

Vivo Participacoes S.A.  
Form 20-F  
May 03, 2007

As filed with the Securities and Exchange Commission on May 3, 2007

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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549**

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**FORM 20-F**

(Mark One)

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

**OR**

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

**For the fiscal year ended December 31, 2006**

**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**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: 001-14493

**Vivo Participações S.A.**

*(Exact name of Registrant as Specified in its Charter)*

**Vivo Holding Company**

*(Translation of Registrant's Name into English)*

**The Federative Republic of Brazil**

*(Jurisdiction of Incorporation or Organization)*

**Av. Doutor Chucri Zaidan 860, 04583-110**

**São Paulo, SP, Brazil**

*(Address of Principal Executive Offices)*

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**

Preferred Shares, without par value  
American Depositary Shares (as evidenced by American  
Depositary Receipts), each representing 1 preferred share

New York Stock Exchange \*  
New York Stock Exchange

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\* Not for trading purposes, but only in connection with the registration on the New York Stock Exchange of American Depositary Shares representing those preferred shares.

**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**

Indicate the number of outstanding shares of each of the issuer's classes of capital or common stock as of the close of the period covered by the annual report.

The number of outstanding shares of each class as of December 31, 2006:

<b>Title of Class</b>	<b>Number of Shares Outstanding</b>
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Common Stock	524,931,665
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Preferred Stock	917,186,080
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Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes                      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

Note: Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

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                      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                      Accelerated filer                      Non-accelerated filer

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

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## TABLE OF CONTENTS

	<u>PAGE</u>	
<u>ITEM 1.</u>	<u>IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS</u>	<u>1</u>
<u>ITEM 2.</u>	<u>OFFER STATISTICS AND EXPECTED TIMETABLE</u>	<u>1</u>
<u>ITEM 3.</u>	<u>KEY INFORMATION</u>	<u>1</u>
<u>ITEM 4.</u>	<u>INFORMATION ON THE COMPANY</u>	<u>16</u>
<u>ITEM 4A.</u>	<u>UNRESOLVED STAFF COMMENTS</u>	<u>43</u>
<u>ITEM 5.</u>	<u>OPERATING AND FINANCIAL REVIEW AND PROSPECTS</u>	<u>43</u>
<u>ITEM 6.</u>	<u>DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES</u>	<u>58</u>
<u>ITEM 7.</u>	<u>MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS</u>	<u>65</u>
<u>ITEM 8.</u>	<u>FINANCIAL INFORMATION</u>	<u>66</u>
<u>ITEM 9.</u>	<u>THE OFFER AND LISTING</u>	<u>73</u>
<u>ITEM 10.</u>	<u>ADDITIONAL INFORMATION</u>	<u>78</u>
<u>ITEM 11.</u>	<u>QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK</u>	<u>93</u>
<u>ITEM 12.</u>	<u>DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES</u>	<u>95</u>
<u>ITEM 13.</u>	<u>DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES</u>	<u>96</u>
	<u>MATERIAL MODIFICATIONS TO THE RIGHTS OF SECURITY HOLDERS AND</u>	
<u>ITEM 14.</u>	<u>USE OF PROCEEDS</u>	<u>96</u>
<u>ITEM 15.</u>	<u>CONTROLS AND PROCEDURES</u>	<u>96</u>
<u>ITEM 16.</u>	<u>[RESERVED]</u>	<u>97</u>
<u>ITEM 16A.</u>	<u>AUDIT COMMITTEE FINANCIAL EXPERT</u>	<u>97</u>
<u>ITEM 16B.</u>	<u>CODE OF ETHICS</u>	<u>97</u>
<u>ITEM 16C.</u>	<u>PRINCIPAL ACCOUNTANT FEES AND SERVICES</u>	<u>97</u>
<u>ITEM 16D.</u>	<u>EXEMPTIONS FROM THE LISTING STANDARDS FOR AUDIT COMMITTEES</u>	<u>98</u>
	<u>PURCHASES OF EQUITY SECURITIES BY ISSUER AND AFFILIATED</u>	
<u>ITEM 16E.</u>	<u>PURCHASERS</u>	<u>98</u>
<u>ITEM 17.</u>	<u>FINANCIAL STATEMENTS</u>	<u>99</u>
<u>ITEM 18.</u>	<u>FINANCIAL STATEMENTS</u>	<u>99</u>
<u>ITEM 19.</u>	<u>EXHIBITS</u>	<u>100</u>

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**INTRODUCTION**

All references in this annual report to:

- 1xRTT are to 1x Radio Transmission Technology, the CDMA 2000 1x technology, which pursuant to the ITU (International Telecommunication Union) and in accordance with the IMT-2000 rules, is the 3G (third generation) technology;
- ADRs are to the American Depositary Receipts evidencing our ADSs;
- ADSs are to our American Depositary Shares, each representing 1 share of our non-voting preferred stock;
- AMPS are to Advanced Mobile Phone System, a radio interface technology for cellular networks based on spectral spreading of the radio signal and channel division in the frequency domain;
- ANATEL are to *Agência Nacional de Telecomunicações* ANATEL, the Brazilian telecommunication regulatory agency;
- BOVESPA are to the *Bolsa de Valores de São Paulo*, the São Paulo stock exchange;
- Brazilian Central Bank, BACEN, Central Bank of Brazil or Central Bank are to the *Banco Central do Brasil*, the Brazilian central bank;
- Brazilian Corporate Law are to Law No. 6,404 of December, 1976, as amended by Law No. 9,457 of May 1997 and by Law No. 10,303 of October 2001;
- Brazilian government are to the federal government of the Federative Republic of Brazil;
- CDMA are to Code Division Multiple Access, an aerial interface technology for cellular networks based on spectral spreading of the radio signal and channel division in the code domain;
- CDMA 2000 1xEV-DO are to a 3G (third generation) access technology with data transmission speed of up to 2.4 megabytes per second;
- Celular CRT are to Celular CRT Participações S.A. and its consolidated subsidiary, formerly Vivo subsidiaries prior to our corporate restructuring;
- Commission are to the U.S. Securities and Exchange Commission;
- Corporate Restructuring are to the restructuring of our operating subsidiaries described in Item 4. Information on the Company Our History and Development Corporate Restructuring of Our Operating Subsidiaries ;
- CVM are to the *Comissão de Valores Mobiliários*, the Brazilian securities commission;
- Federal District are to the federal district of Brasilia, the capital of Brazil;
- General Telecommunications Law are to *Lei Geral de Telecomunicações*, as amended, which regulates the telecommunications industry in Brazil;

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- Global Telecom and GT are to Global Telecom S.A., formerly a Vivo subsidiary prior to our corporate restructuring;
- GSM are to the Global System for Mobile Communications, a service rendered by concession from ANATEL for a specific frequency range;
- Net additions are to the total number of new customers acquired in the period minus the reduction in the number of customers;
- NYSE are to the New York Stock Exchange;
- *real*, *reais* or R\$ are to Brazilian *reais*, the official currency of Brazil;
- SMC are to Serviço Móvel Celular (Mobile Cellular Service), a service rendered pursuant to a concession granted by ANATEL to provide mobile service in a specific frequency range;

- SMP are to *Serviço Móvel Pessoal* (Personal Cellular Service), a service rendered pursuant to an authorization granted by ANATEL to provide mobile service in a specific frequency range;
- SMS are to text messaging services for wireless devices, which allow customers to send and receive alphanumeric messages;
- TDMA are to Time Division Multiple Access, a radio interface technology for cellular networks based on spectral spreading of the radio signal and channel division in the time domain;
- TCO are to Tele Centro Oeste Celular Participações, which includes TCO's B-Band subsidiary and NBT, formerly Vivo subsidiaries prior to our corporate restructuring;
- TCP are to Telesp Celular Participações S.A., our predecessor company;
- TLE are to Tele Leste Celular Participações S.A. and its consolidated subsidiaries, formerly Vivo subsidiaries prior to our corporate restructuring;
- TSD are to Tele Sudeste Celular Participações S.A. and its consolidated subsidiaries, formerly Vivo subsidiaries prior to our corporate restructuring;
- Telebrás are to Telecomunicações Brasileiras S.A. Telebrás;
- Telesp Celular and TC are to Telesp Celular S.A., formerly a Vivo subsidiary prior to our corporate restructuring;
- The Merger are to the merger of the Vivo Companies as discussed in Item 4. Information on the Company Our History and Development Merger of the Vivo Companies ;
- US\$, dollars or U.S. dollars are to United States dollars;
- Vivo, the Company, we, our and us are to Vivo Participações S.A. (formerly Telesp Celular Participações S.A.) and its consolidated subsidiary (unless the context otherwise requires);
- Vivo brand are to the brand used in Brazil in the operations of the Vivo Companies, which together constitute the assets of the Brasilcel joint venture between *Portugal Telecom* and *Telefónica*;
- Vivo Companies are to Vivo, TCO, TLE, TSD, and Celular CRT, collectively;
- Vivo S.A. are to Vivo S.A., a wholly owned subsidiary of Vivo, that since the Restructuring has conducted all of our operators including SMP operators in the following areas:
  - Areas 1 and 2, the state of São Paulo (operations previously provided by Telesp Celular S.A.);
  - Area 3, the states of Rio de Janeiro and Espírito Santo (operations previously provided by Telerj Celular S.A., or Telerj, and Telest Celular S.A., or Telest);
  - Area 5, the states of Paraná and Santa Catarina (operations previously provided by Global Telecom);
  - Area 6, the state of Rio Grande do Sul (operations previously provided by Celular CRT);

Areas 7 and 8, the central western and northern regions, including the states of Goiás, Tocantins, Mato Grosso, Mato Grosso do Sul, Rondônia, Acre, Amapá, Amazonas, Maranhão, Para and Roraima and in the Distrito Federal (operations previously provided by Telegoias Celular S.A., or Telegoias, Telemat Celular S.A., or Telemat, Telems Celular S.A., or Telems, Teleron Celular S.A., or Teleron, Teleacre Celular S.A., or Teleacre, Norte Brasil Telecom S.A., or NBT and TCO); and

Area 9, the states Bahia and Sergipe (operations previously provided by Telebahia Celular S.A., or Telebahia, and Telergipe Celular S.A., or Telergipe); and

- WAP are to Wireless Application Protocol, an open and standardized protocol started in 1997, which allows access to Internet servers through specific equipment, a WAP Gateway at the carrier, and WAP browsers in customers wireless devices.

- wireless devices are to the wireless appliances that we sell, including cellular handsets, wireless handled devices and wireless broadband cards.

Unless otherwise specified, data relating to the Brazilian telecommunications industry included in this annual report were obtained from ANATEL.

## **PRESENTATION OF FINANCIAL INFORMATION**

Our consolidated financial statements as of December 31, 2006 and 2005 and for the three years in the period ended December 31, 2006 and our combined financial statements as of December 31, 2005, and for the two years in the period ended December 31, 2005, have been prepared in accordance with the accounting practices adopted in Brazil, as prescribed by Brazilian Corporate Law, or the Brazilian GAAP Method, which differs in certain significant respects from generally accepted accounting principles in the United States, or U.S. GAAP. Note 37 to our financial statements appearing elsewhere in this annual report describes the principal differences between the Brazilian Corporate Law Method and U.S. GAAP as they relate to us, and provides a reconciliation to U.S. GAAP of net loss and shareholders' equity. These consolidated financial statements have been audited by *Deloitte Touche Tohmatsu Auditores Independentes*.

As described in Note 1 to our financial statements, in February 2006, an extraordinary shareholders' meeting approved the merger of Tele Sudeste Celular Participações S.A. ( TSD ), Tele Leste Celular Participações S.A. ( TLE ) and Celular CRT Participações S.A. ( CRT ) into the Company through exchange of shares and the acquisition of the minority interest in Tele Centro-Oeste Celular Participações S.A. ( TCO ) by exchanging shares of the Company for the shares held by minority shareholders of TCO, after which TCO became a wholly-owned subsidiary of the Company (the Merger ). See Item 4. Information on the Company Our History and Development Merger of the Vivo Companies.

Since the Company was under common control with TSD, TLE and CRT for all periods presented after December 2002 and prior to the above restructuring, financial information combining the historical operations of these entities has been presented for the years ended December 31, 2005, 2004 and 2003. In the combined financial information, all inter-company transactions have been eliminated. The acquisitions of minority interests in TSD, TLE, CRT and TCO were accounted for in our consolidated financial statements on the date that the respective share exchanges occurred, in February 2006. However, the financial statements have been consolidated as from January 1<sup>st</sup>,2006 as described in the protocol of Merger. The combined financial statements have been presented supplementally for the purposes of this annual report in our consolidated financial statements as of December 31, 2006 and 2005 and for the three years in the period ended December 31, 2006 and are not required for statutory reporting purposes in Brazil.

## **FORWARD LOOKING STATEMENTS**

Certain sections in this annual report, principally in Item 3.D. Key Information Risk Factors, Item 4. Information on the Company and Item 5. Operating and Financial Review and Prospects, contain information that is forward-looking, including but not limited to:

- statements concerning our operations and prospects;
- the size of the Brazilian telecommunications market;
- estimated demand forecasts;
- our ability to secure and maintain telecommunications infrastructure licenses, rights of way and other regulatory approvals;



- our strategic initiatives and plans for business growth;
- industry conditions;

- our funding needs and financing sources;
- network completion and product development schedules;
- expected characteristics of competing networks, products and services;
- quantitative and qualitative disclosures about market risks;
- other statements of management's expectations, beliefs, future plans and strategies, anticipated developments and other matters that are not historical facts; and
- other factors identified or discussed under Item 3.D. Key Information Risk Factors.

Forward looking statements may also be identified by words such as believe, expect, anticipate, project, intend, should, seek, estimate, future or similar expressions. Forward-looking information involves risks and uncertainties that could significantly affect expected results. The risks and uncertainties include, but are not limited to:

- the short history of our operations as an independent, private-sector entity and the introduction of competition to the Brazilian telecommunications sector;
- the cost and availability of financing;
- uncertainties relating to political and economic conditions in Brazil;
- inflation, interest rate and exchange rate risks;
- the Brazilian government's telecommunications policy; and
- the adverse determination of disputes under litigation.

We undertake no obligation to update publicly or revise any forward-looking statements because of new information, future events or otherwise. In light of these risks and uncertainties, the forward-looking information, events and circumstances discussed in this annual report might not occur. Our actual results and performance could differ substantially from those anticipated in our forward-looking statements.

**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****A. Selected Financial Data**

The selected financial data as of December 31, 2006 and 2005 and for the three year in the period ended December 31, 2006 included in this annual report have been derived from our audited consolidated and combined financial statements and notes thereto included elsewhere in this annual report and audited by *Deloitte Touche Tohmatsu Auditores Independentes*.

As described in Note 1 to our financial statements, in February 2006, an extraordinary shareholders meeting approved the merger of TSD, TLE and Celular CRT into the Company through exchange of shares and the acquisition of the minority interest in TCO by exchanging shares of the Company for the shares held by minority shareholders of TCO, after which TCO became a wholly-owned subsidiary of the Company (the Merger). See Item 4. Information on the Company Merger of the Vivo Companies.

Since the Company was under common control with TSD, TLE and CRT for all periods presented after December 2002 and prior to the above restructuring, financial information combining the historical operations of these entities has been presented for the years ended December 31, 2005, 2004 and 2003. In the combined financial information, all inter-company transactions have been eliminated. The acquisitions of minority interests in TSD, TLE, CRT and TCO were accounted for in our consolidated financial statements on the date that the respective share exchanges occurred, in February 2006. However, the financial statements have been consolidated as from January 1, 2006 as described in the protocol of Merger. The combined financial statements have been presented supplementally for the purposes of this annual report in our consolidated financial statements as of December 31, 2006 and 2005 and for the three years in the period ended December 31, 2006 and are not required for statutory reporting purposes in Brazil.

Our consolidated and combined financial statements are prepared in accordance with the Brazilian Corporate Law Method, which differs in certain material respects from U.S. GAAP. See note 37 to our financial statements for a summary of (i) the differences between the Brazilian Corporate Law Method and U.S. GAAP as they relate to us, (ii) a reconciliation to U.S. GAAP of shareholders equity as of December 31, 2006 and 2005, and (iii) our net income for the year ended December 31, 2006 and net loss for the years ended December 31, 2005 and 2004.

The following tables present a summary of our selected financial data at the dates and for each of the periods indicated. You should read the following information together with our financial statements and the notes thereto included elsewhere in this annual report and with Item 5. Operating and Financial Review and Prospects.

---

## Year ended December 31,

## Consolidated

## Combined

2006(1)

2005(1)

2004(1)

2003(1)

2002(1)

(in millions of *reais*, except per share data)**Income Statement Data:***Brazilian Corporate Law Method*

Net operating revenue	10,936.7	11,253.8	10,929.4	9,393.5	3,415.0
Cost of services and goods sold	(5,564.2)	(5,337.3)	(5,338.1)	(4,836.1)	(1,739.4)
Gross profit	5,372.5	5,916.5	5,591.3	4,557.4	1,675.6
Operating expenses:					
Selling expenses	(3,787.5)	(3,744.5)	(2,833.0)	(1,968.7)	(526.9)
General and administrative expenses	(1,112.2)	(1,033.3)	(959.2)	(924.4)	(343.2)
Other net operating expenses	(270.6)	(360.1)	(129.2)	(138.7)	(39.8)
Operating income before equity in losses of unconsolidated subsidiary and net financial expenses	202.2	778.6	1,669.9	1,525.6	765.7
Equity in losses of unconsolidated subsidiary					(890.7)
Net financial expenses	(748.0)	(913.1)	(1,088.5)	(1,161.1)	(808.4)
Operating income (loss)	(545.8)	(134.5)	581.4	364.5	(933.4)
Net non-operating income (expenses)	(289.0)	(96.5)	(60.9)	(36.1)	10.0
Extraordinary item					(170.8)
Income (loss) before income taxes and minority interests	(834.8)	(231.0)	520.5	328.4	(1,094.2)
Income taxes	859.1	(363.0)	(438.5)	(407.8)	(46.5)
Minority interests	(8.0)	(173.5)	(480.9)	(347.6)	
Net income (loss)	16.3	(767.5)	(398.9)	(427.0)	(1,140.7)
Net income (loss) per share (R\$)	0.0113	(0.6919)	(0.1765)	(0.2065)	(0.00097)
Dividends declared per thousand preferred shares (R\$)	0.018	0.037	0.058	0.056	
Dividends declared per thousand common Shares (R\$)		0.047	0.083	0.079	
U.S. GAAP					
Net operating revenue	14,152.3	14,407.8	14,856.5	12,159.0	4,575.0
Operating (loss) income	(183.2)	929.7	1,368.5	1,345.5	328.8
Net financial expenses	(666.3)	(914.7)	(992.9)	(138.4)	(1,149.6)
Equity in losses of unconsolidated subsidiaries					- (759.1)
Net non-operating income (expenses)	(11.6)	(14.8)	(12.0)	(35.2)	9.8
Income (loss) before income taxes, minority interests	(861.1)	0.2	363.6	1,171.9	(1,570.1)
Income taxes and minority interest	400.6	(494.4)	(852.6)	(1,034.0)	74.4
Net income (loss)	(460.5)	(494.2)	(489.0)	137.9	(1,495.7)
Basic and diluted net income (loss) per share common (R\$)	(0.99)	(1.19)	(1.43)	0.15	(15.58)
	0.02	0.05	0.08	0.15	(15.58)

Basic and diluted net income (loss) per  
share preferred (R\$)

Weighted average common shares outstanding (2)	481,267,468	443,996,716	371,686,879	335,446,441	163,753,546
Weighted average preferred shares outstanding (2)	841,340,834	637,776,690	532,574,385	487,069,335	178,807,226

Year ended December 31,

	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>Consolidated</b>	<b>Combined</b>	

(in millions of reais)

**Cash Flow Data:**

Cash flows from operating activities	3,100.8	2,302.2	2,068.4
Cash flows from investing activities	(1,922.4)	(2,361.2)	(2,773.8)
Cash flows from financing activities	(1,458.4)	(373.1)	732.6

As of December 31,

	Consolidated		Combined		
	2006(1)	2005(1)	2004(1)	2003(1)	2002(1)
(in millions of reais, except for per share data)					
<b>Balance Sheet Data:</b>					
<i>Brazilian Corporate Law Method</i>					
Property, plant and equipment, net	6,445.5	6,683.2	6,477.5	6,323.1	2,497.2
Total assets	17,542.1	19,259.3	19,803.0	18,977.0	9,654.4
Loans and financing	4,500.4	5,652.8	5,595.5	7,124.0	4,460.8
Shareholders equity	8,371.7	7,047.5	5,830.9	5,967.1	4,010.0
Capital Stock	6,347.8	8,232.4	5,828.9	5,615.8	4,373.7
Number of shares as adjusted to reflect changes in capital	1,437,623	1,109,225	2,259,465,452	2,066,942,500	1,171,784,352
<i>U.S. GAAP</i>					
Property, plant and equipment, net	6,626.2	6,784.7	6,621.4	7,105.2	2,794.5
Total assets	18,392.5	20,367.1	20,092.6	19,148.7	10,202.0
Total liabilities	9,210.4	11,294.7	10,799.5	11,383.2	6,894.7
Shareholders equity	9,126.2	7,165.6	5,685.9	5,904.8	3,307.3
Capital stock	6,325.6	8,232.4	5,828.9	5,615.8	4,373.7
Number of shares as adjusted to reflect changes in capital	1,437,623	1,109,225	903,786	826,777	468,714

(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated financial information of TSD, TLE and CRT as from January 1, 2006. The financial information presented for the 2005, 2004 and 2003 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since these companies were under common control with Vivo for these periods. The financial information presented for the 2002 fiscal year represents information from TCP's financial statements.

(2) As a result of the corporate restructuring in January 2000, the Company was obligated to issue shares to the controlling shareholder for the amount of the tax benefit on the amortization of the intangibles related to concession that was transferred in the Merger. The number of issuable shares, which are determined on the basis of estimates using the Company's share price at the date of the balance sheet, are considered dilutive and are included for the purpose of calculating diluted earnings per share for the years ended December 31, 2002, 2003, 2004, 2005 and 2006. The potentially diluted shares, consisting solely of the estimate of issuable shares mentioned above, have been excluded from the computation for all periods presented as their effect would have been anti-dilutive. As described in Note 37 (j) to the Company's financial statements for the year ended December 31, 2006, the Company adopted Emerging Issues Task Force EITF No. 03.6, Participating Securities and the Two-Class Method under FASB Statement No. 128. Since preferred shareholders have a liquidation preference over common shareholders, net losses are not allocated to preferred shareholders. Prior period earnings per share amounts presented for comparative purposes were restated to conform to the current year presentation. Additionally, loss per share and share amounts for all periods retroactively reflect the effect of the reverse stock split described in Note 22 to the Company's financial statements.

### Exchange Rates

Before March 14, 2005, there were two principal foreign exchange markets in Brazil:

- the commercial rate exchange market; and
- the floating rate exchange market.

Most trade and financial foreign-exchange transactions were carried out on the commercial rate exchange market. The floating market rate generally applied to transactions to which the commercial market rate did not apply. Prior to February 1999, the exchange rate in each market was established independently, resulting in different rates during some periods. Since February 1, 1999, the Central Bank placed the commercial rate exchange market and the floating rate exchange market under identical operational limits, and financial institutions operating in the commercial market were authorized to unify their positions in the two different markets, which led to a convergence in the pricing and liquidity of both markets and a reduction in the difference between their respective rates.

With the enactment of Resolution No. 3,265 dated March 4, 2005 by the National Monetary Council both markets were consolidated into one single foreign exchange market, effective as of March 14, 2005. All foreign exchange transactions are now carried out in this single consolidated market, through institutions authorized to operate in such market.

Foreign exchange rates continue to be freely negotiated, but may be influenced by Central Bank intervention. From March 1995 through January 1999, the Central Bank allowed the gradual devaluation of the *real* against the U.S. dollar. In January 1999, the Central Bank allowed the *real*/U.S. dollar exchange rate to float freely. Since then, the *real*/U.S. dollar exchange rate has been established mainly by the Brazilian interbank market and 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 let the *real* float freely or will intervene in the exchange rate market through a currency band system or otherwise, or that the exchange market will not be volatile as a result of political instability or other factors. In light of these factors, we cannot predict that the *real* will not depreciate or appreciate in value in relation to the U.S. dollar substantially in the future. In addition, exchange rate fluctuations may also affect our financial condition. For more information on these risks, see Risk Factors Risks Relating to Brazil.

The following tables set forth the commercial selling rate, expressed in *reais* per U.S. dollar (R\$/US\$) for the periods indicated, as reported by the Central Bank.

	Exchange Rate of R\$ per US\$			
	Low	High	Average(1)	Year-End
<b>Year ended December 31,</b>				
2002	2.271	3.955	2.931	3.533
2003	2.822	3.662	3.071	2.889
2004	2.654	3.205	2.917	2.654
2005	2.163	2.762	2.434	2.341
2006	2.089	2.301	2.168	2.138

Source: Central Bank of Brazil, PTAX.

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

	Exchange Rate of R\$ per US\$	
	Low	High
<b>Month Ended</b>		
October 31, 2006	2.133	2.168
November 30, 2006	2.135	2.187
December 31, 2006	2.138	2.169
January 31, 2007	2.125	2.156
February 28, 2007	2.077	2.118
March 30, 2007	2.050	2.139

Source: Central Bank of Brazil, PTAX.

## B. Capitalization and Indebtedness

Not applicable.

## C. Reasons for the Offer and Use of Proceeds



Not applicable.

**D. Risk Factors**

*This section is intended to be a summary of more detailed discussions contained elsewhere in this annual report. The risks described below are not the only ones we face. Our business, results of operations or financial condition could be harmed if any of these risks materialize and, as a result, the trading price of the ADSs could decline.*

## Risks Relating to Brazil

*The Brazilian government has exercised, and continues to exercise, significant influence over the Brazilian economy. Brazilian political and economic conditions have a direct impact on our business, operations and the market price of our preferred shares and our ADSs.*

In the past, the Brazilian government has intervened in the Brazilian economy and occasionally made drastic changes in policy. The Brazilian government's actions to control inflation and affect other policies have often involved wage and price controls, currency devaluations, capital controls, and limits on imports, among other things.

Our business, financial condition, results of operations and the market price of our preferred shares and ADSs may be adversely affected by changes in government policies, as well as general economic factors, including:

- currency fluctuations;
- exchange control policies;
- internal economic growth;
- inflation;
- price instability;
- energy policy;
- interest rates;
- liquidity of domestic capital and lending markets;
- tax policies (including reforms currently under discussion in the Brazilian Congress); and
- other political, diplomatic, social and economic developments in or affecting Brazil.

Uncertainty as to future government policies may contribute to an increase in the volatility of the Brazilian securities markets and securities issued abroad by Brazilian companies. The Brazilian economy grew 2.9% in 2006, 2.3% in 2005 and 4.9% in 2004. Due to the limited economic growth in recent years, it is not certain whether the current economic policy will prevail. We cannot predict Brazil's monetary, tax, social security and other policies, nor if such policies will cause an adverse impact on the economy and to our business and results of operations or the market price of our preferred shares and ADSs.

### *Tax reforms may affect our prices.*

The Brazilian government has proposed tax reforms that are currently being considered by the Brazilian Congress. If we experience a higher tax burden as a result of the tax reform, we may have to pass the cost of that tax increase to our customers. This increase may have a material negative impact on the dividends paid by our subsidiary to us and on our revenues and operating results.

### *Political instability may have an adverse impact on the Brazilian economy.*

Political crises in Brazil in the past have affected the trust of investors and the public in general, as well as the development of the economy. Political crises may have an adverse impact on the Brazilian economy, our business, financial condition and results of operations and the market price of our preferred shares and ADSs.

***Inflation and certain government measures to curb inflation may have adverse effects on the Brazilian economy, the Brazilian securities market and/or our business and operations.***

Brazil has historically experienced extremely high rates of inflation. Inflation and certain of the Brazilian government's measures taken in the attempt to curb inflation have had significant negative effects on the Brazilian economy. Since 1994, Brazil's inflation rate has been substantially lower than in previous periods. However, inflationary pressures persist, and actions taken in an effort to curb inflation, coupled with public speculation about possible future governmental actions, have contributed to economic uncertainty in Brazil and heightened volatility in the Brazilian securities market. In 2006, the general price index, or the IGP-DI (the *Índice Geral de Preços Disponibilidade Interna*), an inflation index developed by the *Fundação Getúlio Vargas*, a private Brazilian foundation, reflected inflation of 3.8%, compared to 1.22% in 2005 and 12.13% in 2004.

Future measures taken by the Brazilian government may have an adverse impact on the Brazilian economy, our business, financial condition and results of operation, or on the market price of our preferred shares and ADSs. If Brazil experiences significant inflation, we may be unable to increase service rates to our customers in amounts that are sufficient to cover our increasing operating costs, and our business may be adversely affected. In addition, high inflation generally leads to higher domestic interest rates and, as a result, the cost of servicing our *real*-denominated debt may increase. Inflation and its effect on domestic interest rates can, in addition, lead to reduced liquidity in the domestic capital and lending markets, which could adversely affect our ability to refinance our indebtedness in those markets.

***Fluctuations in the value of the real against the value of the U.S. dollar may adversely affect our ability to pay U.S. dollar-denominated or U.S. dollar-linked obligations and could lower the market value of our preferred shares and ADSs.***

The Brazilian currency has been devalued frequently over the past four decades. Throughout this period, the Brazilian government has implemented various economic plans and used various exchange rate policies, including sudden devaluations, periodic mini-devaluations (during which the frequency of adjustments has ranged from daily to monthly), exchange controls, dual exchange rate markets and a floating exchange rate system. From time to time, there have been significant fluctuations in the exchange rate between the Brazilian currency and the U.S. dollar and other currencies. For example, the *real* depreciated by 34.3% and 22.3% against the U.S. dollar in 2002 and 2003, respectively. In 2004 and 2005, the *real* appreciated against the U.S. dollar by 8.8% and 11.8%, respectively, and in 2006 the *real* appreciated by 8.7% against the U.S. dollar.

Devaluation of the *real* relative to the U.S. dollar could create additional inflationary pressures in Brazil by generally increasing the price of imported products and requiring recessionary government policies to curb aggregate demand. The sharp depreciation of the *real* in relation to the U.S. dollar may generate inflation and governmental measures to fight possible inflationary outbreaks, including the increase in interest rates. 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 the balance of payments, as well as dampen export-driven growth. Devaluations of the *real* would reduce the U.S. dollar value of distributions and dividends on our preferred shares and ADSs and may also reduce the market value of such securities. Any such macroeconomic effects could adversely affect our net operating revenues and our overall financial performance.

Devaluation of the *real* relative to the U.S. dollar may increase the cost of our indebtedness in foreign currency. It would also reduce the U.S. dollar value of our revenues and distribution of dividends. As of December 31, 2006, Vivo had R\$4.5 billion in consolidated total debt, of which approximately 59.0% was denominated in foreign currencies, such as the U.S. dollar, Japanese yen and the UMBNDES (an index of several currencies predominantly influenced by the U.S. dollar). Significant costs relating to our network infrastructure and wireless device costs are payable or linked

to payment by us in U.S. dollars. At the same time, while our foreign currency debt obligations were covered by derivative contracts as of December 31, 2005, and we may derive income from these and other derivative transactions, all of our operating revenues are generated in *reais*. To the extent that the value of the *real* decreases relative to the U.S. dollar, Japanese yen and UMBNDES, our debt becomes more expensive to service and it becomes more costly for us to acquire the technology and the goods that are necessary to operate our business. Although we currently hedge our foreign currency debt, we may decide to change our hedging policy in the future. In

addition, when the value of the *real* increases relative to the U.S. dollar, Japanese yen and UMBNDES, the decrease in the cost of servicing our debt is offset by our losses on the derivatives associated with it. See Item 3. Key Information Selected Financial Data Exchange Rates for more information on exchange rates.

***Fluctuations in interest rates may have an adverse effect on our business and on the market price of our preferred shares and ADSs.***

Between February and July 2002, the Central Bank reduced the basic interest rate from 19% to 18%. Between October 2002 and February 2003, the Central Bank increased the basic interest rate by 8.5 percentage points, to 26.5%. In June 2003, the Central Bank started again reducing the basic interest rate. As of December 31, 2006, the basic interest rate is 13.3%. As of December 31, 2006, Vivo's total indebtedness was R\$4,500.4 million. Approximately 41.0% of such indebtedness is denominated in *reais* and mostly pegged to the CDI (*Certificado Depositário Interbancário*) rate, a Brazilian interbank rate. All other debt was denominated in foreign currencies and fully covered by derivative contracts so that the final cost of the debt and the associated derivative is the CDI rate. As a consequence, an increase in the CDI interest rates and inflation indexes would increase the costs of our debt, which could adversely affect the market's perception of the value of our shares.

***Brazilian government exchange control policies could adversely affect our ability to make payments on foreign currency-denominated debt.***

The purchase and sale of foreign currency in Brazil is subject to governmental control. In the past, the Central Bank has centralized certain payments of principal on external obligations. Many factors could cause the Brazilian government to institute a more restrictive exchange control policy, including, without limitation, the extent of Brazilian foreign currency reserves, the availability of sufficient foreign exchange, the size of Brazil's debt service burden relative to the economy as a whole and political constraints to which Brazil may be subject. A more restrictive policy could affect the ability of Brazilian debtors (including us) to make payments outside of Brazil to meet foreign currency-denominated obligations.

***Deterioration in economic and market conditions in other countries, especially emerging market countries, may adversely affect the Brazilian economy and our business.***

The market for securities issued by Brazilian companies is influenced by economic and market conditions in Brazil and, to varying degrees, market conditions in other Latin American and emerging market countries. Although economic conditions are different in each country, the reaction of investors to developments in one country may cause the capital markets in other countries to fluctuate. Developments or conditions in other emerging market countries have at times significantly affected the availability of credit in the Brazilian economy and resulted in considerable outflows of funds and declines in the amount of foreign currency invested in Brazil. Any adverse economic developments in other emerging markets may adversely affect investor confidence in securities issued by Brazilian companies, including our preferred shares and ADSs, causing the market price and liquidity of those securities to suffer.

## **Risks Relating to the Brazilian Telecommunications Industry and Us**

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

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

- industry policies and regulations;
- licensing;
- tariffs;

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

This extensive regulation and the conditions imposed by our authorization to provide telecommunication services may limit our flexibility in responding to market conditions, competition and changes in our cost structure.

In 2002, ANATEL changed the Personal Mobile Service (*Serviço Móvel Pessoal*), or SMP, regime (first enacted in December 2000), encouraging companies operating under the Mobile Cellular Service (*Serviço Móvel Celular*), or SMC, regime to migrate to the SMP regime.

Under the SMP regime, we no longer receive payment from our customers for outbound long-distance traffic and instead receive payment for the use of our network in accordance with a network usage payment plan, which includes outbound long distance calls. However, the interconnection fees that we receive from long-distance operators may not compensate us for the revenues that we would have received from our customers for outbound long-distance traffic. Until June 30, 2004, SMP service providers were able to opt to establish a price cap or freely negotiate their interconnection charges. Now, free negotiation is the rule, subject to ANATEL regulations relating to the traffic capacity and interconnection infrastructure that must be made available to requesting parties. In 2005, ANATEL began permitting free negotiations for mobile interconnection, or VU-M, fees and by July 2005, local-fixed concessionaires and mobile operators had reached a provisional agreement with respect to VU-M fees for local calls, or VC-1 (the agreement guaranteed a 4.5% increase in mobile operators' fees). ANATEL approved that provisional agreement and in March 2006, approved another provisional agreement for VU-M fees for long-distance calls, or VC-2, VC-3, and international, among the same operators that had made the VC-1 agreement in July 2005. ANATEL is currently studying a new model to determine reference costs for use of mobile networks' RVU-M by SMP providers who have significant market power. These values will be used in arbitration cases involving VU-M's value by ANATEL and is expected to be completed by mid-2007. The free negotiation of the mobile call termination fees (VU-M) continued on 2006, but because mobile and fixed operators did not agree on a new collective agreement for tariff readjustments in 2006. Therefore, the 2005 provisional agreement between the local fixed concessionaires and the mobile operators remains in effect while new attempts at negotiation are in progress.

While a provisional agreement has been reached concerning a new VU-M value, all the mobile and fixed operators requested in early 2005 for ANATEL to arbitrate the definitive value of the mobile termination fee. During this process, ANATEL has recommended that the operators hire a consulting company to conduct a study to determine the new VU-M value. The mobile and fixed operators presented all necessary documents in 2006 during the arbitration process and are currently awaiting a decision from the Brazilian Regulatory Authority.

Under Resolution 438, published in July 2006, the free negotiation of the cost of use of mobile networks' VU-M was maintained. However, in the arbitration by ANATEL, while the cost model is not implemented, ANATEL will decide the new value of VU-M by reference to the existing ratio (as of January 1, 2006), between the value of VU-M and the value of VC-1. In addition, under the ANATEL rules, the retail rates charged to customers for local fixed to mobile calls cannot be less than the sum of the interconnection fees charged on the local fixed and mobile



terminations.

Under Resolution 438, ANATEL also eliminated the partial Bill & Keep rule for network usage between SMP networks. The applicable rule is now full billing, where the SMP operator pays the entire call termination fee of the other mobile network. The rule of the partial Bill & Keep had been maintained by the SMP and SME (trunking) networks. Before full billing, an SMP operator used to pay for the use of another SMP operator's network in the same registration area only if the traffic carried from the first operator to the second exceeded 55% of the total traffic

exchanged between them. In that case, only those calls that surpassed the 55% level were subject to payment for network usage.

We cannot predict whether the current regulatory regime will remain in place or whether any future regulatory change will have an adverse effect on our results of operations.

***If the inflation adjustment index now applied to our prices is changed, the new index may not be adequate.***

The Brazilian government currently uses the General Price Index, or the IGP-DI (the *Índice Geral de Preços Disponibilidade Interna*), an inflation index developed by the *Fundação Getúlio Vargas*, a private Brazilian economic organization, in connection with the prices charged in the wireless telecommunications industry. Starting in 2007, we expect the Brazilian government to begin regulating the telecommunications industry based on an economic model (FAC, or Fully Allocated Costs) that analyzes companies' total costs based on a theoretical company's costs and other factors. In connection with the introduction of this model, the Brazilian government will use a different inflation adjustment mechanism, the IST index (*Índice de Serviços de Telecomunicações*), possibly starting in 2008. Under Resolution 438, after the economic model is implemented, ANATEL will determine the reference cost of using mobile networks (RVU-M) for SMP providers who have significant market power, which will be used in the arbitration case by ANATEL to determine the value of VU-M. The inflation adjustment of the RVU-M value will use the IST index. If this new inflation adjustment mechanism, or any other mechanism chosen by the Brazilian government in the future, does not adequately reflect the true effect of inflation on our prices, our results of operations could be adversely affected.

***ANATEL's proposal regarding the consolidation of prices could have an adverse effect on our results.***

ANATEL has proposed new regulations on interconnection rules, some of which could have an adverse effect on our results. The following regulations on interconnection rules have been promulgated: the new General Regulation of Interconnection (*Regulamento Geral de Interconexão* Resolution number 410/2005, or RGI); the Regulation of Separation and Allocation of Costs (Resolution number 396/2005); the Regulation of Industrial Exploration of Dedicated Lines (*Exploração Industrial de Linha Dedicada* Resolution number 402/2005, or EILD) and the new Regulation of Remuneration of Use of SMP Providers Networks (Resolution number 438/2006). The regulations that may adversely affect our results are (1) the new negotiation rules for VU-M prices by which ANATEL would have a role in determining the reference cost for use of mobile networks (RVU-M) by SMP providers who have significant market power, which will be used in the arbitration case by ANATEL of the value of VU-M, rather than the current, free-market negotiation of prices and (2) the VU-M price unification among SMP providers of the same economic group having significant market power, in the same region of the general authorization plan (*Plano Geral de Autorizações*, or PGA) of SMP, according to criteria which is yet to be defined. These regulations could have an adverse effect on our results of operations because (1) ANATEL may allow more favorable prices for economic groups without significant market power and (2) the prices we charge in some regions in which we operate are higher than those in some other regions, and consolidation of those prices, competitive pressures and other factors could reduce our average prices and thereby reduce our revenues.

ANATEL's Public Consultation number 642 of 2005 relates to alterations in the regulation of SMP. While counter arguments thereunder must have been sent to ANATEL before January 16, 2006, none have been made. In the proposed regulation, ANATEL notes areas of vital importance for mobile business, such as the necessity for retail stores in the cities within an operator's coverage areas, increases in the validity periods of prepaid cards, an extension of the period for blocking use by insolvent customers and a limitation on the period of time after which customers may leave service plans. We have presented our arguments to ANATEL against the proposals that may have adverse effects on our business. If these new regulations take effect, they may have adverse effects on our revenues and results of operations.

In 2006, ANATEL published Public Consultation number 734. The period for public comment regarding this Public Consultation ended on November 6, 2006. This Public Consultation considers regulations that will implement and develop fixed and wireless number portability in Brazil by 2009. For SMP, number portability will only be applied for wireless codes of access of the same registration area. For fixed operators, number portability will only be applied for fixed codes of access of the same local area. For the next step, ANATEL will analyze and evaluate the

suggestions presented by fixed and mobile operators, including Vivo, and will issue the new regulation. There can be no assurance that this new regulation will not have adverse effects on the results of our operations.

Another Public Consultation published by ANATEL in 2006 is number 756. The period for public comment was suspended for judicial sentence. This Public Consultation considers a proposal for an auction to consider bids for exploration of the SMP in the remaining radio frequency bands D and E, and in some bands defined in Resolution 454 to the SMP, including the 1.9 GHz band (band L), previously allocated to the fixed operators. This auction proposal does not include 3G radiofrequencies.

Resolution 454, published by ANATEL in 2006, relates to the new regulation of conditions for the use of radiofrequency bands of 800 MHz, 900 MHz, 1,800 MHz, 1,900 MHz, which was previously allocated for fixed operators to provide services using WLL technology, and 2,100 MHz, which are allocated for SMP.

***We face substantial competition that may reduce our market share and harm our financial performance.***

There is substantial competition in the telecommunications industry. We not only compete with companies that provide SMP service and trunking but also with companies that provide fixed-line telecommunications and Internet access services, due to the trend towards the convergence and substitution of SMP services for these other services.

We expect competition to intensify as a result of the entry of new competitors and the rapid development of new technologies, products and services. Our ability to compete successfully will depend on our marketing techniques and on our ability to anticipate and respond to various competitive factors affecting the industry, including new services that may be introduced, changes in consumer preferences, demographic trends, economic conditions and discount pricing strategies by our competitors. If we do not keep pace with technological advances, or if we fail to respond timely to changes in competitive factors in our industry, we could continue to lose market share and could suffer a decline in our revenue. Competition from other SMP communications service providers in the regions in which we operate has also affected, and may continue to affect, our financial results by causing, among other things, a decrease in our customer growth rate, decreases in prices and increases in selling expenses.

These factors have already contributed to a negative effect on our market share and our results of operations and could have a material adverse effect on our business and results of operations in the future. As a result of competitive pressures, for example, our market share decreased from 44.4% as of December 31, 2005 to 38.2% as of December 31, 2006, and our market share of net additions to our customer base decreased from 21.8% for the twelve months ended December 31, 2005 to a negative percentage of 8.5% for the twelve months ended December 31, 2006. In addition, our net additions of customers decreased 123.5% from the twelve months ended December 31, 2005 to the twelve months ended December 31, 2006.

Recently, there has been consolidation in the Brazilian telecommunications market, and we believe this trend may continue. Consolidation may result in increased competitive pressures within our market. We may be unable to respond adequately to pricing pressures resulting from consolidation, which would adversely affect our business, financial condition and results of operations.

In September 2004, Brasil Telecom, the fixed-line incumbent in nine states in Brazil and the Federal District (ANATEL's Region II), launched GSM operations in those states. Brasil Telecom's authorization area overlaps ours in Brasilia and in the states of Acre, Goias, Mato Grosso, Mato Grosso do Sul, Rondonia, Tocantins, Paraná, Santa Catarina and Rio Grande do Sul. The entrance of Brasil Telecom into these markets will increase the competition that Vivo face in some states. Brasil Telecom has announced that its marketing strategy will be the convergence between its fixed and mobile services, and it is the only company in those states that offers both fixed and cellular services. The entrance of Brasil Telecom into the cellular markets in these states increase competition for Vivo and have a material

adverse effect on our results of operations.

*Our results of operations have been negatively affected by a decrease in our customer growth and could also be affected if our rate of customer turnover increases.*

Our rate of acquisition of new customers has declined significantly, primarily due to competition and increased market penetration. For example, our net additions of customers decreased 123.5% from the twelve months ended

December 31, 2005 to the twelve months ended December 31, 2006 due to a decrease in the addition of new prepaid customers to a loss of 517,373 new prepaid customers in the twelve months ended December 31, 2006, compared to the addition of 2,703,995 new prepaid customers in the comparable period of the prior year. This decrease in the rate of new additions of customers has negatively affected our results of operations and could continue to do so in the future. In addition, if our rate of customer turnover were to increase significantly, our results of operations and our competitive position could be adversely affected. Several factors in addition to competitive pressures could influence our rate of acquisition of new customers and our rate of customer turnover, including limited network coverage, lack of sufficient reliability of our services and economic conditions in Brazil.

***The industry in which we conduct our business is subject to rapid technological changes and these changes could have a material adverse effect on our ability to provide competitive services.***

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

The advent of new products and technologies could have a variety of consequences for us. These new products and technologies may reduce the price of our services by providing lower-cost alternatives, or they may be superior to, and render obsolete, the products and services we offer and the technologies we use, requiring investment in new technology. The cost of upgrading our products and technology in order to continue to compete effectively could be significant, and our ability to fund the upgrading may depend on our ability to obtain additional financing.

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

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

***Our controlling shareholders have a great deal of influence over our business.***

As of December 31, 2006, *PT Móveis SGPS, S.A.* and *Telefónica S.A.*, our principal shareholders, owned, directly and indirectly, approximately 89.3% of our common shares and 62.8% of our total capital. *PT Móveis SGPS, S.A.* is 100% controlled by *Portugal Telecom, SGPS, S.A.* See Item 7.A. Major Shareholders and Related Party Transactions Major Shareholders. Due to their share ownership, our principal shareholders have the power to control us and our subsidiary, including the power to elect our directors and officers and determine the outcome of any action requiring shareholder approval, including corporate reorganizations and the timing and payment of our dividends.

***The cellular industry, including us, may be harmed by reports suggesting that radio frequency emissions cause health problems and interfere with medical devices.***

Media and other reports have suggested that radio frequency emissions from base stations may cause health problems. These concerns could have an adverse effect on the wireless communications industry and, possibly, expose wireless providers, including us, to litigation. According to the World Health Organization (WHO), there is no evidence in the latest medical research that shows any relationship between radio frequency emissions of base stations and health concerns. However, expansion of our network may be affected by perceived risks if we experience problems in finding new sites, which in turn may delay expansion and may affect the quality of our services. On July 2, 2002, ANATEL published Resolution No. 303 that limits emission and exposure for fields with frequencies between 9 kHz and 300 GHz. In addition, the Brazilian government is developing specific legislation for the

deployment of radio frequency transmission stations that will supersede the existing state and municipal laws. The new laws may create additional transmission regulations which, in turn, could have an adverse effect on our business.

***We face risks associated with litigation.***

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

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

For Brazilian GAAP purposes, an impairment is recognized on goodwill if the expected net cash flows generated from the acquired net assets is not sufficient to cover their book value. As of December 31, 2006, the amount of goodwill of the Company is R\$1,012.0 million.

For U.S. GAAP purposes, we are required to test our goodwill for impairment at least annually. The difference between the book value of a company and its market value may indicate that an impairment exists. This impairment test is described in Note 37 to our audited consolidated financial statements. Vivo, in particular, has substantial goodwill, including goodwill related to TCO with a carrying value of R\$648.5 million as of December 31, 2006. It is possible that we may be required to record impairment charges relating to our goodwill in future periods, and this would have an adverse effect on our results of operations.

In addition, we are required to record impairment charges on long-lived assets, including property, plant and equipment and finite-lived intangible assets (including concessions) if the carrying value of those assets exceeds their fair market value for purposes of U.S. GAAP. This annual impairment test is also described in Note 37(m) to our audited consolidated financial statements included in this annual report. When we performed our last impairment test, our evaluation of our ability to recover the carrying value of our long-lived assets was based on projections of future operations that assumed a higher level of revenues and gross margin percentages than we have historically achieved. We may not be successful in achieving these improvements in our revenues and gross margin percentages due to the competitive environment, changes in technology or other factors. If we are unable to achieve these improvements, we may be required to record impairment charges related to our long-lived assets in future periods, and this could have an adverse effect on our operations.

**Risks Relating to Our Securities*****Holders of our preferred shares or ADSs may not receive any dividends.***

According to Brazilian Corporate Law and our by-laws, we must generally pay dividends to all shareholders of at least 25% of our annual net income, as determined and adjusted under the Brazilian Corporate Law. These adjustments to net income for purposes of calculating the basis for dividends include allocations to various reserves that effectively reduce the amount available for the payment of dividends. We were unable to pay minimum dividends for the fiscal years ended December 31, 2002, 2003, 2004 and 2005 because we had net losses. For the fiscal year ended December 2006, we were able to pay dividends because we had net income, but the amounts paid were insufficient to meet the minimum legal requirement. In addition, according to Brazilian Corporate Law, we need not pay dividends to our shareholders in any particular fiscal year if our board of directors determines that such distributions would be inadvisable in light of our financial condition. See Our preferred shares and our ADSs generally do not have voting rights.

Since we are a holding company, our income consists of distributions from our subsidiary in the form of dividends or other advances and payments. We do not generate our own operating revenues, and we are dependent on dividends and other advances and payments for our cash flow, including making any dividend payments and making payments



on our indebtedness.

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

Brazilian law provides that whenever there is a significant imbalance in Brazil's balance of payments or a significant possibility that such imbalance will exist, the Brazilian government may impose temporary restrictions on the remittance to foreign investors of the proceeds of their investment in Brazil (as it did for approximately six

months in 1989 and early 1990) and on the conversion of Brazilian currency into foreign currencies. These restrictions could hinder or prevent the Brazilian custodian of the preferred shares underlying the ADSs or holders who have exchanged the ADSs for the underlying 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 preferred shares will hold the *reais* that it cannot convert for the account of holders of the ADSs who have not been paid. Neither the custodian nor the depositary will be required to invest the *reais* or be liable for any interest.

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

***Actual or anticipated sales of a substantial number of our ADSs could decrease the market prices of our ADSs.***

Sales of a substantial number of our preferred shares could negatively affect the market prices of our preferred shares and ADSs. If, in the future, existing or future holders of preferred shares make substantial sales of shares, the market price of our preferred shares and, by extension, the ADSs may decrease significantly. As a result, holders of the ADSs may not be able to sell the ADSs at or above the price they paid for them.

***The relative volatility and illiquidity of the Brazilian securities markets may adversely affect holders of our ADSs.***

Investments in securities, such as the preferred shares or ADSs, of issuers from emerging market countries, including Brazil, involves a higher degree of risk than investing in securities of issuers from more developed countries.

The Brazilian securities market is substantially smaller, less liquid, more concentrated and more volatile than major securities markets in the United States. There is also significantly greater concentration in the Brazilian securities market than in major securities markets in the United States. These features may substantially limit the ability to sell the preferred shares underlying the ADSs at a price and time at which holders wish to do so. The São Paulo Stock Exchange had a market capitalization of US\$722.6 billion as of December 31, 2006, and an average monthly trading volume of approximately US\$23.4 billion for the first twelve months of 2006.

In comparison, the NYSE had a domestic market capitalization of US\$9,113.5 billion (excluding funds and non-U.S. companies) as of December 31, 2006. A liquid and active market may never develop for our common shares, preferred shares or ADSs, and as a result, the ability of holders to sell at the desired price or time may be significantly hindered.

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

Holders of ADSs are not direct shareholders of our company and are unable to enforce the rights of shareholders under our by-laws and Brazilian Corporate Law. Our corporate affairs are governed by our by-laws and the Brazilian Corporate Law, which differ from the legal principles that would apply if we were incorporated in a jurisdiction in the United States, or elsewhere outside Brazil. Under Brazilian Corporate Law, the rights of a holder of our common shares or preferred shares to protect its interests with respect to actions by us, our directors or executive officers may

be fewer and less well-defined than under the laws of other jurisdictions. In addition, holders of ADSs are not direct shareholders of our company and are unable to enforce the rights of shareholders under our by-laws and Brazilian Corporate Law.

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 or ADSs at a potential disadvantage. In addition, the disclosure required of public companies in Brazil may be less complete or informative than that required of public companies in the United States or in certain other countries.

***Our preferred shares and our ADSs generally do not have voting rights.***

In accordance with Brazilian Corporate Law and our by-laws, holders of our preferred shares, and therefore of our ADSs, are not entitled to vote at meetings of our shareholders, except in limited circumstances. In accordance with Brazilian Corporate Law and our by-laws, holders of preferred shares will have full voting rights in the event that we do not pay minimum dividends to those shareholders for three consecutive fiscal years, and those shareholders will retain those voting rights until we pay minimum dividends again.

Because we did not pay minimum dividends for the years ended December 31, 2001, 2002, 2003, 2004, 2005 and 2006, the holders of preferred shares have been able to exercise voting rights since the general shareholders' meeting held in March 2004. However, once we begin to pay minimum dividends, these voting rights will cease. See "Holders of our preferred shares or ADSs may not receive any dividends" and "Item 10.B Additional Information Memorandum and Articles of Association."

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

Holders of our ADSs may exercise the limited voting rights with respect to our preferred shares represented by the ADSs only in accordance with the deposit agreement related to the ADSs. There are practical limitations upon the ability of 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 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 will receive notice of a shareholders' meeting by mail from the depositary following our notice to the depositary requesting the depositary do so, and so may not receive voting materials in time to instruct the depositary to vote the preferred shares underlying their ADSs. To exercise their voting rights, ADS holders must instruct the depositary on a timely basis. If voting instructions for all or part of the ADSs are not timely received by the depositary, 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 addition, the depositary and its agents are not responsible for failing to carry out voting instructions of the holders of the ADSs or for the manner of carrying out those voting instructions. Accordingly, holders of the ADSs may not be able to exercise voting rights, and will have no recourse if the preferred shares underlying their ADSs are not voted as requested.

***You might be unable to exercise preemptive rights with respect to our preferred shares unless there is a current registration statement in effect that covers those rights or unless an exemption from registration applies.***

You will not be able to exercise preemptive rights related to our preferred shares underlying any ADSs you own unless a registration statement under the U.S. Securities Act of 1933, as amended ( Securities Act ), is effective with respect to those rights, or unless an exemption from the registration requirements of the Securities Act is available. We are not obligated to file a registration statement. Unless we file a registration statement or an exemption from registration applies, you may receive only the net proceeds from the sale of your preemptive rights by the depository, or, if the preemptive rights cannot be sold, they will lapse and you will not receive any value for them. For more information on the exercise of your rights, see Item 10. Additional Information.

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

The ADSs benefit from the certificate of foreign capital registration, which permits The Bank of New York, as depositary, to convert dividends and other distributions with respect to preferred shares into foreign currency, and to remit the proceeds abroad. Holders of ADSs who exchange their ADSs for preferred shares will then be entitled to rely on the depositary's certificate of foreign capital registration for five business days from the date of exchange. Thereafter, they will not be able to remit non-Brazilian currency abroad unless they obtain their own certificate of foreign capital registration, or unless they qualify under Resolution 2,689 of the Central Bank of Brazil, dated January 26, 2000 and issued by BACEN, which entitles certain investors to buy and sell shares on Brazilian stock exchanges without obtaining separate certificates of registration.

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

***Holders of our ADSs could be subject to Brazilian income tax on capital gains from sales of ADSs.***

Brazilian Law No. 10,833, dated December 29, 2003, provides that gains on the disposition of assets located in Brazil by non-residents of Brazil, whether to other non-residents or to Brazilian residents, will be subject to Brazilian taxation. The common shares and preferred shares are expected to be treated as assets located in Brazil for purposes of the law, and gains on the disposition of common shares and preferred shares, even by non-residents of Brazil, are expected to be subject to Brazilian taxation. In addition, the ADSs may be treated as assets located in Brazil for purposes of the law, and therefore gains on the disposition of ADSs by non-residents of Brazil may also be subject to Brazilian taxation. Although the holders of ADSs outside Brazil may have grounds to assert that Law No. 10,833 does not apply to sales or other dispositions of ADSs, it is not possible to predict whether that understanding will ultimately prevail in the courts of Brazil, given the general and unclear scope of Law No. 10,833 and the absence of judicial court rulings in respect thereto. See Item 10. Taxation Brazilian Tax Considerations.

## **ITEM 4. INFORMATION ON THE COMPANY**

### **A. Our History and Development**

#### **General**

We are incorporated under the laws of the Federative Republic of Brazil under the name Vivo Participações S.A., known as Vivo (and prior to the Merger, under the name *Telesp Celular Participações S.A.*). We have the legal status of a *sociedade por ações*, or a stock corporation, operating under Brazilian Corporate Law. Our principal executive offices are located at Avenida Doutor Chucri Zaidan, 860, 04583-110, São Paulo, SP, Brazil. Our telephone number is +55 11 5105-1182, our facsimile number is +55 11 5105-2247, and our website is *www.vivo.com.br*. The information on our website is not part of this Form 20-F. Our agent for service of process in the United States is CT Corporation System, located at 111 Eighth Avenue, New York, New York 10011.

According to market share data published by ANATEL, we are a leading provider of cellular telecommunications services in Brazil through our subsidiary Vivo S.A., whose operations were previously provided by our former subsidiaries *TC*; *GT*; *TCO*; and the subsidiaries of *Celular CRT*; *TLE*; and *TSD*.

The following chart shows our corporate structure as of December 31, 2006:

### **Telebrás and the Privatization**

Vivo was originally incorporated as *Telesp Celular Participações* as a result of a restructuring of Telebrás in 1998. Before 1972, there were more than 900 telecommunications companies operating throughout Brazil. Between 1972 and 1975, Telebrás and its operating subsidiaries, known as the predecessor companies and collectively as the



Telebrás System, were created, acquiring almost all of the telecommunications companies in Brazil, and creating a near monopoly over the public telecommunications services in Brazil.

In 1995, the federal government began a comprehensive reform of Brazil's telecommunications regulatory system. In July 1997, Brazil's national congress adopted the General Telecommunications Law, which provided for the establishment of a new regulatory framework, the introduction of competition and the privatization of the Telebrás System. In January 1998, in preparation for the restructuring and privatization of the Telebrás System, the cellular telecommunications operations of the Telebrás System were spun off into separate companies. In May 1998, the Telebrás System was restructured to form, in addition to Telebrás, twelve new holding companies. Virtually all of the predecessor companies' assets and liabilities were transferred to the new holding companies, which we refer to as the new holding companies. TCP was one of the new holding companies. TCP was awarded all of the share capital held by Telebrás in TC, one of the cellular operating companies that had provided cellular telecommunications service in the state of São Paulo since 1993. The Brazilian government's common shares of Telesp's capital stock were purchased by the Portugal Telecom group.

### **Global Telecom (currently Vivo S.A.)**

Global Telecom (currently Vivo S.A.) is a B Band cellular concessionaire in the states of Paraná and Santa Catarina. GT began commercial operations in December 1998. In February 2001, we acquired an 81.61% indirect economic interest in GT for R\$902 million. On December 27, 2002, we acquired the remaining shares of GT for R\$290.3 million.

### **Brasilcel**

Vivo is controlled by Brasilcel N.V., or Brasilcel, with headquarters in the Netherlands, a joint venture between Portugal Telecom and Telefónica. Through the Vivo Companies, this joint venture controls 29.1% of the total market in Brazil, according to ANATEL, with 29.1 million customers as of December 31, 2006, according to market share data published by ANATEL. Its operations cover an area of approximately 138 million inhabitants, or 73.8% of the Brazilian population, and approximately 83.1% of its GDP. Portugal Telecom and Telefónica are managing the joint venture on an equal basis.

In December 2002, Portugal Telecom and Telefónica transferred to Brasilcel all of their direct and indirect interests in the following companies (whose operations have been conducted by Vivo S.A. since our restructuring):

- *TCP*

TCP controlled an A Band operator in the state of São Paulo, GT, a B Band operator in the states of Paraná and Santa Catarina and TCO S.A. and its subsidiaries in the states of Acre, Amazonas, Amapá, Goiás, Maranhão, Mato Grosso, Mato Grosso do Sul, Pará, Rondônia, Roraima and Tocantins and in the Federal District, Brasília.

- *TLE*

TLE, which controlled A Band operations in the states of Bahia and Sergipe, was one of the operating subsidiaries of Telebrás that was spun off as an individual company in July 1998. It received all the capital stock held by Telebrás in the subsidiaries that provided cellular telecommunication services in the states of Bahia and Sergipe, namely, Telebahia Celular and Telergipe Celular.

TLE was purchased by a consortium formed by Iberdrola Investimentos Sociedade Unipessoal Ltda., an investment company controlled by Iberdrola S.A. and Telefónica Internacional S.A., a subsidiary of Telefónica. On May 17,

1999, Iberoleste Participações S.A. purchased 3.07% of Telebahia's capital stock and 6.54% of Telergipe's capital stock in a tender offer. In February 2000, Telefónica and Iberdrola transferred their shares to Iberoleste, maintaining their same percentage interest in the consortium. On April 5, 2001, Telefónica purchased all the capital stock directly and indirectly held by the Iberdrola Group in TLE.

- *TSD*

TSD, which controlled A Band operators in the states of Rio de Janeiro and Espírito Santo, was one of the operating subsidiaries of Telebrás that was spun off as an individual company in July 1998. TSD received all the capital stock held by Telebrás in the subsidiaries that provided cellular telecommunication services in the States of Rio de Janeiro and Espírito Santo, namely, Telerj Celular and Telest Celular, respectively.

TSD was purchased by a consortium of Telefónica Internacional S.A., Iberdrola Investimentos Sociedade Unipessoal Ltda., NTT Mobile Communications Network, Inc. and Itochu Corporation. In May 2000, Telefónica acquired 67.51% of TSD's capital stock through an exchange offer. On April 5, 2001, Telefónica purchased from the Iberdrola group, with the authorization of ANATEL, 7% of the capital stock of Sudestecel Participações S.A., a holding company that controlled TSD.

- *Celular CRT*

Celular CRT controlled an A Band operator in the state of Rio Grande do Sul. Cellular telecommunications services were first offered in the state of Rio Grande do Sul in December 1992 by a business unit of Celular CRT Companhia Riograndense de Telecomunicações. The fixed and cellular operations of Celular CRT were split on June 25, 1998, and the cellular operations were spun off as Celular CRT. On May 4, 1999, Celular CRT obtained its registration as a publicly held company with the CVM for the trading of its shares on the over-the-counter market organized by Sociedade Operadora do Mercado de Ativos SOMA, starting on May 17, 1999. On September 8, 1999, Celular CRT registered with the Extremo Sul Stock Exchange and BOVESPA, pursuant to the applicable laws. The main shareholder of Celular CRT was the state of Rio Grande do Sul.

In 1996, the state of Rio Grande do Sul sold part of its stake in Celular CRT to Telefónica. In 1998, the remaining stake of the state of Rio Grande do Sul was sold to Telefónica. In 1999, Portugal Telecom subscribed a share capital increase of Celular CRT.

### **Acquisition of TCO**

On April 25, 2003, TCP acquired 64.03% of the outstanding voting capital stock of TCO from Fixcel S.A. for approximately R\$1,505.6 million, corresponding to R\$19.48719845 per each lot of 1,000 shares acquired. TCO is an A Band operator providing cellular telecommunications services in the Federal District of Brazil, as well as in the Brazilian states of Goiás, Mato Grosso do Sul, Mato Grosso, Rondônia, Acre and Tocantins. The agreement also included the acquisition of TCO's B Band subsidiary NBT, which provides cellular telecommunications service in the Brazilian states of Amapá, Amazonas, Maranhão, Pará and Roraima. On May 25, 2003, in compliance with Brazilian legislation, we launched a tender offer for the common shares of TCO not owned by us. The acceptance period ended on November 18, 2003. As a result of the shares tendered, we acquired 74.2% of the outstanding available common shares at the price of R\$16.73 per 1,000 common shares. The total purchase price for the new shares amounted to R\$538.8 million. At December 31, 2003 we held 90.73% of TCO's ordinary shares, representing a 29.31% interest in TCO, excluding treasury stocks. We also announced the intention to launch an exchange offer for the remaining shares of TCO through which we would have become TCO's sole shareholder. This would have been followed by a merger of TCO into TCP. After the launch of the exchange offer, the CVM raised questions on its compliance with Brazilian law. Although TCP and TCO believed, and believe, that the exchange offer complied with applicable law, TCP and TCO decided to terminate the exchange offer in January, 2004. See sections TCO's Corporate Restructuring and Merger of the Vivo Companies below for more information on developments to TCO since we acquired it.

### **Introduction of the Vivo Brand**

In April 2003, Brasilcel launched the brand name Vivo, under which TCP, TCO, TLE, TSD and Celular CRT operate. The creation of the Vivo brand constituted a consolidation of the commercial models throughout the entire country into a common commercial strategy and replaced the different brands under which the different companies offered their services in their respective states. The commercial strategy of Vivo is to increase its customer base as

well as revenues by retaining customers and maintaining their distribution channels. The launching of the Vivo brand was accompanied by loyalty programs and other measures designed to contribute to the success of the commercial strategy. Guided by a common management team, Vivo designs marketing, promotional and other initiatives common to all companies and then tailors those activities to the particular markets of those companies.

### **TCO s Corporate Restructuring**

On June 30, 2004, the management of TCP and TCO approved the corporate restructuring of TCO and its subsidiaries Telegoiás, Telems, Telemat, Teleacre and Teleron. The reasons for restructuring were: (i) to improve TCO and its subsidiaries cash flow, which resulted in the transfer of a R\$511 million tax benefit from TCP to TCO, generated by the amortization of goodwill in the amount of R\$1,503 million, in connection with the acquisition of TCO and its subsidiaries by TCP in 2003 and (ii) to simplify the corporate structure of TCO s subsidiaries, improve TCO s capitalization and benefit the minority shareholders of TCO s subsidiaries.

### **VTO Voluntary Public Tender Offer**

On October 8, 2004, Telesp Celular Participações concluded its public tender offer ( VTO ) for up to 84,252,534,000 preferred shares of TCO by TCP. The number of preferred shares tendered in the VTO exceeded the maximum number to be acquired by TCP. Due to a pro-rata allocation, TCP purchased 0.5547 preferred shares for each preferred share tendered by a TCP holder. After the VTO, on January 7, 2005, the number of TCO shares held by TCP represents 32.76% of the total preferred shares and 50.65% of the total capital stock of TCO. Also under the VTO, Avista Participações Ltda., a subsidiary of Brasilcel, purchased:

- common shares of TLE representing 10.0% of TLE s total common shares and preferred shares of TLE representing 29.51% of TLE s total preferred shares;
- common shares of TSD representing 3.27% of TSD s total common shares and preferred shares of TSD representing 4.89% of TSD s total preferred shares; and
- common shares of Celular CRT representing 4.48% of Celular CRT s total common shares and preferred shares of Celular CRT representing 23.44% of Celular CRT s total preferred shares.

### **Rights Offering**

On November 8, 2004, TCP announced a capital increase of up to R\$2,053,895,871.47, upon private subscription, with an issuance of 410,779,174,294 new shares, of which 143,513,066,618 are common shares and 267,266,107,676 are preferred shares, identical in every aspect to those shares currently existing, at the issuance price of five *reais* (R\$5.00) per lot of one thousand shares, for both types of shares.

The capital increase was carried out in three subscription stages, with due regard to preemptive rights, and ended with an auction of the remaining shares held on January 4, 2005, which was confirmed by the Board of Directors at a meeting held on January 7, 2005. The capital stock was increased to R\$6,427,557,341.20, represented by 1,582,563,526,803 shares, of which 552,896,931,154 are common shares and 1,029,666,595,649 are preferred shares. Following the rights offering, Brasilcel held 94.9% of our common shares, 50.0% of our preferred shares, and 65.7% of our total capital stock.

### **Brasilcel s Share Holding Increases of TLE, TSD, and Celular CRT**

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In July 2005, Brasilcel and its affiliates acquired additional voting capital stock of TLE, TSD and Celular CRT in respective Share Holding increases. As a result of those transactions, Brasilcel held:

- 68.72% of TLE's common shares, 40.95% of TLE's preferred shares and 50.67% of TLE's total capital stock;
- 92.01% of TSD's common shares, 90.27% of TSD's preferred shares and 91.03% of TSD's total capital stock;  
and

- 90.57% of Celular CRT's common shares, 51.47% of Celular CRT's preferred shares and 68.77% of Celular CRT's total capital stock (excluding treasury shares).

## Merger of the Vivo Companies

In February 2006, shareholders of the Vivo Companies approved their consolidation with one another through a Brazilian law procedure (the Merger) whereby TCO became a wholly owned subsidiary of TCP pursuant to a merger of shares (*incorporação de ações*) of TCO and a merger of companies (*incorporação de empresas*) of TLE, TSD and Celular CRT with and into TCP, with TCP as the surviving company. Holders of common shares, preferred shares or (where applicable) ADSs of TCO, TLE, TSD and Celular CRT received common shares, preferred shares or ADSs, respectively, of TCP upon approval of the Merger by the requisite percentage of the voting shareholders of TCP, and of TCO, TLE, TSD and Celular CRT, as applicable. Upon the completion of the Merger, TCP was renamed Vivo Participações S.A. and has become the holding company of TCO and GT and of the remaining subsidiaries of TLE, TSD and Celular CRT.

The boards of directors (*Conselhos de Administração*) of each of the constituent companies to the Merger completed their respective approval processes for the Merger by December 4, 2005, and the respective shareholders approved the transaction as of February 22, 2006. The reasons for the Merger were to align the interests of the shareholders of TCP, TCO, and TLE, TSD and Celular CRT, which were previously under common control; to improve the liquidity of the resultant securities; to simplify the shareholding and organizational structure of the Vivo companies and expand its shareholder base; and to take advantage of important synergies among the companies, which were already operating under the common Vivo brand.

Pursuant to the Merger, Brasilcel and its subsidiaries hold 89.0% of TCP's common shares. Under the Protocol of Merger of Shares and Merger of Companies and Instrument of Justification, the agreements which govern the Merger, TCP underwent a capital increase in the amount of R\$2,631,136,636.01 as a result of the Merger, from R\$6,670,152,498.26 to R\$9,301,289,134.27. The agreements also provided that Celular CRT's preferred shares held in treasury are transferred to TCP in connection with the Merger. At the Vivo Shareholders' Meeting held on February 22, 2006, TCP reduced its capital in the amount of R\$3,147,782,181.54, from R\$6,670,152,498.26 to R\$3,522,370,316.72, as approved by management and the shareholders and in accordance with Brazilian Corporate Law, which permits reductions in capital up to the amount of accumulated losses, allowing a more accurate valuation of the company and the possibility for eventual future distributions of dividends. TCP subsequently changed its corporate name to Vivo. The total capital of Vivo is R\$6,153,506,952.73 due to an increase in the amount of R\$2,631,136,636.01 as a result of the Merger. For more information on the Merger, see the Protocol of Merger of Shares and Merger of Companies and Instrument of Justification among TCP, TSD, TLE and Celular CRT dated December 4, 2005, which is included as an exhibit to this report.

CVM regulations permit the acquiror of a publicly held company to capitalize the tax benefits arising from the amortization of goodwill generated in the acquisition of that company, so long as preemptive rights are extended to the other shareholders of the publicly held company in connection with the capital increase. At the time of the Merger, any rights previously held by Vivo, in connection with its existing investment in TCO, or by certain controlling shareholders, in the case of TSD, TLE and Celular CRT, to capitalize credits of such companies will remain in effect. As a result, at the time of the Merger, Vivo retained its prior rights to capitalize its credits in TCO and such controlling shareholders acquired the right to use their credits in future capital increases of Vivo.

## Capital Increase

On June 08, 2006, the Board of Directors of Vivo Participações approved a capital increase and issued a total of 15,705,528 new common shares at the issue price of R\$12.37 in connection with Brasilcel's capitalization of certain

tax benefits relating to the goodwill it recorded when it acquired us in December 2002 and with preemptive rights exercised by our shareholders. CVM regulations permit buyers of joint stock companies to capitalize tax benefits derived from goodwill, provided preemptive rights related to such capital increase are extended to the other shareholders of the joint stock company. The goodwill Brasilcel capitalized included approximately R\$193.9 million in tax benefits for the fiscal year ending on December 31, 2005 and approximately R\$0.4 million for previous fiscal years, totaling approximately R\$194.3 million.



The issue price was 100% of the weighted average of the closing prices registered by the São Paulo Stock Exchange in the 15 trading sessions held between April 07, 2006 and May 02, 2006. The preemptive rights were authorized to be exercised in the period between May 08, 2006 and June 06, 2006.

As a result of this capital increase Brasilcel's holdings in us consisted of 89.3% of Vivo common shares, 47.5% of Vivo preferred shares and 62.8% of Vivo's total capital.

### Corporate Restructuring of Our Operating Subsidiaries

On October 31, 2006, our shareholders approved the merger of Telergipe, Telebahia, Telerj, Telest, CRT, TC, TCO, Telegoiás, Telemat, Telems, Teleron, Teleacre and NBT (each an Operating Subsidiary and collectively, the Operating Subsidiaries) into Vivo S.A. (formerly known as GT) (the Corporate Restructuring). TCO - IP S.A. remained a separate entity, as it is not an SMP operator.

The remaining rights of the former minority shareholders of TCO, Telegoiás, Telemat, Telems, Teleacre and Teleron survived the Corporate Restructuring of the Operating Subsidiaries as of November 1, 2006 and continue to exist under Vivo S.A.

Due to this Corporate Restructuring, the SMP and SCM services that were offered by the Operating Subsidiaries in their respective areas and regions, along with their clients and users, were transferred to Vivo S.A.

The Corporate Restructuring had no impact on Vivo's consolidated financial statements, capital stock or shareholders.

The benefits of this restructuring included, among others, increased organizational efficiency, a more effective management and streamlined administrative and commercial functions.

### Capital Expenditures

The primary focus of our capital expenditure program has been, and continues to be, the improvement of the capacity of the services we currently offer and the provision of new services as well as the development of information systems.

The following tables set forth our total capital expenditures for the companies and periods indicated:

Vivo	Year ended December 31,		
	2006(1)	2005(1)	2004(1)
	(in millions of reais)		
Switching equipment	375.9	523.0	582.1
Transmission equipment	844.4	862.8	623.8
Information technology	414.8	407.6	291.9
Others(2)	468.8	413.1	442.7
<b>Total capital expenditures</b>	<b>2,103.9</b>	<b>2,206.5</b>	<b>1,940.5</b>

Year ended December 31,

State of São Paulo Areas 1 and 2	2006(1)	2005(1)	2004(1)
	<i>(in millions of reais)</i>		
Switching equipment	121.3	216.2	175.9
Transmission equipment	304.7	309.7	172.8
Information Technology	351.5	360.4	251.5
Others(2)	167.4	120.9	160.7
Total capital expenditures	944.9	1,007.2	760.9

## Year ended December 31,

States of Rio de Janeiro and Espírito Santo

<u>Area 3</u>	2006(1)	2005(1)	2004(1)
	(in millions of reais)		
Switching equipment	65.0	90.2	90.6
Transmission equipment	164.1	112.8	64.8
Information technology	12.9	11.6	
Others(2)	90.3	82.5	86.1
Total capital expenditures	332.3	297.1	241.5

## Year ended December 31,

States of Paraná and Santa Catarina Area

<u>5</u>	2006(1)	2005(1)	2004(1)
	(in millions of reais)		
Switching equipment	30.5	25.4	47.5
Transmission equipment	70.8	123.2	124.5
Information Technology	10.6	6.4	15.7
Others(2)	45.3	30.9	27.9
Total capital expenditures	157.2	185.9	215.6

## Year ended December 31,

State of Rio Grande do Sul Area 6

	2006(1)	2005(1)	2004(1)
	(in millions of reais)		
Switching equipment	89.8	59.7	72.2
Transmission equipment	43.5	118.4	84.5
Information technology	8.0	4.2	
Others(2)	64.3	56.2	47.6
Total capital expenditures	205.6	238.5	204.3

## Year ended December 31,

Central Western and Northern regions Areas 7

<u>and 8</u>	2006(1)	2005(1)	2004(1)
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	<b>(in millions of reais)</b>		
Switching equipment	44.0	101.6	156.7
Transmission equipment	149.8	145.8	153.4
Information Technology	27.0	19.4	18.6
Others(2)	66.5	86.7	89.9
<b>Total capital expenditures</b>	<b>287.3</b>	<b>353.5</b>	<b>418.6</b>

	<b>Year ended December 31,</b>		
<u>States of Bahia and Sergipe Area 9</u>	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Switching equipment	25.3	29.9	39.2
Transmission equipment	111.5	52.9	23.8
Information technology	4.8	5.6	6.1
Others(2)	35.0	35.9	30.5
<b>Total capital expenditures</b>	<b>176.6</b>	<b>124.3</b>	<b>99.6</b>

(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

(2) Consisting primarily of free handset rentals, network construction, furniture and fixtures, office equipment and store layouts.

Our capital expenditure estimate for 2007 is approximately R\$1.7 billion, which includes investments in network expansion, introduction of products and services that aim at maximizing the use of cellular telephony, as well as seeking ways to constantly improve the quality of services provided to our customers.

We intend to fund these capital expenditures mostly with cash generated from operations. See Item 5.B. Operating and Financial Review and Prospects Liquidity and Capital Resources.

## **B. Business Overview**

According to data regarding market share published by ANATEL, we are among the leading providers of cellular telecommunications services in Brazil, with the help of our subsidiary Vivo S.A., the leading cellular operator in Brazil. Vivo S.A. is a cellular operator in the states of São Paulo, Paraná, Santa Catarina, Acre, Amazonas, Amapá, Distrito Federal, Goiás, Maranhão, Mato Grosso, Mato Grosso do Sul, Pará, Rondônia, Roraima, Tocantins, Bahia, Sergipe, Rio de Janeiro, Espírito Santo and Rio Grande do Sul.

In Areas 1 and 2, Vivo S.A. uses a frequency range known as A Band that covers 100% of the municipalities in its authorized areas in the state of São Paulo. At December 31, 2006, Vivo S.A. had 10.684 million cellular lines in service in these areas, which represented a 2.0% increase from December 31, 2005, and a market share of approximately 44.2% in São Paulo.

In Area 3, Vivo S.A. uses the Band A frequency range that covers 100% of the municipalities and 100% of the population in the states of Rio de Janeiro and Espírito Santo. At December 31, 2006, Vivo S.A. had 4.920 million cellular lines in service in this area, which represented a 3.8% net increase from December 31, 2005, and a market share of approximately 39.9% in those states.

In Area 5, Vivo S.A. uses a frequency range known as B Band that covers 60.0% of the municipalities in the states of Paraná and Santa Catarina and 93.0% of the population of Paraná and Santa Catarina. At December 31, 2006, Vivo S.A. had 2.570 million cellular lines in service in this area, which represented a 11.7% net decrease from December 31, 2005, and a market share of approximately 27.6% in those states.

In Area 6, Vivo S.A. uses the Band A frequency range that covers 70% of the municipalities and 96.0% of the population in the state of Rio Grande do Sul. At December 31, 2006, Vivo S.A. had 3.321 million cellular lines in service in this area, which represented a 1.9% net decrease from December 31, 2005, and a market share of approximately 43.8% in that state.

In Areas 7 and 8, Vivo S.A. is the leading cellular operator, by number of customers, in its authorization area and uses a frequency range known as A Band that covers 53.3% of the municipalities in the states of Acre, Distrito Federal, Goiás, Mato Grosso, Mato Grosso do Sul, Rondônia and Tocantins, which covers 90.2% of the population in these states, and also uses a frequency range known as B Band that covers 33.8% of the municipalities in the states of Amazonas, Amapá, Maranhão, Pará and Roraima, which covers 71.2% of the population of these states. At December 31, 2006, Vivo S.A. had 5.912 million cellular lines in service in these areas, which represented a 13.3% net decrease from December 31, 2005, and a market share of approximately 36.1% in those states.

In Area 9, Vivo S.A. uses the Band A frequency range that covers 45.0% of the municipalities and 78.0% of the population in the States of Bahia and Sergipe. At December 31, 2006, Vivo S.A. had 1.647 million cellular lines in service in this area, which represented a 11.5% net increase from December 31, 2005, and a market share of approximately 27.6% in those states.

## **Our Operations**

The following tables set forth information about Vivo S.A.'s cellular telecommunications base, coverage and related matters at the dates and for the years indicated.

**State of São Paulo Areas 1 and 2**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	10,684	10,476	9,232
Contract customers	1,803	1,779	1,603
Prepaid customers	8,881	8,696	7,629
Growth in cellular lines in service during year	2.0%	13.5%	23.2%
Churn(1)	28.6%	18.7%	18.9%
Estimated population of concession areas (in millions)(2)	40.6	39.7	39.1
Estimated covered population (in millions)(3)	40.6	39.7	38.5
Percentage of population covered(4)	100%	100%	98.5%
Penetration at year-end(5)	59.6%	53.0%	42.7%
Percentage of municipalities covered	100%	100%	79.6%
Market share(6)	44.2%	49.2%	55.2%

**States of Rio de Janeiro and Espírito Santo Area 3**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	4,920	4,740	4,376
Contract customers	1,343	1,476	1,259
Prepaid customers	3,577	3,264	3,117
Customer growth during the year	3.8%	8.3%	18.0%
Churn(1)	32.6%	29.5%	31.3%
Estimated population of Region at year-end (millions)(2)	19.1	18.8	18.6
Estimated covered population at year-end (millions)(3)	19.1	18.8	18.6
Percentage of population of Region covered at year-end(4)	100%	100%	100%
Penetration at year-end(5)	64.3%	58.8%	49.1%
Percentage of municipalities covered	100%	100%	100%
Market share(6)	39.9%	42.6%	47.7%

**States of Paraná and Santa Catarina Area 5**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	2,570	2,910	2,579
Contract customers	406	366	298
Prepaid customers	2,164	2,543	2,281
Growth in cellular lines in service during year	(11.7)%	12.8%	52.5%
Churn(1)	44.1%	20.0%	13.7%

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Estimated population of concession areas (in millions)(2)	16.5	16.1	15.9
Estimated covered population (in millions)(3)	15.2	14.9	14.0
Percentage of population covered(4)	93%	92.3%	88.0%
Penetration at year-end(5)	56.6%	51.4%	39.8%
Percentage of municipalities covered	60.0%	59.0%	42.3%
Market share(6)	27.6%	34.5%	41.3%

**State of Rio Grande do Sul Area 6**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	3,321	3,387	3,215
Contract customers	790	829	788



	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Prepaid customers	2,530	2,558	2,427
Growth in cellular lines in service during year	(2.0)%	5.3%	27.4%
Churn(1)	27.5%	21.7%	19.5%
Estimated population of concession areas (in millions)(2)	10.6	10.5	10.3
Estimated covered population (in millions)(3)	10.2	10.0	9.9
Percentage of population covered(4)	96%	96.0%	95.6%
Penetration at year-end(5)	71.3%	65.6%	55.2%
Percentage of municipalities covered	70.0%	69.9%	55.2%
Market share(6)	43.8%	48.3%	54.8%

**Central Western and Northern regions Areas 7 and 8**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	5,912	6,815	5,820
Contract customers	836	970	945
Prepaid customers	5,075	5,845	4,875
Growth in cellular lines in service during year	(13.3)%	17.1%	41.6%
Churn(1)	47.3%	19.2%	23.4%
Estimated population of concession areas (in millions)(2)	34.6	33.8	33.0
Estimated covered population (in millions)(3)	28.0	27.1	25.5
Percentage of population covered(4)	81.0%	80.4%	77.2%
Penetration at year-end(5)	47.3%	44.0%	34.8%
Percentage of municipalities covered	46.0%	44.7%	41.3%
Market share(6)	36.1%	45.5%	51.3%

**States of Bahia and Sergipe Area 9**

	<b>Year ended December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Cellular lines in service at year-end (in thousands)	1,647	1,477	1,320
Contract customers	331	323	292
Prepaid customers	1,316	1,154	1,028
Customer growth during the year	11.5%	11.9%	17.3%
Churn(1)	32.1%	33.6%	35.3%
Estimated population of region at year-end (million)(2)	16.0	15.8	15.6
Estimated covered population at year-end (million)(3)	12.4%	11.1%	10.8%
Percentage of population covered at year-end(4)	78.0%	70.3%	69.3%
Penetration at year-end(5)	38.6%	29.2%	19.9%

Percentage of municipalities covered	45.0%	33.1%	31.3%
Estimated market share(6)	26.6%	31.8%	42.3%

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- (1) Churn is the number of customers that leave us during the year, calculated as a percentage of the simple average of customers at the beginning and the end of the year.
- (2) Projections based on estimates of the *Instituto Brasileiro de Geografia e Estatística* (IBGE).
- (3) Number of people within our Region that can access our cellular telecommunications signal.
- (4) Percentage of the population in our Region that can access our cellular telecommunications signal.
- (5) Number of cellular lines in service in our Region, including those of our competitors, divided by the population of our Region.
- (6) Estimate based on all lines in service in our Region at year-end.

**Our Services**

We provide cellular telecommunications services using GSM/EDGE, CDMA and TDMA. Our network provides both CDMA digital service and AMPS, an analog service that we have substantially phased out. We provide cellular telecommunications services in the frequency of 850 MHz using digital technology CDMA/TDMA and analog technology AMPS, which has been substantially phased out. All our services are provided in the frequency of 850 MHz.

We provide voice and ancillary services, including voicemail and voicemail notification, call forwarding, three-way calling, caller identification, short messaging, limitation on the number of used minutes, cellular chat room, and data service such as wireless application protocol service through which clients can access WAP sites and portals. We offer direct access to the Internet through either PCMCIA cards (Personal Computer Memory Card International Association, an organization consisting of some 500 companies that has developed standardized small, credit card-sized devices, called PC Cards) designed to connect compatible PDAs (Personal Digital Assistant, a handheld device that combines computing, telephone/fax, Internet and networking features) and laptops or cellular phones by a cable connection that offers corporate subscribers secure access to their intranet and office resources. We also offer some new services like Multimedia Message Service and MExE (Mobile Execution Environment), which enables the wireless device to download applications and execute them on the mobile along with a user interface that contains icons on the wireless device to identify the main services (such as Voice Mail, Downloads and text messaging (SMS)) for easier access to our services.

In 2004, we launched:

Vivo Direto service this service allows users to make individual and group calls;

Vivo Encontra (LBS) a group of location based services, including Vivo Localiza, using GPSOne as a location technology, a service that allows users to locate each other;

Vivo Aqui Perto a city-guide application;

Vivo Agenda (Synchronized Agenda) this service allows users to back up their contact lists and to recover any information lost in case of robbery or loss;

Vivo em Ação an alternative-reality game that encourages the client to use different ancillary services;

Vivo Avisar makes the client aware of calls missed when their phone is unavailable;

Olho Vivo (video monitoring, launched in March 2004) was the first monitoring application in Brazil. Subscribers can see real-time images of a webcam connected to a PC through their personal mobiles at a rate of 4 frames per second;

TV no Celular (video streaming launched in October 2004) was the first application of streaming video in Brazil. Subscribers can see real-time audio and television images through their personal mobiles.

In 2005, we launched:

Vivo Play 3G a multimedia service that leverages the 3rd generation CDMA EV-DO network to provide users with downloading and streaming of video content as cartoons, news, soccer, adult content, weather forecasts and sitcoms exclusively created for mobile phones. The service also offers users the option to download full track music to

mobile phones;

Vivo Zap 3G a wireless broadband Internet access for computers and handhelds using PCMCIA cards or cell phones that achieves a high data transfer rate of up to 2.4 Mbps using the 3rd generation CDMA EV-DO network and gives users an experience similar to that achieved with wired broadband connections but with the advantage of mobility;

Smart Mail a Wireless PIM solution that enables real-time access for corporate e-mail service or personal e-mail accounts through a PDA providing on-line e-mail notifications and calendar or contact synchronization;

World Phone using the same wireless device and number, the World Phone allows Vivo subscribers to automatically roam over CDMA/GSM networks in more than 170 countries;

Instant Messenger the most popular Internet instant messenger application (MSN) available for Vivo wireless device through WAP; and

MMS Interoperability interoperability agreements established with six main mobile operators in Brazil that allows Vivo subscribers to send and receive multimedia messages from other operators subscribers.

In addition, in 2006 we launched:

Vivo Localiza Familia a location based service that allows children to be located and monitored by their parents via cellular phones or the internet;

Vivo Localiza Amigos a location based service that enables customers to locate their friends, as well as to be located by their friends, via the relevant address and a map of the region;

Vivo Co-Piloto a location based service that assists the user in moving from one point to another in several Brazilian cities, and that is offered in the form of a Brew application, which is an application development platform created by Qualcomm for mobile phones;

Vivo Bolão an interactive game that tests the user s knowledge of soccer;

Instant Messenger the most popular Internet instant messenger application (MSN), which is now made available for Vivo wireless devices through SMS;

Vivo ao Vivo - new interface for Vivo GSM terminals;

Vivo e Você na Copa exclusive CBF (Brazilian Soccer Confederation) content (including games, tones, wallpapers, videos and a voice portal) during the World Cup;

Vivo Chip - a service menu on GSM SIM Cards;

Vivo Flash a fixed-wireless connection to the internet; and

Vivo Torpedo E-Mail Corporate a service that transforms the cellular phone number into an email address, and enables users to receive every email sent to them as SMS .

Further, Vivo has improved its current product offerings, as follows:

TV no Celular (video streaming) now includes RTP (Radio e Televisão de Portugal) programming;

Vivo Play 3G now includes music content from Warner Music and Universal Music; and

Vivo Portal de Voz an exclusive reverse auction service with SBT (Sistema Brasileiro de Televisão).

We offer roaming services through agreements with local cellular service providers throughout Brazil and other countries that allow our subscribers to make and receive calls while out of our concession areas. We also provide reciprocal roaming services for subscribers of such other cellular service providers while they are in our concession areas.

**Our Region**

Vivo provides mobile telecommunications services on the A and B Band frequency in 19 Brazilian states in addition to Distrito Federal, which represents approximately 7.3 million square kilometers and 85.6% of the Brazilian territory. This area includes more than 138.8 million people, representing 73.8% of Brazil's population, and 212 municipalities with a population in excess of 100,000. The GDP of this area reached approximately 83.1% of Brazil's total GDP, as of December 2004.

The following tables set forth population, gross domestic product (GDP), and per capita income statistics for each state in our Region at the dates and for the years indicated:

Area	Frequency Range	At December 31, 2006		Last Available IBGE Data		
		Population (in thousands)(1)	Percent of Brazil's population (1)	GDP (in millions of reais)(2)(3)	Percent of Brazil's GDP(3)	Per capita income (in reais)(2)(3)
São Paulo state	A Band	41,361	22.0%	546,607	30.9%	13,725
Paraná state	B Band	10,450	5.6%	108,699	6.2%	10,725
Santa Catarina state	B Band	6,004	3.2%	70,208	4.0%	12,159
Goiás state	A Band	5,786	3.1%	41,316	2.3%	7,501
Tocantins state	A Band	1,346	0.7%	4,768	0.3%	3,776
Mato Grosso state	A Band	2,884	1.5%	27,935	1.6%	10,162
Mato Grosso do Sul state	A Band	2,315	1.2%	19,954	1.1%	8,945
Rondônia state	A Band	1,576	0.8%	9,744	0.6%	6,238
Acre state	A Band	690	0.4%	3,242	0.2%	5,143
Amapá state	B Band	626	0.3%	3,720	0.2%	6,796
Amazonas state	B Band	3,355	1.8%	35,889	2.0%	11,434
Maranhão state	B Band	6,225	3.3%	16,547	0.9%	2,748
Pará state	B Band	7,180	3.8%	34,196	1.9%	4,992
Roraima state	B Band	409	0.2%	1,864	0.1%	4,881
Federal District	A Band	2,409	1.3%	43,522	2.5%	19,071
Bahia state	A Band	14,017	7.5%	86,882	4.9%	6,350
	A Band	2,017	1.1%	13,121	0.7%	6,782

Sergipe state						
Rio de Janeiro state	A Band	15,650	8.3%	222,564	12.6%	14,639
Espírito Santo state	A Band	3,492	1.9%	34,488	2.0%	10,289
Rio Grande do Sul state	A Band	11,022	5.9%	142,874	8.1%	13,320
Vivo		138,814	73.8%	1,468,140	83.1%	10,210

Source: *Instituto Brasileiro de Geografia e Estatística* (IBGE)

(1) Estimates from IBGE for the year end 2006.

(2) According to the most recent IBGE data (2004).

(3) Nominal Brazilian GDP was R\$1,766,621 million as of December 2004 calculated by IBGE.

### Marketing and Sales

We closely follow the developments in the markets where we operate and constantly launch new promotions and advertising campaigns. A strong customer acquisition policy has been implemented across all of the company's operators through aggressive mass sales promotions and segmented actions. Efforts to acquire new customers for prepaid and postpaid services have mostly been made through joint promotions designed to increase intranet traffic and stimulate the use of data services.



With the premise of keeping a sustainable customer base, the acquisition promotions have also been open to current customers who wished to change their cell phones. We are actively involved in a high-value customer loyalty program by offering aggressive discounts on cell phones through direct marketing actions.

On December 31, 2006, Vivo possessed 307 sales outlets (94 in São Paulo, 50 in the states of Rio de Janeiro and Espírito Santo, 33 in the state of Rio Grande do Sul, 37 in the states of Paraná and Santa Catarina, 24 in the states of Bahia and Sergipe, and 69 in the states that make up the midwestern and northern regions of Brazil). It also has an efficient network of 7,837 authorized retail and resales dealerships. Consequently, Vivo has maintained its market leadership position, with a total of 8,144 points of sale.

Prepaid telephone card recharging was available at 322,863 locations, including our own stores, dealers, lottery shops, physical and online card distributors, and at smaller shops, drugstores, newspaper stands, book stores, bakeries, gas stations, bars and restaurants. Online recharging is also provided by several banks' websites.

### **Customer Service**

Vivo has continued its policy of outsourcing, keeping 100% of customer services in the hands of specialized companies, while maintaining full management control. These services are available 24 hours from our call center and our website.

#### ***Satisfaction evaluation***

Customer satisfaction is evaluated by regular satisfaction surveys. In the second half of 2006, 3,200 customers of Vivo and 2,200 customers of other non-affiliated companies were interviewed all over the country about customer assistance, products and services. Vivo's satisfaction mark was ranked 8.21 on a range from 1 to 10, with the market average being 8.27. Several actions have been taken in order to increase our customer satisfaction. For example, one of the most frequent complaints from our customers was related to billing. Therefore, every step of the billing process, from inside the call center to the back office, was reworked in order to speed up customer response time, to assure the quality of customer service, and to front-load the response process in order to increase the likelihood of first-call resolution (FCR).

One of the most important objectives of 2006 was to retain our customers by increasing their satisfaction when using our services. A new administrative structure was designed to better track our premium customers and suggest ways to improve retention.

#### ***Higher quality, with lower cost***

We implemented a strategy to increase the quality of our services while lowering costs. While achieving the best signal quality, surpassing all of our competitors (according to ANATEL's scoring system), we also improved the level of service of our customer care, generating greater customer satisfaction with our call centers and stores. We additionally take steps to reduce billing errors, leading to fewer claims against us. This strategy has been successful in increasing our satisfaction rating and in lowering costs.

### **Our Network**

Before November 1998, our network used only AMPS analog technology. After privatization, we began to use CDMA and TDMA digital technologies. In 2006, we began to implement a GSM Network. Digitalization offers certain advantages, such as greater network capacity and additional revenue through the sale of value-added services. We continue to increase network capacity and coverage to improve our quality of service and to meet customer

demand.

By December 31, 2006, Vivo S.A.'s telecommunications network in the state of São Paulo, which provides both CDMA digital and GSM digital services, covered 100% of the municipalities. Vivo S.A.'s network is connected primarily through a fiber-optic and radio transmission system of its own and as leased mainly from Telecomunicações de São Paulo S.A., or Telesp, and consists of cellular switches, base stations and other network elements such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, PDSN and

gateways. NEC do Brasil S.A., Nortel Networks Northern Telecom do Brasil, Motorola do Brasil Ltda., Lucent Technologies do Brasil, Ind. e Com. Ltda., Huawei do Brasil Telecomunicações Ltda. and Ericsson Telecomunicações S.A. are Vivo S.A.'s main suppliers in the state of São Paulo.

Vivo S.A. began its activities in the states of Parana and Santa Catarina ( Vivo PR/SC ) in December 1998 and, until 2005, offered services only through CDMA digital technology. As of December 31, 2006, the telecommunications network in PR/SC that provides both CDMA digital and GSM digital services covered 59.8% of the municipalities, or 92.6% of the population, in its region. The PR/SC network is primarily connected by a fiber-optic and radio transmission system of its own and as leased mainly from fixed operating companies (Brasil Telecom and Embratel) and Copel Companhia Paranaense de Energia S.A., and consists of cellular switches, base stations and other network elements, such as voicemail, prepaid service, Home Location Registers, Signaling Transfer Points and gateways. Motorola do Brasil Ltda., Huawei do Brasil Telecomunicações Ltda., Alcatel Telecomunicações S/A. and Ericsson Telecomunicações S.A. are Vivo S.A.'s main suppliers in PR/SC.

As of December 31, 2006, Vivo S.A. in the midwestern and northern regions ( CO/N ) provided CDMA Digital, GSM digital, TDMA digital and AMPS analog services, which have been substantially phased out, covering 45.8% of the municipalities, or 80.9% of the population in its region. Our network is connected primarily through a fiber-optic and radio transmission system of our own and leased from incumbent wire line companies and consists of cellular switches, base-stations and other network elements such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point and gateways. Nortel Networks Northern Telecom do Brasil, Motorola do Brasil Ltda. (presently Motorola Industrial Ltda. and Motorola Services Ltda.), Huawei do Brasil Telecomunicações Ltda. and Ericsson Telecomunicações are Vivo S.A.'s principal suppliers in CO/N.

As of December 31, 2006, the telecommunications network of Vivo S.A. in Bahia and Sergipe ( BA/SE ) covered 44.7% of the municipalities, or 77.6% of the population, of its region. Its network provides both CDMA digital, GSM digital and AMPS analog services, which have been substantially phased out. The network is connected primarily through a fiber-optic and radio transmission system of our own and leased mainly from Tele Norte Leste Participações S.A., or Telemar. It also includes cellular switches, base stations, and other communication devices such as voicemail, prepaid service, Short Message Service and Home Location Registers. NEC do Brasil S.A., Ericsson Telecomunicações S.A., Nortel Networks Northern Telecom do Brasil, Motorola Industrial Ltda., Motorola Services Ltda. and Lucent Technologies do Brasil, Ind. e Com. Ltda. are Vivo S.A.'s main suppliers in BA/SE.

As of December 31, 2006, the telecommunications network of Vivo S.A. in the states of Rio de Janeiro and Espírito Santo covered 100% of the municipalities in its area. Its network provides both CDMA digital, GSM digital and AMPS analog services, which have been substantially phased out. This network is connected primarily through a fiber-optic and radio transmission system of our own and leased mainly from the incumbent wire line companies, and consists of cellular switches, base stations and other communication devices such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, PDSN and gateways. NEC do Brasil S.A., Nortel Networks Northern Telecom do Brasil, Ericsson Telecomunicações S.A., Huawei do Brasil Telecomunicações Ltda. and Lucent Technologies do Brasil, Ind. e Com. Ltda. are Vivo S.A.'s principal suppliers in these states.

As of December 31, 2006, Vivo S.A.'s network in the state of Rio Grande do Sul ( RS ) provides CDMA, GSM digital and TDMA digital and AMPS analog services, which have been substantially phased out, covering 70.1% of the municipalities, or 96.0% of the population, of this region. The RS network is connected primarily through a fiber-optic and radio transmission system of our own and leased mainly from Brasil Telecom, and consists of cellular switches, base stations and other communication devices such as voicemail, prepaid service, Short Message Service, Home Location Registers and gateways. Nortel Networks Northern Telecom do Brasil, Huawei do Brasil Telecomunicações Ltda., and Ericsson Telecomunicações S.A. are Vivo S.A.'s principal suppliers in RS.

Our advanced network management technology ensures global management and supervision of all our network processes and network performance. The network management centers are located in São Paulo and Brasília. The network management center of São Paulo monitors the critical network operational parameters of São Paulo, Paraná, Santa Catarina and Rio Grande do Sul. The network management center in Brasília monitors the critical network

operational parameters in CO/N, Rio de Janeiro, Espirito Santo, Bahia and Sergipe. These centers are able to identify abnormalities in both our network and in third parties' networks, using failure and signaling monitoring systems. In addition, quality and service standards are constantly monitored. The network management centers are integrated with maintenance and operations teams that maintain and operate cellular network elements, as well as cellular infrastructure and transmission, in addition to the radio network elements and computing bases, service platforms and communications backbones.

Our network is prepared to provide continuity of service for our customers in the event of network interruptions. We have developed contingency plans for potential catastrophes in our switching centers, power supply interruptions and security breaches.

We are obligated to meet certain requirements for service quality and annual network expansion. See Regulation of the Brazilian Telecommunications Industry Obligations of Telecommunications Companies. We have already achieved all of our required network expansion obligations for 2006.

### Sources of Revenue

We generate revenue from:

- usage charges, which include measured service charges for calls, monthly subscription charges and other similar charges;
- interconnection charges (or network usage charges), which are amounts we charge other cellular and fixed-line service providers for the use of our network;
- the sale of wireless devices and accessories; and
- other charges, including charges for call forwarding, call waiting, text messaging (SMS), call blocking and Data Services, such as WAP, downloads and MMS services, which are charged only when the customer's plan does not include these services.

Our rates are subject to approval by ANATEL. See Regulation of the Brazilian Telecommunications Industry.

The table below sets forth total net operating revenues in each of our operating subsidiaries for the last three years.

### Vivo

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	7,243.9	7,399.0	6,377.8
Sales of wireless devices and accessories	2,742.6	3,051.7	2,984.6
Interconnection	4,338.1	4,304.4	4,590.9
Other	1,130.1	1,005.3	767.7
Total gross operating revenue	15,454.7	15,760.4	14,721.0

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Value-added and other indirect taxes	(3,094.1)	(3,157.7)	(2,756.1)
Sales and services discount and return of goods sold	(1,423.9)	(1,348.9)	(1,035.5)
Net operating revenues (2)	10,936.7	11,253.8	10,929.4

**State of São Paulo Areas 1 and 2**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	2,568.8	2,545.9	2,342.9
Sales of wireless devices and accessories	1,029.3	1,243.7	1,209.5
Interconnection	1,813.5	1,841.1	1,913.7
Other	401.7	348.6	315.9
<b>Total gross operating revenue</b>	<b>5,813.3</b>	<b>5,979.3</b>	<b>5,782.0</b>
Value-added and other indirect taxes	(1,012.2)	(1,054.1)	(986.2)
Sales and services discount and return of goods sold	(560.2)	(544.2)	(466.8)
<b>Net operating revenues</b>	<b>4,240.9</b>	<b>4,381.0</b>	<b>4,329.0</b>

**States of Rio de Janeiro and Espírito Santo Area 3**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	1,621.8	1,541.8	1,257.7
Sales of wireless devices and accessories	545.7	626.4	584.1
Interconnection charges	805.4	734.3	792.5
Other	186.3	137.7	69.5
<b>Total gross operating revenue</b>	<b>3,159.2</b>	<b>3,040.2</b>	<b>2,703.8</b>
Value-added and other indirect taxes	(693.1)	(667.8)	(553.3)
Discounts granted and return of goods	(275.6)	(294.5)	(223.3)
<b>Net operating revenues</b>	<b>2,190.5</b>	<b>2,077.9</b>	<b>1,927.2</b>

**States of Paraná and Santa Catarina Area 5**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>

	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	434.3	459.1	347.9
Sales of wireless devices and accessories	210.6	220.8	257.1
Interconnection	310.9	321.5	356.2
Other	115.8	102.6	62.7
 Total gross operating revenue	 1,071.6	 1,104.0	 1,023.9
Value-added and other indirect taxes	(198.5)	(207.2)	(179.4)
Sales and services discount and return of goods sold	(91.9)	(76.2)	(43.0)
 Net operating revenues	 781.2	 820.6	 801.5



**State of Rio Grande do Sul Area 6**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	823.3	886.4	688.9
Sales of wireless devices and accessories	209.1	246.2	291.7
Interconnection charges	395.3	406.3	453.9
Other	137.8	139.4	117.6
<b>Total gross operating revenue</b>	<b>1,565.5</b>	<b>1,678.3</b>	<b>1,552.1</b>
Value-added and other indirect taxes	(364.9)	(387.3)	(287.6)
Discounts granted and return of goods	(95.9)	(108.6)	(90.2)
<b>Net operating revenues</b>	<b>1,104.7</b>	<b>1,182.4</b>	<b>1,174.3</b>

**Central Western and Northern regions Areas 7 and 8**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>
	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	1,460.2	1,625.4	1,420.7
Sales of wireless devices and accessories	570.8	521.0	486.8
Interconnection	791.9	797.6	872.1
Other	224.7	227.6	170.1
<b>Total gross operating revenue</b>	<b>3,047.6</b>	<b>3,171.6</b>	<b>2,949.7</b>
Value-added and other indirect taxes	(652.7)	(681.9)	(610.8)
Sales and services discount and return of goods sold	(303.7)	(218.3)	(128.5)
<b>Net operating revenues</b>	<b>2,091.2</b>	<b>2,271.4</b>	<b>2,210.4</b>

**States of Bahia and Sergipe Area 9**

	<b>Year ended December 31,</b>		
	<b>2006(1)</b>	<b>2005(1)</b>	<b>2004(1)</b>

	<b>(in millions of reais)</b>		
Usage and additional charges and monthly subscription charges	394.4	381.7	319.7
Sales of wireless devices and accessories	177.1	193.6	155.4
Interconnection charges	221.1	203.6	202.5
Other	63.8	49.4	31.9
Total gross operating revenue	856.4	828.3	709.5
Value-added and other indirect taxes	(172.7)	(159.4)	(138.8)
Discounts granted and return of goods	(96.6)	(107.1)	(83.7)
Net operating revenues	587.1	561.8	487.0

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(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

(2) Includes the following amounts that have been eliminated upon consolidation and combination of financial statements:

**Vivo Intercompany net operating revenues**

	Year ended December 31,		
	2006(1)	2005(1)	2004(1)
	<b>(in millions of reais)</b>		
Net operating revenues	(58.9)	(41.3)	na

***Contract Customers***

Since October 1994, cellular telecommunications service in Brazil has been offered on a calling party pays basis, under which customers pay only for calls that they originate. In addition, customers pay roaming charges on calls made or received outside their home registration area.

Customer charges are calculated based on the customer's calling plan, the location of the party called, the place from which the call originates and certain other factors, as described below. Our Region is divided into areas designated for payment purposes, called registration areas, as follows:

- Areas 1 & 2 9 areas in the state of São Paulo.
- Areas 7 & 8 18 areas, comprised of 9 areas in Brasilia and the states of Goiás, Mato Grosso do Sul, Mato Grosso, Rondônia, Acre and Tocantins and 9 areas in the states of Amapá, Amazonas, Maranhão, Pará and Roraima (TCO's B Band subsidiary NBT).
- Area 5 9 areas, comprised of 6 areas in the state of Paraná and 3 areas in the state of Santa Catarina.
- Area 9 6 areas, comprised of 5 areas in the state of Bahia and 1 area in the state of Sergipe.
- Area 3 5 areas, comprised of 1 area in the metropolitan area of Rio de Janeiro, two areas in upstate Rio de Janeiro and two areas in the state of Espírito Santo.
- Area 6 4 areas in the state of Rio Grande do Sul.

***Interconnection Charges***

We earn revenue from any call that originates from another cellular or fixed-line service provider network connecting one of our customers. We charge the service provider from whose network the call originates a network usage charge for every minute that our network is used in connection with the call. See Business Overview Operating Agreements Interconnection Agreements. Tariff increases are subject to ANATEL's review and approval.

***Bill and Keep***

ANATEL adopted partial Bill & Keep rules for interconnection charges in July 2003. The rules provided that an SMP operator paid for the use of another SMP operator's network in the same registration area only if the traffic

carried from the first operator to the second exceeded 55% of the total traffic exchanged between them. In that case, only those calls that surpassed the 55% level were subject to payment for network usage. Under Resolution 438 published in 2006, ANATEL eliminated the rule of the partial bill and keep. The current rule is full billing, in which the SMP operator pays the entire call termination fee of the other mobile network. The rule of the partial Bill & Keep was maintained between SMP and SME (trunking) networks.

***Roaming Fees***

We receive revenue pursuant to roaming agreements with other cellular service providers. When a customer of another cellular service provider makes a call within our area, that service provider pays us for the call at the applicable rate. Conversely, when one of our customers makes a cellular call outside of our Region, we must pay the

charges associated with that call to the cellular service provider in whose Region the call originates. See [Operating Agreements](#) [Roaming Agreements](#).

### ***Wireless Device Sales***

We sell only CDMA dual-mode (800MHz CDMA-1xRTT/AMPS and 800MHz CDMA/AMPS), GSM and tri-mode (800/1900 CDMA and 800MHz AMPS), and dual technology (CDMA and GSM) cellular wireless devices and data devices in CDMA EVDO technology (PCMCIA, USB and deskmodem) through our own stores and dealers. We have overlaid our TDMA network with a CDMA network and we have stopped selling TDMA handsets. Although we still have some customers using analog service (approximately 0.1% of our total customer base as of December 31, 2006), we have implemented a series of actions, such as providing discounts on digital wireless devices, discounts on monthly fees for digital services, digital wireless device rentals and free wireless devices, to encourage analog and TDMA customers to transfer to CDMA service. Our current suppliers for wireless devices are Motorola, LG, Samsung, Nokia, Pantech, SonyEricsson, BenQ-Siemens, Aiko and Kyocera.

### **Operating Agreements**

We have agreements with major fixed-line and mobile operators in Brazil in order to lease physical space, real estate, air conditioning, energy, security and cleaning services. We also lease transmission capacity necessary to complete the construction of our network infrastructure.

### ***Interconnection Agreements***

The terms of our interconnection agreements include provisions with respect to the number of connection points and traffic signals. See [Regulation of the Brazilian Telecommunications Industry](#) [Obligations of Telecommunications Companies](#) and [Regulation of the Brazilian Telecommunications Industry](#) [Interconnection](#).

We believe that our subsidiary has adequate interconnection agreements with necessary fixed-line operators in order to provide services. We also believe that our subsidiary has all the necessary interconnection agreements with long-distance carriers.

### ***Roaming Agreements***

We are a member of the Brazilian Roaming Association (the [Association](#) ), a group composed of all companies providing cellular services in Brazil. The Association was created to standardize roaming services in Brazil and elsewhere. The roaming agreements require us and the other cellular service providers to provide service to roaming customers on the same basis that each member provides to its own customers, and to carry out a monthly reconciliation of roaming customer usage charges.

We offer CDMA automatic international roaming in the United States, Argentina, Uruguay, Chile, Canada, China, Mexico, Venezuela, Porto Rico, New Zealand, Dominican Republic and South Korea. We have provided international GSM services through third-party partners using GSM wireless devices in most parts of Europe, Africa, the Americas, Asia and Oceania.

### **Taxes on Telecommunications Services and Wireless Device Sales**

The cost of telecommunications services and wireless device sales to customers incorporates a variety of taxes, including:

- **ICMS** (*Imposto sobre Circulação de Mercadorias e Serviços*) is a state tax imposed at varying rates, from 7% to 35% on certain revenues from the sale of goods and services, including telecommunications services.
- **COFINS** (*Contribuição para Financiamento da Seguridade Social*) is a federal social contribution tax imposed on the gross operating revenue less discounts and returns. In December 2003, Law No. 10,833 was enacted, making such contribution noncumulative and increasing the rate from 3.0% to 7.60%, except in connection with telecommunication services, where the rate continues to be 3.0%.

- **PIS** (*Programa de Integração Social*) is a federal social contribution tax which corresponds to 1.65% of the gross operating revenue less discounts and returns, except in connection with telecommunication services, where the rate is 0.65%.
- **FUST** (*Fundo de Universalização dos Serviços de Telecomunicações*) is a federal social contribution which corresponds to 1% of the net revenue generated by telecommunications services (other than interconnection charges). The purpose of the FUST is to fund a portion of the costs incurred by telecommunication service providers to meet the universal service targets required by ANATEL, in case the service providers are unable to fund, in whole or in part, such costs.
- **FUNTTEL** (*Fundo para Desenvolvimento Tecnológico das Telecomunicações*) is a federal social contribution which corresponds to 0.5% of the net revenue generated by telecommunications services (other than interconnection charges). The purpose of FUNTTEL is to promote the development of telecommunications technology in Brazil and to improve competition.
- **FISTEL** (*Fundo de Fiscalização das Telecomunicações*) is a federal tax applicable to telecommunications transmission equipment. The purpose of FISTEL is to provide financial resources for the Brazilian federal government to control and inspect the industry. This tax is divided in two parts: *Taxa de Fiscalização de Funcionamento* and *Taxa de Fiscalização de Instalação*. *Taxa de Fiscalização de Funcionamento* is based on the total number of customers and radio stations at the end of the previous fiscal year. *Taxa de Fiscalização de Instalação* is based on (i) the net monthly additions (new customers less churn) and (ii) the movement of radio stations.

## Billing

Vivo uses Atlys, a billing solution that combines software and hardware resources, from the supplier company Convergys as the billing system for centralized postpaid invoicing in the city of São Paulo. The billing system operates via a batch processing concept using Vivo customers' voice and data traffic. This system functions by segregating voice and data traffic on a daily basis, according to which of seven total billing preferences a customer elects. Each cycle has a specific due date for each of the consumer and corporate segments.

For prepaid services, Vivo uses the Next Generation Intelligence Network (NGIN) platform, a prepaid platform, from the supplier company PTI, which also works in a centralized way in the city of São Paulo. In order for the NGIN platform to process correctly, the same system for postpaid invoicing is used. This system separates the module for customer information, called Care, which is a services platform, from the Voice and Data traffic processing module used, called Core, which is a tariff platform.

During 2006, the RJ/ES and CO/N centralization billing (postpaid and prepaid) were completed. The BA/SE centralization process was completed in April 1, 2007.

## Cobilling

ANATEL has defined the obligations surrounding cobilling service for long distance carriers in the Brazilian market, which has made possible collecting all types of calls and services in the postpaid in one telephone account. Similarly, it defined the basic rules for mobile companies' prepaid services, making national and international long-distance calls possible within this segment. Mobile companies charge long-distance operators for the services given for both segments (prepaid and postpaid). The settlement collection, where the physical and financial data are

provided, occurs monthly. Mobile companies only pass to the long-distance carriers the fees collected from the customer's postpaid segment and debited from the customer's prepaid segment. ANATEL authorizes the customer to select whichever cobilling service provider it prefers for its individual calls, whereas neither the mobile company nor the long distance carrier has discretion in this area.



## Value Added Services (VAS)

Entertainment, information and online interactivity services are available to all Vivo customers through agreements with content suppliers. These agreements are based on a revenue-sharing model through the processes of postpaid and prepaid categories, with all divergences between these categories being demonstrated to the content suppliers.

## Collection

We have a uniform policy dealing with accounts of postpaid customer in default according to its segment. If the payment is more than 15 days late, service is partially suspended, and if payment is more than 40 days late, service is fully suspended until payment is made. We offer an installment payment plan for those with past due balances. However, if accounts are not paid after 90 days, the contract is cancelled and reported to Serasa, a credit bureau. After 105 days of default, accounts are directed to independent agencies for collection and the Consumer Protection Service.

All payments that are over 90 days late are considered either bad debt or written off. We account for late payments in accordance with Brazilian Legislation, which permits a bad debt write-off for late payments of R\$0 to R\$5,000 if they are over 180 days late or R\$5,001 to R\$30,000 if they are over 365 days late. Write-offs of late payments of over R\$30,001 that are open for more than 365 days require the commencement of a lawsuit.

## Fraud Detection and Prevention

In 2006, we led a campaign against subscription and cloning fraud. Cloning is a fraud that consists of duplicating the cellular signal of a bona fide customer, enabling the perpetrator of the fraud to make calls using the customer's signal. We also implemented significant procedures to detect, prevent and reduce subscription fraud.

Subscription fraud occurs when a person, typically using false or stolen documents, obtains cellular telecommunications service, and then incurs substantial charges that are billed to a customer who does not exist or who did not request the service.

In December 2006, our campaign against these two types of fraud was conducted through specific projects and the authentication of our cell phone base, which resulted in a 95.0% decrease in the total number of cloning fraud cases from December 2005 and a 19.0% decrease in the total number of subscription fraud cases from December 2005.

With the assistance of various officers and the Committee for the Campaign against Fraud and Cloning, created in January 2006, we were able to significantly reduce the number of fraud and cloning occurrences. Our initiatives focused on authenticating our wireless network and the cell phone bases.

## Competition

We face intense competition in all the areas in which we operate, principally from other cellular service providers and also from fixed-line operators. Many of these competitors are part of a large, national or multinational group and therefore have access to financing, new technologies and other benefits that are derived from being a part of such a group. Fixed-line operators generally charge much lower tariffs than cellular service providers.

Our principal cellular competitor in the state of São Paulo is Claro. The main fixed-line operator in this area is *Telecomunicações de São Paulo S.A. Telesp*, known as *Telefónica*.

Our principal cellular competitor in the states of Paraná and Santa Catarina is *Tele Celular Sul Participações S.A.*, or *TIM Sul*. The main fixed-line operator in this area is Brasil Telecom S.A.

Our principal cellular competitors are: Claro, in the region encompassing the states of Mato Grosso do Sul, Mato Grosso, Goiás, Tocantins, Rondônia and Acre and the Federal District, and *TIM*, in the region encompassing the states of Amazonas, Roraima, Pará, Amapá and Maranhão. The main fixed-line operators in this area are: Brasil Telecom S.A., in the region encompassing the states of Mato Grosso do Sul, Mato Grosso, Goiás, Tocantins,

Rondônia and Acre and the Federal District, and *Telemar Norte Leste S.A.* *Telemar*, in the region encompassing the states of Amazonas, Roraima, Pará, Amapá and Maranhão. Other competitors are Oi (Telemar mobile operator) and TIM.

In the Salvador and Sergipe service areas, our principal cellular competitor is Oi (TNL PCS S.A.). Other cellular competitors are TIM (Maxitel S.A.), which also operates in the state of Minas Gerais, and Claro (Stemar Telecomunicações Ltda.). The principal fixed-line competitor in this area is Telemar Norte Leste S.A.

In the Rio de Janeiro and Espírito Santo service areas, our principal cellular competitor is Claro, which operates in the states of Rio de Janeiro and Espírito Santo. Claro is controlled by a consortium led by the Telecom Américas Ltd. (controlled by América Móvil S.A. de C.V.). Claro began providing cellular telecommunications services in this Region at the end of 1998. The rights and obligations under Claro's license are substantially identical to our rights and obligations. Although Claro provides only digital service, its customers use TDMA dual mode cellular handsets that can operate on an analog network and GSM handsets. The principal fixed-line operator in this area is Telemar Norte Leste S.A. Oi is the third competitor and is integrated with Telemar (a fixed-line operator).

In Rio Grande do Sul, our principal cellular competitor is Claro, which operates in several regions in Brazil, including Celular CRT's region. Other cellular competitors are Brasil Telecom S.A. and TIM. The main fixed-line competitor in this area is Brasil Telecom.

We also compete with certain other wireless telecommunications services in specific segments, such as mobile radio (including digital trunking technology, offered by Nextel), paging and beeper services, which are used by some operators in our areas as a substitute for cellular telecommunications services. These competing wireless telecommunications services are generally less expensive than mobile telecommunications services.

Satellite-operated services, which provide nationwide coverage, are also available in Brazil. Although these services have the advantage of covering much larger areas than those covered by the cellular telecommunications services, they are considerably more expensive than the cellular telecommunications services we offer and do not provide competitive coverage inside buildings.

There can be no assurances that the entry of new competitors will not have significant adverse effects on our business, financial condition, or the results of our operations or prospects. Any adverse effects on our market share, which results from pressures originating from competition, will depend on several factors that cannot be assessed with precision and which are therefore beyond our control. Among such factors are the identity of the competitors, their strategy and ability to conduct business, market conditions prevailing at the time, rules applicable to the new market participants and to us, as well as the effectiveness of our efforts to prepare for and face competition. There may also be competitors with higher technical capacity and more resources than we have.

## **Regulation of the Brazilian Telecommunications Industry**

### ***General***

Our business, the services we provide, and the prices we charge are subject to regulation under the General Telecommunications Law and various administrative enactments, which regulate the services provided by Brazilian telecommunications operators.

ANATEL is the agency that regulates telecommunications under the General Telecommunications Law and the July 2001 Regulamento da Agência Nacional de Telecomunicações, known as the ANATEL Decree. ANATEL is financially and administratively independent of the Brazilian government. However, ANATEL maintains a close

relationship with the Ministry of Communications. Any regulation proposed by ANATEL is subject to a period of public comment, which may include a public hearing. ANATEL's actions can be challenged in the Brazilian courts. On November 25, 1998, ANATEL enacted Resolution 73 Regulation of Telecommunication Services, which explains in detail the new comprehensive regulatory framework for the provision of telecommunications services in Brazil established by the General Telecommunications Law.

### ***Concessions and Authorizations***

Before January 2000, ANATEL had only authorized two mobile service providers in each of the ten franchise areas under A Band and B Band. A Band and B Band mobile service providers were granted concessions pursuant to the *Lei Mínima*, or the Minimum Law. Each concession is a specific grant of authority to supply cellular telecommunications services, subject to certain requirements contained in the applicable list of obligations appended to each concession. If a mobile service provider wishes to offer any telecommunications services other than those authorized by its concession, it may apply to ANATEL for an authorization to offer such other services.

In accordance with the General Telecommunications Law, a concession relates to the provision of telecommunication services under the public regime, as determined by the public administration. A concession may only be granted upon a prior auction bidding process. As a result, regulatory provisions are included in the relevant concession agreements and the concessionaire is subject to public service principles of continuity, changeability and equal treatment of customers. In addition, ANATEL is empowered to direct and control the performance of the services, to apply penalties and to declare the expiration of the concession and the return of assets of the concessionaire to the government authority upon termination of the concession. Another distinctive feature is the right of the concessionaire to maintain certain economic and financial standards. The concession is granted for a fixed period of time and is generally renewable only once.

An authorization is a permission granted by the public administration under the private regime, which may or may not be granted upon a prior auction bidding process, to the extent that the authorized party complies with the objective and subjective conditions deemed necessary for the rendering of the relevant type of telecommunication service in the private regime. The authorization is granted for an indeterminate period of time. Under an authorization, the government does not guarantee to the authorized company the economic-financial equilibrium, as is the case under concessions.

### ***SMP Regulation***

In November 2000, ANATEL adopted certain regulations for the issuance of new licenses, which are authorizations to provide wireless communication services through SMP, personal mobile service, to compete with the then existing cellular operators in the various regions of Brazil. These regulations divided Brazil into three main regions covering the same geographic area as the concessions for the fixed-line telecommunication services. ANATEL organized auctions for three new licenses for each of those regions. The new licenses provided that the new services would be operated in the 1,800 MHz radio frequency bands, and were denominated C Band, D Band and E Band. These new licenses were auctioned by ANATEL and awarded during the first quarter of 2001, at the end of 2002, in September of 2004 and in March of 2006.

Under these new licenses:

- services are to be provided using the 1,800 MHz frequency;
- each operator may optionally provide domestic and international long-distance services in its licensed area;
- existing cellular service providers, as long as they do not have partnerships with fixed-line operators, as well as new entrants into the Brazilian telecommunications market can bid for C Band, D Band and E Band licenses. However, fixed-line operators, their controlling shareholders and affiliated cellular providers can only bid for D Band and E Band licenses;

- a cellular operator, or its respective controlling shareholders, may not have geographical overlap between licenses; and
- current A Band and B Band cellular service providers can apply for an extra frequency range.

Pursuant to the SMP services regulation each of the three main regions is divided into registration areas, or tariff areas.

On February 3, 2003, TCO replaced its SMC Concession Contracts for Personal Mobile Service Agreements (*Termos de Autorização do Serviço Móvel Pessoal*, or SMP) in Regions I (sub-range of B frequencies) and II (subrange of A frequencies) of the General Granting Plan (*Plano Geral de Outorgas*, or PGO). On July 27, 2006, ANATEL published Act 59867 authorizing the incorporation of TCO, Teleacre, Telegoiás, Teleron, Telems, Telemat, NBT, Telerj, Telest, Telebahia, Telergipe, Celular CRT and TC by GT, as well as the transfer of the respective SMP service authorization titles and of the SMP radio-frequency rights-of-use titles. Act 59867 also provides for the automatic termination of the authorizations for Multimedia Communication Services (*Serviços de Comunicação Multimídia*, or SCM) of TCO, Teleacre, Telegoiás, Teleron, Telems, Telemat, NBT, Telerj, Telest, Telebahia, Telergipe, Celular CRT and TC, upon each of their respective incorporations.

In order to transfer our services to SMP, we were required to comply with several technical and operational conditions, including, among other things, the adoption of a carrier selection code for long-distance calls originating from our network. Under the General Telecommunications Law, all mobile telecommunications service providers must provide interconnection upon the request of any other mobile or fixed-line telecommunications service provider. Until June 30, 2004, SMP service providers could opt to establish a price cap or freely negotiate their interconnection charges. The conditions of the network usage fee negotiation are regulated by ANATEL. Thereafter, the terms and conditions of the interconnection have been freely negotiated between wireless and fixed-line operators, effective as of 2005, subject to compliance with regulations established by ANATEL. ANATEL submitted to public consultation new regulations on interconnection rules. ANATEL promulgated the following regulations on interconnection rules: the new General Regulation of Interconnection ( *Regulamento Geral de Interconexão* Resolution number 410/2005, or RGI ); the Regulation of Separation and Allocation of Costs (Resolution number 396/2005); the Regulation of Industrial Exploration of Dedicated Lines ( *Exploração Industrial de Linha Dedicada* Resolution number 402/2005, or EILD ) and the new Regulation of Remuneration of Use of SMP Providers Networks (Resolution number 438/2006).

ANATEL's Public Consultation number 642 of 2005 relates to alterations in the regulation of SMP. While counter-arguments thereunder must have been sent to ANATEL before January 16, 2006, none have been made. In the proposed regulation, ANATEL notes areas of vital importance for mobile business, such as the necessity for retail stores in the cities within an operator's coverage areas, increases in the validity periods of prepaid cards, an extension of the period for blocking use by insolvent customers and limits on the period of time after which customers may leave service plans. We have presented our arguments to ANATEL against proposals that may have adverse effects on our business. If these new regulations take effect, they may have an adverse effect on our revenues and results of operations.

If the parties cannot reach an agreement on the terms of interconnection, including with respect to the interconnection tariff, ANATEL will act as the final arbiter. Because ANATEL considers us to be affiliated with Telefónica, which already provides wireline long-distance services in the state of São Paulo and was awarded a license to provide these services nationwide, ANATEL will not award a wireline long-distance license to us. Though we and other mobile operators have requested that ANATEL revise the current SMP regime, there can be no assurance it will do so. Under the SMP regime, we will receive revenues from interconnection fees paid to us by wireline long-distance operators due to long-distance traffic originating and terminating on our network.

The authorizations consist of two licenses – one to provide mobile telecommunications services, and another to use the frequency spectrum for a period of 15 years. The frequency license is renewable for another 15-year period upon the payment of an additional license fee.

The new SMP licenses include the right to provide cellular services for an unlimited period of time but restrict the right to use the spectrum according to the schedules listed in the old licenses Celular CRT until 2022 (renewed in 2006, only once, for a fifteen-year period); Telerj until 2020 (renewed in 2005, only once, for a fifteen-year period); Telest until 2008; Telebahia and Telergipe until 2008; TC until 2008 or 2009 (for the cities of Ribeirão Preto and

Guatapar); GT until 2013, TCO until 2021 (for Brazil's Federal District, renewed in 2006, only once, for a fifteen-year period); Teleacre, Teleron, Telemat and Telems until 2009; Telegoias until 2008; and NBT until 2013). Spectrum rights may be renewed only once for a fifteen-year period.



### ***Obligations of Telecommunications Companies***

As a telecommunications service provider, we are subject to regulations concerning quality of service and network expansion, as established in our authorizations and our original concession agreements.

Any breach by the companies of telecommunications legislation or of any obligation set forth in their authorizations may result in a fine of up to R\$50 million.

The mobile service authorizations of TC, GT, TCO, Telegoiás, Telemat, Telems, Teleron, Teleacre, NBT, Telebahia, Telergipe, Telerj, Telest and Celular CRT involve obligations to meet some quality of service standards such as the system's ability to make and receive calls, call failure rates, the network's capacity to handle peak periods, failed interconnection of calls and customer complaints. ANATEL published the method for collecting these quality service standards data on April 23, 2003 (ANATEL Resolution No. 335/03).

### ***Interconnection***

Under the General Telecommunications Law, telecommunications service providers are classified as providers of either collective or restricted services. All cellular operators, including SMP service providers, are classified by ANATEL as collective service providers. All providers of collective services are required to provide interconnection upon request to any other collective service provider. The terms and conditions of interconnection are freely negotiated between parties, subject to price caps and other rules established by ANATEL. Providers must enter into interconnection agreements, regarding, among other things, tariffs, commercial conditions and technical issues, with all requesting parties on a non-discriminatory basis. If the parties cannot agree upon the terms and conditions of interconnection, ANATEL may determine terms and conditions by arbitration.

Starting in 2005, in order to have a more homogeneous system and to accelerate the negotiations of interconnection contracts, ANATEL required a standard interconnection network from STFC and SMP Operators through an offer made publicly and equitably.

Interconnection agreements must be approved by ANATEL and may be rejected if they are contrary to the principles of free competition and the applicable regulations.

### ***Rate Regulation***

With respect to our Basic Plan and certain roaming charges incurred in connection with alternative service plans, our authorizations continue to provide for a price cap mechanism to set and adjust rates on an annual basis. The cap is the value with the rate of inflation deducted from the productivity estimated by ANATEL. The price cap is revised annually to reflect the rate of inflation as measured by the IGP DI. However, mobile operators are able to freely set the rates for alternative service plans.

The initial price cap agreed to by ANATEL and us in our authorizations had been based on the previously existing or bidding prices, and was adjusted annually on the basis of a formula contained in our authorizations. The price cap has been revised to reflect the rate of inflation as measured by the IGP DI.

Other telecommunications companies that interconnect with and use our network must pay certain fees, primarily an interconnection fee. The interconnection fee is a flat fee charged per minute of use. The interconnection fee charged by us and other A and B Band service providers was subject to a price cap stipulated by ANATEL. This price cap was valid until June 30, 2004 and, thereafter, the terms and conditions of the interconnection are freely negotiated among the operators, effective as of 2005, subject to ANATEL regulations. In 2005, ANATEL began permitting free

negotiations for mobile interconnection, or VU-M, fees and by July 2005, local-fixed concessionaires and mobile operators had reached a provisional agreement with respect to VU-M fees for local calls, or VC-1 (the agreement guaranteed a 4.5% increase in fees). ANATEL approved that provisional agreement, and in March 2006, approved another provisional agreement for VU-M fees for long-distance calls, VC-2, VC-3 and international, among the same operators that made the VC-1 agreement. ANATEL is currently studying a new model to determine values of reference of remuneration for use of mobile networks RVU-M of SMP providers having significant market power, which will be used in the case of arbitration by ANATEL of the value of VU-M, and is expected to be

completed by mid-2007. In 2006 the free negotiation of the mobile call termination fees that was started in 2005 (VU-M) was maintained, although ANATEL did not accept the new agreements proposed by mobile and fixed operators. Therefore the provisional agreement between the local fixed concessionaires and the mobile operators reached in 2005 is still in effect, while new attempts at negotiation are in progress. See [SMP Regulation](#) for more information on the status of this agreement.

### ***Internet and Related Services in Brazil***

In Brazil, Internet service providers, or ISPs, are deemed to be suppliers of value-added services and not telecommunications service providers. ANATEL's Resolution 190 requires cable operators to act as carriers of third-party Internet service providers. The Brazilian House of Representatives is considering a law that would penalize Internet service providers for knowingly providing services that allow illegal goods or services to be sold on the Internet, and would impose confidentiality requirements on Internet service providers regarding nonpublic information transmitted or stored on their networks.

### **C. Organizational Structure**

As of December 31, 2006, our voting shares were indirectly controlled by two major shareholders: Portugal Telecom and Telefónica, through Brasilcel N.V., with 89.3% of our voting stock, 47.5% of our preferred shares and 62.8% of our total capital stock. Portugal Telecom and Telefónica share their participation in Brasilcel in equal percentages after the Merger, controlling 89.0% of our voting stock, 47.53% of our preferred shares and 62.40% of our total capital stock.

Following the Merger, our subsidiaries are: TC, GT, TCO, Telebahia, Telergipe, Telerj, Telest and Celular CRT (all of these subsidiaries have now been merged into Vivo S.A. See [Our History and Development](#) [Corporate Restructuring of Our Operating Subsidiaries](#) ). Substantially all our assets consist of shares in our subsidiaries. We rely very substantially on dividends from our subsidiaries to meet our needs for cash, including cash to pay dividends to our shareholders. See [Item 5. Operating and Financial Review and Prospects](#) [Liquidity and Capital Resources](#).

For a more detailed description of our ownership structure and the joint venture between Portugal Telecom and Telefónica, see [Our History and Development](#) and [Exhibit 8.1](#).

### **D. Property, Plant and Equipment**

Our principal physical property consists of transmission equipment, switching equipment, base stations, and other communication devices, such as voicemail, prepaid service, Short Message Service, Home Location Registers, Signaling Transfer Point, Packet Data Switching Network and gateways. All switches, cell sites, administrative buildings, administrative facilities, warehouses and stores are insured against damages for operation risks.

As of December 31, 2006, we had 56 cellular switches in São Paulo and other equipment installed in 12 owned spaces, two leased spaces and 18 shared spaces. In São Paulo, we lease most of the sites in which our cellular telecommunications network equipment is installed. The average term of these leases is five years (subject to renewal for additional five-year terms). Our 3,229 base stations and other network equipment are installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, in Sao Paulo we own administrative buildings (approximately 5,126 square meters) and one retail store and we lease five administrative facilities (approximately 76,549 square meters), warehouse space (approximately 6,000 square meters), 11 administrative areas (approximately 6,257 square meters), 11 kiosks and 82 retail stores.

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As of December 31, 2006, Vivo S.A., in the states of Parana and Santa Catarina ( PR/SC ), had 18 cellular switches and other equipment installed in six owned spaces. In PR/SC, Vivo S.A. leases most of the sites in which its cellular telecommunications network equipment is installed. The average term of these leases is five years (subject to renewal for additional five-year terms). Its 1,435 base stations and other network equipment were installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, Vivo S.A. in PR/SC has one administrative building (approximately 4,582 square meters) and leases two administrative facilities (approximately 7,367 square meters), warehouse space (approximately 4,526 square meters), and 38 retail stores.

As of December 31, 2006, Vivo S.A. in the midwest region ( CO ) had 21 cellular switches and other equipment installed in 11 owned spaces and one shared space. In CO, Vivo S.A. leases most of the sites in which its cellular telecommunications network equipment is installed. The average term of these leases is five years. Its 1,807 base stations and other network equipments were installed in cell sites, administrative buildings, administrative facilities and warehouses. Also in this region, Vivo S.A. owns six administrative buildings (approximately 35,380 square meters), two warehouse spaces (approximately 1,300 square meters), one administrative area (approximately 491 square meters) and three retail stores, and leases four administrative facilities (approximately 3,958 square meters), six warehouse spaces (approximately 8,288 square meters), three administrative areas (approximately 2,890 square meters) and 47 retail stores.

As of December 31, 2006, Vivo S.A. in the northern region had 16 cellular switches and other equipment installed in 12 owned spaces and one leased space. Vivo S.A. leases in this region most of the sites in which its cellular telecommunications network equipment is installed. The average term of these leases is five years. Its 572 base stations were installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, the northern region owns a warehouse space (approximately 600 square meters) and leases five administrative facilities (approximately 5,556 square meters), five warehouse spaces (approximately 15,705 square meters) and 23 retail stores.

As of December 31, 2006, Vivo S.A. in the states of Bahia and Sergipe had nine cellular switches and other equipment installed in two owned spaces and three shared spaces. Its operating companies lease most of the sites where their cellular telecommunications network equipment is installed. The average term of these leases is five years. Their 622 base stations were installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, they have their own administrative building with warehouse space (approximately 19,455 square meters both) and lease one administrative facility (approximately 872 square meters) and 24 retail stores throughout this region.

As of December 31, 2006, Vivo S.A. in the states of Rio de Janeiro and Espirito Santo had 23 cellular switches and other equipment installed in four owned spaces, three shared spaces and one leased space. Its operating companies lease most of the sites where their cellular telecommunications network equipment is installed. The average term of these leases is five years. Our 2,124 base stations were installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, they have their own administrative buildings (approximately 3,122 square meters) and one retail store, and also lease an administrative facility (approximately 28,175 square meters), two warehouse spaces (approximately 11,977 square meters), eight kiosks and 44 retail stores throughout this Region.

As of December 31, 2006, Vivo S.A. in the state of Rio Grande do Sul had 19 cellular switches and other equipment installed in two owned spaces, two leased spaces and 10 shared spaces. Its operating companies lease most of the sites where their cellular telecommunications network equipment is installed. The average term of these leases is five years. Our 2,122 base stations were installed in cell sites, administrative buildings, administrative facilities and warehouses. In addition, they have their own administrative building (approximately 1,484 square meters) and also lease an administrative facility (approximately 4,549 square meters), two warehouse spaces (approximately 7,524 square meters), four kiosks and 27 retail stores throughout this Region.

#### **ITEM 4A. UNRESOLVED STAFF COMMENTS**

Not applicable.

#### **ITEM 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS**

You should read the following discussion in conjunction with our consolidated financial statements and accompanying notes and other financial information included elsewhere in this annual report, and in conjunction with the financial information included under Item 3.A. Key Information Selected Financial Data. As discussed in Presentation of Financial Information, in February 2006, we merged with TSD, TLE and CRT. Under Brazilian GAAP, the Merger was recorded as from January 1, 2006. Since we were under common control with these entities

since 2002, the financial information presented in Item 5 Operating and Financial Review and Prospects combines our operations with those of TSD, TLE and CRT for periods prior January 1, 2006.

### **Critical Accounting Policies**

In preparing our consolidated financial statements, we have 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 financial condition and results and utilize management's most difficult, subjective or complex judgments, estimates and assumptions. The significant accounting policies that we believe are critical to aid in fully understanding and evaluating our reported financial position and results of operations reported under Brazilian GAAP are described in Note 3 to our consolidated and combined financial statements. A description of the differences in accounting policies between Brazilian GAAP and U.S. GAAP is included in Note 37 to our consolidated and combined financial statements. The application of these critical accounting policies often requires judgments made by our management regarding the effects of matters that are inherently uncertain on the carrying value of our assets and liabilities and the results of our operations. Our results of operation and financial condition may differ from those set forth in our consolidated and combined financial statements, if our actual experience differs from management's assumptions and estimates. The following is a discussion of our critical accounting policies, including some of the variables, assumptions and sensitivities underlying the estimates relating to:

- goodwill impairment;
- revenue recognition;
- depreciation of property, plant and equipment;
- valuation of property, plant and equipment;
- provisions for contingencies;
- deferred income taxes; and
- financial instruments.

### ***Goodwill impairment***

Under Brazilian GAAP, the amount of goodwill and other intangible asset impairment, if any, is measured based on projected undiscounted future operating cash flows. Under U.S. GAAP, pursuant to SFAS No. 142 Goodwill and Other Intangible Assets goodwill is no longer amortized and is subject to a yearly impairment test. In performing the yearly impairment test, we identify our reporting units and determine the carrying value of each reporting unit by assigning the assets and liabilities, including the existing goodwill and intangible assets. We then determine the fair value of each reporting unit and compare it to the carrying amount of the reporting unit. If the carrying amount of a reporting unit exceeds the fair value of the reporting unit, we would be required to perform the second step of the impairment test that involves the determination of the implicit fair value of the reporting unit by performing a hypothetical purchase accounting calculation. If the implicit value of the goodwill exceeds the book value, an impairment is recognized. In October 2006, we completed restructurings resulting in a change in the Company's management structure and operating segments. As a result, the Company had one reportable segment, which represented a reporting unit as of December 31, 2006.

A determination of the fair value and the undiscounted future operating cash flows of our cellular business requires management to make certain assumptions and estimates with respect to projected cash inflows and outflows related to future revenues and expenditures and expenses. These assumptions and estimates can be influenced by different external and internal factors, such as economic tendencies, industry trends, and interest rates, changes in our business strategies and changes in the type of services we offer to the market. The use of different assumptions and estimates could significantly change our financial statements. If assumptions and estimates about the expected future



net cash flows change in the future, we may have to recognize impairment charges on goodwill, which would decrease our results of operations and shareholders' equity.

### ***Revenue recognition***

Under Brazilian GAAP and U.S. GAAP, we recognize revenues as the services are provided. Sales of wireless devices to dealers are recognized when the respective wireless device is activated by the end user. Prepaid service revenue is deferred and amortized based on subscriber airtime usage. Under U.S. GAAP, revenue from sales of wireless devices along with the related cost of the wireless devices are deferred and amortized over their estimated useful life. The excess of the cost over the amount of deferred revenue is recognized on the date of sale. From January 1, 2004, we began to segregate free minutes given in connection with sales of wireless devices and recharges on prepaid phone plans. These minutes are recognized as used based on their respective estimated fair values.

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 collectibility, uncertainties regarding our right to receive certain revenues (mainly revenues for usage of our network) and the estimation of fair value for certain transactions. 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.

### ***Depreciation and amortization***

Depreciation on property, plant and equipment is calculated on a straight-line method of the estimated useful lives of the underlying assets, which consider historical information available to us, as well as known industry trends. The sensitivity of an impact in changes in the useful lives of property, plant and equipment was assessed by applying a hypothetical 10% decrease to the useful lives of switching and transmission equipment existing at December 31, 2006. This hypothetical 10% decrease would cause a R\$130 million increase in our annual depreciation expense in the year of the change.

### ***Valuation of long-lived assets***

Under Brazilian GAAP, an impairment is recognized on long-lived assets such as property, plant and equipment and concession intangibles if the expected net cash flows generated by the respective asset are not sufficient to cover its book value. Under U.S. GAAP, in accordance with SFAS No. 144, long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to the estimated undiscounted future cash flows expected to be generated by the asset. If the carrying amount of an asset exceeds its estimated future cash flows, an impairment charge is recognized in the amount by which the carrying amount of the asset exceeds the fair value of the asset.

A determination of the fair value of an asset requires management to make certain assumptions and estimates with respect to projected cash inflows and outflows related to future revenues and expenditures and expenses. These assumptions and estimates can be influenced by different external and internal factors, such as economic tendencies, industry trends, interest rates and changes in the marketplace. A change in the assumptions and estimates that we use could change our estimate of the expected future net cash flows and lead to the recognition of an impairment charge on our property, plant and equipment or concession intangibles, which would decrease our results of operations and shareholders' equity.

### ***Provisions for contingencies***

We are subject to proceedings, lawsuits and other claims related to tax, labor and civil matters. We are required to assess the likelihood of any adverse judgments or outcomes to these matters as well as potential ranges of probable losses. A determination of the amount of reserves required, if any, for these contingencies is made after careful analysis of each individual issue, based on legal advice. The required reserves may change in the future due to new developments in each matter or changes in our approach in dealing with these matters, such as a change in settlement

strategy. Future possible changes in the recorded reserve amounts would impact our results of operations in the period that such changes are recorded.

### ***Deferred income taxes***

We compute and pay income taxes based on results of operations under Brazilian GAAP. Under U.S. GAAP, we recognize deferred tax assets and liabilities based on the differences between the financial statement carrying amounts and the tax bases of assets and liabilities. We regularly review the deferred tax assets for recoverability and establish a valuation allowance if it is more likely than not that the deferred tax assets will not be realized, based on historical taxable income, projected future taxable income, and the expected timing of the reversals of existing temporary differences. When performing such reviews, we are required to make significant estimates and assumptions about future taxable income. In order to determine future taxable income, we need to estimate future taxable revenues and deductible expenses, which are subject to different external and internal factors such as economic tendencies, industry trends, interest rates, changes in our business strategies and changes in the type of services we offer to the market. The use of different assumptions and estimates could significantly change our financial statements. A change in assumptions and estimates with respect to our expected future taxable income could result in the recognition of a valuation allowance on deferred income tax assets, which would decrease our results of operations and shareholders equity. If we operate at a loss or are unable to generate sufficient future taxable income, if there is a material change in the actual effective tax rates, if the time period within which the underlying temporary differences become taxable or deductible, or there is any change in our future projections, we could be required to establish a valuation allowance against all or a significant portion of our deferred tax assets resulting in a substantial increase of our effective tax rate and a material adverse impact on our operating results.

### ***Financial instruments***

With respect to financial instruments, we must make assumptions as to future foreign currency exchange and interest rates. For a discussion of the possible impact of fluctuations in the foreign currency exchange and interest rates on our principal financial instruments and positions, see Item 11. Quantitative and Qualitative Disclosures About Market Risk.

### **A. Operating Results**

On April 25, 2003, we acquired 64.03% of TCO's common stock. Subsequently, we increased our ownership interest to 90.73% of TCO's common stock through a public tender offer. Since May 1, 2003, we have consolidated 100% of the results of TCO.

The comparability of the TCP figures for the fiscal years ended December 31, 2003 and 2004 has been affected by the consolidation of the operating results of TCO from May 1, 2003.

In February 2006, pursuant to the Merger, TCO became our wholly owned subsidiary and each of TLE, TSD and CRT merged with and into us. Under the Merger, the Vivo Companies consolidated with one another through a Brazilian law procedure, whereby TCO became a wholly owned subsidiary of Vivo pursuant to a merger of shares (*incorporação de ações*) of TCO and a merger of companies (*incorporação de empresas*) of TLE, TSD and Celular CRT with and into Vivo, with Vivo as the surviving company. Holders of common shares, preferred shares or (where applicable) ADSs of TCO, TLE, TSD and Celular CRT received common shares, preferred shares or ADSs, respectively, of Vivo upon approval of the Merger by the requisite percentage of the voting shareholders of Vivo, and of TCO, TLE, TSD and Celular CRT, as applicable. Upon the completion of the Merger, TCP was renamed Vivo Participações S.A. and has become the holding company of TCO and of the subsidiaries TLE, TSD and Celular CRT.

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Pursuant to the Merger, Brasilcel and its subsidiaries hold all of our common shares. Under the Protocol of Merger of Shares and Merger of Companies and Instrument of Justification agreements which govern the Merger, we underwent a capital increase in the amount of R\$2,631,136,636 as a result of the Merger, from R\$6,670,152,498 to R\$9,301,289,134. The agreements also provided that Celular CRT's preferred shares held in treasury be transferred to TCP in connection with the Merger.

At a Vivo Shareholders Meeting held on February 22, 2006, Vivo reduced its capital in the amount of R\$3,147,782,181, from R\$6,670,152,498 to R\$3,522,370,316, as approved by management and the shareholders and

in accordance with Brazilian Corporate Law, which permits reductions in capital up to the amount of accumulated losses, allowing a more accurate valuation of the company and the possibility for eventual future distributions of dividends. The total capital of Vivo is R\$6,153,506,952, owing to an increase in the amount of R\$2,631,136,636 as a result of the Merger. For more information on the Merger, see the Protocol of Merger of Shares and Merger of Companies and Instrument of Justification among TCP and TCO, TSD, TLE and Celular CRT dated December 4, 2005, which is included as an exhibit to this report.

Under Brazilian GAAP, the Merger was recorded as from January 1, 2006. Since we were under common control with TSD, TLE and CRT since 2002, the financial information presented in this Item 5 Operating and Financial Review and Prospects combines the results of our operations with those of TSD, TLE and CRT for periods prior to January 1, 2006.

The Extraordinary General Shareholders Meeting held on October 31, 2006 approved the Merger between the fully owned subsidiary GT with Vivo's other fully owned subsidiaries, including Telergipe, Telebahia, Telerj, Telest, Celular CRT, TC and TCO, as well as TCO's subsidiaries, Telegoiás, Telemat, Telems, Teleron, Teleacre, and NBT.

The objective of the corporate restructuring was to simplify the corporate and operational structure by unifying the general business administration of the operations. Operations will now be concentrated in a single operating company controlled by Vivo, to take full advantage of the synergies between the companies involved, increase Vivo shareholder value and continue the process approved in the Extraordinary General Shareholders Meeting held on February 22, 2006. Upon completion of the corporate restructuring, the name GT was changed to Vivo S.A.

### Results of Operations for 2006, 2005 and 2004 for Vivo

The following table sets forth certain components of our results for the periods presented.

#### Statement of Operations

	Year ended December 31,			Percent change	
	2006 (1) Consolidated	2005 (1) Combined	2004 (1) Combined	2006-2005	2005-2004
	(in millions of reais)				
Net operating revenue	10,936.7	11,253.8	10,929.4	(2.8)	3.0
Cost of services and goods	(5,564.2)	(5,337.3)	(5,338.1)	4.3	0.0
Gross profit	5,372.5	5,916.5	5,591.3	(9.2)	5.8
Operating expenses:					
Selling	(3,787.5)	(3,744.5)	(2,833.0)	1.1	32.2
General and administrative	(1,112.2)	(1,033.3)	(959.2)	7.6	7.7
Other operating expenses, net	(270.6)	(360.1)	(129.2)	(24.9)	178.7
Total operating expenses	(5,170.3)	(5,137.9)	(3,921.4)	0.6	31.0
Operating income before financial expense, net	202.2	778.6	1,669.9	(74.0)	(53.4)
Net financial expenses	(748.0)	(913.1)	(1,088.5)	(18.1)	(16.1)
Operating income (loss)	(545.8)	(134.5)	581.4	305.8	na
Net non-operating expense	(289.0)	(96.5)	(60.9)	199.5	58.5
Net income (loss) before income and social contribution taxes and minority interests	(834.8)	(231.0)	520.5	261.4	na

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Income and social contribution taxes	859.1	(363.0)	(438.5)	Na	(17.2)
Minority interests	(8.0)	(173.5)	(480.9)	(95.4)	(63.9)
Net Income (loss)	16.3	(767.5)	(398.9)	Na	92.4

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(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

### ***Operating Revenues***

Our operating revenues consist of the following:

- usage charges, which include charges for outgoing calls, monthly subscription charges, roaming and similar service;
- revenues from the sale of wireless devices and accessories;
- interconnection charges (or network usage charges), which are amounts we charge other cellular and fixed-line or long-distance service providers for the use of our network; and
- other charges, including charges for the text messaging services (SMS), WAP, downloads, call forwarding, call waiting, voicemail, and call blocking.

The composition of our operating revenues has been affected by the shift in the composition of customers to prepaid services (which generate usage charges and interconnection charges but do not generate monthly subscription charges, and which have attracted lower income customers to our services), by our strategic focus on profitability and selective customer growth, and also by the change in the recognition of revenues related to prepaid services.

Vivo's net additions (number of new customers less churn) generated a 3.5% decrease in the number of contract customers to 5.5 million in 2006, from 5.7 million in 2005. The 2005 figure represented a 9.6% increase from 5.2 million in 2004. Similarly, net additions generated a 2.5% decrease in the number of prepaid customers to 23.5 million in 2006, from 24.1 million in 2005. The 2005 figure represented a 12.6% increase from 21.4 million in 2004.

ANATEL authorizes cellular operators to increase tariffs based upon the prior twelve-month period's cumulative inflation, measured by the IGP-DI variation from February to January of each year.

As of July 6, 2003, cellular telecommunications operators in Brazil were required by the SMP rules to implement long-distance carrier selection codes (*códigos de seleção de prestadora*, or CSP) used by customers to choose their carrier for domestic long-distance services (VC2 and VC3) and international cellular calls. As a result, Vivo no longer receives direct revenues or incurs costs in connection with VC2 or VC3 or international calls.

Additionally, in accordance with ANATEL's regulations, Bill & Keep rules were adopted for interconnection charges in July 2003. The rules provide that companies under the SMP regime are not required to pay tariffs for the use of the local network of other SMP providers as long as customers use local service (i.e., make calls in the same registration area) and as long as there is a traffic balance between them. However, if traffic from the SMP provider that originates the call to the SMP provider that terminates the call represents more than 55% of the total local traffic between the two providers, the SMP provider who originates the higher traffic through the other provider's network must pay to such other provider the local usage tariff for the portion of the traffic that exceeds 55%. On July 14, 2006, ANATEL eliminated the rule of the partial Bill & Keep in the remuneration of network usage between SMP networks.

The composition of operating revenues by category of service is presented in our consolidated financial statements and discussed below. We do not present operating revenues on a net basis (i.e., after deduction of taxes) by category of service.

The following table sets forth the components of our net operating revenues for the periods presented.





	Year ended December 31,			Percent change	
	2006 (1)	2005 (1)	2004 (1)	2006-2005	2005-2004
	(in millions of reais)				
Usage, additional call and monthly subscription charges	7,243.9	7,399.0	6,377.8	(2.1)	16.0
Interconnection charges	4,338.1	4,304.4	4,590.9	0.8	(6.2)
Sales of wireless devices and accessories	2,742.6	3,051.7	2,984.6	(10.1)	2.3
Other	1,130.1	1,005.3	767.7	12.4	30.9
Gross operating revenue	15,454.7	15,760.4	14,721.0	(1.9)	7.1
Value-added and other indirect taxes	(3,094.1)	(3,157.7)	(2,756.1)	(2.0)	14.6
Discounts granted and return of goods	(1,423.9)	(1,348.9)	(1,035.5)	5.6	30.3
Net operating revenues (1)	10,936.7	11,253.8	10,929.4	(2.8)	3.0

(1) The financial information presented for the 2006 fiscal year represents information from Vivo's consolidated financial statements. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo and TSD, TLE and CRT.

Net operating revenues decreased by 2.8% to R\$10,936.7 million in 2006 and from R\$11,253.8 million in 2005, which in turn represented a 3.0% increase from R\$10,929.4 million in 2004. The reduction in 2006 reflects mainly a decrease in revenue from sales of wireless devices and accessories and usage charges, partially offset through an increase in interconnection charges and other revenues. The growth in 2005 reflects mainly an increase from usage charges, other revenues and sales of wireless devices and accessories, partially offset by a decrease in interconnection charges and monthly subscription charges.

*Usage, additional call and monthly subscription charges.* Revenues from usage charges decreased by 2.1% to R\$7,243.9 million in 2006, from R\$7,399.0 million in 2005, which in turn represented a 16.0% increase from R\$6,377.8 million in 2004. The decrease in usage charges in 2006 was mainly due to a decrease of 2.3% in our customer base to 29.1 million. The increase in usage charges in 2005 was mainly due to an increase of 12.5% in our customer base to 29.8 million customers in 2005 as compared to 26.5 million customers in 2004, in addition to an increase in traffic due to an increase of 10.8% in contract customers.

*Interconnection charges.* Revenues from interconnection charges increased by 0.8% to R\$4,338.1 million in 2006, from R\$4,304.4 million in 2005, which in turn represented a 6.2% decrease from R\$4,590.9 million in 2004. The increase in interconnection charges in 2006 was principally due to the end of the partial Bill & Keep rule in July 2006, which was partially offset by the reduction of fixed-line to mobile traffic in substitution for mobile-to-mobile traffic. By eliminating the effects of the partial Bill & Keep rule in 2006, interconnection charges decreased 14.3%. The decrease in interconnection charges in 2005 was principally due to a trend toward a greater volume of cellular-to-cellular calls and a reduction in the volume of fixed-line to cellular calls and to the effect of the partial Bill & Keep system under ANATEL's Personal Mobile Service (*Serviço Móvel Pessoal*, or SMP) regime, as described in Item 3. Key Information.

*Sales of wireless devices and accessories.* Revenues from sales of wireless devices and accessories decreased by 10.1% to R\$2,742.6 million in 2006 and from R\$3,051.7 million in 2005, which in turn represented a 2.3% increase from R\$2,984.6 million in 2004. The decrease in 2006 was mainly due to a reduction in the ratio of additional clients

to our own wireless devices and a decrease in the average selling price due to competition. The increase in 2005 was mainly due to the increase in our customer base, described above, which resulted in part from promotional campaigns to acquire new customers.

Revenues from sales of wireless devices and accessories are reported before commissions and promotional discounts, and include value-added taxes. In general, the purpose of wireless device sales is to encourage growth in customers and traffic (and not necessarily to generate profits). Accordingly, we subsidize part of the costs of wireless devices. The subsidy strategy resulted in a gross loss (calculated as the difference of net operating revenues from sales minus the cost of goods sold) for Vivo of R\$521.8 million, R\$783.5 million and R\$928.5 million in 2006, 2005 and 2004, respectively.

*Other.* Revenues from other services increased 12.4% to R\$1,130.1 million in 2006, and from R\$1,005.3 million in 2005, which in turn represented a 30.9% increase from R\$767.7 million in 2004. The increase was principally due to the increase in the use of data-related services by our customers, including text message services, or SMS, wireless Internet services and other value-added services. The increase in 2005 was principally due to an increase in our customer base and an increase in the use of data-related services by our customers, including text message services, or SMS, wireless Internet services and other value-added services. This increase is a consequence of the development of products and the increased adoption of these services by users, reflecting widespread access and use of the tools, in addition to the increase in the wireless device portfolio.

*Value-added and other indirect taxes.* Value-added and other indirect taxes decreased 2.0% to R\$3,094.1 million from R\$3,157.7 million in 2005, which in turn represented a 14.6% increase from R\$2,756.1 million in 2004. The decrease was principally due to a decrease in gross operating revenue, particularly in revenue from the sales of wireless devices and accessories and usage charges. The increase in 2005 occurred principally because of the increase in gross operating revenues other than from interconnection fees (which are not subject to these taxes). The effective rate of taxes on gross operating revenues varies depending on the composition of our revenues, since the interconnection charges are not subject to ICMS. Accordingly, value-added taxes and other indirect taxes corresponded to 20.0%, 20.0% and 18.7% of our gross operating revenues in 2006, 2005 and 2004, respectively.

*Sales and services discounts and return of goods sold.* Discounts and returns increased by 5.6% in 2006 to R\$1,423.9 million, from R\$1,348.9 million in 2005, which in turn represented a 30.3% increase from R\$1,035.5 million in 2004. Discounts and returns corresponded to 9.2%, 8.6% and 7.0% of our gross operating revenues in 2006, 2005 and 2004, respectively. The increase was principally due to the increase of discounts on services due to competition. The increase in 2005 was principally due to increases in discounts on wireless devices and accessories in response to aggressive competition from other providers and to higher commissions for prepaid card sales.

### ***Cost of Services and Goods***

The following table sets forth the components of our costs of services and goods sold for 2006, 2005 and 2004, as well as the percentage change from the previous year.

	<b>Year ended December 31,</b>			<b>Percent change</b>	
	<b>2006 (1)</b>	<b>2005 (1)</b>	<b>2004 (1)</b>	<b>2006-2005</b>	<b>2005-2004</b>
	<b>(in millions of reais)</b>				
Cost of goods sold	(1,898.3)	(2,424.7)	(2,682.0)	(21.7)	(9.6)
Depreciation and amortization	(1,327.5)	(1,240.4)	(1,237.9)	7.0	0.2
Supplies, outside services other	(517.9)	(399.4)	(279.4)	29.7	42.9
Interconnection charges add	(785.0)	(242.7)	(347.6)	223.4	(30.2)
Rent, insurance, condominium fees, and leased lines	(429.3)	(438.2)	(380.3)	(2.0)	15.2
Personnel	(88.7)	(98.2)	(91.2)	(9.7)	7.7
Taxes	(517.5)	(493.7)	(319.7)	4.8	54.4
<b>Cost of services and goods</b>	<b>(5,564.2)</b>	<b>(5,337.3)</b>	<b>(5,338.1)</b>	<b>4.3</b>	<b>0.0</b>

- (1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

Cost of services and goods increased by 4.3% in 2006 to R\$5,564.2 million, from R\$5,337.3 million in 2005, which remained stable compared to 2004, which reached R\$5,338.1 million. The increase in 2006 was principally due to an increase in interconnection costs resulting from the end of the "Bill & Keep" rule in July 2006, an increase of third-party costs and the depreciation and amortization costs, partially offset by a reduction in the cost of goods sold. The increase in 2005 was mainly due to increases in tax payments, depreciation and amortization and the cost of third party services. This increase was partially offset by a decrease in interconnection charges paid to other providers and the cost goods sold. Gross margin (gross profit as a percent of net revenues) corresponded to 49.1%, 52.6% and 51.2% in 2006, 2005 and 2004, respectively.

*Cost of goods sold.* Cost of wireless devices and accessories decreased 21.7% to R\$1,898.3 million in 2006, from R\$2,424.7 million in 2005, which in turn represented a decrease of 9.6% from R\$2,682.0 million in 2004. The decrease in 2006 was mainly due to the decrease in the ratio of additional clients to our own wireless devices, lower costs as a result of negotiations with suppliers and valuation of the *real* against the U.S. dollar. The decrease in 2005 was principally due to lower costs negotiated with suppliers and fewer new customers in 2005 compared to 2004.

*Depreciation and amortization.* Depreciation and amortization expenses increased 7.0% to R\$1,327.5 million in 2006, from R\$1,240.4 million in 2005, which in turn represented an increase of 0.2% from R\$1,237.9 million in 2004. The increase in 2006 was principally due to investments and completion of projects, in particular the expansion and coverage of our network and the amortization of intangible goods such as software. The increase in 2005 was principally due to expansion of our transmission network and other assets driven by the expansion in our customer base.

*Supplies, outside services and other.* Cost of materials and third-party services increased 29.7% to R\$517.9 million in 2006, from R\$399.4 million in 2005, which in turn represented an increase of 42.9% from R\$279.4 million in 2004. The increase in 2006 was principally due to an increase in the costs of public services and the cost of the network for service data. The increase in 2005 was principally due to increase in the cost of third-party services and rental payments, such as network maintenance services and the costs of rented circuits and transmission lines.

*Interconnection charges.* Interconnection charges increased by 223.4% to R\$785.0 million in 2006, and from R\$242.7 million in 2005, which in turn represented a decrease of 30.2% from R\$347.6 million in 2004. The increase in 2006 is due to the end of the *Bill & Keep* rule in July 2006. By eliminating the effects of *Bill & Keep* in 2006, interconnection charges decreased 31.6% as a result of the reduction in the mobile-to-fixed tariff, partially offset by an increase in total traffic mainly in mobile-to-mobile traffic.

*Rent, insurance, condominium fees, and leased lines.* Rent, insurance, condominium fees, and leased lines expenses decreased 2.0% to R\$429.3 million in 2006, from R\$438.2 million in 2005, which in turn represented an increase of 15.2% from R\$380.3 million in 2004. The decrease in 2006 was principally due to a decrease in payment for the connection through the utilization of the circuits and through renegotiating leases. The increase in 2005 was principally a result of increases in lease payments for shared space, paid for by a reduction in commercial equipment leases.

*Personnel.* Personnel expenses decreased 9.7% to R\$88.7 million in 2006, from R\$98.2 million in 2005, which in turn represented an increase of 7.7% from R\$91.2 million in 2004. The decrease in 2006 was principally due to a larger number of employees having been allocated to capital expenditure projects, such as the construction of networks, partially offset by the increase in salaries under the terms of our collective bargaining agreement and the increase in the number of employees. The increase in 2005 was mainly due to an approximate 6% increase in salaries under the terms of our collective bargaining agreement, which we renegotiate annually and which takes effect on November 1, and to training program costs.

*Taxes.* Taxes increased 4.8% to R\$517.5 million in 2006, compared to R\$493.7 million in 2005, which in turn represented a 54.4% increase from R\$319.7 million in 2004. The increase in 2006 was principally due to the increase in FISTEL taxes. The increase in 2005 was principally due to a change in accounting policies at TCO to bring TCO's accounting for FISTEL and other taxes in line with that of TCP. Beginning in January of 2005, TCO began to accrue amounts monthly for these taxes, as does TCP, rather than recognize the entire tax amount in December of a given fiscal year.

### ***Operating Expenses***

The following table sets forth the components of our operating expenses for each of the years ended December 31, 2006, 2005 and 2004, as well as the percentage change from the prior year.

	Year ended December 31,			Percent change	
	2006 (1)	2005 (1)	2004 (1)	2006-2005	2005-2004
	(in millions of reais)				
Selling expenses	(3,787.5)	(3,744.5)	(2,833.0)	1.1	32.2
General and administrative expenses	(1,112.2)	(1,033.3)	(959.2)	7.6	7.7
Other net operating expenses	(270.6)	(360.1)	(129.2)	(24.9)	178.7
Total	(5,170.3)	(5,137.9)	(3,921.4)	0.6	31.0

(1) The financial information presented for the 2006 fiscal year represents information from Vivo's consolidated financial statements. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo and TSD, TLE and CRT.

Vivo's operating expenses increased 0.6% to R\$5,170.3 million in 2006, from R\$5,137.9 million in 2005, which in turn represented an increase of 31.0% from R\$3,921.4 million in 2004. The increase in operating expenses in 2006 was principally due to the increase in general and administrative expenses compensated through a reduction in other operating expenses. The increase in operating expenses in 2005 was principally due to an increase in selling expenses, which in 2005 totaled R\$3,744.5 million, a 32.2% increase from R\$2,833.0 million in 2004.

*Selling expenses.* Selling expenses increased 1.1% to R\$3,787.5 million in 2006, from R\$3,744.5 million in 2005, which in turn represented a 32.2% increase from R\$2,833.0 million in 2004. The increase in 2006 was principally due to a 11.4% increase of debtors in default that totaled R\$720.5 million in 2006, an increase in third-party costs, especially in customer service, and an increase in depreciation and amortization, partially offset by a reduction in advertising costs. The increase in debtors in default in 2006, which includes an incremental value, occurred in the second quarter of R\$161.5 million, mostly due to a migration of clients to new systemic platforms that caused delays in billing and collection in the period that followed the implementation of such platforms. The increase in 2005 was principally due to increases in expenses for third-party services (such as marketing, client care and call center services); increases in the provision for doubtful accounts; and expenses for depreciation of stores, equipment and other assets. Provisions for doubtful accounts increased 93.1% to R\$647.0 million for the year ended December 31, 2005 from R\$335.1 million for the year ended December 31, 2004, mainly due to an increase in our customer base and the effect of changes in how we recognize acquisitions of new customers and receivables from calls made through networks of other operators. Such values, according to the present regulations, are necessarily paid to the cited operators, independent of recognition of such calls from our customers. Provisions for doubtful accounts were 4.7%, 4.1% and 2.28% of gross revenues for 2006, 2005, and 2004, respectively.

*General and administrative expenses.* General and administrative expenses increased by 7.6% in 2006 to R\$1,112.2 million, and from R\$1,033.3 million in 2005, which in turn represented an increase of 7.7% in 2004 from R\$959.2 million in 2004. The increase in 2006 was principally due to the increase in depreciation and amortization of expenses beyond the increase in personnel, leasing and insurance costs and housing association fees, offset partially by a reduction in third-party costs, especially consulting and general structure costs. The increase in general and administrative expenses in 2005 was primarily due to increases in outsourcing, especially for data processing and network maintenance and to larger depreciation and amortization expenses.

*Other net operating expenses.* The net amount of other operating expenses decreased by 24.9% to R\$270.6 million in 2006, from R\$360.1 million in 2005, which in turn represented an increase of 178.7% from R\$129.2 million in

2004. The decrease in 2006 was principally due to the reversal of provision for PIS and COFINS in the amount of R\$149.1 million, recorded as recovered expenses, and the decrease in goodwill amortization, partially offset by the increase in reserve for contingencies. The increase in 2005 was mainly caused by the amortization of goodwill generated in the acquisition of additional shares of TCO.

***Net Financial Expenses***

The following table sets forth certain components of our net financial expenses, as well as the percentage change of each component from the previous year, for each of the years ended December 31, 2006, 2005 and 2004.



	Year ended December 31,			Percent Change	
	2006 (1)	2005 (1)	2004 (1)	2006-2005	2005-2004
	(in millions of reais)				
Financial income	286.8	439.7	379.6	(34.8)	15.8
Exchange gains and losses	323.0	466.3	359.2	(30.7)	29.8
Gains (Losses) on foreign currency derivative contracts	(764.3)	(1,120.0)	(1,030.2)	(31.8)	8.7
Financial expenses	(593.5)	(699.1)	(797.1)	(15.1)	(12.3)
	(748.0)	(913.1)	(1,088.5)	(18.1)	(16.1)

(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

Net financial expense reflects, among other things, the net effect of interest income and expense, and the net effect of exchange rate fluctuation affecting our loans, financings and derivative operations. See Note 28 to our financial statements. Our net financial expenses decreased 18.1% to R\$748.0 million in 2006, from R\$913.1 million in 2005, which in turn represented a decrease of 16.1% from R\$1,088.5 million in 2004. The decrease in 2006 was principally due to the reduction in net indebtedness, which occurred due to the corporate reorganization and financial liabilities restructuring, as well as to the decrease in the interest rates during the period (15.0% in 2006 and 19.0% in 2005).

Vivo's net financial expenses decreased between 2004 and 2005 primarily due to a reduction in our cost of net debt obtained from the renewal of financial agreements, which offset the higher interest rates during the period (from 16.17% per year in 2004 to 19.0% per year in 2005).

As of December 31, 2006, all of our foreign exchange indebtedness (R\$2,651.2 million) was covered by long positions under hedging agreements. Under those derivative agreements, our subsidiaries' foreign exchange-denominated obligations are swapped for *real*-denominated obligations bearing interest at rates linked to the *Certificado de Depósito Interfinanceiro* (Interbank Deposit Certificate), or CDI. This resulted in a gain of R\$335.0 million in our foreign currency-denominated debt (a gain of R\$460.1 million in 2005 and a gain of R\$355.3 million in 2004), which was offset by losses in our currency and interest rate derivatives contracts of R\$764.3 million in 2006 (a loss of R\$1,120.0 million in 2005 and a loss of R\$1,030.2 million in 2004).

### ***Net non-operating Expense***

The net non-operating expense increased by 199.5% to R\$289.0 million from R\$96.5 million in 2005, which in turn represented a 58.5% increase from R\$60.9 million in 2004. In 2006, we recorded a provision for loss in property, plant and equipment in the amount of R\$278.0 as a result of our analysis of the recoverability of assets related to the technologies.

### ***Income and Social Contribution Taxes Income (Expense)***

We recorded income from income and social contribution taxes in the amount of R\$859.1 million in 2006, a variation from an expense of R\$363.0 million that we recorded in 2005, which in turn represented a 17.2% decrease from an expense of R\$438.5 million in 2004. This shift from expense to income in 2006 resulted from the Corporate Restructuring process. See Note 30 to our financial statements.

***Minority Interest***

Minority interests decreased by 95.4% to R\$8.0 million in 2006, from R\$173.5 million in 2005. The minority interest recorded for the year ended December 31, 2006 represents the minority interest in TCO on January 2006. In February 2006, pursuant to the Merger, TCO became a wholly owned subsidiary of Vivo.

## *Vivo's Segments*

As described in Item 4 Information of the Company Our History and Development Corporate Restructuring of Our Operating Subsidiaries, during 2006, we completed corporate restructurings to simplify our corporate legal structure and create a single legal operating company. This resulted in changes to our management structure and operating segments. By the end of the year ended December 31, 2006, we had one operating segment, cellular telecommunications services. Consequently, no separate segment information has been presented.

## **B. Liquidity and Capital Resources**

### **Sources of Funds**

Vivo generated cash flow from operations of R\$3,100.8 million, R\$2,302.2 million and R\$2,068.4 million in 2006, 2005 and 2004, respectively.

Vivo had net cash used in financing activities of R\$1,458.4 million as of December 31, 2006. Although Vivo obtained new loans in the aggregate amount of R\$2,200.7 million in that period, these were more than offset by loan repayments of R\$2,962.0 million and net settlements on derivatives contracts of R\$640.5 million.

Vivo had R\$2,910.1 million in long-term loans and financing as of December 31, 2006. Vivo's R\$1,590.3 million in short-term indebtedness as of December 31, 2006 consisted primarily of funding from financial institutions. As of December 31, 2006, Vivo had a working capital (current assets minus current liabilities) deficit of R\$27.5 million compared to a working capital of R\$1,326.3 million as of December 31, 2005. As of December 31, 2004, Vivo had a working capital (current assets minus current liabilities) deficit of R\$352.0 million.

On May 1, 2005, Vivo issued debentures in the aggregate principal amount of R\$1.0 billion in two series, both maturing in May 2015. The first series, in the aggregate amount of R\$200.0 million, bears interest at 103.3% of the average daily interbank deposit rate for deposits of one day (*DI Depósitos Interfinanceiros de um dia, extragrupo*), payable semiannually, and is subject to renegotiation of terms (*repactuação*) in May 2009. The second series, in the aggregate amount of R\$800.0 million, bears interest of 104.2% of the average daily interbank deposit rate, payable semiannually, and is subject to renegotiation of terms in May 2010. The proceeds of the issuance of these debentures were used for the repayment of short-term debt.

Also, in October of 2004, TCP held a voluntary public tender offer to acquire shares of TCO in the amount of R\$902.0 million, with the objective of increasing the ownership interest of the Company in the capital stock of TCO. The number of preferred shares of capital stock of TCO held by TCP and by persons directly and indirectly linked to TCP increased to 84,252,534,000 preferred shares, representing 32.76% of the total preferred shares and representing an increase from 28.86% to 50.65% of the ownership interest of the Company in the total capital stock of TCO.

We believe that our available borrowing capacity, together with funds generated by operations, should provide sufficient liquidity and capital resources to pursue our business strategy for the foreseeable future, with respect to working capital, capital expenditures and other operating needs.

### **Uses of Funds**

Our principal uses of funds are for capital expenditures, servicing our debt and payment of dividends to our shareholders.

Our capital expenditures (including capitalized interest) amounted to R\$2,103.9 million, R\$2,206.5 million and R\$1,940.5 million in 2006, 2005 and 2004, respectively. Payment of debt and derivative instruments consumed cash flows of R\$3,602.5 million, R\$4,080.5 million and R\$5,134.4 million in 2006, 2005 and 2004, respectively. Dividends and interest on equity payments consumed cash flows of R\$63.2 million, R\$184.7 million and R\$176.5 million in 2006, 2005 and 2004, respectively.

**Capital Expenditures**

The following table sets forth our total capital expenditures for the periods indicated:

<b>Vivo</b>	<b>Year ended December 31,</b>		
	<b>2006 (1)</b>	<b>2005 (1)</b>	<b>2004 (1)</b>
	<b>(in millions of reais)</b>		
Switching equipment	375.9	523.0	582.1
Transmission equipment	844.4	862.8	623.8
Information technology	414.8	407.6	291.9
Others(2)	468.8	413.1	442.7
<b>Total capital expenditures</b>	<b>2,103.9</b>	<b>2,206.5</b>	<b>1,940.5</b>

(1) The financial information presented for 2006 represents information from Vivo's consolidated financial statements in which Vivo has consolidated TSD, TLE, and CRT as from January 1, 2006. The financial information presented for the 2005 and 2004 fiscal years represents the combined financial data for Vivo, TSD, TLE and CRT, since the companies were under common control with Vivo for these periods.

(2) Consisting primarily of free wireless device rentals, network construction, furniture and fixtures, office equipment and store layouts.

Our capital expenditures over the past three years related primarily to increasing our network capacity and coverage. The Company continued its projects for improvement and expansion of the capacity of services rendered, which provided support to increase the CDMA 1XRTT and EVDO network, expansion of transmission routes, system centralization and integration (billing, collection and CRM, among others), development of new services and opening and renovating points of sale and terminals for the corporate segment.

In the aggregate, R\$2,103.9 million were invested during the year ended December 31, 2006, which included investment in the GSM/EDGE network and in the current CDMA/EV-DO network. This amount represented 19.28% of our net operating revenues.

Our capital expenditures for 2007 include investments in network expansion on GSM/EDGE overlay, introduction of new products and services to maximize the use of cellular phones, expansion of our stores and the continual improvement of the quality of services provided to our customers (the amount will be approved at a general shareholders' meeting). We intend to pay these expenses with funds generated by operations and our available borrowing capacity.

**Payments of Dividends to Shareholders**

The holders of preferred shares are entitled to exercise voting rights since the 2005 general shareholders' meeting and until we pay the minimum dividends. However, this has no significant impact on our ownership structure, since our controlling shareholders own more than 50% of our total capital. See Item 8. Financial Information Consolidated Statements and Other Financial Information Dividend Policy and Dividends Payment of Dividends.

**Debt**

As of December 31, 2006, Vivo's total debt position was as follows:

<b>Debt</b>	<b>Amount Outstanding as of December 31, 2006</b>
	<b>(in millions of reais)</b>
Financing from financial institutions	4,358.5
Fixcel (acquisition of TCO)	10.7
Interest	131.2
Long-term debt(1)	2,910.1
Short-term debt	1,590.3
Total debt	4,500.4

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(1) Excludes the short-term portion of long-term debt.

As of December 31, 2006, Vivo's total debt was R\$4.5 billion, of which R\$2.7 billion, or 59%, was denominated in foreign currencies and therefore exposed to currency fluctuations. Of that amount, R\$1,651 million was denominated in U.S. dollars (US\$772 million), R\$902.8 million was denominated in yen (¥50,286 million), and R\$28 million was denominated in UMBNDES, which comprises a mix of different currencies. Devaluation of the *real* results in exchange losses on our foreign currency indebtedness. In order to protect against this risk, we have entered into over-the-counter derivatives transactions with international and domestic financial institutions. In 2006, we incurred financial expense from foreign currency derivative transactions of R\$764 million against financial income from monetary and foreign exchange variations of R\$335 million. At December 31, 2006, we had derivative contracts that covered 99% of our foreign currency-denominated debt and other foreign currency liabilities. The unrealized costs (net of unrealized gains on foreign exchange derivatives contracts) at December 31, 2006 were R\$501 million.

We are exposed to interest rate risk as a consequence of our floating rate debt. At December 31, 2006, approximately 52% of our interest-bearing liabilities bore interest at floating rates and primarily LIBOR for U.S. dollar-denominated debt and CDI, IGPM and TJLP for *real*-denominated debt. Accordingly, our financing expenses will increase if market interest rates rise. At December 31, 2006, all of our foreign currency derivatives contracts bore interest payments linked to the Brazilian CDI rate. Vivo protected against the risk of interest rates increasing (LIBOR) by entering into derivative contracts in the total amount of US\$232 million and R\$1,864.0 million, respectively. The CDI rates as of December 31, 2006 and 2005 were 13.17% and 19.0%, respectively.

Some of the debt agreements of Vivo contain restrictive covenants. Financial ratios apply to some indebtedness and involve (1) current ratios, (2) capitalization ratios, (3) EBITDA margins, (4) interest coverage ratios and (5) debt-to-capital ratios. Vivo S.A. has indebtedness and financing with the National Economic and Social Development Bank (BNDES), which as of December 31, 2006 totaled R\$191.9 million. In accordance with contractual obligations, there are several economic and financial indicators that must be maintained annually. Vivo S.A. did not meet the required level of EBITDA Margin (EBITDA over net operational revenue), EBITDA Margin without wireless devices (eliminating net income of the sale of goods and cost of wireless devices sold), and the current liquidity (current assets over current liabilities) as of December 31, 2006. We have already obtained a waiver from the bank for the non-fulfillment of such obligations. Vivo S.A. has indebtedness and financing with the Europe Bank of Investments, which as of December 31, 2006 totaled R\$240.5 million. On that same day, various economic and financial indicators were met by Vivo S.A.

### ***U.S. GAAP Reconciliation***

We prepare our consolidated financial statements in accordance with the Brazilian Corporate Law Method, which differs in significant respects from U.S. GAAP. Net losses for 2006, 2005 and 2004 were R\$460.5 million, R\$494.2 million and R\$489.0 million under U.S. GAAP, compared to net income (losses) of R\$16.3 million, R\$(767.5) million and R\$(398.9) million, respectively, under the Brazilian Corporate Law Method. Shareholder's equity at December 31, 2006, 2005 and 2004 was R\$9,126.2 million, R\$7,165.6 million and R\$5,685.9 million, respectively, under U.S. GAAP, compared to R\$8,371.7 million, R\$7,047.5 million and R\$5,830.9 million, respectively, under the Brazilian Corporate Law Method.

See Note 37 to our audited consolidated financial statements for a description of the principal differences between the Brazilian Corporate Law Method and U.S. GAAP as they relate to us, and a reconciliation to U.S. GAAP of net income/loss and total shareholders' equity.

### **New Accounting Pronouncements**

In June 2006, the Emerging Issues Task Force (EITF) ratified the consensus on EITF 06-3, How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement. EITF 06-3

provides that taxes imposed by a governmental authority on a revenue producing transaction between a seller and a customer should be shown in the income statement on either a gross or a net basis, based on the seller's accounting policy, which should be disclosed pursuant to Accounting Principles Board Opinion No. 22, Disclosure



of Accounting Policies. Amounts that are allowed to be charged to customers as an offset to taxes owed by a company are not considered taxes collected and remitted. If such taxes are significant and are presented on a gross basis, the amounts of those taxes should be disclosed. EITF 06-3 will be effective for interim and annual reporting periods beginning after December 15, 2006. We are currently evaluating the impact EITF 06-3 to determine the impact on its consolidated financial statements.

In July 2006, the FASB issued FASB Interpretation No. 48, ( FIN 48 ), Accounting for Uncertainty in Income Taxes , an Interpretation of FASB Statement No. 109 which clarifies the accounting for and disclosure of uncertain tax positions. This guidance seeks to reduce the diversity in practice associated with certain aspects of the recognition and measurement related to tax positions with uncertainty. FIN 48 requires that a tax position taken or expected to be taken in a tax return be recognized in the financial statements when it is more likely than not (i.e., a likelihood of more than fifty percent) that the position would be sustained upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement. The Company will adopt the provisions of FIN 48 effective January 1, 2007. We are evaluating the potential impact of this interpretation on our financial statements but we do not anticipate any such impact to be material.

In September 2006, the FASB issued Statement of Financial Accounting Standards No. 157, Fair Value Measurements. FAS 157 defines fair value, establishes a framework for measuring fair value and expands disclosures about fair value measurements. FAS 157 applies under other accounting pronouncements that require or permit fair value measurement. FAS 157 does not require any new fair value measurements and we do not expect the application of this standard to change our current practice. FAS 157 requires prospective application for fiscal years ending after November 15, 2007.

In September 2006, the FASB issued SFAS No. 158, Employers Accounting for Defined Benefit Pension and Other Postretirement Plans, which requires an employer that is a business entity who sponsors one or more single-employer defined benefit plans to (i) recognize the funded status of a benefit plan in its statement of financial position; (ii) recognize as a component of other comprehensive income, net of tax, the gains or losses and prior service costs or credits that arise during the period but are not recognized as components of net periodic benefit cost pursuant to SFAS No. 87, Employers Accounting for Pensions, or No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions ; (iii) measure defined benefit plan assets and obligations as of the date of the employers fiscal year-end statement of financial position; and (iv) disclose in the notes to financial statements additional information about certain effects on net periodic benefit cost for the next fiscal year arising from the delayed recognition of the gains or losses, prior service costs or credits, and transition net assets or obligations. We adopted SFAS 158 recognition and related disclosure provisions as of December 31, 2006, which resulted in a gain of R\$29,645, net of income taxes, recorded directly in accumulated other comprehensive income (AOCI).

In February 2007, the FASB issued SFAS No. 159, The Fair Value Option for Financial Assets and Financial Liabilities, a standard that provides companies with an option to report selected financial assets and liabilities at fair value. The standard requires companies to provide additional information that shows the effect of the company s choice to use fair value on its earnings. It also requires entities to display the fair value of those assets and liabilities for which the company has chosen to use fair value on the face of the balance sheet. The new statement does not eliminate disclosure requirements included in other accounting standards, including requirements for disclosures about fair value measurements included in FASB Statements No. 157, Fair Value Measurements, and No. 107, Disclosures about Fair Value of Financial Instruments. This statement is effective as of the beginning of an entity s first fiscal year beginning after November 15, 2007. We will be evaluating the impact SFAS No. 159 will have on our financial statements during 2007.

### **C. Research and Development**

Vivo maintains partnerships with the Universidade Federal do Rio Grande do Sul (UFRGS) and with Pontificia Universidade Católica do Rio Grande do Sul (PUCRS). Such partnerships permit Vivo to have laboratories at the universities, which conduct research and development of new technologies, and which support and push innovative processes. We also solidified a partnership at the end of 2004 with the Centro de Pesquisas e Desenvolvimento em Campinas - São Paulo (CPqD), to assess and study new technologies.

The Company incurred no significant cost in 2006, 2005 and 2004.

#### D. Trend Information

In 2007, the rate of growth in Brazil's cellular market is expected to exceed Brazil's economic growth. In addition, we expect continued strong competition from other operators, greater focus on data and value-added services, targeted growth on average revenue per user, and further enhancements related to customer service. We expect that we will maintain our leadership position in the Brazilian cellular market, focusing on differentiation in the development of integrated solutions and the application of new technologies. We plan to continue to offer services and products of high quality in order to meet our clients' expectations.

#### E. Off-balance sheet arrangements

As of December 31, 2006, there were no off-balance sheet arrangements. We have no majority-owned subsidiaries that are not included in our consolidated financial statements, nor do we have any interests in, or relationships with, any special purpose entities that are not reflected in our consolidated financial statements.

#### F. Tabular disclosure of contractual obligations

The following table represents our contractual obligations and commercial commitments as of December 31, 2006:

	<b>Payments due by Period</b>				
	<b>Total</b>	<b>Less than 1 year</b>	<b>1-3 years</b>	<b>4-5 years</b>	<b>After 5 years</b>
	<b>(in millions of reais)</b>				
Contractual obligations:					
Long-term debt(1)	4,405.7	1,495.7	1,761.7	148.3	1,000.0
Operating leases	2,893.4	341.9	658.5	604.3	1,288.7
Unconditional purchase obligations	125.9	85.7	40.2	-	-
Other long-term obligations(2)	63.8	37.2	26.6	-	-
<b>Total contractual cash obligations(3)</b>	<b>7,488.8</b>	<b>1,960.5</b>	<b>2,487.0</b>	<b>752.6</b>	<b>2,288.7</b>

(1) Includes short-term portions of long-term debt.

(2) Contracted long-term suppliers or contracted short-term suppliers with penalties for early termination and exclusivity fees paid to dealers.

(3) Excludes pension fund obligations.

In addition, we have a rental commitment with Telecomunicações de São Paulo S.A. Telesp, a related party, in an annual amount of R\$120.0 million, including all costs related to the rental of certain facilities used in providing telecommunications services, such as electrical and air conditioning equipment.

**ITEM 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES**

**A. Directors and Senior Management**

Our company is managed by a Board of Directors and a Board of Executive Officers. Our shareholders elect the members of the Board of Directors. The Board of Directors must have between three and twelve members, each serving a three-year term. The board currently consists of nine members. The terms of the current members of the board of directors will expire in April 2009. The Board of Directors hold regular quarterly meetings, and the chairman or two board members may call special meetings.

The following are the current members of our Board of Directors and their respective positions.

Name	Position	Date Elected
Luis Miguel Gilpérez López	Chairman	March 22, 2007

Name	Position	Date Elected
João Pedro Amadeu Baptista	Vice Chairman	May 10, 2006 March 26,
Shakhaf Wine	Director	2006
Félix Pablo Ivorra Cano	Director	March 26, 2006
Ignacio Aller Malo	Director	March 26, 2006
Rui Manuel de Medeiros D Espiney Patrício	Director	May 10, 2006
Luiz Kaufman	Director	March 26, 2006
Henry Philippe Reichstul	Director	March 26, 2006
António Gonçalves de Oliveira	Director	March 26, 2006

Set forth below are brief biographical descriptions of our directors.

*Luis Miguel Gilpérez López*, born on December 7, 1959, is General Director of the Mobile division of Telefónica International and a member of the Supervisory Board of Brasilcel N.V. He was a board member of TCP, Celular CRT, TSD, TCO, Teleacre, Telegoiás, NBT, Telemat, Telems, TCO-IP S.A. and Teleron from 2004 to 2005. He began working for the Telefónica group in 1981, having assumed growing responsibilities in areas including networks, infrastructure, product and services development and marketing. He has a degree in Industrial Engineering and a master's degree in Business Administration.

*João Pedro Amadeu Baptista*, born on March 23, 1958, is currently the Vice Chairman of the Supervisory Board of Brasilcel N.V.; Vice Chairman of the Board of Directors of Vivo; Chairman of the Supervisory Board of Portugal Telecom - Investimentos Internacionais Consultoria Internacional, S.A.; PT Móveis - Serviços de Telecomunicações, SGPS, S.A.; PT Acessos de Internet WI-FI, S.A.; PT Ventures, SGPS, S.A.; Portugal Telecom Brasil, S.A. and Mobitel; member of the Board of Directors of Universo Online - UOL and Unitel, SARL; Chairman of the Manager Board of Directel, since 2006. He is a member of the Audit Committee of Victoria and Albert Museum em Londres, since 2005. Mr. Baptista was leader of the global team of telecommunications and partner of Booz Allen Hamilton, in the United Kingdom, from 2005 until 2006. Mr. Baptista was global leader for the group of technology, information and entertainment industry of March & McLennan Companies Inc., from 2004 until 2005. He was member of Executive Commission and partner of Mercer Management Consulting, from 1997 until 2005; global responsibility for the group of technology, information and entertainment, from 2000 until 2005; co-leader for the United Kingdom, from January 2001 until 2005. He holds a degree in Engineering Mechanics, a post-graduate degree in Energy from the Federal Polytechnical Scholl of Lausanne, Switzerland, and a MBA from Stanford Graduate School of Business, Stanford, CA, EUA.

*Shakhaf Wine*, born on June 13, 1969, is the President of Portugal Telecom Brasil S.A, an executive board member of PT Investimentos Internacionais S.G.P.S., a member of the board of directors of Brasilcel N.V. and a member of the board of directors of Vivo and Universo Online S.A. Previously Mr. Wine was a board member at TCP, TCO, TSD, Celular CRT and Banco1.Net S.A. Before joining Portugal Telecom in April 2003, Mr. Wine was a Director of Investment Banking and a Relationship Manager for European corporate clients in the Global Telecommunications Group of Merrill Lynch International from 1998 to 2003, based in London. Additionally, he was Senior Associate

Director of the Latin American and Telecommunications groups of Deutsche Morgan Grenfell from 1993 until 1998, also based in London. Previously Mr. Wine was a foreign exchange trader and dealer for the Brazilian Central Bank at Banco Icatu S.A. He holds a degree in Economics from the Pontificia Universidade Católica do Rio de Janeiro.

*Félix Pablo Ivorra Cano*, born on July 1, 1946, was the President of the Board of Directors from February 1999 to September 2005. Mr. Ivorra is currently a member of the Boards of Directors of Telecomunicações de São Paulo S.A., Brasilcel N.V, Vivo Participações. He was a member of the Board of Directors of TSD, TLE, TCO and Celular CRT until February 2006. He joined the Telefónica Group in July 1972 and served in the areas of Technical Specifications, Network Planning, Commercial Planning and as General Director of Advanced Communications. In 1993, he was appointed General Director of the team that founded Telefónica Servicios Móviles, where he held several positions including General Commercial Director and General Director of Business Development until January 2006. During 1997 and part of 1998, he was chairman of the board of Telefónica Móviles group companies Mensatel, S.A. and Radiored, S.A. He has a degree in Telecommunications Engineering from Escola Técnica

Superior de Engenharia ETSI in Madrid, and a post-graduate degree in Business Administration from the Instituto Católico de Administração de Empresas ICADE also in Madrid.

*Ignacio Aller Malo*, who was born on December 1, 1945, is a member of the Board of Directors of Telefónica Móviles México, S.A. de C.V., Brasilcel N.V, Vivo Participações, S.A. He was a member of the Board of Directors of TSD, TLE and Celular CRT until February 2006. Mr. Aller has served as Chief Operating Officer of Telefónica Móviles S.A. since 2003 and has held several positions at Telefónica de España since 1967.

*Rui Manuel de Medeiros D Espiney Patrício*, born on August 17, 1932, is a member of the Board of Directors of Monteiro Aranha S.A., Monteiro Aranha Participações, Klabin S.A., Vivo, Jerónimo Martins (Portugal) and Espirito Santo International Holding. He was a member of the Board of Directors of Banco Boavista S.A. from 1997 until 2000; member of the Board of Directors of Banco Inter-Atlântico S.A. from 1980 until 1997, member of the Board of Directors of Ericsson do Brasil from 1979 until 1997, Managing Director and Executive Vice-President of Monteiro Aranha S.A. from 1976 until 1992, Representative of the Monteiro Aranha Group in Europe from 1975 until 1976, and worked at Financiadora Volkswagen do Brasil from 1974 until 1975. Mr. Patrício was Minister for Foreign Affairs of Portugal from 1970 until 1974, Under-Secretary of State for Overseas Economic Development of Portugal from 1965 until 1970, Member of the Commission for Overseas Development Plan from 1963 until 1965, Economic Advisor of Sacor (Oil Company) from 1958 until 1964, and between 1958 and 1963 he was Assistant Professor at Lisbon University. Mr. Patrício has a degree in Law from the University of Lisbon 1955, a post-graduate degree in Political Economics from University of Lisbon 1956 and Business Administration from Fundação Getúlio Vargas (São Paulo) 1975.

*Luiz Kaufmann*, born on August 7, 1945, has been a member of the Board of Directors and Audit Committee of Vivo since July 2005. He was a member of the Board of Directors and Audit Committee of TSD, TLE, TCO and Celular CRT, since July 2005 and until February 2006. Mr. Kaufmann is President and CEO of Medial Saude S/A, a health care company. Mr. Kaufmann is also a member of the Board of Directors of Gol Linhas Aéreas Inteligentes and chairman of its audit committee. Mr. Kaufmann is a partner at L. Kaufmann Consultores Associados, a boutique investment bank, through which Mr. Kaufmann was in charge of the turn-around and sale of Vésper Brazil from May 2001 to November 2003 and in the turn-around and sale of Primesys from October 2004 to October 2005. Mr. Kaufmann was partner of GP Investimentos from 1999 to 2001 and a Board member of several companies controlled by GP, CEO of Aracruz Celulose S.A. and Chairman of the Board of Directors of Tecflor from November 1993 to April 1998. Previously he spent several years as Managing Director of Arthur D. Little in Brazil. Mr. Kaufmann began his career at Serete S.A. Engenharia as project engineer in 1968, rising to the position of Director of Finance and Control by 1974. Mr. Kaufmann then held various other executive positions prior to those described above. Mr. Kaufmann holds a degree from Universidade Federal do Paraná and a Master of Sciences in Industrial Engineering from Illinois Institute of Technology.

*Henry Philippe Reichstul*, born on April 12, 1949, is a member of the Board of Directors and Audit Committee of Vivo since July 2005. He was a member of the Boards of Directors and Audit Committees of TSD, TLE, TCO and Celular CRT, since July 2005 and until February 2006. Mr. Reichstul is also a member of the Boards of Prisma Energy International, TAM-Linhas Aéreas S.A., Pão de Açúcar Group, Repsol YPF S.A., Member of the Advisory Board of Lhoist do Brasil Ltda, Member of the Consulting Board of Peugeot Citroen do Brasil, Member of the Strategic Board of ABDIB-Associação Brasileira da Infra-Estrutura e Indústrias de Base, Member of Coinfra-Conselho Superior da Infra-Estrutura da FIESP, and Vice Chairman of the Board of the Brazilian Foundation for Sustainable Development. Mr. Reichstul was the Chief Executive Officer of Petrobrás Petróleo Brasileiro S.A. from March 1999 to December 2001 and was the Chief Executive Officer of Globopar in 2002. Prior to that time, Mr. Reichstul held various positions as an economist and as an executive. Mr. Reichstul has served on the Boards of Directors of Telebrás from 1985 to 1986, Eletrobrás Centrais Elétricas S.A. from 1985 to 1987 and BNDES from 1986 to 1989. Mr. Reichstul holds a degree in Economics from *Universidade de São Paulo* and did post-graduate

work at Hertford College of Oxford University.

*Antonio Gonçalves de Oliveira*, born on May 4, 1944, is currently a member of the Board of Directors and Audit Committee of Vivo since July 2005, and a member of the Board of Directors of TCP, since March 2001. Mr. Gonçalves de Oliveira was a member of the Boards of Directors and Audit Committees of TSD, TLE, TCO and Celular CRT, since July 2005 and until February 2006. He is a member of the Board of Auditors of COELBA -



Companhia de Eletricidade da Bahia, since April, 2006 at the appointment of *Caixa de Previdência dos Funcionários do Banco do Brasil*, a large Brazilian pension fund and shareholder of COELBA, President of AAMAC - Associação de Amigos do Museu de Arte Contemporânea da USP, an important participant in the contemporary cultural scene (2004/2006) and member of the council of representatives of FIESP (Federation of Industries of the state of Sao Paulo) (2003/2007). Mr. Gonçalves de Oliveira is also a member of the Social and Economic Development Council of the Brazilian Government, a board member of the Small and Medium Company Working Group sponsored by the Brazilian Government, the vice president of the Brazilian Businessmen's Association for Market Integration (ADEBIM), a member of the orientation and steering council of Banco do Povo do Estado de São Paulo and President of the decision council of the National Employee Association of Banco do Brasil (ANABB). From 1991 to 1995, he served as director of the Latin American Sociology Association and from 1993 to 1994 he served as the executive coordinator of the Small and Medium Company National Movement (MONAMPE). He holds a degree in Social Sciences from the University of São Paulo, Brazil, and a master's degree in Communication Sciences from the same university.

In accordance with the shareholders' agreement between Portugal Telecom SGPS, S.A., PT Movéis SGPS, S.A. and Telefónica Móviles S.A., PT Movéis is responsible for the appointment of our Chief Executive Officer and Telefónica Móviles is responsible for the appointment of our Chief Financial Officer. PT Movéis appointed three and Telefónica Móviles appointed three of the nine members of our Board of Directors.

### **Board of Executive Officers**

Our by-laws provide for a Board of Executive Officers with six positions, each elected by the Board of Directors for a term of three years. Our Board of Executive Officers currently has six members. In the absence or temporary inability to perform his duties, the Chief Executive Officer will be replaced by the Executive Vice President of Finance, Planning and Control. In the case of a vacancy in any position on the Board of Executive Officers, the respective replacement shall be appointed by the Board of Directors; in case of any inability, the Chief Executive Officer shall choose a replacement for that officer among the remaining officers. One officer may be elected for more than one position on the Board of Executive Officers, but the members of the Board of Executive Officers cannot be elected to the Board of Directors. The Board of Directors may remove executive officers from office at any time.

The following are the current executive officers and their respective positions.

<b>Name</b>	<b>Position</b>	<b>Date appointed</b>
Roberto Oliveira de Lima	Chief Executive Officer	April 12, 2006
Ernesto Gardelliano	Executive Vice President of Finance, Planning and Control and Investor Relations Officer	April 12, 2006
Paulo Cesar Pereira Teixeira	Executive Vice President of Operations	April 12, 2006
Eduardo Aspesi	Executive Vice President of Marketing and Innovation	October 10, 2006
Javier Rodríguez García	Vice President of Networks	April 12, 2006
Sérgio Assenço Tavares dos Santos	Vice President of Regulatory Matters	April 12, 2006

Set forth below are brief biographical descriptions of our executive officers.

*Roberto Oliveira de Lima*, born on April 1, 1951, is Chief Executive Officer of Vivo, Vivo S.A. and TCO-IP S.A. and formerly of TCO, Telerj, Telest, Telebahia, Telergipe, Celular CRT, TC, GT, Telegoiás, Telemat, Telems,

Teleacre, Teleron and NBT. Mr. Oliveira de Lima has also been a director of Avista Participações Ltda., Tagilo Participações Ltda., Sudestecel Participações Ltda., TBS Celular Participações Ltda., Ptelecom Brasil S.A., Portelcom Participações S.A. and all affiliates of Brasilcel, since 2005. He was the Chief Executive Officer of TSD, TLE and Celular CRT until February 2006. Mr. Oliveira de Lima was Chairman of the Board of Directors of Grupo Credicard from 1999 to 2005 and Chief Executive Officer of Banco Credicard S.A. from 2002 to 2005. Before 1999, Mr. Oliveira de Lima held executive positions at Accor Brasil S.A., Rhodia Rhone Poulec S.A. and Saint Gobain S.A. Mr. Oliveira holds a degree in Administration and an MBA from Fundação Getulio Vargas, Brasil, and a master's degree in finance and strategic planning from Institute Superieur des Affaires, Jouy en Josas, France. Mr. Oliveira is a Brazilian citizen.

*Ernesto Gardelliano*, born on January 15, 1962, is Executive Vice President of Finance, Planning and Control and Investor Relations Officer of Vivo, Vivo S.A. and TCO-IP S.A. and formerly of TCO, Telerj, Telest, Telebahia, Telergipe, Celular CRT, TC, GT, Telegoiás, Telemat, Telems, Teleacre, Teleron and NBT. Mr. Gardelliano has also been a director of Avista Participações Ltda., Tagilo Participações Ltda., Sudestecel Participações Ltda., TBS Celular Participações Ltda., Ptelecom Brasil S.A., Portelcom Participações S.A. and all affiliates of Brasilcel. He joined Coopers & Lybrand in Argentina in 1984 where he developed his career in the Audit Department. During 1990, Mr. Gardelliano was transferred to Italy. In January 1993, he joined Movicom, the first mobile telecom operator in Argentina. The Company was a Joint Venture led by BellSouth and Motorola. Mr. Gardelliano acted as the Financial Controller until 1997, when he was promoted to Chief Financial Officer. In 2005, and after the sale of the Latin American Assets of BellSouth, he became Regional Director for Argentina, Chile and Uruguay for Telefónica Móviles and transferred to Brazil to take over responsibilities in the Finance area of the above mentioned Companies, namely Vivo. Mr. Gardelliano is a Certified Public Accountant, a graduate of the University of Buenos Aires and holds a degree in Upper Management from the Instituto de Altos Estudios at the Universidad Austral.

*Paulo Cesar Pereira Teixeira*, born on June 18, 1957, is the Executive Vice President of operations of Vivo since 2003, Vivo S.A. and TCO-IP S.A. and formerly of TCO, Telerj, Telest, Telebahia, Telergipe, Celular CRT, TC, GT, Telegoiás, Telemat, Telems, Teleacre, Teleron and NBT. Mr. Teixeira is also a director of Avista Participações Ltda., Tagilo Participações Ltda., Sudestecel Participações Ltda., TBS Celular Participações Ltda., Ptelecom Brasil S.A. and Portelcom Participações S.A. He was the Executive Vice-President of Operations of TSD, TLE and Celular CRT until February 2006. Since 1998 Mr. Teixeira has acted as Vice-President of Telerj, Telest, Telebahia, Telergipe, Celular CRT and he was member of the Board of Directors of TSD, TLE and Celular CRT from 2001 until 2003. In 1998 he was a Director of Telepar, Telesc and CTMR Celular S.A., companies of Telecomunicações Brasileiras S.A. Telebrás, and Vice President of Tele Celular Sul S.A. Mr. Teixeira was Director of telecommunications engineering of Mato Grosso do Sul S.A. Telems, a company of Telecomunicações Brasileiras S.A. Telebrás, from 1995 through 1998. During 1995, he was a Department Manager of investment management. In 1994 he was an Assistant to the Director of Engineering. From 1990 until 1994, Mr. Teixeira served as Divisional Manager of coordination and expansion of Telebrás Holdings. Mr. Teixeira was engineer in the areas of service development and investment control of Telebrás Holding from 1988 through 1990. From 1980 until 1987, Mr. Teixeira performed several different managerial duties at Companhia Riograndense de Telecomunicações S.A. CRT and was also a member of the board of directors from 1985 to 1986. In 1987 and 1988, he held several different positions at Telebrás affiliates. Mr. Teixeira holds an Electrical Engineering degree from the Catholic University of Pelotas, Brazil.

*Javier Rodríguez García*, born on December 8, 1955, is Executive Vice President of Technology and Networks Vivo, Vivo S.A. and TCO-IP S.A. since April 2005. He was the Executive Vice President of Technology and Networks of TSD, TLE and Celular CRT, until February 2006 and of Telerj, Telest, Telebahia, Telergipe, Celular CRT, TC, since May 2003, TCO, Telegoiás, Telemat, Telems, Teleacre, Teleron and NBT, until October 2006. From 1986 until 1988, Mr. García worked at INDELEC Indústria Electrónica de Comunicaciones S.A., as the manager responsible for the implementation of an automatic mobile telecommunications project for Telefónica de España S.A. From 1988 until 1990, he worked at Rede Electrica de España S.A. as the person responsible for the installation and maintenance of radio mobile systems in Spain. From 1990 until 1992, Mr. García served as an engineering manager at Telcel S.A., where he was responsible for the implementation of automatic mobile telecommunications system for Telefónica de España S.A. in Barcelona, Madrid and Palma de Mallorca. From 1992 until 1996, he was an engineering manager responsible for the installation and maintenance of systems at Compañia Europea de Radiobusqueda S.A., and from 1996 until 1998, he worked in cellular businesses for Telefónica Group in Spain and Peru, as a network quality manager and technical area sub-manager, respectively. From 1998 until 2000, Mr. García was the technology manager in the cellular business of Telefónica Group in Brazil and from 2000 until 2003 was the network manager of Telerj and Telest He holds a degree in Technical Telecommunications Engineering from the Technical University of Madrid, Spain.

*Sérgio Assenço Tavares dos Santos*, born on June 3, 1948, is the Vice President of Regulatory Matters of Vivo Participações, Vivo S.A., and TCO-IP S.A. From January 2006 until February 2006, he was a Vice-President of Regulatory Matters and Institutional Relations of TSD, Celular CRT and TLE and from January 2006 until October 2006, Mr. Tavares dos Santos was a Vice-President of Regulatory Matters and Institutional Relations TCO, Telerj, Telest, Telebahia, Telergipe, Celular CRT, TC, Telegoiás, Telemat, Telems, Teleacre, Teleron, NBT. From October

2004 until December 2005, he was the Regional Director of TCO and subsidiaries, including NBT; from January 2003 until September 2004, he was the President and Vice-President of TCO and subsidiaries, including NBT; from October 1998 until December 2002, he was the Director of Engineering and Operations of TCO and subsidiaries, including NBT; from February 1998 until September 1998, he was Executive Vice-President of TCO, Telegoiás Celular, Telemat Celular, Telems Celular, Teleacre Celular and Teleron Celular. He was Director of Engineering and operations of Telecomunicações de Brasília S.A. Telebrasília S/A, a fixed telecommunications company, between July 1995 and January 1998, and was also Manager of the Business Unit of Advanced Telecommunications of the Operations Department of Telebrasília from April 1994 until July 1995 and Assessor and Coordinator of Special Projects of the Engineering Department of Telebrasília from September 1993 until March 1994. He held several different positions at Telebrás from July 1990 until August 1993 and also held several different positions at Telebrasília between March 1976 and July 1990. Mr. Assenço holds an Electrical Engineering degree from Brasília University, Brazil. Mr. Assenço is a Brazilian citizen.

*Eduardo Aspesi*, born on August 13, 1959, is the Executive Vice President of Marketing and Innovation of Vivo Participações, Vivo S.A and TCO-IP S.A. He was General Manager of Hispamar Satélites S.A. from 2005 until October 2006. Mr. Aspesi was Retail Superintendent Director of Telemar between 2001 and 2004. From 1999 until 2001, he was General Director of RBS Direct. Mr. Aspesi was Marketing and New Business Director of Net Sul Comunicações S/A from 1994 until 1999. He worked of Rádio e TV Gaúcha, between 1991 and 1994. From 1985 until 1991, he held several different positions at RBS Group. He was also Auditor and Department Chief of Companhia Estadual de Energia Elétrica Rio Grande do Sul (CEEE), from 1982 until 1985. He holds a degree in Administration from Pontifícia Universidade Católica de Porto Alegre, RS and Economics from Federal University of Rio Grande do Sul. Mr. Aspesi holds a post-graduate degree in finance and marketing from the Federal University of Rio Grande do Sul.

## **Board of Auditors**

Brazilian Corporate Law requires us to have a Board of Auditors (*Conselho Fiscal*) which is composed of three to five members elected at the general shareholders meeting. The Board of Auditors operates independently from our management and from our external auditors. Its main function is to examine the financial statements of each fiscal year and provide a formal report to our shareholders. Our board of auditors consists of three members and three alternates and meets quarterly. Our Board of Auditors is elected annually at the annual general shareholders meeting.

The Board of Auditors is responsible for overseeing our management. Its main duties are:

- to review and provide an opinion on the annual report of our management;
- to review and approve the proposals of the management bodies to be submitted to the shareholders meeting regarding changes to share capital, issuance of debentures and subscription rights, capital investment plans and budgets, distributions of dividends, changes in corporate form, consolidations, mergers or split-ups; and
- to review and approve the financial statements for the fiscal year.

The Board of Auditors holds regular meetings every three months and special meetings when called by the President or by any member of the Board of Auditors.

Listed below are the current members of our Board of Auditors and their respective positions:

Name	Position	Date Appointed
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Claudio José Carvalho de Andrade (1)	Member	March 15, 2007
Paula Bragança França Mansur (2)	Member	March 15, 2007
Fabiana Faé Vicente Rodrigues (2)	Member	March 15, 2007
Daniel Vidal de Almeida (1)	Alternate	March 15, 2007
Norair Ferreira do Carmo (2)	Alternate	March 15, 2007
João Renato Pierre (2)	Alternate	March 15, 2007

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(1) Appointed by our preferred shareholders.

(2) Appointed by our controlling shareholder.

**B. Compensation**

For the year ended December 31, 2006, we paid our directors and executive officers, and the directors and executive officers of our subsidiary, as compensation an aggregate amount of R\$11.8 million, including bonuses and profit-sharing plans. This amount includes performance remuneration and profit-sharing arrangements applicable to all employees. Furthermore, the members of our Board of Executive Officers are eligible to participate in the same complimentary retirement pension plan available to our employees.

**C. Board Practices**

For more detailed information, see Directors and Senior Management Board of Executive Officers, and Directors and Senior Management Board of Auditors, above, and Item 9.C. The Offer and Listing Committees.

There are no service contracts between us or our subsidiary and any of our directors providing for benefits upon termination of employment.

**D. Employees**

At December 31, 2006, we had 5,896 full-time employees and 225 temporary employees.

The following table sets forth the number of our employees and a breakdown of employees by main category of activity as of the dates indicated:

	<b>December 31,</b>		
	<b>2006</b>	<b>2005</b>	<b>2004</b>
Total number of employees (including trainees)	5,896	6,084	6,350
Number by category of activity:			
Technical and operations area	1,865	1,437	1,565
Sales and marketing	2,117	2,347	2,706
Finance and administrative support	1,330	1,448	1,196
Customer service	584	852	883

Employees are represented by the *Sindicato dos Trabalhadores em Empresas de Telecomunicações e Operadoras de Mesas Telefônicas no Estado de São Paulo* (SINTETEL). We negotiate new collective-bargaining agreements every year with the labor unions. The collective-bargaining agreements currently in force include a salary increase of 2.9% and a benefit increase of approximately 12.5%, effective as of December 31, 2006.

Our management considers the relations between our workforce and us to be satisfactory. We have not experienced any work stoppage that materially affected our operations.

Each of our subsidiaries negotiates a new collective-bargaining agreement every year with each local union. The collective-bargaining agreements now in force expire on October 31, 2007.

At the time of the privatization, employees had the right to maintain their rights and benefits in *Fundação SISTEL de Seguridade Social*, or SISTEL, a multi-employer defined benefit plan that supplements government-provided retirement benefits. Under the SISTEL plan, we made monthly contributions to SISTEL equal to a percentage of the salary of each employee who was a SISTEL member. Each employee member also made a monthly contribution to

SISTEL on the basis of age and salary. Members of SISTEL qualified for pension benefits when they qualified for the government-provided retirement benefits. SISTEL operates independently from us, and its assets and liabilities are fully segregated from us. Employees hired since January 1999 are not members of SISTEL.



Before December 1999, the SISTEL plan covered the employees of the former Telebrás System and we were contingently liable for all of the unfunded obligations of the plan. In January 2000, we and the other companies that formerly belonged to the Telebrás system agreed to divide the existing SISTEL plan into 15 separate plans, resulting in the creation of private plans covering those employees already enrolled in the SISTEL plan. These new private pension plans are still administered by SISTEL and have retained the same terms and conditions of the SISTEL plan. The division was carried out so as to allocate liability among the companies that formerly belonged to the Telebrás system according to each company's contributions with respect to its own employees. Joint liability among the SISTEL plan sponsors will continue with respect to retired employees, who will necessarily remain members of the SISTEL plan.

We maintained the plans *TCPPREV*, *TCOPREV* and *VISÃO CELULAR*, new private pension plans for our employees. Unlike SISTEL's defined benefits plan, the plans *TCPPREV* and *Visão Celular* call for defined contributions by our operating subsidiaries, as sponsors, and by our employees, as participants. *TCOPREV* is a variable contribution plan. As of December 31, 2006, 60.1% of our employees were members of these plans. We continue to have a contingent liability for the unfunded obligations of the plans with respect to all inactive employees of the former Telebrás system and all post-retirement healthcare benefits for former Telebrás employees and current employees that have not changed to the new plan.

### E. Share Ownership

As of December 31, 2006, each of the members of the Board of Directors and the Board of Executive Officers owned, directly or indirectly, less than 0.01% of any class of our shares. We do not offer stock option plans to any of our directors or employees.

## ITEM 7. MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

### A. Major Shareholders

The following table sets forth the principal holders of common and preferred shares and their respective shares as of December 31, 2006:

Name	Number of common shares owned	Percentage of outstanding common shares	Number of preferred shares owned	Percentage of outstanding preferred shares
Brasilcel	222,877,507	42.5	364,350,055	39.7
Sudestecel Partic Ltda (1)	88,255,178	16.8	1,224,498	0.1
TBS Celular Partic Ltda (1)	68,818,554	13.1	1,165,797	0.1
Portelcom Partic. S.A. (1)	67,349,733	12.8	1,843	(2)
Tagilo Partic. Ltda (1)	12,061,046	2.3	22,625,728	2.5
Avista Partic. Ltda (1)	9,630,458	1.8	46,613,811	5.1
All directors and executive officers as a group	42	(2)	1,759	(2)

(1) Subsidiary of Brasilcel.

(2) Less than 1% of aggregate.

Any significant change in the percentage ownership held by any major shareholders during the past three years is disclosed in Item 4.A. Information on the Company Our History and Development and Item 4.C. Information on the Company Organizational Structure.

We are not aware of any other shareholder owning more than 5.0% of the common shares.

Brasilcel does not have different voting rights, but as a result of owning more than 50.0% of our common shares, it has the ability to control the election of our Board of Directors and the direction of our future operations. See also Item 4.A. Information on the Company Our History and Development Brasilcel.

**B. Related Party Transactions**

The main transactions with unconsolidated related parties are as follows:

- Use of network and long-distance (roaming) cellular communication: These transactions involve companies owned by the same controlling group: Telecomunicações de São Paulo S.A. - Telesp and subsidiaries. Some of these transactions were established based on contracts signed by Telebrás with the concessionaire operators during the period prior to privatization, when conditions were regulated by ANATEL. These transactions also include call-center services to Telecomunicações Móveis Nacionais – TMN customers in connection with roaming services in the Company's network.
- Technical assistance: Refers to the provision of corporate management advisory services by Portugal Telecom, SGPS, S.A. and technical assistance by Telefónica S.A., Telefónica International S.A. and TBS Celular Participações S.A., based on a percentage of the net services revenue, monetarily restated in accordance with the currency variation.
- Corporate services: These are passed on to the subsidiary at the cost incurred for these services.
- Call-center services: Provided by Atento Brasil S.A. and Mobitel S.A. – Dedic to users of the telecommunications services of the subsidiary, contracted for 12 months and renewable for the same period.
- Systems development and maintenance services: Provided by Portugal Telecom Inovação Brasil S.A.
- Maintenance: Maintenance of the modular profitability analysis system (MARE) and cost control system by Telefónica Mobile Solution do Brasil Ltda., contracted for 12 months, renewable for an equal period.
- Allocation of corporate costs: With operators of the same group, allocated at the cost incurred for the services.
- Operating logistical services, accounting and financial assistance: Provided by Telefónica Serviços Empresariais do Brasil Ltda.
- Voice content portal service provider: Provided by Terra Network Brasil S.A.

We have engaged in a number of other transactions with related parties. See Note 34 to our financial statements.

**C. Interests of Experts and Counsel**

Not applicable.

**ITEM 8. FINANCIAL INFORMATION****A. Consolidated Statements and Other Financial Information**

See Item 3.A. Key Information – Selected Financial Data and Item 18. Financial Statements.

**Legal Matters**

We are party to several administrative and legal proceedings that, if decided adversely, could have a material adverse effect on our business, financial condition and results of operations. We have recorded provisions in our

financial statements equivalent to the full amount of the estimated losses associated with those claims where the likelihood of an unfavorable outcome is deemed probable by our legal counsel. However, we do not record provisions in those instances where the likelihood of an unfavorable outcome is deemed possible or remote by our legal counsel. Below is a summary of our material pending administrative and legal proceedings:

## *Civil*

### *Consumer s rights*

We are a party to several law suits brought against us by individual consumers or civil associations representing consumers rights that allege our failing to properly provide our products and services. None of these law suits are individually material. Based on the opinion of our counsel, we believe that probable losses with respect to these claims total approximately R\$123.2 thousand, an amount for which we have made provisions, and that possible losses with respect to these claims total approximately R\$264.0 thousand.

### *ANATEL*

We are also part of several administrative and legal actions brought by Anatel that allege non-compliance with regulatory requirements related to SMP service, in the approximate total amount of R\$12.7 thousand. Based on the opinion of our counsel, we believe that the likelihood of unfavorable outcomes with respect to these claims are probable.

### *Breakup of Telebrás*

Telebrás, our legal predecessor, is a defendant in a number of administrative and legal proceedings and is subject to various claims and contingencies. Under the terms of the Telebrás breakup, the liability for any claims arising out of acts committed by Telebrás prior to the effective date of the breakup remains with Telebrás, except for labor and tax claims (for which Telebrás and the companies incorporated as a result of the breakup are jointly and severally liable by operation of law) and any liability for which specific accounting provisions have been assigned to us or one of the other companies incorporated as a result of the breakup of Telebrás. In addition, the legality of the breakup of Telebrás has been challenged in numerous legal proceedings, some of which have not been dismissed and are still pending. We believe, based on the opinion of outside counsel, that the likelihood of an unfavorable outcome with respect to these claims is remote.

### *Tax Credits*

Vivo and the other new holding companies incorporated in connection with the privatization of the telecommunications companies offset certain tax debts against the premiums paid by their controlling shareholders. A claim was filed against all the new holding companies, including Vivo and TCO, seeking relief in the form of the annulment of the administrative acts that recognized these offsets. Although we believe that the restructuring was implemented in accordance with Brazilian law, we believe, based on the opinion of outside counsel, that the likelihood of an unfavorable outcome with respect to this claim is possible. We would be required to pay all the taxes that were offset against goodwill. We are unable to determine at this time the extent of any potential liabilities with respect to this claim.

### *Ownership of Caller ID*

*Lune Projetos Especiais Telecomunicação Comércio e Ind. Ltda.*, a Brazilian company, filed lawsuits against 23 wireless telecommunications operators, including Telesp Celular Participações and its subsidiaries. The lawsuits allege that those operators violated patent number 9202624-9, related to *Equipamento Controlador de Chamadas Entrantes e do Terminal do Usuário*, or Caller ID, granted to Lune by the Brazilian Intellectual Property Agency INPI, on September 30, 1997. Lune calls on the operators to cease to provide Caller ID services and seeks payment from them for the unauthorized use of the Caller ID system in an amount equivalent to the payment of fees received by such operators for use of the Caller ID system. However, Lune s right to use patent number 9202624-9 was suspended by a

federal judge in response to a lawsuit filed against Lune and INPI by *Ericsson Telecomunicações S.A.*, *TC* and *Telerj Celular* filed identical lawsuits against Lune and INPI and those lawsuits are still pending before the courts. In connection with this proceeding, a third company, Sonintel, and its two partners also brought an *Ação de Oposição*, whereby they reinvoked their rights to a previous patent related to Caller ID, and to which the above mentioned patent (number 9202624-9) was linked. We believe, based on the opinion of outside counsel that the likelihood of an unfavorable outcome with respect to Lune's claim against us is possible. We are unable to determine at this time the extent of any potential liabilities with respect to this claim.

### *Validity of Prepaid Plan Minutes*

We and our subsidiary, together with other Brazilian wireless telecommunications operators, are defendants in various lawsuits brought by the public prosecutor's office and consumer protection associations challenging the imposition of a deadline for the use of purchased prepaid minutes. The plaintiffs allege that purchased prepaid minutes should not expire after any specified deadline. Conflicting decisions have been issued by the courts reviewing this matter. Although we believe that our criteria for imposing the deadline is in compliance with ANATEL's rules, we believe, based on the opinion of outside counsel, that the likelihood of an unfavorable outcome with respect to this claim is possible.

### *Litigation Relating to the Charging of a Monthly Subscription Fee*

*GT, Telegoiás Celular* and *Telems Celular*, together with other mobile telecommunications operators, are defendants in class action suits brought by the federal public prosecutor's office and local agencies for consumers protection, which challenged the charging, by these operators, of monthly subscription tariffs, alleging that there is no legal provision authorizing such a charge. According to the plaintiff, the charging of monthly subscription tariffs also violates Brazilian Consumer Law.

Based on the opinion of our legal counsel, we believe that the possibility of an unfavorable decision in this lawsuit is remote, given that the charging of monthly subscription tariffs is expressly allowed by Brazilian telecommunications regulations.

### *Litigation Relating to Telebrás Loans*

In June 15, 1999, TCO filed a lawsuit against *Tele Centro Sul* (one of the holding companies arising from the breakup of *Telebrás*, now *Brasil Telecom Participações S/A*), *Telebrás* itself and KPMG (the auditors during the breakup of *Telebrás*), regarding the distribution of debts and credits of former *Telebrás* loans, after its breakup.

In response to the lawsuit filed against it, *Brasil Telecom Participações S/A* filed two countersuits in October 1999 against *Telebrasília* (which has since merged into TCO) and *Telegoiás* seeking payment of the *Telebrás* loans in the amount of R\$41.3 million from TCO and R\$24.1 million from *Telegoiás*.

The lawsuit filed by TCO against *Brasil Telecom Participações S/A*, *Telebrás* and KPMG, was dismissed. In the two other lawsuits, filed by *Brasil Telecom Participações S/A* against TCO and *Telegoiás*, the court ruled partially in favor of *Brasil Telecom Participações S/A*. In the Court of Appeals of the Federal District, TCO's and *Telegoiás*' appeal was denied. *Brasil Telecom Participações S/A*'s appeal was granted. Since the Court of Appeals of the Federal District rendered unfavorable decisions in these actions, TCO filed an appeal to the Superior Court of Justice and has been awaiting trial since May 2004. On December 17, 2004, the plaintiff in these actions initiated an enforcement proceeding, claiming the amounts owed to be R\$91.5 million from TCO and R\$59.3 million from *Telegoiás*. On August 31, 2005, TCO and *Telegoiás* filed a motion to stay the enforcement, in which they challenge the amounts sought by the plaintiff and on which the court never ruled.

On October 20, 2006, we entered into a settlement agreement with the claimants in this action, whereby we paid R\$153 million to be released from all liability in connection with the claim.

### *Difference in Shares*

Various lawsuits were brought by fixed-subscribers against the holding companies created as a result of the breakup of the *Telebrás* system. *Celular CRT* is also named in these lawsuits, rendered by the predecessor company,

*Companhia Rio-Grandense de Telecomunicações*, currently *Brasil Telecom S.A.*, in the state of Rio Grande do Sul.

Prior to the privatization process, telecommunications network expansion was partially financed by plans under the Ministry of Communication's Order 1,361/76, which entitled fixed telephone line subscribers to receive a certain number of capital stock shares of the respective fixed telephone service provider, based on amounts that these subscribers have paid for their fixed phone line subscriptions.



The plaintiffs claim to have rights regarding contracts entered into by the predecessor telecommunication company for fixed phone line subscriptions. They claim that the amount they paid for their fixed telephone subscriptions would be convertible to a certain amount of the Company's shares after a 12-month subscription period.

The plaintiffs allege that the procedure by which the s