changed addresses or low-income customers from whom we generate revenues at a rate below our average revenue per customer.

We and TNL have sought to combat the general trend in the Brazilian telecommunications industry of substitution of mobile services in place of local fixed-line services by (1) offering value-added services to our fixed-line customers, primarily subscriptions for broadband services, and (2) promoting convergence of our telecommunications services through offerings of bundled packages of local fixed-line, long-distance, mobile and broadband services. As a result of these service offerings, we expect that the rate of decline in number of our fixed lines in service will be reduced. As of December 31, 2011, 29.8% of our fixed lines in service in Region II also subscribed for ADSL service and 23.7% of TNL s fixed lines in service in Region I also subscribed for ADSL service. As of December 31, 2011, 4.0% of our local fixed-line customers in Region II subscribed for bundled service packages, which account for 23.0% of our post-paid mobile subscribers as each fixed-line subscriber may include multiple mobile devices in a bundled plan, and 11.0% of TNL s local fixed-line customers in Region I subscribed for bundled service packages, which account for 43.0% of TNL s post-paid mobile subscribers.

We are required under ANATEL regulations and our concession contracts to offer a basic service plan to our fixed-line residential customers that permits 200 minutes of usage of our fixed-line network to make local calls. A basic plan customer pays a monthly fee for this service, and when the customer makes local calls in excess of this limit, we charge the customer for the excess minutes on a per-minute basis. We offer alternative local fixed-line plans that include significantly larger numbers of minutes and charge higher monthly fees for these plans, although these monthly fees represent a discount from the amount that the customer would be charged under our basic plan if the customer used the number of minutes included in the alternative plan. As the number of our customers selecting these alternative plans has grown in response to our marketing and promotional efforts, we have recorded increased revenues for monthly subscription fees, offset by corresponding declines in revenues for the use of excess minutes. Subscribers to our alternative fixed-line plans represented 75.8% of our fixed lines in service in Region II as of December 31, 2011 as compared to 51.3% as of December 31, 2008, and subscribers to TNL s alternative fixed-line plans represented 95.9% of its fixed lines in service in Region I as of December 31, 2011 as compared to 46.2% as of December 31, 2008. We believe that our alternative local fixed-line plans contribute to a net increase in our local fixed-line revenue as many subscribers of our alternative fixed-line plans do not use their full monthly allocations of local minutes.

The substantial increase in the number of mobile service users in Brazil has also negatively impacted the use of our public telephones. As the incumbent local fixed-line service provider in Region I and Region II, we are required under ANATEL regulations and our concession contracts to meet specified targets with respect to the availability of public telephones throughout our concession area. However, as a larger portion of the population of Region I and Region II uses mobile handsets to make calls when not in proximity to a fixed-line telephone, use of our public telephones in Region II declined by 77.3% from 2008 to 2011 and use of TNL s public telephones in Region I declined by 77.8% from 2008 to 2011.

Demand for Our Mobile Services

We believe that our customer base for mobile services in Region II has grown from 5.6 million at December 31, 2008 to 8.6 million at December 31, 2011 primary as a result of the success of our marketing and promotion campaigns and the rebranding of our mobile services and the launch of new services as part of our effort to align our service offerings with those of Telemar following the acquisition of control of our company by TNL in January 2009.

We believe that the primary reason that TNL s customer base for mobile services in Region I has grown from 24.4 million at December 31, 2008 to 28.3 million at December 31, 2011 has been the success of TNL s marketing and promotion campaigns. In addition, TNL s commencement of mobile services in the State of São Paulo in October 2008 led to the addition of 8.6 million mobile customers in Region III as of December 31, 2011.

The market for mobile services is extremely competitive in each of the regions that we serve. During 2011, the average monthly churn rate of our mobile services segment was 4.9% per month in Region II, and the average monthly churn rate of TNL s mobile services segment was 3.1% per month in Region I and 4.1% per month in Region III. As a result, (1) we incur selling expenses in connection with marketing and sales efforts designed to retain existing mobile customers and attract new mobile customers, and (2) from time to time the discounts that we offer in connection with our promotional activities lead to charges against our gross operating revenue from mobile services. In addition, competitive pressures have in the past required us to introduce service plans under which the monthly and per-minute rates that we charge our mobile customers are lowered, reducing our average revenue per customer.

We expect our overall mobile services business to continue to grow in terms of its customer base, traffic volumes and revenues from value-added services. However, due to market saturation, we expect future growth in our mobile services business in Region I and Region II to occur at lower rates than we and TNL have historically achieved. We cannot predict the effects of the eventual curtailment of the promotional activities that TNL has undertaken in connection with the launch of its mobile services in the State of São Paulo on the retention of our customer base in Region III.

Demand for Our Data Transmission Services

Our broadband services customer base in Region II has grown from approximately 1.8 million at December 31, 2008 to 2.0 million at December 31, 2011, and TNL s broadband services customer base in Region I has grown from approximately 2.0 million at December 31, 2008 to 2.9 million at December 31, 2011.

We believe that this growth has resulted from (1) our marketing and promotional campaigns, (2) the growth in the number of households in Region I and Region II that own personal computers, and (3) a shift in consumer preferences that has led an increasing number of our fixed-line customers to value the data transmission speeds available through our broadband services. We expect the number of our fixed-line customers that subscribe to our broadband services to continue to increase in the near term.

Effects of Expansion of Mobile Data Transmission Services

In December 2007, we acquired the authorizations and radio frequency licenses necessary for us to commence the offering of 3G services throughout Region II and TNL acquired the authorizations and radio frequency licenses necessary for us to commence the offering of 2G services in the State of São Paulo and 3G services throughout Region I and Region III. During 2009, 2010 and 2011, we and TNL undertook extensive capital expenditure projects to install the network equipment necessary to expand our offerings of these services.

In 2011, our mobile data transmission services in Region II, consisting of 2G and 3G services to mobile handsets and mini-modems, captured net additions (calculated based on the number of subscribers at the end of a period less the number of subscribers at the beginning of that period) of approximately 53,000. In 2011, TNL s mobile voice services in the State of São Paulo captured net additions of 7,000. In 2011, TNL s mobile data transmission services in Region I and Region III captured net additions of approximately 406,000. We expect that these services will generate significant additions to our mobile customer base and lead to long-term increases in our revenues and operating income before financial income (expenses) and taxes.

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The cost of our authorizations and radio frequency licenses was R$709 million and the cost of TNL s authorizations and radio frequency licenses for Region I and Region III was R$3,057 million, which we will pay to ANATEL in installments through 2023. During 2009, 2010 and 2011, we invested R$443 million, R$137 million, and R$94 million, respectively, in the network equipment necessary to offer these services, which has increased in our depreciation expenses. During 2009, 2010 and 2011, TNL invested R$1,899 million, R$609 million, and R$757 million, respectively, in the network equipment necessary to offer these services in Region I and Region III. We and TNL financed the purchase and installation of our network equipment through loans and vendor financing.

The marketing and promotion campaigns related to our offerings of mobile data transmission services contributed to an increase in the selling expenses of our respective mobile services segment and to an increase in the amount of discounts that we and TNL recorded against gross operating revenue.

Under our 3G radio frequency licenses, we are required to meet certain service expansion obligations that will require capital expenditures through 2016. If we are unable to fund these capital expenditures through our operating cash flows, we may incur additional indebtedness or vendor financing obligations, which would increase our outstanding indebtedness and financial expenses.

Effects of Competition on the Rates that We Realize and the Discounts We Record

The Brazilian telecommunications industry is highly competitive. The competitive environment is significantly affected by key trends, including the convergence of technology and services enables telecommunications service providers that were previously limited to providing a single service to provide services in other industry segments, such as in the case of broadband services provided by cable television service providers and by mobile service providers (using 3G technology) and in the case of traditional fixed-voice services transmitted by mobile telecommunications service providers.

In response to these competitive pressures, (1) we may offer our services at rates below the rate caps established by ANATEL, and (2) from time to time we offer our services with promotional discounts or offer additional complimentary services with the purchase of some of our services. We record the services sold at the rates established under our service plans or at rates approved by ANATEL and record the amount of these services represented by the promotional discounts or delivered on a complimentary basis as discounts and returns in our income statement.

Effects of Changes in Regulatory Requirements

Compliance with new regulations applicable to the telecommunications industry that are adopted by ANATEL from time to time and compliance with the obligations included in our concession contracts have required us to make capital expenditures, affected the revenues that we generate and imposed additional costs of service on our company.

Amendments to Our Concession Agreements and the General Plan on Universal Service

Our concession contracts to provide fixed-line services in Region I and Region II provide that these contracts may be amended by the parties every five years prior to the expiration date. On June 30, 2011, we entered into a concession agreement with ANATEL that governs our concession to provide fixed-line services and a concession agreement with ANATEL that governs our concessions to provide domestic long-distance services. These concession agreements consolidated our previously existing concession agreements for the Federal District and each of the states of Region II in a single concession agreement governing our concession to provide fixed-line services and a single concession agreement governs our concession to provide domestic long-distance services. In addition to the terms of our existing obligations under our previously existing local fixed-line concession and domestic long-distance concession agreements, the new concession agreements:

- remove the restrictions that had been in our local fixed-line concession agreements which had prohibited us from offering subscription television services, such as IP TV, over our fixed-line network;

- expands the scope of revenue generating activities that we must use to calculate the biannual fees that we owe in connection with our concession agreement, while allowing us to apply the amount of such fees to finance the expanded service obligations created by the amended General Plan on Universal Service in lieu of making payment to ANATEL;
- requires us to implement electronic billing systems;
- establishes new conditions under which ANATEL may access information from us;
- removes the grace period during which we can repair systemic service interruptions without incurring fines; and
- requires us to rescind our contracts if ANATEL determines they are contrary to any rules or regulations, economic order or public interest.

On June 30, 2011, the General Plan on Universal Service was amended. Among other things, these amendments:

- expanded our obligations to provide individual access to fixed-line voice services to economically disadvantaged segments of the Brazilian population within our service area, through programs to be established and regulated by ANATEL;
- reduced the density requirements applicable to our obligation to provide public telephones in urban areas within our service area; and
- expanded our obligation to provide universal service in rural and remote areas in the event that we obtain authorizations to use radio spectrum in the 450 Mhz band, including increased obligations to provide individual and group access to fixed-line voice services.

Because this amendment reduced the number of public telephones that we are required to maintain by approximately 300,000, we believe that the effects of these amendments will not have a material impact on our results of operations. In addition, we believe that the capital expenditures required to meet the increased obligations to provide individual access to fixed-line voice services to economically disadvantaged segments of the Brazilian population will not be material.

Adoption of Mobile Interconnection Regulations

In November 2011, ANATEL adopted new regulations under which ANATEL was authorized to reduce the then-current VC-1, VC-2 and VC-3 rates by as much as 18% in 2011, 12% in 2012 and 10% in 2013, after giving effect to an inflation adjustment based on the IST measured from June 2009. In February 2012, ANATEL reduced our VC-1, VC-2 and VC-3 rates by approximately 10%, although we are appealing the calculation of this rate reduction. These regulations also provided procedures under which ANATEL adopted a maximum VU-M rate that is applicable in the event that providers cannot agree upon the VU-M applicable in their interconnection agreements. In November 2011, ANATEL adopted new regulations that provided procedures under which ANATEL adopted a maximum VU-M rate that is applicable in the event that providers cannot agree upon the VU-M applicable in their interconnection agreements. The maximum VU-M rate established by ANATEL is R$0.35 per minute. As we are a provider of both fixed-line and mobile services, the effects of these new regulations and rates on our results of operations is uncertain.

Effects of Adjustments to Our Regulated Rates and Inflation

Telecommunications services rates are subject to comprehensive regulation by ANATEL. Our rates for local fixed-line services, domestic long-distance services, mobile services, interconnection to our fixed-line network, and EILD and SLD services are subject to regulation by ANATEL. We are required to obtain ANATEL approval prior to offering new alternative fixed-line or mobile plans. The rates established or approved by ANATEL for our services act as caps on the prices that we charge for these services, and we are permitted to offer these services at a discount from the rates approved by ANATEL. After ANATEL establishes or approves rate caps for these services, these rate caps are subject to annual adjustment based on the rate of inflation, as measured by the IST. Rate caps for local fixed-line plans are adjusted by inflation, as measured by the IST, less an amount that serves as a proxy for productivity gains achieved by our company and the local fixed-line services industry as a whole.

Because substantially all of our cost of services and operating expenses are incurred in *reais* in Brazil, these rate increases act as a natural hedge against inflation and, as a result, our operating margins have not been materially affected by inflation. However, because these rate adjustments are only made on an annual basis, in periods of severe inflation, we may not be able to pass our increased costs through to our customers as incurred.

A significant portion of our *real*-denominated debt bears interest at the TJLP or the CDI rate, which are partially adjusted for inflation, and, as a result, inflation results in increases in our interest expenses and debt service obligations.

Effects of Claims by ANATEL that Our Company Has Not Fully Complied with Our Quality of Service and Other Obligations

As a fixed-line service provider, we must comply with the provisions of the General Plan on Quality Goals. As a public regime service provider, we must comply with the network expansion and modernization obligations under the General Plan on Universal Service and our concession agreements. Our personal mobile services authorizations set forth certain network expansion obligations and targets and impose obligations on us to meet quality of service standards. In addition, we must comply with regulations of general applicability promulgated by ANATEL, which generally relate to quality of service measures.

If we fail to meet quality goals established by ANATEL under the General Plan on Quality Goals, fail to meet the network expansion and modernization targets established by ANATEL under the General Plan on Universal Service and our concession agreements, fail to comply with our obligations under our personal mobile services authorizations or fail to comply with our obligations under other ANATEL regulations, we may be subject to warnings, fines, intervention by ANATEL, temporary suspensions of service or cancellation of our concessions and authorizations.

On an almost weekly basis, we receive inquiries from ANATEL requiring information from us on our compliance with the various service obligations imposed on us by our concession agreements. If we are unable to respond satisfactorily to those inquiries or comply with our service obligations under our concession agreements, ANATEL may commence administrative proceedings in connection with such noncompliance. We have received numerous notices of commencement of administrative proceedings from ANATEL, mostly due to our inability to achieve certain targets established in the General Plan on Quality Goals and the General Plan on Universal Service.

At the time that ANATEL notifies us it believes that we have failed to comply with our obligations, we evaluate the claim and, based on our assessment of the probability of loss relating to that claim, may establish a provision. We vigorously contest a substantial number of the assessments made against us. As of December 31, 2011, the total estimated contingency in connection with all pending administrative proceedings brought by ANATEL against us in which we deemed the risk of loss as probable totaled R$278 million and we had recorded an aggregate provision related to these proceedings in the same amount, and the total estimated contingency in connection with all pending administrative proceedings brought by ANATEL against TNL in which TNL deemed the risk of loss as probable totaled R$941 million on a consolidated basis and TNL had recorded an aggregate provision related to these proceedings in the same amount.

During 2011, we recorded provisions related to administrative proceedings brought by ANATEL in the amount of R$41 million, and TNL recorded provisions related to administrative proceedings brought by ANATEL in the amount of R$123 million on a consolidated basis. Our provisions related to administrative proceedings brought by ANATEL generally have been sufficient to pay all amounts that we were ultimately required to pay with respect to claims brought by ANATEL.

Effects of Fluctuations in Exchange Rates between the Real and the U.S. Dollar

Substantially all of our cost of services and operating expenses are incurred in *reais* in Brazil. As a result, the appreciation or depreciation of the *real* against the U.S. dollar does not have a material effect on our operating margins. However, the costs of a substantial portion of the network equipment that we purchase for our capital expenditure projects are denominated in U.S. dollars or are U.S. dollar-linked. This network equipment is recorded on our balance sheet at its cost in *reais* based on the applicable exchange rate on the date the transfer of ownership, risks and rewards related to the purchased equipment occurs. As a result, depreciation of the *real* against the U.S. dollar results in this network equipment being more costly in *reais* and leads to increased depreciation expenses. Conversely, appreciation of the *real* against the U.S. dollar results in this network equipment being less costly in *reais* and leads to reduced depreciation expenses.

Our consolidated indebtedness denominated in U.S. dollars represented less than 0.1% of our outstanding indebtedness at December 31, 2011, and TNL s consolidated indebtedness denominated in U.S. dollars and euros represented 23.0% and 6.2%, respectively, of its consolidated outstanding indebtedness at December 31, 2011. As a result, when the *real* appreciates against the U.S. dollar or the euro:

- the interest costs on our indebtedness denominated in U.S. dollars or euros declines in *reais*, which positively affects our results of operations in *reais*;
- the amount of our indebtedness denominated in U.S. dollars or euros declines in *reais*, and our total liabilities and debt service obligations in *reais* decline; and
- our net interest expenses tend to decline as a result of foreign exchange gains that we record.

A depreciation of the *real* against the U.S. dollar has the converse effects.

In order to mitigate the effects of foreign exchange variations, we have established a hedging policy under which our exposure to foreign exchange variations is subject to limits set by our board of directors. In compliance with this policy, we typically enter into derivative transactions to swap the foreign exchange rate variation for variations the CDI. At December 31, 2011, TNL had entered into hedging transactions in respect of 96.2% of its consolidated indebtedness affected by exchange rate variations. The purpose of these hedging transactions is to seek to match the currency of our debt with that of our revenues to mitigate foreign exchange risk.

Effect of Level of Indebtedness and Interest Rates

At December 31, 2011, our total outstanding indebtedness on a consolidated basis was R$8,105 million, and TNL s total outstanding indebtedness on a consolidated basis was R$29,768 million. The level of our indebtedness results in significant interest expenses that are reflected in our income statement. Financial expenses consist of interest expense, exchange variations of U.S. dollar- and other foreign currency-denominated debt, foreign exchange losses or gains, and other items as set forth in note 7 to our consolidated financial statements. In 2011, we recorded total financial expenses of R$1,478 million, of which R$448 million consisted primarily of interest expenses on loans and financing and debentures payable to third parties. In 2011, TNL recorded total financial expenses of R$5,669 million on a consolidated basis, of which R$2,254 million consisted primarily of interest expenses on loans and debentures payable to third parties and R$1,030 million consisted of losses from monetary correction and exchange differences on third-party loans and financing. The interest rates that we pay depend on a variety of factors, including prevailing Brazilian and international interest rates and risk assessments of our company, our industry and the Brazilian economy made by potential lenders to our company, potential purchasers of our debt securities and the rating agencies that assess our company and its debt securities.

Standard & Poor s, Moody s and Fitch maintain ratings of our company and our debt securities. Any ratings downgrades in the future would likely result in increased interest and other financial expenses relating to loans and financings, including debt securities, and could adversely affect our ability to obtain such financing on satisfactory terms or in amounts required by us.

Seasonality

We do not have material seasonal operations.

Recent Developments

Corporate Reorganization

In February 2012, the shareholders of TNL, Telemar, Coari and Brasil Telecom approved a series of transactions which resulted in our merging with TNL and Telemar becoming a wholly-owned subsidiary of Brasil Telecom. For more information regarding the corporate reorganization, see Corporate Reorganization.

Disbursement Under Line of Credit with FINNVERA

In January 2012, Telemar received a disbursement in the aggregate principal amount of US$91.9 million under a financing agreement with Finnish Export Credit Ltd., or FINNVERA, that it had entered into in August 2009.

Disbursement Under Line of Credit with Crédit Agricole

In February 2012, Telemar received a disbursement in the aggregate principal amount of US$88.8 million under a financing agreement with Crédit Agricole Corporate and Investment Bank, or Crédit Agricole, that it had entered into in April 2010.

Offering of 5.75% Senior Notes due 2022

In February 2012, we issued US$1,500 million aggregate principal amount of our 5.75% Senior Notes due 2022. The net proceeds of this offering will be used for general corporate purposes, including the redemption and repayment of existing indebtedness.

Offering of Debentures

In March 2012, we issued two series of simple, unsecured non-convertible debentures in Brazil. The first series, in the aggregate principal amount of R$400 million, bears interest at the CDI rate plus 0.94% per annum, payable semi-annually in arrears, and matures in March 2017. The second series, in the aggregate principal amount of R$1,600 million, bears interest at the rate of IPCA plus 6.20% per annum, payable semi-annually in arrears, and is payable in two equal annual installments commencing in March 2019. We intend to use the proceeds of the offering of these debentures to refinance existing indebtedness.

Redemption of Debentures

In March 2012, we redeemed all R$1,500 million aggregate principal amount of simple, unsecured non-convertible debentures originally issued by TNL in May 2011.

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Results of Operations

The following discussion of our results of operations is based on our consolidated financial statements prepared in accordance with IFRS. The discussion of the results of our business segments is based upon financial information reported for each of the segments of our business, as presented in the table below.

The following tables set forth the operating results of each of our segments and the reconciliation of these results of our segments to our consolidated income statement. This segment information was prepared on the same basis as the information that our senior management uses to allocate resources among segments and evaluate their performance. We evaluate and manage the performance of our segments based on information prepared in accordance with IFRS and reflected in our consolidated financial statements.

	Year Ended December 31, 2011				
	Fixed-Line and Data Transmission Services	Mobile Services	Other	Eliminations	Consolidated
			(in millions of *reais*)		
Net operating revenue	R$ 8,048	R$ 2,006	R$ 607	R$ (1,415)	R$ 9,246
Cost of sales and services	(4,087)	(1,309)	(351)	1,161	(4,587)
Gross profit	3,960	697	256	(254)	4,659
Selling expenses	(992)	(436)	(135)	402	(1,161)
General and administrative expenses	(1,193)	(169)	(101)	19	(1,445)
Other operating income (expenses), net	(256)	(44)	(20)	(166)	(486)
Operating income before financial income (expenses) and taxes	R$ 1,519	R$ 48	R$	R$ 1	R$ 1,567

	Year Ended December 31, 2010				
	Fixed-Line and Data Transmission Services	Mobile Services	Other	Eliminations	Consolidated
			(in millions of *reais*)		
Net operating revenue	R$ 8,893	R$ 1,937	R$ 629	R$ (1,196)	R$ 10,263
Cost of sales and services	(4,015)	(1,379)	(323)	985	(4,732)
Gross profit	4,878	558	306	(211)	5,531
Selling expenses	(859)	(403)	(125)	361	(1,025)
General and administrative expenses	(1,270)	(173)	(163)	66	(1,539)
Other operating income (expenses), net	(268)	(17)	(10)	(213)	(508)
Operating income (loss) before financial income (expenses) and taxes	R$ 2,481	R$ (34)	R$ 9	R$ 4	R$ 2,460

	Year Ended December 31, 2009				
	Fixed-Line and Data Transmission Services	Mobile Services	Other	Eliminations	Consolidated
			(in millions of *reais*)		
Net operating revenue	R$ 9,431	R$ 1,894	R$ 677	R$ (1,081)	R$ 10,920
Cost of sales and services	(4,744)	(1,516)	(315)	812	(5,764)

Gross profit	4,686	378	362	(270)	5,156
Selling expenses	(1,117)	(524)	(188)	410	(1,418)
General and administrative expenses	(1,205)	(161)	(145)	77	(1,435)
Other operating income (expenses), net	(3,142)	(11)	(9)	(217)	(3,380)
Operating income (loss) before financial income (expenses) and taxes	R$ (778)	R$ (318)	R$ 19	R$ 0	R$ (1,077)

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In the following discussion, references to increases or decreases in any period are made by comparison with the corresponding prior period, except as the context otherwise indicates.

Year Ended December 31, 2011 Compared with Year Ended December 31, 2010

The following table sets forth the components of our consolidated income statement, as well as the percentage change from the prior year, for the years ended December 31, 2011 and 2010.

	Year ended December 31,		
	2011	2010	% Change
	(in millions of *reais*, except percentages)		
Net operating revenue	R$ 9,245	R$ 10,263	(9.9)
Cost of sales and services	(4,587)	(4,732)	(3.1)
Gross profit	4,659	5,531	(15.8)
Operating income (expenses)			
Selling expenses	(1,161)	(1,025)	13.2
General and administrative expenses	(1,445)	(1,539)	(6.1)
Other operating income (expenses), net	(486)	(508)	(4.3)
Operating income before financial income (expenses) and taxes	1,567	2,460	(36.3)
Financial income	1,406	979	43.5
Financial expenses	(1,478)	(1,060)	39.5
Financial expenses, net	(72)	(80)	(10.4)
Income before taxes	1,495	2,379	(37.1)
Income tax and social contribution	(490)	(408)	19.9
Net income	R$ 1,006	R$ 1,971	(49.0)

Net Operating Revenue

The composition of gross operating revenue by category of service before deduction of value-added and other indirect taxes and discounts is discussed below. We do not determine net operating revenue for each category of service as we do not believe such information to be useful to investors.

Gross operating revenue declined by 6.9% in 2011, principally due to a 7.5% decline in gross operating revenue of our fixed-line and data transmission services segment. The effects of this decline were partially offset by a 7.4% increase in gross operating revenue of our mobile services segment.

Net operating revenue declined by 9.9% in 2011, principally due to a 9.5% decline in net operating revenue of our fixed-line and data transmission services segment, the effects of which were partially offset by a 3.5% increase in net operating revenue of our mobile services segment. Net operating revenue generated by intersegment sales, which are eliminated in the consolidation of our financial statements, increased by 18.4% in 2011.

Net Operating Revenue of Our Fixed-Line and Data Transmission Services Segment

The following table sets forth the components of the gross operating revenue and net operating revenue of our fixed-line and data transmission services segment, as well as the percentage change from the prior year, for the years ended December 31, 2011 and 2010.

	Year Ended December 31,		
	2011	2010	% Change
	(in millions of *reais*, except percentages)		
Local fixed-line services	R$ 4,310	R$ 4,735	(9.0)
Local fixed-to-mobile calls (VC1)	1,373	1,569	(12.5)
Long-distance fixed-line services	1,392	1,732	(19.6)
Long-distance fixed-to-mobile calls (VC2 and VC3)	344	424	(18.9)
Remuneration for the use of the fixed-line network	484	501	(3.5)
Data transmission services	5,681	5,781	(1.7)
Public phones	156	194	(19.9)
Other fixed-line services	638	610	4.7
Total gross operating revenue	**14,377**	**15,546**	(7.5)
Value-added and other indirect taxes	(2,877)	(3,254)	(11.3)
Discounts and returns	(3,452)	(3,399)	1.2
Net operating revenue	**R$ 8,048**	**R$ 8,893**	(9.5)

Gross operating revenue of our fixed-line and data transmission services segment declined by 7.5% in 2011, principally due to:

- a 9.0% decline in gross operating revenue from local fixed-line services;
- a 19.6% decline in gross operating revenue from long-distance fixed-line calls;
- a 12.5% decline in gross operating revenue from local fixed-to-mobile calls;
- a 1.7% decline in gross operating revenue from data transmission services; and
- an 18.9% decline in gross operating revenue from long-distance fixed-to-mobile calls.

Gross Operating Revenue from Local Services

Gross operating revenue from local fixed-line services declined by 9.0% in 2011, primarily due to a 6.4% decline in gross operating revenue from monthly subscription fees, and a 26.2% decline in gross operating revenue from metered services.

Gross operating revenue from monthly subscription fees declined primarily as a result of a 6.3% decline in the average number of lines in service to 7.0 million during 2011 from 7.5 million during 2010, which occurred primarily as a result of the general trend in the Brazilian telecommunications industry to substitute mobile services in place of local fixed-line services.

Gross operating revenue from metered services charges declined principally due to the 29.0% decline in total billed minutes, which are the number of local minutes that exceed the monthly allowance under a customer s service plan, primarily as a result of (1) the decline in the average number of our lines in service, (2) the migration of our fixed-line customers from our basic service plans to our alternative plans that have higher monthly allowances of minutes, including our *Oi Fixo ilimitado* plans which we introduced in 2011 under which we offer an unlimited number of local fixed-to-fixed minutes and a larger number of fixed-to-fixed long distance minutes than under our other alternative plans at similar prices, and (3) the migration of local traffic origination to mobile handsets.

Gross Operating Revenue from Local Fixed-to-Mobile Calls

Gross operating revenue from local fixed-to-mobile calls, which are charged at the VC1 rate, declined by 12.5% in 2011, principally as a result of a 13.4% decline in the total number of local fixed-to-mobile minutes in 2011 as a result of (1) the 5.2% decline in the number of our fixed-line customers, (2) the migration of local traffic origination to mobile handsets as callers take advantage of mobile plans and promotions under which mobile service providers offer bonus mobile-to-mobile minutes within their networks at rates that are lower than a fixed-to-mobile minute, and (3) the introduction of our *Oi Fixo ilimitado* plans in 2011 under which we offer a larger number of fixed-to-mobile minutes for use to call the mobile customers of our company than under our other alternative plans.

Gross Operating Revenue from Long-Distance Fixed-Line Services

We account for revenue from long-distance calls that (1) originate and terminate on a fixed-line, (2) originate and terminate on a mobile device, or (3) originate on a mobile device and terminate on a fixed-line as revenue from long-distance fixed-line services. Gross operating revenue from long-distance fixed-line services declined by 19.6% during 2011, primarily due to an 18.6% decline in the total number of long-distance minutes, primarily as a result of (1) an aggressive discounting campaign undertaken by our competitors, which resulted in a decline in the total number of long-distance minutes, (2) the effects of the 5.2% decline in the number of our fixed-line customers, who are more likely to choose our long-distance fixed-line services than customers of other fixed-line providers, and (3) the introduction of our *Oi Fixo ilimitado* plans in 2011 under which we offer a larger number of fixed-to-fixed long distance minutes than under our other alternative plans and has led to a decline in the number of minutes that we record as long-distance fixed-line services.

Gross Operating Revenue from Long-Distance Fixed-to-Mobile Calls

We account for revenue from long-distance calls that originate on a fixed-line and terminate on a mobile device as revenue from long-distance fixed-to-mobile calls. Gross operating revenue from long-distance fixed-to-mobile calls, which are charged at the VC2 or VC3 rate, declined by 18.9% in 2011, principally as a result of a decline of 18.2% in the total number of fixed-to-mobile minutes charged at VC2 rates and VC3 rates, primarily as a result of (1) an aggressive discounting campaign undertaken in 2011 by one of our competitors, and (2) the effects of the 5.2% decline in the number of our fixed-line customers, who are more likely to choose our long-distance services for mobile-to-mobile long-distance calls than customers of other fixed-line providers.

Gross Operating Revenue from Remuneration for the Use of the Fixed-Line Network

Gross operating revenue from remuneration for the use of the fixed-line network declined by 3.5% in 2011, primarily as a result of a decline in gross operating revenue from interconnection fees paid to us for completing calls on our fixed-line network that were originated on the networks of other fixed-line service providers, and (2) a decline in gross operating revenue from interconnection fees paid to us for completing calls on our fixed-line network that were originated on the networks of mobile service providers, both primarily as a result of the 5.2% decline in the number of our fixed-line customers.

Of our gross operating revenue from remuneration for the use of the fixed-line network, 21.2% in 2011 and 23.5% in 2010 represented interconnection fees paid by Brasil Telecom Mobile for the use of our fixed-line network to complete mobile-to-fixed calls and was eliminated in the consolidation of our financial statements.

Gross Operating Revenue from Data Transmission Services

Gross operating revenue from data transmission services declined by 1.7% in 2011, principally due to (1) a 9.1% decline in gross operating revenue from ADSL subscriptions, the effects of which were partially offset by a 9.4% increase in gross operating revenue from commercial data transmission services.

Gross operating revenue from ADSL subscriptions declined primarily due to a 7.8% decline in our average gross operating revenue per subscriber as a result of aggressive promotions that we launched during 2011 in an effort to expand our base of broadband customers, the effects of which were partially offset by a 5.3% increase in the average number of ADSL subscriptions to approximately 2,032,000 during 2011 from approximately 1,953,000 during 2010. As of December 31, 2011, our ADSL customer base represented 29.8% of our total fixed lines in service as compared to 26.8% as of December 31, 2010.

Gross operating revenue from commercial data transmission services increased primarily as a result of a 23.3% increase in gross operating revenue from IP services principally as a result of the increased demand for these services, particularly from public entities, banks and card payment companies, the effects of which were partially offset by a 37.0% decline in gross operating revenue from switching packs and frame relay services. Of our gross operating revenue from commercial data transmission services, 16.0% during 2011 and 8.5% during 2010 represented fees paid by Brasil Telecom Mobile and was eliminated in the consolidation of our financial statements.

Gross Operating Revenue from the Sale of Pre-paid Calling Cards for Use in Public Telephones

Gross operating revenue from the sale of pre-paid calling cards for use in public telephones declined by 19.9% in 2011, principally due to the decline in the number of public phone credits used as a result of a general trend to reduce usage of pre-paid calling cards for use in public telephones as customers substitute usage of mobile handsets in place of usage of public phones in response to promotions by mobile service providers to the pre-paid segment, including bonus calls and pre-paid card recharges at promotional reduced rates.

Charges Against Gross Operating Revenue

Value-Added and Other Indirect Taxes

Value-added and other indirect taxes on our fixed-line and data transmission services declined by 11.3% in 2011, primarily reflecting the decline in the gross operating revenue of the principal fixed-line services with respect to which these taxes are assessed.

We are required to contribute to the Universal Telecommunications Service Fund (*Fundo de Universalização dos Serviços de Telecomunicações*), which we refer to as the FUST, and the Fund for the Technological Development of Telecommunications (*Fundo para o Desenvolvimento Tecnológico das Telecomunicações Brasileiras*), which we refer to as the FUNTTEL. We are required to contribute 1.0% of our gross operating revenue from the rendering of telecommunications services, net of (1) the Social Integration Program (*Programa de Integração Social*), or PIS, taxes, (2) the federal Contribution for Social Security Financing (*Contribuição para Financiamento da Seguridade Social COFINS*), or COFINS, and (3) ICMS, to the FUST. We are required to contribute 0.5% of our gross operating revenue from the rendering of telecommunications services, net of PIS, COFINS and ICMS taxes, to the FUNTTEL.

Discounts

Discounts offered on our fixed-line services generally applied to data transmission services, monthly subscription fees and intelligent network services (such as caller ID, call forwarding and conference calling). Discounts on our fixed-line and data transmission services increased by 1.2% in 2011, primarily as a result of an increase in discounts offered for our broadband services as a result of increased competition for other providers and as part of our efforts to promote the migration of our broadband customers to higher bandwidth subscriptions.

Net Operating Revenue

As a result of the foregoing, net operating revenue of our fixed-line and data transmission services segment declined by 9.5% to R$8,048 million in 2011 from R$8,893 million in 2010.

Net Operating Revenue of Our Mobile Services Segment

The following table sets forth the components of the gross operating revenue and net operating revenue of our mobile services segment, as well as the percentage change from the prior year, for the years ended December 31, 2011 and 2010.

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	Year Ended December 31,		
	2011	2010	% Change
	(in millions of *reais*, except percentages)		
Mobile telephone services	R$ 1,658	R$ 1,490	12.2
Remuneration for the use of the mobile network	1,204	1,134	6.1
Sales of handsets and accessories	16	53	(70.2)
Total gross operating revenue	**2,877**	**2,677**	7.5
Value-added and other indirect taxes	(492)	(445)	10.5
Discounts and returns	(379)	(295)	28.6
Net operating revenue	**R$ 2,006**	**R$ 1,937**	3.5

Gross operating revenue of our mobile services segment increased by 7.5% in 2011, due to (1) a 12.2% increase in gross operating revenue from mobile telephone services, and (2) a 6.1% increase in gross operating revenue from remuneration for the use of our mobile network.

Gross Operating Revenue from Mobile Services

Gross operating revenue from mobile services increased by 12.2% in 2011, principally due to (1) a 5.9% increase in gross operating revenue from monthly subscription fees, and (2) a 21.0% increase in gross operating revenue from billed minutes (originating calls).

The average number of our pre-paid mobile customers increased by 11.5% to 7.1 million during 2011 from 6.3 million during 2010, primarily as a result of our launch of new promotions that include bonus minutes for long distance calls, packages of data services and credits for use for our short message services, or SMS. The average number of our post-paid mobile customers, including customer that subscribe to our *Oi Controle* plans, increased by 2.4% to approximately 1,050,000 during 2011 from approximately 1,025,100 during 2010, primarily as a result of the success of our advertising campaigns to promote our principal mobile services, such as *Oi a vontade*. As of December 31, 2011, pre-paid customers represented 86.5% of our mobile customer base and post-paid customers represented 13.5% of our mobile customer base. Our average monthly net revenue per user (calculated based on the total revenue for the year divided by the monthly average customer base for the year divided by 12) declined by 1.9% to R$21.0 during 2011 from R$21.4 during 2010.

Gross operating revenue from monthly subscription fees, which includes gross operating revenue from our mobile data transmission services, increased primarily as a result of (1) an increase in the number of our post-paid customers, and (2) the migration of our post-paid customer base to plans offering a greater number of minutes and with higher subscription fees.

Gross operating revenue from billed minutes, which are the number of local minutes used by pre-paid customers plus the number of local minutes used by post-paid customers in excess of the monthly allowance under the customer s service plan, increased primarily as a result of (1) the 11.5% increase in the average number of our pre-paid mobile customers, and (2) the increase in sales of promotional pre-paid service packages which permit our customers to make calls to mobile customers within our networks and send SMS messages to mobile subscribers of any Brazilian mobile service provider.

Gross Operating Revenue from Remuneration for the Use of the Mobile Network

Gross operating revenue from remuneration for the use of the mobile network increased by 6.1% in 2011, primarily due to a 10.4% increase in the number of our mobile customers, the effects of which were partially offset by customers of others mobile providers taking advantage of promotions offered by those providers that include packages of minutes and SMS services for on net traffic.

Of the gross operating revenue from remuneration for the use of the mobile network, 45.2% in 2011 and 40.8% in 2010 represented interconnection fees paid by Oi for the use of Brasil Telecom Mobile s network to complete fixed-to-mobile calls and was eliminated in the consolidation of our financial statements.

Charges Against Gross Operating Revenue

Value-Added and Other Indirect Taxes

Value-added and other indirect taxes on our mobile services increased by 10.5% in 2011, primarily reflecting the increase in the gross operating revenue of our mobile services segment in 2011.

Discounts

Discounts offered on our mobile services generally consist of rebates on pre-paid telephone cards (typically having commissions of approximately 10.0% over the face amount sold), local fixed-line calls, long-distance calls, and intelligent network services (such as caller ID, call forwarding and conference calling). Discounts on our mobile services increased by 28.6% in 2011, primarily as a result of our strategy to increase discounts to maintain and increase our market share.

Net Operating Revenue

As a result of the foregoing, revenue from sales and services of the mobile services segment increased by 3.5% to R$2,006 million in 2011 from R$1,937 million in 2010.

Cost of Sales and Services

Cost of sales and services declined by 3.1% in 2011, principally due to a 5.1% decline in cost of sales and services of our mobile services segment, the effects of which were partially offset by a 1.8% increase in cost of sales and services of our fixed-line and data transmission services segment.

Of the cost of sales and services of our fixed-line and data transmission services segment, 13.4% in 2011 and 4.7% in 2010 represented interconnection fees paid by Oi for the use of Brasil Telecom Mobile s mobile network to complete fixed-to-mobile calls. These fees were eliminated in the consolidation of our financial statements.

Of the cost of sales and services of our mobile services segment, 21.9% in 2011 and 23.4% in 2010 represented (1) interconnection fees paid by Brasil Telecom Mobile for the use of Oi s fixed-line network to complete mobile-to-fixed calls, and (2) fees paid by Brasil Telecom Mobile for EILD services. These fees were eliminated in the consolidation of our financial statements.

The following table sets forth the components of our cost of sales and services, as well as the percentage change from the prior year, for the years ended December 31, 2011 and 2010.

	Year Ended December 31,		
	2011	**2010**	**% Change**
	(in millions of *reais*, except percentages)		
Interconnection	R$ 1,711	R$ 1,982	(13.7)
Depreciation and amortization	843	807	4.4
Grid maintenance service	687	616	11.4
Rental and insurance	504	471	7.0
Personnel	375	335	12.0
Costs of handsets and accessories	24	48	(50.1)
Concession contract renewal fee	49	57	(13.6)
Other costs of sales and services	394	416	(5.2)
Total cost of sales and services	R$ 4,587	R$ 4,732	(3.1)

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Cost of Sales and Services of Our Fixed-Line and Data Transmission Services Segment

Cost of sales and services of our fixed-line and data transmission services segment increased by 1.8% in 2011, principally due to:

- a 27.2% increase in rental and insurance costs to R$654 million in 2011 from R$514 million in 2010, primarily as a result of increases in rental expenses incurred for leases of physical space, increases in right-of-way costs and increases in tower rental costs; and

- an 11.7% increase in network maintenance costs to R$627 million in 2011 from R$562 million in 2010, primarily as a result of our implementation of a plan to improve network quality.

The effects of these increases was partially offset by an 8.0% decline in interconnection costs to R$1,834 million in 2011 from R$1,993 million in 2010, primarily as a result of the reduction in fixed-to-mobile traffic and long distance fixed-line traffic.

The gross profit of our fixed-line and data transmission services segment declined by 18.8% to R$3,960 million in 2011 from R$4,878 million in 2010. As a percentage of net operating revenue of this segment, gross profit declined to 49.2% in 2011 from 54.9% in 2010.

Cost of Sales and Services of Our Mobile Services Segment

Cost of sales and services of our mobile services segment declined by 5.1% in 2011, principally due to:

- an 8.6% decline in interconnection costs to R$526 million in 2011 from R$575 million in 2010, primarily as a result of the reduction in fixed-to-mobile traffic and long distance fixed-line traffic;

- a 50.1% decline in the cost of handsets and accessories to R$24 million in 2011 from R$48 million in 2010, primarily as a result of the reduction of our sales of premium mobile devices, such as smart phones; and

- a 24.8% decline in third-party service costs to R$34 million in 2011 from R$45 million in 2010, primarily as a result of our program to reduce costs by consolidating our third-party services in a smaller number of suppliers.

The gross profit of our mobile services segment increased by 24.9% to R$697 million in 2011 from R$558 million in 2010. As a percentage of net operating revenue of this segment, gross profit increased to 34.7% in 2011 from 28.8% in 2010.

Gross Profit

As a result of the foregoing, our consolidated gross profit declined by 15.8% to R$4,659 million in 2011 from R$5,531 million in 2010. As a percentage of net operating revenue, gross profit declined to 50.4% in 2011 from 53.9% in 2010.

Operating Expenses

Selling Expenses

Selling expenses increased by 13.2% during 2011, principally due to (1) a 15.5% increase in selling expenses of our fixed-line and data transmission services segment, and (2) an 8.2% increase in selling expenses of our mobile services segment.

Fixed-Line and Data Transmission Services Segment

Selling expenses of our fixed-line and data transmission services segment increased by 15.5% in 2011, principally due to:

- a 17.2% increase in contact center expenses to R$340 million in 2011 from R$290 million in 2010, primarily due to the renegotiation of some collective bargaining agreements by our contact center, which is included in our other segment, and expenditures related to service quality campaigns conducted to support our broadband service;
- a 54.6% increase in personnel expenses to R$119 million in 2011 from R$77 million in 2010, primarily as a result of an increase in the number of employees and increases in the compensation of some of our employees as a result of the renegotiation of some of our collective bargaining agreements at the end of 2010;
- a 24.9% increase in third-party service expenses to R$156 million in 2011 from R$125 million in 2010, primarily due to increased commissions paid in relation to sales of our *Oi Velox* internet service; and
- an 766.7% increase in materials expenses to R$26 million in 2011 from R$3 million in 2010, primarily due to an increase in purchases of modems as a result of the introduction of our campaign to deliver free modems to mobile subscribers of *Oi Velox* beginning in April 2011.

As a percentage of net operating revenue of this segment, selling expenses increased to 12.3% in 2011 from 9.7% in 2010.

Mobile Services Segment

Selling expenses of our mobile services segment increased by 8.2% in 2011, principally due to:

- a 60.2% increase in third-party service expenses to R$235 million in 2011 from R$147 million in 2010, primarily as a result of (1) an increase in the number of promotional bonus credits we distributed to our pre-paid costumers upon their purchase of additional paid credits for use to make pre-paid calls, and (2) an increase in sales commission expenses in the post-paid segment, and increased commission expenses relating to our *Oi Conta Total* plans, part of which are allocated to this segment; and
- a 36.8% increase in publicity and advertising expenses to R$60 million in 2011 from R$44 million in 2010, primarily as a result of an increase in expenditures on our advertising campaigns to support our principal mobile services, such as our *Oi a vontade* and *Oi cartão* services and our use of sponsorship of concerts and other events and alternative media to raise brand awareness of our services.

The effects of these increases were partially offset by (1) a 56.8% decline in contact center expenses to R$27 million in 2011 from R$61 million in 2010, and (2) an 82.1% decline in materials expenses to R$7 million in 2011 from R$37 million in 2010, primarily as a result of our decision in 2010 to end our subsidies for mini-modems used by our mobile data transmission customers.

As a percentage of net operating revenue of this segment, selling expenses increased to 21.7% in 2011 from 20.8% in 2010.

General and Administrative Expenses

General and administrative expenses declined by 6.1% during 2011, principally due to a 6.0% decline in general and administrative expenses of our fixed-line segment and a 37.7% decline in general and administrative expenses of our other segment.

Fixed-Line and Data Transmission Services Segment

General and administrative expenses of our fixed-line and data transmission services segment declined by 6.0% in 2011, principally due to:

- a 16.8% decline in third-party service expenses to R$351 million in 2011 from R$422 million in 2010, primarily as a result of reduced postage expenses due to a change in our billing and collection procedures as part of which we no longer rely on mailing invoices to collect accounts due from customers that are in arrears by more than two months; and

- a 17.1% decline in depreciation and amortization expenses to R$158 million in 2011 from R$195 million in 2010, primarily as a result of the increase in the amount of the property, plant and equipment of this segment that has been fully depreciated.

The effects of these declines were partially offset by (1) a 25.1% increase in personnel expenses to R$259 million in 2011 from R$207 million in 2010, primarily as a result of an increase in the number of employees and increases in the compensation of some of our employees as a result of the renegotiation of some of our collective bargaining agreements at the end of 2010, and (2) an 8.2% increase in consulting expenses to R$218 million in 2011 from R$202 million in 2010, primarily as a result of an increase in expenses for consulting and legal advice related to the corporate reorganization.

As a percentage of net operating revenue of this segment, general and administrative expenses increased to 14.8% in 2011 from 14.3% in 2010.

Mobile Services Segment

General and administrative expenses of our mobile services segment declined by 2.3% in 2011, primarily due to (1) a 44.5% decline in third-party service expenses to R$39 million in 2011 from R$70 million in 2010, primarily as a result of our program to reduce costs and expenses in this segment, and (2) a 35.8% decline in depreciation and amortization expenses to R$23 million in 2011 from R$36 million in 2010, primarily as a result of the increase in the amount of the property, plant and equipment of this segment that has been fully depreciated.

As a percentage of net operating revenue of this segment, general and administrative expenses declined to 8.4% from 8.9% in 2010.

Other Segment

General and administrative expenses of our other segment declined by 37.7% in 2011, primarily due to a (1) a 50.1% decline in personnel expenses to R$33 million in 2011 from R$66 million in 2010, primarily as a result of a reduction in the number of employees of our internet portal companies, and (2) a 35.4% decline in third-party service expenses to R$32 million in 2011 from R$49 million in 2010, primarily as a result of reduction in our costs relating to data processing.

Other Operating Expenses, Net

Other Operating Income

Other operating income increased by 6.9% to R$560 million in 2011 from R$524 million in 2010, primarily as a result of (1) our recognition of R$50 million in prescribed dividends during 2011, and (2) a 33.7% increase in rental of infrastructure to R$120 million in 2011 from R$90 million in 2010, primarily as a result of increased demand for these services from other service providers as a result of the growth of their customer bases. The effects of these factors was partially offset by a 60.3% decline in income on disposal of property, plant and equipment to R$21 million in 2011 from R$54 million in 2010.

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Other Operating Expense

Other operating expenses increased by 1.4% to R$1,046 million in 2011 from R$1,032 million in 2010, primarily as a result of:

- a 40.9% increase in provisions for contingencies to R$571 million in 2011 from R$405 million in 2010, primarily as a result of (1) the effects on our other operating expenses during 2010 of a R$140 million reversal of our provisions relating to ICMS tax credits as a result of a favorable court decision in 2010, and (2) the constitution of additional provisions of R$26 million during 2011 relating to new labor and civil matters and changes in the estimate of some of our provision; and

- an 11.7% increase in taxes to R$309 million in 2011 from R$276 million in 2010, primarily as a result of PIS and COFINS taxes recorded on the increased distributions of interest on shareholders equity received from some of our subsidiaries.

The effects of these factors was partially offset by (1) a 72.7% decline in employee and management profit sharing to R$28 million in 2011 from R$103 million in 2010, primarily as a result of the decline of the performance of indicators used to estimate this provision, and (2) a 66.3% decline in write-offs of property, plant and equipment to R$28 million in 2011 from R$83 million in 2010.

Operating Income before Financial Income (Expenses) and Taxes

As a result of the foregoing, our consolidated operating income before financial income (expenses) and taxes declined by 36.3% to R$1,567 million in 2011 from R$2,460 million in 2010. As a percentage of net operating revenue, operating income before financial income (expenses) and taxes declined to 17.0% in 2011 from 24.0% in 2010.

Fixed-Line and Data Transmission Services Segment

The operating income before financial income (expenses) and taxes of our fixed-line and data transmission services segment declined by 38.8% to R$ 1,519 million in 2011 from R$2,481 million in 2010. As a percentage of the net operating revenue of this segment, operating income before financial income (expenses) and taxes declined to 18.9% in 2011 from 27.9% in 2010.

Mobile Services Segment

The operating income before financial income (expenses) and taxes of our mobile services segment was R$48 million in 2011 compared to operating loss before financial income (expenses) and taxes of R$34 million in 2010. As a percentage of the net operating revenue of this segment, operating income before financial income (expenses) and taxes was 2.4% in 2011 compared to operating loss before financial income (expenses) and taxes of 1.7% in 2010.

Financial Expenses, Net

Financial Income

Financial income increased by 43.5% to R$1,406 million in 2011 from R$979 million in 2010, primarily due to:

- a 359.1% increase in interest and inflation adjustment on other assets to R$345 million in 2011 from R$75 million in 2010, primarily as a result of an exchange gain on the foreign currency time deposits in which the proceeds of our issuance of 9.75% Senior Notes due 2016 were held prior to the use of these proceeds;

- a 33.9% increase in income from short-term investments to R$384 million in 2011 from R$287 million in 2010, primarily as a result of an increase in the average amount of our financial investments; and

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a 29.70% increase in interest and inflation adjustment on amounts due from related parties to R$307 million in 2011 from R$236 million in 2010, primarily as a result of accrued interest and inflation adjustments on the debentures of Telemar that we hold.

Financial Expenses

Financial expenses increased by 39.5% to R$1,478 million in 2011 from R$1,060 million in 2010, primarily due to (1) a 73.9% increase in interest and inflation adjustments on other liabilities to R$474 million in 2011 from R$273 million in 2010, primarily as a result of a R$122 million exchange loss on foreign currency time deposits of a portion of the proceeds of our 9.75% Senior Notes due 2016, and a R$42 million increase in inflation adjustment to our tax financing program debt as a result of an increase in the Selic interest rate, and (2) inflation adjustment estimates of judicial deposits of R$199 million during 2011. The effects of these factors was partially offset by a 34.2% decline in inflation adjustments of provisions to R$167 million in 2011 from R$254 million in 2010, primarily as a result of an inflation adjustment estimate on labor contingencies in 2011.

Income Tax and Social Contribution

The composite corporate statutory income tax and social contribution rate was 34% in each of 2011 and 2010. Income tax and social contribution expense increased by 19.9% to R$490 million in 2011 from R$408 million in 2010. Our effective tax rate was 33.0% in 2011 and 17.1% in 2010. The table below sets forth a reconciliation of the composite corporate statutory income tax and social contribution rate to our effective tax rate for each of the periods presented.

	Year Ended December 31,	
	2011	**2010**
Composite corporate statutory income tax and social contribution rate	34.0%	34.0%
Tax effects of interest on shareholders equity		(5.2)
Tax effects of permanent exclusions (additions)	(1.0)	(5.2)
Tax effects of compensation of tax loss carryforwards		(1.0)
Tax effects of unrecognized deferred tax assets		0.2
Tax effects of recognized deferred tax assets	0.0	(5.7)
Effective rate	33.0%	17.1%

Our effective tax rate was 33.0% in 2011, primarily as a result of the tax effects of non-taxable income and non-deductible expenses, which lowered our effective tax rate by 1.0%.

Our effective tax rate was 17.2% in 2010, primarily as a result of (1) the tax effect of our recognition of deferred tax assets accrued during prior years, but not previously recognized due to uncertainty regarding their eventual realization, which lowered our effective tax rate by 5.7%, (2) the tax effect of our payment of interest on shareholders equity, which lowered our effective tax rate by 5.2%, and (3) the tax effects of non-deductible expenses of prior years, primarily amortization expenses of Copart 1, Copart 2 and Brasil Telecom Holding and adjustments made to the income tax and social contribution calculation of prior year, which lowered our effective tax rate by 5.2%.

Net Income

Our consolidated net income declined by 49.0% to R$1,006 million in 2011 from R$1,971 million in 2010. As a percentage of net operating revenue, net income declined to 10.9% in 2011 from 19.2% in 2010.

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Year Ended December 31, 2010 Compared with Year Ended December 31, 2009

The following table sets forth the components of our consolidated income statement, as well as the percentage change from the prior year, for the years ended December 31, 2009 and 2010.

	Year ended December 31,		
	2010	2009	% Change
	(in millions of *reais*, except percentages)		
Net operating revenue	R$ 10,263	R$ 10,920	(6.0)
Cost of sales and services	(4,732)	(5,764)	(17.9)
Gross profit	5,531	5,156	7.3
Operating income (expenses)			
Selling expenses	(1,025)	(1,418)	(27.7)
General and administrative expenses	(1,539)	(1,435)	7.3
Other operating income (expenses), net	(508)	(3,380)	(85.0)
Operating income before financial income (expenses) and taxes	2,460	(1,077)	n.m
Financial income	979	630	55.4
Financial expenses	(1,060)	(912)	16.2
Financial expenses, net	(80)	(281)	(71.5)
Income (loss) before taxes	2,379	(1,358)	n.m
Income tax and social contribution	(408)	339	(220.6)
Net income (loss)	R$ 1,971	R$ (1,019)	n.m.

n.m. Not meaningful

Net Operating Revenue

The composition of gross operating revenue by category of service before deduction of value-added and other indirect taxes and discounts is discussed below. We do not determine net operating revenue for each category of service as we do not believe such information to be useful to investors.

Gross operating revenue declined by 1.1% in 2010, principally due to a 1.0% decline in gross operating revenue of our fixed-line and data transmission services segment. The effects of this decline were partially offset by a 4.8% increase in gross operating revenue of our mobile services segment.

Net operating revenue declined by 6.0% in 2010, principally due to a 5.7% decline in net operating revenue of our fixed-line and data transmission services segment, the effects of which were partially offset by a 2.3% increase in net operating revenue of our mobile services segment. Net operating revenue generated by intersegment sales, which are eliminated in the consolidation of our financial statements, increased by 10.6% in 2010.

Net Operating Revenue of Our Fixed-Line and Data Transmission Services Segment

The following table sets forth the components of the gross operating revenue and net operating revenue of our fixed-line and data transmission services segment, as well as the percentage change from the prior year, for the years ended December 31, 2009 and 2010.

	Year Ended December 31,		
	2010	2009	% Change
	(in millions of *reais*, except percentages)		
Local fixed-line services	R$ 4,735	R$ 4,663	1.5
Local fixed-to-mobile calls (VC1)	1,569	1,819	(13.7)
Long-distance fixed-line services	1,732	1,963	(11.8)
Long-distance fixed-to-mobile calls (VC2 and VC3)	424	583	(27.3)
Remuneration for the use of the fixed-line network	501	467	7.3
Data transmission services	5,781	5,248	10.2
Public phones	194	393	(50.6)
Other fixed-line services	610	574	6.3
Total gross operating revenue	**15,546**	**15,710**	(1.0)
Value-added and other indirect taxes	(3,254)	(3,554)	(8.4)
Discounts and returns	(3,399)	(2,725)	24.7
Net operating revenue	**R$ 8,893**	**R$ 9,431**	(5.7)

Gross operating revenue of our fixed-line and data transmission services segment declined by 1.0% in 2010, principally due to (1) a 13.7% decline in gross operating revenue from local fixed-to-mobile calls, (2) an 11.8% decline in gross operating revenue from long-distance fixed-line calls, (3) an 27.3% decline in gross operating revenue from long-distance fixed-to-mobile calls, and (4) a 50.6% decline in gross operating revenue from the sale of pre-paid calling cards for use in public telephones. The effects of these declines were partially offset by (1) a 10.2% increase in gross operating revenue from data transmission services, (2) a 1.5% increase in gross operating revenue from local fixed-line services, and (3) a 7.3% increase in gross operating revenue from remuneration for the use of our fixed-line network.

Gross Operating Revenue from Local Services

Gross operating revenue from local fixed-line services increased by 1.5% in 2010, primarily due to a 5.5% increase in gross operating revenue from monthly subscription fees, the effects of which were partially offset by a 22.9% decline in gross operating revenue from metered services.

Gross operating revenue from monthly subscription fees increased primarily as a result of (1) a 5.9% increase in the number of subscriptions to our alternative plans to 6.8 million at December 31, 2010 from 6.4 million at December 31, 2009, (2) rate increases for our basic service plans of 0.98% in October 2009 and 0.98% in February 2010, and (3) rate increases for our alternative plans that reflected increases in inflation of 0.98% in 2009 and 5.65% in 2010, as measured by the IST. The effects of these increases were partially offset by a 5.8% decline in the average number of lines in service to 7.5 million during 2010 from 7.9 million during 2009.

Gross operating revenue from metered services charges declined principally due to the 26.9% decline in total billed minutes, which are the number of local minutes that exceed the monthly allowance under a customer s service plan, primarily as a result of (1) the migration of our fixed-line customers from our basic service plans to our alternative plans that have higher monthly allowances of minutes, and (2) the migration of local traffic origination to mobile handsets as callers take advantage of mobile plans and promotions under which mobile service providers offer mobile-to-mobile minutes within their networks at rates that are lower than fixed-to-mobile minutes. The effects of this decline were partially offset by rate increases for metered services of 0.98% in October 2009 and 0.98% in February 2010.

Gross Operating Revenue from Local Fixed-to-Mobile Calls

Gross operating revenue from local fixed-to-mobile calls, which are charged at the VC1 rate, declined by 13.7% in 2010, principally as a result of a 47.2% decline in the total number of local fixed-to-mobile minutes in 2010 as our fixed-line customers opted to take advantage of mobile service plans under which the charge for a mobile-to mobile minute is less than the charge for a fixed-to-mobile minute. This decline was partially offset by increases in the VC1 rate of 0.98% in February 2010.

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Gross Operating Revenue from Long-Distance Fixed-Line Services

Gross operating revenue from long-distance fixed-line services declined by 11.8% during 2010, primarily due to (1) an 8.3% decline in gross operating revenue from long-distance calls originating on mobile devices, and (2) a 15.6% decline in gross operating revenue from fixed-to-fixed intrasectorial long-distance calls. This was principally as a result of decline in the total number of mobile-to-mobile long-distance calls minutes, primarily as a result of an aggressive discounting campaign undertaken in 2010 by one of our competitors.

We account for calls as intrasectorial calls if they are:

- originated on a fixed-line telephone and terminated on a fixed-line telephone in which callers are located in the same sector, but in different local areas, which are charged at long-distance rates regulated in accordance with the distance separating callers. A sector is a set of local areas, as established by ANATEL, that generally corresponds to a Brazilian state.

- originated by a mobile subscriber registered in one home registration area and terminated on (1) a fixed-line telephone or (2) a mobile handset in another home registration area sharing the same first digit (for example, Brasília (area code 61) and Goiânia (area code 62), which are charged at the VC2 or VC3 rate.

We account for calls as intersectorial calls if they are:

- originated on a fixed-line telephone and terminated on a fixed-line telephone in which callers are located in the same service region, but in different sectors, which are charged at long-distance rates regulated in accordance with the distance separating callers; or

- originated by a mobile subscriber registered in one home registration area and terminated on (1) a fixed-line telephone or (2) a mobile handset in another home registration area that does not share the same first digit (for example, Brasília (area code 61) and São Paulo (area code 11), which are charged at the VC2 or VC3 rate, as intersectorial long-distance calls.

Gross operating revenue from intrasectorial long-distance calls and intersectorial long-distance calls declined principally as a result of a 15.0% decline in the total number of intrasectorial long-distance minutes, primarily as a result of (1) an aggressive discounting campaign undertaken in 2010 by one of our competitors, (2) a 5.9% increase in the number of subscriptions to our alternative plans, which include some long-distance minutes, which has led to a decline in the number of minutes that we record as long-distance fixed-line services, and (3) the effects of the decline in the number of our fixed-line customers, who are more likely to choose our long-distance services than customers of other fixed-line providers. The effects of these declines were partially offset by an increase in our regulated long-distance rates of 0.98% and 0.66% that were implemented in September 2009 and October 2010, respectively.

Gross Operating Revenue from Long-Distance Fixed-to-Mobile Calls

Gross operating revenue from long-distance fixed-to-mobile calls, which are charged at the VC2 or VC3 rate, declined by 27.3% in 2010, principally as a result of declines of 12.3% and 4.0% in the total number of fixed-to-mobile minutes charged at VC2 rates and VC3 rates, respectively, primarily as a result of (1) an aggressive discounting campaign undertaken in 2010 by one of our competitors, (2) a 5.9% increase in the number of subscriptions to our alternative plans, which include some long-distance minutes, which has led to a decline in the number of minutes that we record as long-distance mobile services, and (3) the effects of the decline in the number of our fixed-line customers, who are more likely to choose our long-distance services than customers of other fixed-line providers. The effects of these declines were partially offset by increases in the VC2 and VC3 rates of 0.98% that were implemented in February 2010.

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Gross Operating Revenue from Remuneration for the Use of the Fixed-Line Network

Gross operating revenue from remuneration for the use of the fixed-line network increased by 7.3% in 2010, primarily as a result of promotions offered in 2010 by mobile service providers, including Oi and Brasil Telecom Mobile, which provided complimentary minutes to mobile customers that could be used for mobile-to-fixed calls.

Of our gross operating revenue from remuneration for the use of the fixed-line network, 23.5% in 2010 and 20.6% in 2009 represented interconnection fees paid by Brasil Telecom Mobile for the use of our fixed-line network to complete mobile-to-fixed calls and was eliminated in the consolidation of our financial statements.

Gross Operating Revenue from Data Transmission Services

Gross operating revenue from data transmission services increased by 10.2% in 2010, principally due to (1) a 17.4% increase in gross operating revenue from commercial data transmission services, and (2) a 5.8% increase in gross operating revenue from ADSL subscriptions.

Gross operating revenue from commercial data transmission services increased primarily as a result of (1) a 25.1% increase in gross operating revenue from IP services principally as a result of the increased demand for these services, particularly from public entities, banks and card payment companies, and (2) a 28.6% increase in gross operating revenue from EILD services, principally as a result of the increased demand for these services, due to the integration of the Telemar and Oi networks. Of our gross operating revenue from commercial data transmission services, 8.5% during 2010 and 4.2% during 2009 represented fees paid by Brasil Telecom Mobile and was eliminated in the consolidation of our financial statements.

Gross operating revenue from ADSL subscriptions increased primarily due to a (1) a 3.7% increase in the average number of ADSL subscriptions to approximately 1,953,000 during 2010 from approximately 1,884,000 during 2009, and (2) the migration of customers to higher bandwidth subscriptions. As of December 31, 2010, our ADSL customer base represented 26.8% of our total fixed lines in service as compared to 26.2% as of December 31, 2009.

Gross Operating Revenue from the Sale of Pre-paid Calling Cards for Use in Public Telephones

Gross operating revenue from the sale of pre-paid calling cards for use in public telephones declined by 50.6% in 2010, principally due to the 54.2% decline in the number of public phone credits used, primarily due to customers substituting usage of mobile handsets in place of usage of public phones as a result of promotions by mobile service providers to the pre-paid segment, including bonus calls and pre-paid card recharges at promotional reduced rates. This decline was partially offset by rate increases for public phone usage of 0.98% in October 2009 and 0.98% in February 2010.

Charges Against Gross Operating Revenue

Value-Added and Other Indirect Taxes

Value-added and other indirect taxes on our fixed-line and data transmission services declined by 8.4% in 2010, primarily reflecting the decline in the gross operating revenue of our fixed-line and data transmission services segment in 2010 and the change in revenue mix, as fewer taxes or lower tax rates apply to some of our services, such as interconnection services.

Discounts

Discounts offered on our fixed-line services generally consist of local fixed-line calls, long-distance calls, and intelligent network services (such as caller ID, call forwarding and conference calling). Discounts on our fixed-line and data transmission services increased by 24.7% in 2010, primarily as a result of an increase in discounts offered for our broadband services as a result of increased competition for other providers and as part of our efforts to promote the migration of our broadband customers to higher bandwidth subscriptions.

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Net Operating Revenue

As a result of the foregoing, net operating revenue of our fixed-line and data transmission services segment declined by 5.7% to R$8,893 million in 2010 from R$9,431 million in 2009.

Net Operating Revenue of Our Mobile Services Segment

The following table sets forth the components of the gross operating revenue and net operating revenue of our mobile services segment, as well as the percentage change from the prior year, for the years ended December 31, 2009 and 2010.

	Year Ended December 31,		
	2010	**2009**	**% Change**
	(in millions of *reais*, except percentages)		
Mobile telephone services	R$ 1,490	R$ 1,358	9.7
Remuneration for the use of the mobile network	1,134	1,083	4.7
Sales of handsets and accessories	53	114	(53.5)
Total gross operating revenue	**2,677**	**2,555**	4.8
Value-added and other indirect taxes	(445)	(428)	4.0
Discounts and returns	(295)	(233)	26.6
Net operating revenue	**R$ 1,937**	**R$ 1,894**	2.3

Gross operating revenue of our mobile services segment increased by 4.8% in 2010, due to (1) a 9.7% increase in gross operating revenue from mobile telephone services, and (2) a 4.7% increase in gross operating revenue from remuneration for the use of our mobile network.

Gross Operating Revenue from Mobile Services

Gross operating revenue from mobile services increased by 9.7% in 2010, principally due to (1) a 24.3% increase in gross operating revenue from additional services, (2) a 10.9% increase in gross operating revenue from monthly subscription fees, and (3) a 3.1% increase in gross operating revenue from billed minutes.

The average number of our pre-paid mobile customers increased by 16.4% to 6.3 million during 2010 from 5.5 million during 2009, primarily as a result of (1) the launch beginning in May 2009 of the entire portfolio of Oi s service plans in Region II, including the *Bônus Diário* prepaid service plan, and (2) the strategy of reinforcing our retail promotion efforts and intensifying our advertising campaigns. The average number of our post-paid mobile customers, including customer that subscribe to our *Oi Controle* plans, was approximately 1,025,100 during 2010 and approximately 1,027,000 during 2009. As of December 31, 2010, pre-paid customers represented 87.5% of our mobile customer base and post-paid customers represented 12.5% of our mobile customer base. Our average monthly net revenue per user declined by 14.7% to R$21.4 during 2010 from R$25.9 during 2009.

Gross operating revenue from additional services, consisting primarily of our mobile data transmission services, increased primarily as a result of a 67.1% increase in gross operating revenue from mobile internet services.

Gross operating revenue from monthly subscription fees increased primarily as a result of the migration of our post-paid customer base to plans offering a greater number of minutes and with higher subscription fees.

Gross operating revenue from billed minutes, which are the number of local minutes used by pre-paid customers plus the number of local minutes used by post-paid customers in excess of the monthly allowance under the customer s service plan, increased by 3.1% primarily as a result of the increase in sales of promotional pre-paid service packages which permit our customers to make calls to mobile customers within our networks and send SMS messages to mobile subscribers of any Brazilian mobile service provider.

Gross Operating Revenue from Remuneration for the Use of the Mobile Network

Gross operating revenue from remuneration for the use of the mobile network increased by 4.7% in 2010 a result of a 37.8% increase in interconnection fees paid to us for completing calls on our mobile network that were originated on the networks of other mobile service providers, primarily as a result of (1) the increase in the number of our mobile customers, and (2) the trend of consumers to make mobile-to-mobile calls, which are less expensive than fixed-to-mobile calls, instead of fixed-to-mobile calls.

The effects of this increase were partially offset by a 43.1% decline in gross operating revenue from interconnection fees paid to us for completing calls on our mobile network that were originated on the networks of fixed-line service providers, primarily due to the trend of consumers to make mobile-to-mobile calls instead of fixed-to-mobile calls.

Of the gross operating revenue from remuneration for the use of the mobile network, 40.8% in 2010 and 41.2% in 2009 represented interconnection fees paid by Oi for the use of Brasil Telecom Mobile s network to complete fixed-to-mobile calls and was eliminated in the consolidation of our financial statements.

Charges Against Gross Operating Revenue

Value-Added and Other Indirect Taxes

Value-added and other indirect taxes on our mobile services increased by 4.0% in 2010, primarily reflecting the increase in the gross operating revenue of our mobile services segment in 2010.

Discounts

Discounts on our mobile services increased by 26.6% in 2010, primarily as a result of our strategy to increase discounts to maintain and increase our market share.

Net Operating Revenue

As a result of the foregoing, revenue from sales and services of the mobile services segment increased by 2.3% to R$1,937 million in 2010 from R$1,894 million in 2009.

Cost of Sales and Services

Cost of sales and services declined by 17.9% in 2010, principally due to a 15.4% decline in cost of sales and services of our fixed-line and data transmission services segment and, to a lesser extent, a 9.1% decline in cost of sales and services of our mobile services segment.

Of the cost of sales and services of our fixed-line and data transmission services segment, 4.7% in 2010 and 3.2% in 2009 represented interconnection fees paid by Oi for the use of Brasil Telecom Mobile s mobile network to complete fixed-to-mobile calls. These fees were eliminated in the consolidation of our financial statements.

Of the cost of sales and services of our mobile services segment, 23.4% in 2010 and 23.2% in 2009 represented (1) interconnection fees paid by Brasil Telecom Mobile for the use of Oi s fixed-line network to complete mobile-to-fixed calls, and (2) fees paid by Brasil Telecom Mobile for EILD services. These fees were eliminated in the consolidation of our financial statements.

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The following table sets forth the components of our cost of sales and services, as well as the percentage change from the prior year, for the years ended December 31, 2009 and 2010.

	Year Ended December 31,		
	2010	2009	% Change
	(in millions of *reais*, except percentages)		
Interconnection	R$ 1,982	R$ 2,026	(2.2)
Depreciation and amortization	807	1,356	(40.5)
Grid maintenance service	616	826	(25.3)
Rental and insurance	471	515	(8.5)
Personnel	335	397	(15.6)
Costs of handsets and accessories	48	89	(46.1)
Concession contract renewal fee	57	71	(19.7)
Other costs of sales and services	416	484	(14.0)
Total cost of sales and services	R$ 4,732	R$ 5,764	(17.9)

Cost of Sales and Services of Our Fixed-Line and Data Transmission Services Segment

Cost of sales and services of our fixed-line and data transmission services segment declined by 15.4% in 2010, principally due to:

- a 35.2% decline in depreciation and amortization costs to R$583 million in 2010 from R$900 million in 2009, primarily as a result of revisions of the useful lives of our fixed assets that were applied as from September 30, 2009; and

- a 25.9% decline in network maintenance costs to R$562 million in 2010 from R$758 million in 2009, primarily as a result of our program to reduce costs by consolidating our network maintenance services in a smaller number of suppliers.

The gross profit of our fixed-line and data transmission services segment increased by 4.1% to R$4,878 million in 2010 from R$4,686 million in 2009. As a percentage of net operating revenue of this segment, gross profit increased to 54.9% in 2010 from 49.7% in 2009.

Cost of Sales and Services of Our Mobile Services Segment

Cost of sales and services of our mobile services segment declined by 9.1% in 2010, principally due to a 51.0% decline in depreciation and amortization costs to R$223 million in 2010 from R$454 million in 2009, , primarily as a result of revisions of the useful lives of our fixed assets that were applied as from September 30, 2009. The effects of this decline were partially offset by a 70.1% increase in rental and insurance costs to R$327 million in 2010 from R$192 million in 2009, primarily as a result of an increase in satellite leasing costs and an increase in right-of-way costs.

The gross profit of our mobile services segment increased by 47.9% to R$558 million in 2010 from R$378 million in 2009. As a percentage of net operating revenue of this segment, gross profit increased to 28.8% in 2010 from 19.9% in 2009.

Gross Profit

As a result of the foregoing, our consolidated gross profit increased by 7.3% to R$5,531 million in 2010 from R$5,156 million in 2009. As a percentage of net operating revenue, gross profit increased to 53.9% in 2010 from 47.2% in 2009.

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Operating Expenses

Selling Expenses

Selling expenses declined by 27.7% during 2010, principally due to (1) a 23.1% decline in selling expenses of our fixed-line segment, and (2) a 23.1% decline in selling expenses of our mobile services segment.

Fixed-Line and Data Transmission Services Segment

Selling expenses of our fixed-line and data transmission services segment declined by 23.1% in 2010, principally due to:

- a 46.6% decline in provision for doubtful accounts to R$271 million in 2010 from R$508 million in 2009, primarily as a result of our program to improve our billing and collection practices and the lower rate of customer defaults as a result of the improved economic outlook in Brazil, which resulted in decline in our provision for doubtful accounts as a percentage of net operating revenue of this segment to 3.4% in 2010 from 5.3% in 2009; and

- a 39.8% decline in personnel expenses to R$77 million in 2010 from R$128 million in 2009, primarily as a result of the synergies obtained in the process of integrating our company with Telemar.

The effects of these declines were partially offset by a 103.5% increase in publicity and advertising expenses to R$82 million in 2010 from R$40 million in 2009, primarily as a result of our efforts to introduce the *Oi* brand and services in our service area and launch new services and service plans, including *Oi Fixo Controle* and *Oi Fixo Economia*.

As a percentage of net operating revenue of this segment, selling expenses declined to 9.7% in 2010 from 11.8% in 2009.

Mobile Services Segment

Selling expenses of our mobile services segment declined by 23.1% in 2010, principally due to:

- a 57.0% decline in materials expenses to R$37 million in 2010 from R$86 million in 2009, primarily as a result of our decision in 2010 to end our subsidies for mini-modems used by our mobile data transmission customers;

- a 24.0% decline in third-party service expenses to R$147 million in 2010 from R$193 million in 2009, primarily as a result of a R$23 million reduction in expenses of bonus credits to our pre-paid customers; and

- a 50.6% decline in publicity and advertising expenses to R$44 million in 2010 from R$88 million in 2009, primarily as a result of a decrease in spending on advertising production, cooperative advertising and broadcasting, which were enhanced during 2009 to support our launch of Oi s service plans.

As a percentage of net operating revenue of this segment, selling expenses declined to 20.8% in 2010 from 27.6% in 2009.

General and Administrative Expenses

General and administrative expenses increased by 7.3% during 2010, principally due to a 5.4% increase in operating expenses of our fixed-line segment.

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Fixed-Line and Data Transmission Services Segment

General and administrative expenses of our fixed-line and data transmission services segment increased by 5.4% in 2010, principally due to:

- a 28.7% increase in third-party service expenses to R$422 million in 2010 from R$328 million in 2009, primarily due to an increase in billing expenses, expenses relating to distributing telephone books and maintenance expenses;

- a 77.2% increase in consulting expenses to R$202 million in 2010 from R$114 million in 2009, primarily as a result of (1) our engagement of several consulting firms to advise us as to steps that we can take to increase the market share and profitability of this segment, and (2) our engagement of information technology consultants to assist us in the digitalization of documents relating to our pending litigation against our company; and

- an increase in other expenses to R$99 million in 2010 from R$27 million in 2009, primarily due to an increase in expenses for electrical energy used for our administrative offices as a result of increases in prices and the amounts consumed.

The effects of these increases were partially offset by a 46.7% decline in depreciation and amortization expenses to R$195 million in 2010 from R$366 million in 2009, primarily as a result of revisions of the useful lives of our fixed assets that were applied as from September 30, 2009.

As a percentage of net operating revenue of this segment, general and administrative expenses increased to 14.3% in 2010 from 12.8% in 2009.

Mobile Services Segment

General and administrative expenses of our mobile services segment increased by 7.1% in 2010, primarily due to a 75.0% increase in third-party service expenses to R$70 million in 2010 from R$40 million in 2009, principally due to R$21 million of costs of external content providers due to higher demand from our customers. The effects of this increase were partially offset by a 41.9% decline in depreciation and amortization expenses to R$36 million in 2010 from R$62 million in 2009, primarily as a result of revisions of the useful lives of our fixed assets that were applied as from September 30, 2009.

As a percentage of net operating revenue of this segment, general and administrative expenses increased to 8.9% in 2010 from 8.5% in 2009.

Other Operating Expenses, Net

Other Operating Income

Other operating income declined by 20.6% to R$524 million in 2010 from R$660 million in 2009, primarily as a result of (1) a 92.4% decline in taxes recoverable to R$16 million in 2010 from R$209 million in 2009, primarily as a result of a reversal of a provision for the COFINS tax of R$119 million in 2009, (2) a 42.1% decline in income on disposal of property, plant and equipment to R$54 million in 2010 from R$93 million in 2009, primarily as a result of the substitution of automatic switching equipment in 2009 for upgrading network capacity, and (3) an 84.6% decline in recovery of pension fund expenses to R$6 million in 2010 from R$40 million in 2009, primarily as a result of revised actuarial calculations of our pension liabilities. The effects of these declines was partially offset by a R$132 million increase in recovered expenses to R$136 million in 2010 from R$4 million in 2009, primarily as a result of the recover of ICMS taxes in 2009.

Other Operating Expense

Other operating expenses declined by 74.5% to R$1,032 million in 2010 from R$4,040 million in 2009, primarily as a result of an 87.9% decline in provisions for contingencies to R$405 million in 2010 from R$3,340 million in 2009. As a result of certain judicial decisions in 2009, we reclassified the probability of loss in certain civil proceedings involving CRT, the leading fixed-line telecommunications service company in the State of Rio Grande do Sul that we acquired in July 2000, from possible to probable. With the assistance of our internal and external legal advisors, we reviewed the process we use to estimate provisions for civil contingencies in connection with the financial participation agreements entered into in connection to the expansion plans of CRT. As a result, we recorded an additional provision of R$2,325 million in 2009. For a more detailed description of these proceedings, see Item 8. Financial Information Legal Proceedings Civil Proceedings. In addition, as the result of Telemar s acquisition of control of our company in January 2009, we have changed our criteria for estimating probable losses in connection with labor proceedings and the recognition of Tax on the Circulation of Merchandise and Services (*Imposto Sobre a Circulação de Mercadorias e Serviços*), or ICMS (a state value-added tax on sales and services), tax credits in order to align our policies with those of Telemar. As a result, we recorded additional provisions for labor proceedings and tax proceedings in 2009 in the amount of R$334 million and R$387 million, respectively.

Operating Income (Loss) before Financial Income (Expenses) and Taxes

As a result of the foregoing, our consolidated operating income before financial income (expenses) and taxes was R$2,460 million in 2010 compared to consolidated operating loss before financial income (expenses) and taxes of R$1,077 million in 2009. As a percentage of net operating revenue, operating income before financial income (expenses) and taxes was 24.0% in 2010 compared to operating loss before financial income (expenses) and taxes of 9.9% in 2009.

Fixed-Line and Data Transmission Services Segment

The operating income before financial income (expenses) and taxes of our fixed-line and data transmission services segment was R$2,481 million loss in 2010 compared to operating loss before financial income (expenses) and taxes of R$778 million income in 2009. As a percentage of the net operating revenue of this segment, operating income before financial income (expenses) and taxes was 27.9% in 2010 compared to operating loss before financial income (expenses) and taxes of 8.2% in 2009.

Mobile Services Segment

The operating loss before financial income (expenses) and taxes of our mobile services segment declined by 89.4% to R$34 million in 2010 from R$318 million in 2009. As a percentage of the net operating revenue of this segment, operating loss before financial income (expenses) and taxes declined to 1.7% in 2010 from 16.8% in 2009.

Financial Expenses, Net

Financial Income

Financial income increased by 55.4% to R$979 million in 2010 from R$630 million in 2009, primarily due to (1) a 225.0% increase in interest and monetary correction on amounts due from related parties to R$236 million in 2010 from R$73 million in 2009, primarily as a result of the increase in amounts owed to us by related parties as a result of our merger with Brasil Telecom Holding in September 2009, which had issued debentures to Telemar in aggregate principal amount of R$1,200 million, and (2) a 96.5% increase in investment yield to R$287 million in 2010 from R$146 million in 2009, primarily as a result of an increase in the average amount of our financial investments.

In February 2009, Brasil Telecom Holding subscribed private debentures issued by Telemar. As a result of the merger of Brasil Telecom Holding into our company on September 30, 2009, we became the holders of these debentures. In March 2009, Brasil Telecom Mobile subscribed additional private debentures issued by Telemar. The outstanding principal amount of these debentures is payable at maturity in December 2013. These debentures bear interest at a rate of CDI plus 4.0% per annum, payable with the principal at maturity. At December 31, 2010, the outstanding amount of these debentures was R$1,911 million.

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Financial Expenses

Financial expenses increased by 16.2% to R$1,060 million in 2010 from R$912 million in 2009, primarily due to a R$2 million expense related to monetary correction and exchange differences on third-party loans and financing in 2010 compared to a R$186 million gain in 2009, primarily as a result of the effects of exchange rate variations on our indebtedness. The effects of this change were partially offset by a 91.2% decline in losses on derivative transactions to R$9 million in 2010 from R$101 million in 2009, primarily as a result of the fluctuations of the exchange rate of the Japanese Yen (the *real* appreciated by 9.0% against the Japanese Yen in 2010 compared to 27.1% in 2009).

Income Tax and Social Contribution

The composite corporate statutory income tax and social contribution rate was 34% in each of 2010 and 2009. Income tax and social contribution was an expense of R$408 million in 2010 compared to a benefit of R$339 million in 2009. Our effective tax rate was 17.1% in 2010 and 24.9% in 2009. The table below sets forth a reconciliation of the composite corporate statutory income tax and social contribution rate to our effective tax rate for each of the periods presented.

	Year Ended December 31,	
	2010	2009(1)
Composite corporate statutory income tax and social contribution rate	34.0%	(34.0)%
Tax effects of interest on shareholders equity	(5.2)	
Tax effects of permanent exclusions (additions)	(5.2)	3.3
Tax effects of compensation of tax loss carryforwards	(1.0)	(1.4)
Tax effects of unrecognized deferred tax assets	0.2	7.2
Tax effects of recognized deferred tax assets	(5.7)	
Effective rate	17.1%	(24.9)%

(1) The composite corporate statutory income tax and social contribution rate is represented as (34.0)% for the year ended December 31, 2009 as a result of our recording a loss before taxes during the year ended December 31, 2009. The application of the negative effective rate for this year to our loss before taxes resulted in our recording a tax benefit in this year.

Our effective tax rate was 17.2% in 2010, primarily as a result of (1) the tax effect of our recognition of deferred tax assets accrued during prior years, but not previously recognized due to uncertainty regarding their eventual realization, which lowered our effective tax rate by 5.7%, (2) the tax effect of our payment of interest on shareholders equity, which lowered our effective tax rate by 5.2%, and (3) the tax effects of non-deductible expenses of prior years, primarily amortization expenses of Copart 1, Copart 2 and Brasil Telecom Holding and adjustments made to the income tax and social contribution calculation of prior year, which lowered our effective tax rate by 5.2%.

Our effective tax rate was 24.9% in 2009, primarily as a result of (1) the tax effect of an unrecognized tax loss, which lowered our effective tax rate by 7.2%, and (2) the tax effects of our generation of certain non-taxable income, which lowered our effective tax rate by 3.3%.

Net Income (Loss)

Our consolidated net income was R$1,971 million in 2010 compared to loss of R$1,019 million in 2009. As a percentage of net operating revenue, net income was 19.2% in 2010 compared to loss of 9.3% in 2009.

Liquidity and Capital Resources

Our principal cash requirements consist of the following:

- working capital requirements;
- servicing of our indebtedness;
- capital expenditures related to investments in operations, expansion of our networks and enhancements of the technical capabilities and capacity of our networks; and
- dividends on our shares, including in the form of interest attributable to shareholders equity.

Unless our board of directors deems it inconsistent with our financial position, payment of dividends is mandatory under our by-laws and, consequently, may give rise to significant cash requirements in future periods.

Our principal sources of liquidity have traditionally consisted of the following:

- cash flows from operating activities;
- short-term and long-term loans; and
- sales of debt securities in domestic and international capital markets.

During 2011, cash flow generated by operations was used primarily for investing activities, for working capital requirements and to service our outstanding debt obligations. As of December 31, 2011, our consolidated cash and cash equivalents and cash investments amounted to R$7,089 million. As of December 31, 2011, we had working capital of R$3,627 million. We believe that our working capital is sufficient for our requirements during 2012.

Projected Sources and Uses of Cash

We anticipate that we will be required to spend approximately R$15.4 billion to meet our short-term contractual obligations and commitments and budgeted capital expenditures during 2012, and an additional approximately R$28.4 billion to meet our long-term contractual obligations and commitments and budgeted capital expenditures in 2013 and 2014. We expect that we will meet these cash requirements for (1) our operating and maintenance activities through sales of our services, and (2) our debt service and capital expenditure commitments through a combination of cash generated from operating activities and cash generated by financing activities, including new debt financings and the refinancing of our existing indebtedness as it becomes due.

We have commitments from several financial institutions to provide us with financing in the future, including commitments from under a revolving credit facility that we entered into in November 2011, an export credit facility that we entered into in December 2011 and unused commitments under various other credit facilities described under Indebtedness and Financing Strategy. We pay commitment fees to these financial institutions in connection with their commitments. As of December 31, 2011, an aggregate principal amount of US$1,751 million was available for disbursement under these facilities.

In November 2011, Oi, Brasil Telecom Mobile, Telemar and TNL PCS entered together into a revolving credit facility with a syndicate of international institutions. Under this facility, up to US$1 billion aggregate principal amount will be available for disbursement to the borrowers during the five-year term of this facility. Outstanding amounts under this facility bear interest at the rate of LIBOR plus 0.90% per annum. As of

December 31, 2011, there were no outstanding loans under this facility.

In December 2011, Telemar entered into an export credit facility with FINNVERA under which FINNVERA agreed to disburse loans in the aggregate principal amount of up to US$200 million. Loans under this facility bear interest at the rate of LIBOR plus 0.90% per annum, payable semi-annually in arrears. The principal amount of these loans is payable in 17 semiannual installments commencing on the first anniversary of the disbursements. As of December 31, 2011, no loans have been disbursed under this facility.

Cash Flow

Cash Flows from Operating Activities

Our primary source of operating funds is cash flow generated from our operations. Net cash provided by operating activities was R$1,839 million in 2011, R$3,416 million in 2010 and R$3,573 million in 2009. We consider cash flows provided by our operating activities to be sufficient for our expected cash requirements related to operations. However, we generally finance our investments in property, plant and equipment through the use of bank loans, vendor financing, capital markets and other forms of financing.

Cash Flows Used in Investing Activities

Investing activities used net cash of R$2,089 million in 2011, R$1,560 million in 2010 and R$3,005 million in 2009.

During 2011, investing activities for which we used cash primarily consisted of (1) net judicial deposits (consisting of deposits less redemptions) of R$1,224 million, primarily related to provisions for labor, taxes and civil contingencies, and (2) investments of R$884 million in additions to property, plant and equipment, primarily related to the expansion of our data communications network and the implementation of regulatory projects to meet ANATEL s requirements.

During 2010, investing activities for which we used cash primarily consisted of (1) net judicial deposits (consisting of deposits less redemptions) of R$808 million, primarily related to provisions for labor, taxes and civil contingencies, and (2) investments of R$755 million in additions to property, plant and equipment, primarily related to the expansion of our data communications network and the implementation of regulatory projects to meet ANATEL s requirements.

During 2009, investing activities for which we used cash primarily consisted of (1) net judicial deposits (consisting of deposits less redemptions) of R$1,317 million, primarily related to provisions for labor, taxes and civil contingencies, (2) investments of R$1,397 million in additions to property, plant and equipment, primarily related to the expansion of our data communications network and the implementation of regulatory projects to meet ANATEL s requirements, and (3) investments in private debentures issued by Telemar in the amount of R$300 million.

Cash Flows from Financing Activities

Financing activities provided net cash of R$2,920 million in 2011, and used net cash of R$356 million in 2010 and R$565 million in 2009.

During 2011, our principal sources of borrowed funds consisted of (1) issuance of R$2,350 million aggregate principal amount of non-convertible debentures due 2018, (2) the issuance of R$1,100 million aggregate principal amount of 9.75% Senior Notes due 2016, and (3) the issuance of R$1,000 million aggregate principal amount of non-convertible debentures due 2017.

During 2011, we used cash to (1) to repay R$1,096 million principal amount of our outstanding loans and financing, derivatives and leases, (2) to pay dividends and interest on shareholders equity in the aggregate amount of R$462 million, and (3) to pay R$79 million of fees related to our licenses and concessions.

During 2010, our principal sources of borrowed funds consisted of (1) R$531 million aggregate principal amount borrowed under a credit facility with BNDES that we entered into in December 2009, and (2) R$511 million aggregate net proceeds of a real estate securitization transaction that we entered into in August 2010.

During 2010, we used cash to (1) to repay R$1,279 million principal amount of our outstanding loans and financing, derivatives and leases, and (2) to pay R$115 million of fees related to our licenses and concessions.

During 2009, our principal sources of borrowed funds consisted of:

R$313 million aggregate principal amount borrowed under a credit facility with BNDES that we entered into in November 2006; and

R$300 million aggregate principal amount borrowed under a credit facility with BNDES that we entered into in December 2009.

During 2009, we used cash (1) to repay R$867 million principal amount of our outstanding loans and financing, derivatives and leases, (2) to pay dividends and interest on shareholders equity in the aggregate amount of R$268 million, and (3) to pay R$188 million of fees related to our licenses and concessions.

Indebtedness and Financing Strategy

As of December 31, 2011, our total outstanding indebtedness on a consolidated basis was R$8,105 million, consisting of R$1,144 million of short-term indebtedness, all of which represented current portion of long-term indebtedness (or 14.1% of our total indebtedness), and R$6,962 million of long-term indebtedness (or 85.9% of our total indebtedness).

On a consolidated basis, our *real*-denominated indebtedness as of December 31, 2011 was R$8,104 million and our foreign currency-denominated indebtedness was R$1 million. As of December 31, 2011, our *real*-denominated indebtedness bore interest at an average rate of 11.27% per annum, and our foreign currency denominated indebtedness bore interest at an average rate of 1.3% per annum for loans denominated in U.S. dollars. As of December 31, 2011, 84.1% of our debt bore interest at floating rates, including the effect of swap operations.

Short-Term Indebtedness

Our consolidated short-term debt, consisting of the current portion of long-term loans and financings and debentures, was R$1,144 million as of December 31, 2011. Under our financing policy, we generally do not incur short-term indebtedness, as we believe that our cash flows from operations generally will be sufficient to service our current liabilities.

Long-Term Indebtedness

The following table sets forth selected information with respect to our principal outstanding long-term debt instruments as of December 31, 2011.

Instrument	Outstanding Principal Amount (in millions of *reais*)	Final Maturity
Debentures	720	June 2013(1)
Debentures	1,000	August 2017
Debentures	2,350	December 2018(2)
9.75% Senior Notes due 2016	1,100	September 2016
BNDES credit facilities:		
Oi 2006 credit facility:		
A loans	1,011	May 2014
B loans	15	May 2014
Brasil Telecom Mobile 2008 loan agreement	214	September 2017

Oi 2009 credit facility:

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Instrument	Outstanding Principal Amount (in millions of *reais*)	Final Maturity
Floating-rate loans	397	December 2018(3)
Fixed-rate loans	93	December 2018(3)
Brasil Telecom Mobile 2009 credit facility:		
Floating-rate loans	479	December 2018(3)
Fixed-rate loans	12	December 2018(3)

(1) The outstanding principal amount of these debentures is payable in two equal annual installments commencing in June 2011.
(2) The outstanding principal amount of these debentures is payable in three equal annual installments commencing in December 2016.
(3) Amortization on this facility commences in January 2012.

Some of our debt instruments require that we comply with financial covenants, the most restrictive of which are as follows:

- Consolidated debt to consolidated EBITDA for the prior 12-month period less than or equal to 3.75 to 1.0 at the end of each fiscal quarter until maturity;

- Consolidated EBITDA for the prior 12-month period to consolidated interest expense for the prior 12-month period greater than or equal to 1.95 to 1.0 at the end of each fiscal quarter until maturity; and

- Consolidated debt to consolidated debt plus shareholders equity less than or equal to 0.95 to 1.0 at the end of each fiscal quarter until maturity.

We were in compliance with these financial covenants as of December 31, 2011, and we believe that we will be able to comply with these financial covenants during 2012. In addition, we believe that our compliance with these financial covenants will not adversely affect our ability to implement our financing plans.

The instruments governing a substantial portion of our indebtedness contain cross-default or cross-acceleration clauses and the occurrence of an event of default under one of these instruments could trigger an event of default under other indebtedness or enable the creditors under other indebtedness to accelerate that indebtedness.

As of December 31, 2011, all of our indebtedness to BNDES was secured by pledges of certain of our accounts receivable.

The following discussion briefly describes certain of our significant financing transactions.

Debentures

In June 2006, we issued non-convertible debentures in the aggregate principal amount of R$1,080 million. The outstanding principal amount of these debentures is payable in two equal annual installments in June 2012 and June 2013. These debentures bear interest at the capitalized DI rate plus 3.5% per annum, payable semi-annually in arrears in June and December of each year.

In August 2011, we issued non-convertible debentures in an offering made in Brazil. The aggregate principal amount of the debentures was R$1,000 million. These debentures mature in August 2017 and bear interest at the CDI rate plus 1.00% per annum. We used the net proceeds of this offering for working capital and amortization of indebtedness.

In December 2011, we issued non-convertible debentures in an offering made in Brazil. The aggregate principal amount of the debentures was R$2,350 million. These debentures bear interest at the CDI rate plus 1.15% per annum, payable semi-annually, and the principal amount of these debentures is payable in three annual installments beginning in December 2016. We used the net proceeds of this offering for working capital and amortization of indebtedness.

Fixed-Rate Notes

In September 2011, we issued R$1,100 million aggregate principal amount of our 9.75% Senior Notes due 2016. These notes are denominated in *reais* and payments of principal and interest under these notes are payable in U.S. dollars at prevailing exchange rates at the time of payment. We used the net proceeds of this offering for general corporate purposes, including investments and the redemption and repayment of existing indebtedness.

BNDES Facilities

Oi 2006 Credit Facility

In November 2006, Oi entered into a credit facility with BNDES under which BNDES and several financial institutions agreed to disburse loans in multiple tranches in an aggregate principal amount of up to R$2,104 million. The proceeds of these loans were used to fund investments in our fixed-line network and in operational improvements to meet the targets established in the General Plan on Universal Service and in the General Plan on Quality Goals.

Each tranche disbursed under this credit facility consists of (1) a loan that bears interest at the TJLP rate plus 4.3% per annum, which is currently payable monthly in arrears, and (2) a loan that bears interest at the TJLP rate plus 2.3% per annum, which is currently payable monthly in arrears. The outstanding principal amount of each of these loans is payable in 60 equal monthly installments commencing in June 2009.

As of December 31, 2011, the aggregate principal amount outstanding under the loans bearing interest at the TJLP rate plus 4.3% was R$1,011 million and the aggregate principal amount outstanding under the loans bearing interest at the TJLP rate plus 2.3% was R$15 million.

Brasil Telecom Mobile 2008 Loan Agreement

In February 2008, Brasil Telecom Mobile entered into a loan agreement with BNDES under which BNDES disbursed a loan in the principal amount of R$259 million. The proceeds of this loan agreement were used to fund our investment in the expansion and modernization of our wireless network. This loan bears interest at the TJLP rate plus 3.52% per annum, payable quarterly in arrears through September 2010 and monthly in arrears thereafter. The principal amount of this loan is payable in 84 equal monthly installments commencing in October 2010. At December 31, 2011, the outstanding principal amount under this loan was R$214 million.

Oi 2009 Credit Facility

In December 2009, Oi entered into credit facilities with BNDES under which BNDES agreed to disburse loans in two tranches in an aggregate principal amount of up to R$623 million. The proceeds of the loans under this credit facility are to be used to fund investments in expansion and improvement of our fixed-line networks and in operational improvements to meet the targets established by ANATEL during the period from 2009 through 2011.

Each tranche disbursed under this credit facility consists of (1) a loan that bears interest at the TJLP rate plus 3.95% per annum, payable quarterly in arrears through December 2011 and monthly in arrears thereafter, and (2) a loan that bears interest at a fixed rate of 4.5% per annum, payable quarterly in arrears through December 2011 and monthly in arrears thereafter. The outstanding principal amount of each of these loans is payable in 84 equal monthly installments commencing in January 2012.

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As of December 31, 2011, the aggregate principal amount outstanding under the loans bearing interest at the TJLP rate plus 3.95% was R$397 million and the aggregate principal amount outstanding under the loans bearing interest at 4.5% was R$93 million.

Brasil Telecom Mobile 2009 Credit Facility

In December 2009, Brasil Telecom Mobile entered into credit facilities with BNDES under which BNDES agreed to disburse loans in two tranches in an aggregate principal amount of up to R$766 million. The proceeds of the loans under this credit facility are to be used to fund investments in expansion and improvement of our mobile networks and in operational improvements to meet the targets established by ANATEL during the period from 2009 through 2011.

Each tranche disbursed under this credit facility consists of (1) a loan that bears interest at the TJLP rate plus 3.95% per annum, payable quarterly in arrears through December 2011 and monthly in arrears thereafter, and (2) a loan that bears interest at a fixed rate of 4.5% per annum, payable quarterly in arrears through December 2011 and monthly in arrears thereafter. The outstanding principal amount of each of these loans is payable in 84 equal monthly installments commencing in January 2012.

As of December 31, 2011, the aggregate principal amount outstanding under the loans bearing interest at the TJLP rate plus 3.95% was R$479 million and the aggregate principal amount outstanding under the loans bearing interest at 4.5% was R$12 million.

Real Estate Securitization Transaction

In August 2010, Oi transferred 101 real estate properties to Copart 5 Participações S.A., or Copart 5, our wholly-owned subsidiary. Oi entered into lease contracts with terms of up to 12 years for the continued use of all of the properties transferred to Copart 5.

Copart 5 assigned the receivables representing all payments under these leases to Brazilian Securities Companhia de Securitização, which issued Real Estate Receivables Certificates (*Certificados de Recebíveis Imobiliários*), or CRIs, backed by these receivables. The CRIs were purchased by Brazilian financial institutions.

We received net proceeds from the assignment of lease receivables in the total aggregate amount of R$511 million, and we record our obligations to make the assigned payments as short- and long-term debt in our consolidated financial statements. The aggregate net effective interest rate on this transaction is 102% of the CDI rate. We have used the proceeds raised in this transaction to repay short-term debt. As of December 31, 2011, the aggregate liability under these leases was R$457 million.

Off-Balance Sheet Arrangements

We do not currently have any transactions involving off-balance sheet arrangements.

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Contractual Commitments

The following table summarizes our significant contractual obligations and commitments as of December 31, 2011:

	Payments Due by Period				
	Less than One Year	One to Three Years	Three to Five Years	More than Five Years	Total
	(in millions of *reais*)				
Loans and financing (1)	R$ 1,532	R$ 3,310	R$ 2,515	R$ 889	R$ 8,246
Debentures (2)	906	1,599	3,278	877	6,660
Swap adjustments (3)	26				26
Purchase obligations (4)	373				373
Concession fees (5)		182	91	418	691
Usage rights (6)	132	408	137		677
Pension plan contributions(7)	111	332	221	442	1,106
Total contractual obligations and commitments	R$ 3,080	R$ 5,831	R$ 6,242	R$ 2,626	R$ 17,779

(1) Includes estimated future payments of interest on our loans and financings, calculated based on interest rates and foreign exchange rates applicable at December 31, 2011 and assuming that all amortization payments and payments at maturity on our loans and financings will be made on their scheduled payment dates.

(2) Includes estimated future payments of interest on our debentures, calculated based on interest rates applicable as of December 31, 2011 and assuming that all amortization payments and payments at maturity on our debentures will be made on their scheduled payment dates.

(3) Includes estimated future payments of interest on our derivative obligations, calculated based on interest rates and foreign exchange rates applicable as of December 31, 2011 and assuming that all payments on our derivative obligations will be made on their scheduled payment dates.

(4) Consists of purchase obligations for network equipment pursuant to binding obligations which include all significant terms, including fixed or minimum quantities to be purchased; fixed, minimum or variable price provisions; and the approximate timing of the transaction.

(5) Consists of estimated bi-annual fees due to ANATEL under our concession agreements expiring in 2025. These estimated amounts are calculated based on the amounts paid in 2011.

(6) Consists of payments due to ANATEL for radio frequency licenses. Includes accrued and unpaid interest as of December 31, 2011.

(7) Consists of expected contributions to amortize the actuarial deficit of the BrTPREV plan and the Fundador/Alternativo plan.

We are also subject to contingencies with respect to tax, civil, labor and other claims and have made provisions for accrued liability for legal proceedings related to certain tax, civil, labor and other claims of R$4,415 million as of December 31, 2011. See Item 8. Financial Information Legal Proceedings and note 23 to our consolidated financial statements.

Supplemental Information Regarding TNL

As described in Corporate Reorganization, on February 27, 2012, the shareholders of TNL, Telemar, Coari and Brasil Telecom approved a corporate reorganization including the Coari merger and the TNL merger. We will account for the Coari merger and the TNL merger using historical cost, whereby the financial statements of our company will record the historical carrying values of the assets and liabilities of TNL, Telemar, and Coari as from the date of the reorganization. The historical carrying values of Coari reflect the purchase accounting recorded under IFRS in accordance with IFRS 3(R), Business Combinations, under which 100% of the identifiable assets acquired, the liabilities assumed, and any non-controlling interest in the subsidiaries of our company were recorded at their fair values on January 8, 2009, the date on which TNL acquired control of our company. The financial statements of TNL as of and for the year ended December 31, 2011 have not been presented elsewhere in this annual report and have not been filed with the SEC. The historical financial statements of our company will not be restated to account for the impacts of the corporate reorganization on a retroactive basis. As a result, our financial statements that are presented after the completion of the corporate reorganization will reflect a significant increase in non-current intangible assets and property, plant and equipment, a significant increase in liabilities, particularly loans, financings and debentures, and a significant increase in total equity. In addition, we will record an increase in depreciation and amortization expenses reflecting this step-up in the carrying value of our intangible assets and property, plant and equipment, and an increase in financial expenses reflecting the increase in our loans, financings and debentures, with a consequent negative effect on our gross profit, operating income and net income.

TNL maintained their books and records in *reais*. TNL prepared their consolidated financial statements in accordance with IFRS.

The financial and other data included in this annual report regarding TNL and its consolidated subsidiaries as of December 31, 2011 and earlier dates and for periods ended on December 31, 2011 and earlier dates is historical in nature and includes financial and other data regarding Brasil Telecom, a subsidiary of TNL prior to February 27, 2012.

In order to assist investors in evaluating our company following the corporate reorganization, we have included:

- historical supplemental information regarding the results of operations of TNL for the years ended December 31, 2011 and 2010;

- historical supplemental information regarding the cash flows of TNL for the years ended December 31, 2011;

- historical supplemental information regarding the material short-term and long-term indebtedness as of December 31, 2011 of TNL; and

- supplemental information regarding TNL s contractual commitments as of December 31, 2011.

The supplemental financial information is provided for illustrative purposes only and does not purport to represent, and you should not rely on the supplemental financial information as an indication of, (1) what the actual consolidated results of operations or the consolidated financial position of our company will be after February 28, 2012, or (2) our future consolidated results of operations or financial position. The supplemental financial information does not reflect, for example, (1) any integration costs that may be incurred as a result of the split-off and share exchange, the Coari merger and the TNL merger, (2) any synergies, operating efficiencies and cost savings that may result from these transactions, (3) any benefits that may be derived from the combined company s growth prospects, or (4) any changes in rates for services or exchange rates subsequent to the dates of the supplemental financial information.

Supplemental Information Regarding Results of Operations of TNL For the Year Ended December 31, 2011 Compared with Year Ended December 31, 2010

The following discussion of TNL s results of operations is based on TNL s consolidated financial statements as of and for the years ended December 31, 2011 and 2010 prepared in accordance with IFRS as issued by the IASB. TNL implemented an organizational structure that it believed reflected its business activities and corresponded to the principal services that it provided. TNL reported its results in three segments to reflect this organizational structure:

- *Fixed-Line Services* This segment included TNL s local fixed-line services (including public telephones), its long-distance services, its fixed-line data transmission services, and interconnections to its fixed-line network.

- *Mobile Services* This segment included its mobile services, including voice, mobile data communications and other value-added services, and interconnections to its mobile network.

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Other This segment included its television services, its ISP services, its internet portal, its mobile phone payment system and its call center.

The following tables set forth the operating results of each of TNL s segments and the reconciliation of these results of TNL s segments to its consolidated income statement. This segment information was prepared on the same basis as the information that TNL s senior management used to allocate resources among segments and evaluate their performance. TNL evaluated and managed business segment performance based on information prepared in accordance with IFRS, and, accordingly, the segment data included below is presented under IFRS. The discussion of the results of TNL s business segments is based upon financial information reported for each of the segments of its business, as presented in the table below.

	Year Ended December 31, 2011				
	Fixed-Line Services	Mobile Services	Other	Eliminations	Consolidated
	(in millions of *reais*)				
Net operating revenue	R$ 20,795	R$ 10,731	R$ 1,022	R$ (4,641)	R$ 27,907
Cost of sales and services	(14,288)	(5,856)	(547)	4,480	(16,210)
Gross profit	6,507	4,875	475	(161)	11,697
Selling expenses	(3,047)	(2,119)	(419)	491	(5,095)
General and administrative expenses	(2,169)	(718)	(203)	4	(3,085)
Other operating income (expenses), net	(94)	(122)	2	(352)	(566)
Operating income (loss) before financial income (expenses) and taxes	R$ 1,197	R$ 1,916	R$ (145)	R$ (17)	R$ 2,951

	Year Ended December 31, 2010				
	Fixed-Line Services	Mobile Services	Other	Eliminations	Consolidated
	(in millions of *reais*)				
Net operating revenue	R$ 22,655	R$ 10,001	R$ 1,046	R$ (4,222)	R$ 29,479
Cost of sales and services	(14,811)	(5,454)	(492)	4,118	(16,639)