

# Report of the Board of Auditors to the Meeting of the Shareholders of Telecom Italia S.p.A. pursuant to Article 153 of Legislative Decree no. 58/1998

Dear Shareholders,

This report is made up of three separate sections: the First Section explains the activities performed by the Board of Auditors during the course of the financial year 2011 and up to today's date, as required by Consob Notice no. DEM/1025564 of 6 April 2001 and subsequent amendments and supplements; the Second Section provides an update on the specific activities of supervision and monitoring performed by the Board of Auditors during 2011 regarding the so-called Greenfield Project, that is to say the internal analysis initiated by the top management of Telecom Italia in relation to certain allegedly illegal acts committed in previous years to the detriment of the Company, and sets out the Board of Auditors' views of the results of this Project; the Third Section contains the report on the financial statements at 31 December 2011 of Telecom Italia Audit & Compliance Services S.c.a.r.l., a company incorporated into Telecom Italia S.p.A. with effect from 1 January 2012.

## First Section

During the 2011 financial year the Board of Auditors performed the supervisory activities required by the applicable legislation, also taking account of the principles of conduct recommended by CNDCEC (the Italian board of chartered accountants and accounting consultants) and the Consob notices on company controls and the activities of the Board of Auditors.

The Control Body has acquired the information necessary for the performance of the tasks of general supervision assigned to it by attending the meetings of the Board of Directors and board Committees (i.e. the Executive Committee, the Committee for Internal Control and Corporate Governance, the Nomination and Remuneration Committee), and by interviewing Company management, as well as by special analyses conducted directly or in joint meetings with the Committee for Internal Control and Corporate Governance.

1. On the basis of the information received and as a result of the analyses conducted by the Board of Auditors, it has become clear that the transactions carried out by the Company which have major impact on revenues, finances and assets, including transactions performed through companies in which the Company has a direct or indirect stake, are essentially made up as follows:
  - Sofora Telecomunicaciones S.A.  
On 13 October 2010 the Sofora – Telecom Argentina group became part of the consolidation perimeter of the Telecom Italia Group, after the latter increased its holding from 50% to 58%.  
During 2011, Telecom Italia Group made further purchases of shares, increasing its holding in the Telecom Italia Argentina group from 16.2% (at 31 December 2010) to 22.7% (at 31 December 2011). These operations have not changed the Telecom Argentina Group governance rights laid down in the agreement signed by Telecom Italia Group and its partner Wertheim, or the undertakings given by Telecom Italia Group to the Argentine antitrust authorities.
  - Sale of EtecS.A.  
The sale of the 27% of the share capital of Cuban operator EtecS.A. held by Telecom Italia International N.V. was completed on 31 January 2011.
  - Acquisition of control of the 4G group  
On 27 July 2011, after receiving the authorisation by Italian antitrust authority, Telecom Italia completed the purchase of 71% of the share capital of 4G Holding S.p.A., which holds 100% of 4G Retail S.r.l. The transaction was carried out through TLC Commercial Services S.r.l., a company wholly controlled by Telecom Italia.
  - Acquisition of licences to use LTE frequencies in Italy  
In the second half of 2011, Telecom Italia participated in the Procedure to assign use rights to frequencies in the 800, 1800, 2000 and 2600 MHz bands, throughout Italy, to be used to offer public landline broadband electronic communication services.  
These rights were formally adjudicated by the Italian Ministry for Economic Development on 3 October 2011; the rights were assigned in February 2012.

- Sale of Loquendo S.p.A.  
Loquendo S.p.A. was sold on 30 September 2011, and as a result the company was no longer included in the consolidation perimeter.
- Acquisition of control of Tim Fiber SP and Tim Fiber RJ  
On 31 October 2011 the process to acquire two companies in the AES Atimus group, a telecommunications infrastructure operator in the states of San Paolo and Rio de Janeiro (Brazil), by Companhia Brasileira de Energia through subsidiary Tim Celular S.A., was completed. This operation involved the purchase of all the share capital of Eletropaulo Telecomunicações Ltda (now Tim Fiber SP) and 98.3%, subsequently increased to 99.1%, of AES Communications Rio de Janeiro S.A. (Tim Fiber RJ). An offer to purchase the remaining 0.9% of the latter, concluded at the end of February 2012, brought the share owned to 99.7%.

In 2011 the following notes were issued:

- on 25 January 2011 Telecom Italia S.p.A. issued a note for the amount of Euro 1 billion, with coupon rate 5.125% and maturity on 25 January 2016.
- on 25 May 2011 Telecom Italia S.p.A. issued a note for the amount of Euro 750 thousand, with coupon rate 4.750% and maturity on 25 May 2018.
- on 20 October 2011 Telecom Italia S.p.A. issued a note for the amount of Euro 750 thousand, with coupon rate 7.00% and maturity on 20 January 2017.
- on 3 November 2011 Telecom Italia S.p.A. issued a note for the amount of Euro 250 thousand, with coupon rate 7.00% and maturity on 20 January 2017.

All the transactions indicated above are listed in the notes to the consolidated financial statements of the Telecom Italia Group and the notes to the separate balance sheet of Telecom Italia S.p.A., as well as in the report on operations for the year 2011. The Board of Auditors has verified that the above transactions comply with the law, the Company bylaws and the principles of correct administration, and has made sure that they were not manifestly imprudent or hazardous, in potential conflict of interest, or contrary to the resolutions adopted by the Shareholders' Meeting or likely to compromise the integrity of the corporate assets.

2. During the course of 2011 the Board of Auditors did not encounter atypical and/or unusual corporate transactions with third parties or related parties (including the companies within the Group).

The information relating to the principal infragroup transactions and with other related parties executed in the financial year 2011, and the description of their characteristics and economic effects is contained in the notes to the separate financial statements of Telecom Italia S.p.A. and to the consolidated financial statements of the Telecom Italia Group.

In terms of transactions with related parties, the Board of Auditors emphasises that, in compliance with the regulatory prescriptions by Consob contained in its Resolution no. 17221 of 12 March 2010 (and subsequent amendments and supplements), the Company has adopted an appropriate procedure which classifies transactions into different categories, applying to each of them a specific path to validation and approval, according to a structured procedure, explained in detail in the Report on corporate governance and share ownership for the financial year 2011 of Telecom Italia S.p.A., to which reference should therefore be made.

The Board of Auditors has overseen the conformity of the procedures adopted by the Company with the principles indicated by Consob, as well their observance.

3. Taking account of the size and structure of the Company and of the Telecom Italia Group, given that there were no atypical and/or unusual transactions, the Board of Auditors believes that the report on the Company's transactions with related and infragroup parties, given in the notes to the separate financial statements of Telecom Italia S.p.A. and in the notes to the consolidated financial statements of the Telecom Italia Group, should be considered adequate.
4. On 12 April 2012, Statutory Auditor PricewaterhouseCoopers issued the reports pursuant to Article 14 of Legislative Decree no. 39 of 27 January 2010, in which it states that the separate financial statements of Telecom Italia S.p.A. and the consolidated financial statements of the Telecom Italia Group at 31 December 2011 comply with the International Financial Reporting Standards (IFRS) adopted by the European Union, as well as with the provisions issued in implementation of Article 9 of Legislative Decree no. 38 of 2005, that they are drafted with clarity and that they represent truthfully and correctly the finances and assets of the company, the profit and loss results, and the cash flows of the Company and the Group.

Furthermore, the Statutory Auditor also considers that the report on operations and the information in subsection 1, letters c), d), f), l) and m) and subsection 2, letter b) of Article 123-bis of Legislative Decree no. 58 of 1998 (the so-called Consolidated

Finance Law, also referred to as “CFL”), presented in the report on corporate governance and share ownership, are consistent with the Company’s separate financial statements and the consolidated financial statements for the Group at 31 December 2011.

Telecom Italia is registered with the US Securities and Exchange Commission as a ‘foreign issuer’ and listed on the New York Stock Exchange, and is thus also subject to United States law. To this end it is the Board of Auditors that carries out the tasks required of an “Audit Committee” by US legislation.

In particular, in implementation of the obligations that derive from its role as Audit Committee of the Company, the Board of Auditors has adopted a specific procedure for the receipt, retention and treatment of ‘whistle blowing’ reports it receives since 2005. These reports may consist of:

- “complaints” from shareholders concerning what is considered to be improper behaviour;
- “complaints” or notifications, from anyone, shareholders or otherwise, concerning alleged anomalies, irregularities, misconduct or, more generally, any problem or issue which is thought to merit investigation by the Control Body;
- “complaints”, from anyone, concerning “accounting, internal accounting controls or auditing matters”,
- “concerns”, which may be submitted anonymously, from employees of the Company or the Group, concerning “questionable accounting or auditing matters”.

There are instructions on the Governance section of the Company’s website (Governance System – Procedures), for sending such whistle blowing reports to the Board of Auditors/Audit Committee of the Company.

5. In the period from 25 February 2011 to 29 March 2012, two complaints under Article 2408 of the Civil Code were made to the Board of Auditors. The investigations carried out by the Board of Auditors, and its assessments, are illustrated briefly below.

On 30 September 2011, a complaint of alleged improper behaviour regarding the selection of the professional consultant designated by Telecom Italia S.p.A. to work as representative in the Meeting of the ordinary shareholders in April 2011, pursuant to article 135-undecies of Legislative Decree no. 58/1998, and the resulting cost incurred, was received from a shareholder.

After performing the appropriate checks, the Board of Auditors acknowledged that the Company, in fulfilment of the new legal provisions, had appointed a professional expert in proxy voting services and assigned a lump sum fee for their services, and found no omissions or irregularities to report to the Shareholders’ Meeting of the Company.

On 14 December 2011, a complaint of alleged improper behaviour regarding – among other things – some press reports concerning the start of an investigation into the ex-Chairman of the Company, Marco Tronchetti Provera, was received from a shareholder. In particular, the shareholder emphasised that *“all the costs of illegal spying activities – for a sum of over 40 million euros – initially paid by Pirelli in 2003, subsequently became the burden of Telecom Italia, as evidenced by the financial statements for 2008, 2009 and 2010”*. The preliminary comment of the Board of Auditors was that the issue of the costs of the Security Function in the period from 2000 to 2007 has already been the subject of an audit by the Board of Auditors, as previously reported to the shareholders’ meetings in its reports on the financial statements for 2006, 2008, 2009 and 2010, and a further inquiry was undertaken as part of the internal investigation undertaken in the Greenfield Project. No new element emerged from the investigations undertaken by the Board of Auditors after receipt of this complaint.

For completeness, we would confirm that, as announced at the last meeting of the shareholders, the Company has formulated a request for reimbursement of approximately one million euros from Pirelli, relative to the operations wholly referable to Pirelli, charged to and paid for by Telecom Italia: the Board of Auditors will monitor how the situation develops.

6. Between 25 February 2011 and 29 March 2012 the Board of Auditors received fifteen reports (or groups of “reports”, treated as units in the case of several communications from a single individual, even if at separate times), which complained, for the most part, of technical service issues and failures of a commercial, accounting and administrative nature. The Board of Auditors investigated these complaints appropriately, with the support of the Group Compliance Officer and some Company departments, but no irregularities to be reported to the Shareholders’ Meeting have emerged to date.

7. Report on any appointments conferred on the statutory auditor and the corresponding costs

During the 2011 financial year Telecom Italia S.p.A. appointed PricewaterhouseCoopers S.p.A. to undertake various tasks other than audits of financial statements, the fees for which, before VAT, are summarised below:

<b>PricewaterhouseCoopers S.p.A.</b>	(in Euro)
Execution of agreed audit procedures on data used to draw up the profit and loss account and “reconstructed” balance sheet of the “fixed network services” perimeters.	50,000.00
Execution of agreed audit procedures on data used to draw up the profit and loss account and “reconstructed” balance sheet of the “mobile network services” perimeters.	40,000.00
Agreed procedures connected with the issue of the comfort letter in relation to the issue of notes that are part of the € 20,000,000,000 “Euro Medium Term Note Programme”.	145,000.00
Accounts auditing of the summary of costs for the staff engaged in research and development for Telecom Italia S.p.A. for the financial year 2010 allowed as deductible for the purposes of IRAP [Regional Tax], in accordance with Article 11, subsection 1, letter A) no. 5) of Legislative Decree no. 446/97 and subsequent amendments	20,000.00
Agreed procedures and declarations regarding tender bids	15,000.00
Activities connected with updating the €20,000,000,000 Euro Medium Term Note Programme:	40,000.00
Limited review of the abbreviated half-yearly consolidated financial statements of Telecom Italia S.p.A. at 30 June 2011, prepared in accordance with the IFRS issued by the International Accounting Standards Board for the purposes of Form 6-K for filing with the Securities and Exchange Commission (“SEC”)	18,000.00
Agreed due diligence procedures connected with the sale of a shareholding	150,000.00
Accounting advice and consultation activities carried out in financial years 2010 and 2011.	365,000.00
Accounting advice and consultation in relation to the Securities and Exchange Commission (“SEC”) review of the Telecom Italia S.p.A. Form 20-F 2010.	48,790.00
<b>Total</b>	<b>891,790.00</b>

8. In the course of the 2011 financial year, Telecom Italia S.p.A. conferred, also through its Branch Office in Argentina, a number of tasks on parties connected by continuing relationships with PricewaterhouseCoopers S.p.A. and/or on companies belonging to the latter’s international network (i.e. PricewaterhouseCoopers Advisory S.p.A. and Price Waterhouse & Co. Asesores de Empresas S.R.L.) for which the fees, excluding VAT, are summarised below:

<b>PricewaterhouseCoopers Advisory S.p.A.</b>	in euro
Additional audits regarding the examination of the sustainability report:	
• audit of the sustainability information and data of Telecom Argentina	15,000.00
• audit of the greenhouse gas emissions reported in the CDP (Carbon Disclosure Project) questionnaire	5,000.00
• audit of stakeholder consultation activities (5,000 euros per consultation)	5,000.00
<b>Total</b>	<b>25,000.00</b>

<b>Price Waterhouse &amp; Co. Asesores de Empresas S.R.L. (Argentina)</b>	in euro
Auditing the financial statements as at 31.12.2011 of "Sucursal Argentina" (Argentina Branch Office). Equivalent of 30,000 Argentinian Pesos (ARS) at the average exchange rate for financial year 2011: 1 Euro = 5.74419 ARS	5,223.00
Declarations on the documentation and accounts records of funds provided by Telecom Italia S.p.A. in favour of "Sucursal Argentina" (Argentina Branch Office), as required by the local Authorities. Equivalent of 12,000 Argentinian Pesos (ARS) at the average exchange rate for financial year 2011: 1 Euro = 5.74419 ARS	2,090.00
<b>Total</b>	<b>7,313.00</b>

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It should be noted that the Shareholders' meeting held on 29 April 2010, on the basis of the proposal put forward by the Board of Auditors, conferred the office of Statutory Auditor (separate financial statements of Telecom Italia S.p.A., annual consolidated financial statements, abbreviated half-yearly consolidated financial statements, annual report for the purposes of the US Laws) on PricewaterhouseCoopers S.p.A. for the nine year period 2010 -2018.

The auditor appointed by the Parent company Shareholders' Meeting is the main auditor for the entire Telecom Italia Group. To protect the independence of the appointed auditor, the Guidelines establish the principle under which the appointment of further assignments (when allowed by the reference regulations) is limited to the services and activities closely related to the audit of the financial statements. Conferment of a single further appointment is subject to the prior approval of the Board of Auditors of the Parent company; for some types of appointment ("preapproved appointments"), approval is given in advance. In each case, the Board of Auditors may establish the guidelines and quali-quantitative criteria regarding the appointment of auditors valid for the entire Group. Exercising this right, the Board of Auditors has requested that an operating procedure be introduced from 1 January 2012 that requires prior analysis by the Board of Auditors even for preapproved appointments, when particular qualitative conditions are present, or if specific quantitative thresholds are exceeded. The Board of Auditors would also make clear that, with an adequate flow of information, it will adopt the corresponding determinations made by the audit committees of the SEC registered subsidiary companies (i.e. TIM Participações S.A., Nortel Inversora S.A. and Telecom Argentina S.A.) provided they comply with the locally applicable law, U.S. law and the Group Guidelines on this subject.

The Board of Auditors acknowledged the request made by PriceWaterhouseCoopers S.p.A. to supplement their fee on a final account basis for auditing of the internal controls that govern the process of drafting the consolidated financial statements of the Telecom Italia Group, pursuant to section 404 of the Sarbanes-Oxley Act.

Regarding the additional audit activities connected to the acquisition of control of the Sofora Telecomunicaciones S.A. group, it should be noted that on 15 February 2011, PricewaterhouseCoopers S.p.A. had formulated a specific request to supplement their audit fee for the consolidated financial statements as at 31 December 2010, for the activities carried out in 2010, and for the consolidated financial statements as at 31 December 2011, for the activities to be carried out in 2011. In this context, the Board of Auditors acknowledged the PricewaterhouseCoopers S.p.A. communication in which the statutory auditor confirmed that the additional activities specified had been carried out and completed in 2011, detailing the audit hours and costs in line with the information contained in the aforementioned request for a supplement to its fees.

9. During 2011 the Board of Auditors issued a favourable opinion of the Senior Executive compensation package proposed (by the Nomination and Remuneration committee) for the three year period 2011-2013, pursuant to article 2389, subsection 3 of the Italian Civil Code.

The Board of Auditors issued a favourable opinion on the confirmation of Mr. Andrea Mangoni as the manager responsible for preparing the corporate accounting documents, pursuant to article 154-bis, subsection 1 of Legislative Decree no. 58/1998.

The incorporation into Telecom Italia of Telecom Italia Audit and Compliance Services S.c.a.r.l., previously identified as the internal control manager for Telecom Italia, has resulted – among other things – in the need to identify a new internal control

manager. Regarding this, the Board of Auditors expressed its favourable opinion, pursuant to the Self-Regulatory Code of the Company, of the appointment as internal control manager of Telecom Italia of Mr. Federico Maurizio d'Andrea, who previously represented Telecom Italia Audit and Compliance Services in this role.

See the Company Remuneration report published pursuant to article 123-ter of the CFL for information on the remuneration of the directors, general managers and executives with strategic responsibilities. The Board of Auditors acknowledges that, with the aforementioned document, Telecom Italia complies with the new requirement to apply with the aforementioned regulatory provision.

10. Over the course of financial year 2011, the Company's Board of Directors and Executive Committee held thirteen and five meetings, respectively, at which the Board of Auditors was always present.

The Committee for Internal Control and Corporate Governance met fourteen times (five of which jointly with the Board of Auditors, given the issues dealt with); the Nomination and Remuneration Committee met eleven times.

During 2011, there were thirty four meetings of the Board of Auditors (5 of which held jointly with the Committee for Internal Control and Corporate Governance, given the issues dealt with).

It should also be noted that the Board of Auditors attended all meetings of the Committee for Internal control and Corporate Governance and – from the renewal of the Board of Directors in April 2011 – was present at all meetings of the Nomination and Remuneration Committee, by the attendance of its Chairman or another Auditor designated by the Chairman.

The Board of Auditors took part in the Shareholders' Meeting, held on 12 April 2011.

11. In accordance with its obligations, the Board of Auditors obtained information and supervised compliance with the principles of correct administration, by constant attendance at the meetings of the Board of Directors, via interviews, direct observation, investigations, the receipt of information from the management of the Company, and meetings with the internal control manager, the manager responsible for preparing the corporate accounting documents and the Company Group Compliance Officer.

The Board of Auditors – occasionally through its Chairman – met the Executive Chairman, the Vice Chairman, and statutory auditor PriceWaterhouseCoopers S.p.A for the reciprocal exchange of relevant information and data pursuant to article 150, subsection three of the CFL, and attended the meetings of the Committee for Internal Control and Corporate Governance and the Nomination and Remuneration Committee.

The Board of Auditors believes that the governance arrangements and tools adopted by the Company constitute a valid supervisory framework to ensure that the principles of correct administration are respected in operational practice. In particular, in relation to the decision-making processes of the Board of Directors, the Control Body has supervised, including by attendance at board meetings, the compliance of management decisions made by the Directors with the law and the company by-laws, and checked that the related resolutions were adequately supported by information, analysis and audit processes – also involving consultation with the board subcommittees and external professionals, when necessary – regarding, primarily, the economic and financial consistency of transactions and their alignment with the interests of the Company.

12. The Board of Auditors has supervised the adequacy of the organisational structure of the Company, by collecting information from the appropriate structures, interviews with the managers of the various company departments, and meetings with those responsible for internal and external audit.

The Board of Directors plays an active role, in both the strategic guidance of the Company and in the control of operations, and the full board has the power to develop strategic policy and the responsibility to intervene directly in the most important decisions about the activities of the Company and the Group. In particular, the Board reserves to itself the right, among others:

- to review and approve the strategic, business and financial plans, as well as the budget;
- to review and approve strategic operations;
- to ascertain the adequacy of the organisational, administrative and accounting structure, with particular reference to the internal control system;
- to draw up and adopt the Company rules of corporate governance and to define the Group corporate governance guidelines; to define the limits, operating methods and intervals at which the delegated bodies must report on their activities;
- to appoint the offices of Chairman and Chief Executive Officer of subsidiaries of strategic importance;
- to supervise the general trend in operations, periodically comparing the results achieved with the results planned.

The attribution (and revocation) of powers to the Directors is reserved to the Board of Directors, which defines the object, limits and methods for the exercise of these powers, and receives a continuous flow of information on the activity carried out, the general trend in operations and the transactions of major impact on the revenues, finances and assets of the Company.

On 13 April 2011, following the renewal approved by the Shareholders' Meeting on 12 April 2011, the Board of Directors appointed Franco Bernabè Chairman of the Board and Chief Executive Officer, Aldo Minucci Vice Chairman and Marco Patuano Managing Director and Chief Operating Officer.

In addition to the power to legally represent the Company, as laid down in the Bylaws, and all the powers necessary for performing actions pertinent to the activity of the company in its various manifestations - to be exercised with a single signature - the overall governance of the Group, including coordination of the activity of the Managing Director and Chief Operating Officer, and the definition of the Company's strategic guidelines were conferred on the Chairman of the Board and Chief Executive Officer. The Chairman of the Board and CEO was also assigned responsibility for extraordinary transactions and extraordinary finance operations to be proposed to the Board of Directors.

The powers conferred on the Vice Chairman were the representation of the Company, as laid down in the Bylaws, in the event that the Chairman is absent or unable to act, and a proxy relating to the functioning of the internal control system.

In addition to the power to legally represent the Company, as laid down in the Bylaws, and to exercise, with a single signature, all powers required to perform actions pertinent to the activity of the company in its various manifestations, the Managing Director and Chief Operating Officer was made responsible for the overall governance of operations in Italy.

On 7 July 2011, after the alignment of the corporate structures with the organisational structure defined by resolution of the board on 13 April 2011, the Board of Directors approved the redefinition of the perimeter of the so-called managers with strategic responsibilities (also referred to as key managers or executive officers), including among them the temporary Managers of Administration, Finance and Control & International Development, Human Resources and Organization, Legal Affairs, National Wholesale Services, Public & Regulatory Affairs, Supply Chain & Real Estate, Technology, Consumer, Tim Brasil and Telecom Argentina, and confirmed the Senior Executives as strategic managers.

Moreover, after the organisational changes made to the Domestic division at the end of 2011 (i.e., the previously separate Top Clients and Public Sector departments merged into the Top Clients and Public Sector department), on 23 January 2012 the Board of Directors updated the board decisions of 7 July 2011, adding the temporary Manager of the Top Clients and Public sector department in the perimeter of the so-called key managers.

Regarding the new organisational structure of the Company, the system of management committees, focussed on the governance and operational integration of the activities of the group, was renewed in July 2011. The Board of Auditors would point out that the Group Committees System is an important element of the organisational structure, and, in particular, fulfils the aim of (i) monitoring the implementation of strategies and the development of plans; (ii) guaranteeing that the overall operations of the Group and specific businesses are monitored; (iii) strengthening the operational synergies needed between the different departments involved in technological, business and support processes.

The merger by incorporation of TI Audit and Compliance Services S.c.a r.l. into Telecom Italia came into effect on 1 January 2012. This operation is the result of a review of the control governance structure of the Telecom Italia Group that concentrates activity and expertise in control and compliance matters in the Parent company. After completion of the incorporation of this consortium company, the organisational model adopted places the group audit and compliance activities to report to the Vice Chairman of Telecom Italia, with delegated authority for the operation of the internal control system, without changing the reporting of the "operational" compliance function to the Domestic Managing Director.

Given the extremely complex structure of the Company and the Group, and having noted the opportunity identified by the Directors to focus on the resources based on the main business and geographic areas, taking into account that in a complex enterprise organizational systems are essentially subject to a permanently on-going evolution process, the Board considers the organizational structure of the Company and the Group to be adequate.

13. The internal control system is a set of rules, procedures and organizational structures that, through a process of identifying, measuring, managing and monitoring the principal risks, allows the sound, fair and consistent operation of the company in line with the pre-established objectives.

Pursuant to the Self-Regulatory Code that the Company has adopted, in exercising its responsibility for the internal control system the Board of Directors appoints as manager a person with an adequate level of independence and means suitable to perform this duty. The internal control manager is responsible for supporting the management and control boards in assessing

the adequacy, operation and effectiveness of the control system, and consequently for proposing corrective measures in case of irregularities and/or deficiencies. The internal control manager reports on his work to the Director delegated for this purpose, to the Board of Auditors and to the Committee for Internal Control and Corporate Governance.

The oversight role of the internal control manager is directed towards expressing an assessment in terms of reasonable certainty about the capacity of the internal control system to impact on the actual achievement of the objectives assigned to individual company structures (effectiveness profile), taking account of the rational use of resources for their realization (efficiency profile) in the light of the (qualitative/quantitative) risk factors present and the probability of their affecting the achievement of those objectives.

For the purposes of an overall assessment of the internal control system, the Manager takes as a methodological reference for his interventions the following components of the CoSo Report<sup>1</sup>:

- "Control environment" and "Information and Communication", which have a significant impact on, inter alia, oversight of the compliance and auditing methodologies, dissemination of the control culture and consolidation of the ethical values of the business;
- "Risk assessment" and "Control activities", which require a process of identifying and managing audit projects, as well as oversight of the compliance of processes and business operations with applicable laws and internal procedures of reference;
- "Monitoring", which requires the continuous performance of activities to control the business areas at the greatest risk, aimed at determining the effective overcoming of the weaknesses reported.

The Board of Auditors closely supervised the internal control system adopted by the Company and the Group, evaluating its adequacy, also through periodic meetings with the Manager responsible for internal control and with the audit and compliance structures, the statutory auditor, interviews with management and with the head of Enterprise Risk Management, joint meetings or attendance at meetings of the Committee for Internal Control and Corporate Governance and by acquiring documentation.

Up until 31 December 2011 the role of internal control manager was assigned to Telecom Italia Audit & Compliance Services S.c.a r.l., represented by its Vice Chairman (ex Chairman) and General Manager, Federico Maurizio d'Andrea.

In August the Boards of Directors of Telecom Italia and Telecom Italia Audit & Compliance Services approved a plan for merger by incorporation of the latter into the former, in accordance with the policy of reviewing the control governance structures of the Group, which concentrates activities and expertise in the matter of internal controls in the Parent company. The process of incorporation of Telecom Italia Audit & Compliance Services concluded with the drafting of the deed of merger in December 2011 and the incorporation consequently took effect from 1 January 2012.

In its meeting on 1 December 2011, given this process of integration, and in substantial continuity with the pre-existing situation, the Board of Directors of Telecom Italia assigned the role of internal control manager to Mr. D'Andrea, as Manager of the Audit Division of the Company. Favourable opinions were expressed on this choice by the Board of Auditors and the Committee for Internal Control and Corporate Governance.

The Board of Auditors has monitored the activities of the internal control manager, noting a positive evolution (in the various contexts) of the elements that make up the internal control system, and the fact that most of the improvements identified have been implemented by the management within the timescales specified. In general, audits have found that the principal improvement processes have regarded projects on network quality, further strengthening the security of the systems and network, commercial processes and oversight of subsidiary companies. In addition the audits have triggered improvements in the Group procedures system. In this context the Board of Auditors has also noted the overall assessment of the internal control system expressed by the internal control manager, which is reported in full below: "With reference to the specific operational contexts analysed, and considering the system weaknesses of various intensity identified by the audits on the one hand, and the regular (and practically integral) implementation of the defined improvement actions on the other, I believe that the current internal control system, as a whole, has reduced risk profiles to a level that is physiologically acceptable for the correct functioning of the processes.

As part of the aforementioned activity to monitor the adequacy of the internal control system, the Board of Auditors has also arranged a series of specific and in-depth meetings with the manager of the audit department Brazilian subsidiary TIM Participações S.A.; moreover, again in the context of monitoring the internal control system, the Board of Auditors has met with the Chairmen of the Boards of Auditors of the principal Italian subsidiaries and the Chairman of the Board of Auditors has met the Chairman of the Conselho Fiscal of Tim Participações, and the Chairman of the Comité de Auditoria of Telecom Argentina

As part of its verification of the adequacy of the internal control system to comply with legislative decree no. 231/2001, which disciplines the liability of organisations for unlawful administrative acts consequent on crime, the Board of Auditors reports

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<sup>1</sup> Control model developed by the Committee of Sponsoring Organisations (CoSO) of the Treadway Commission.

that Telecom Italia has adopted an Organisational Model designed to prevent the commission of criminal acts that might constitute liabilities for the Company. This Organizational Model is comprised of:

- (i) the Code of Conduct and Ethics of the Telecom Italia Group, which enunciates the general principles (transparency, fairness, loyalty) that guide the Company in the carrying out and management of business;
- (ii) the General Principles of Internal Control, i.e. the set of tools to provide a guarantee with regard to the objectives of efficiency and operational effectiveness, reliability of financial and management information, compliance with laws and regulations, safeguarding of assets against possible fraud;
- (iii) the Principles of Conduct, which introduced specific rules for relations with representatives of central or local government and for all compliance and activities of a corporate nature;
- (iv) the Schemes of Internal control, developed for all business processes at risk, both operational and instrumental.

The Organisational Model is subject to periodic revisions, both to take account of elements that have emerged from how it has worked in practice, and to incorporate its extension to further criminal categories as predicate offences.

During 2011 the Organisational Model was updated by the adoption of the scheme to prevent the "231 risk" consequent on the inclusion of environmental crimes (pursuant to legislative decree no. 121/2011) in the category of predicate offences and abrogation (due to its subsequent irrelevance with respect to the perimeter of the Telecom Italia Group) of the internal control scheme "Management and protection of the marine environment".

A special body (the "Supervisory Body") oversees the operation of and compliance with the Organizational Model and reports on these matters to the Board of Directors, the Committee for Internal Control and Corporate Governance and the Board of Auditors. To carry out its activities, the Supervisory Body is supported by dedicated Company offices.

The currently serving Supervisory Body was constituted by the Board of Directors of the Company by resolution on 5 May 2011, and it is composed of a Standing Auditor (Ferdinando Superti Furga – Chairman of the Body), an Independent Director and member of the Committee for Internal Control and Corporate Governance (Jean Paul Fitoussi), the internal control manager of the Company (Federico Maurizio d'Andrea), and an external member (Professor Vincenzo Salafia). With the approval of the Committee for Internal Control and Corporate Governance and of the Board of Auditors, the Board of Directors of the Company subsequently supplemented the membership of the Supervisory Body to include the presence of the Group Compliance Officer (currently Francesca Petralia),

With specific reference to the Organisational Model, the Board of Auditors noted that no risk situation had been reported in relation to the financial year 2011.

To create a global approach to risk management, the Telecom Italia Group has implemented and is perfecting a process inspired by Enterprise Risk Management (ERM), which requires a top-down approach (based on self-evaluation of the risk profile by the management) through which risks are identified, assessed and managed.

The process of managing risks (defined as "potential events whose occurrence could compromise the achievement of strategic objectives") is governed by the Group Risk Management Committee, chaired and coordinated by the Administration, Finance and Control & International Development Manager. The Group management committee reports to the Board of Directors and periodically reports to the Committee for Internal Control and Corporate Governance and the Board of Auditors.

The ERM process defines:

- the mapping of risks, assessed by level of impact and probability of occurrence, with a specific focus on the most significant risks (Top Risks). The assessment is performed at "current" level (evaluation of the risk at the time of assessment, expressing the size of risk to be treated);
- the degree of maturity of the management process at Entity level and at Top Risks level. A maturity index, traceable over time, is identified for each Top Risk and for the Risk Management system at Entity level;
- treatment of risk, performed by risk owner company structures by identifying and implementing specific action plans, aimed at both reducing the level of residual risk and increasing the maturity index.

The Board of Auditors monitors the evolution of the project particularly closely, by acquiring information from Company management, in specific interviews as well as in meetings held jointly with the Committee for Internal Control and Corporate Governance.

The Board of Auditors would point out that the Company is currently undertaken an in-depth examination of the arrangements for harmonising the ERM activities into the structures of the internal control system as a whole. The need to verify the organisational design for ERM is shared by the Board of Auditors, also in the light of the centrality assigned to the issue in the new Self-Regulatory Code of Borsa Italiana.

With particular reference to the internal controls for the preparation of the financial statements, the Board of Auditors notes that Telecom Italia has adopted the Internal Control - Integrated Framework model issued by the Committee of Sponsoring Organizations of the Treadway Commission as its reference framework for the definition and assessment of its internal control system.

The Board of Auditors has supervised the financial reporting process, verifying the adequacy and efficacy of the procedure through which financial information is produced and disseminated to the public, also by obtaining information from the Company management.

14. The Board of Auditors evaluated and supervised the adequacy of the administrative and accounting system of the Company and its ability to fairly represent operations, by direct observation, obtaining information from Company management, examining company documents and analysing the results of the activities undertaken by PricewaterhouseCoopers S.p.A..

The Board of Auditors acknowledged the statements issued by the Chairman of the Board and CEO, the Domestic Managing Director and the Manager responsible for preparing the corporate accounting documents of Telecom Italia S.p.A. concerning the adequacy – in relation to the characteristics of the company – and the actual application during 2011 of the administrative and accounting procedures for the preparation of the financial statements and the consolidated financial statements.

On the question of the impairment test, the Board of Auditors reports that in Telecom Italia it is applied in a consolidated and structured way, coordinated by the Administration, Finance and Control & International Development Function, with the intervention of an independent external expert of acknowledged professional expertise. The implementation of the process is analysed and discussed in special meetings of the Committee for Internal Control and Corporate Governance that precede the Board of Directors meetings to approve the financial reports to which the impairment test must be applied. These meetings are held jointly with the Board of Auditors.

The Board of Auditors reports that the impairment test procedure was applied to the 2011 financial statements in terms coherent with the procedure approved by the Board of Directors on 23 February 2012.

Finally, the Board of Auditors would clarify that the process followed to determine if the goodwill value has been reduced in value, to determine if this value can be recovered, and the assumptions used for this purpose are described in detail in the notes to the financial statements, as requested by the reference accounting principles. In particular, “the differences between the values in use and the carrying amounts at 31 December 2011” and the “values of the key variables for estimating the value in use”, and the “changes in key variables needed to render the recoverable amount equal the carrying amount” are indicated in the report on the consolidated financial statements (Note 4 – Goodwill).

Regarding the provisions of article 36, subsection 1, letter c, ii) of the Market Regulations (conditions for the listing of shares of controlling companies and of companies registered in and regulated by the laws of States that are not members of the European Union), the Board of Auditors has not ascertained facts and circumstances that would indicate that the administrative-accounting system of the controlled companies is not adequate to ensure that the data on the revenues, finances and assets of the companies needed for the preparation of the consolidated financial statements regularly reaches the management and auditor of the controlling company.

15. The Board of Auditors has been made aware of the instructions imparted by the Company to its subsidiaries, pursuant to art. 114, section 2 of the CFL, and considers them adequate to comply with the obligations regarding communication established by the law. In this respect it should be noted that the Company regulates the flow of information it receives from its subsidiary companies on transactions of particular impact, with specific procedures.

The Company has adopted the “Procedure for the handling and communication to the public of sensitive information”, which disciplines the handling of sensitive information about Telecom Italia, its unlisted subsidiaries and the listed financial instruments of the Group. This is directed at all members of corporate bodies, employees and external collaborators who have access to information that might evolve into sensitive information (“market sensitive information”). It also applies as an instruction to all subsidiaries in order to obtain from them, without delay, the information necessary for the timely and proper fulfilment of the public disclosure obligations.

This Procedure also disciplines the maintenance of the register of people with access to sensitive information.

16. The Board of Auditors has ascertained, from information obtained from Statutory Auditor PricewaterhouseCoopers and from the management of the Company, that the IAS/IFRS principles, and the other legal and regulatory provisions that apply to the preparation and presentation of the separate financial statements, the consolidated financial statements and the accompanying report on operations are complied with.

The Board of Auditors acknowledges that, from the report issued by PricewaterhouseCoopers S.p.A. on 19 April 2011 pursuant to article 19, subsection 3 of Legislative Decree no. 39 of 27 January 2010, no “fundamental issues” during statutory auditing or “significant shortcomings” in the internal control system on the financial reporting process of Telecom Italia S.p.A. emerged for the financial year that ended on 31 December 2010.

17. The Board of Auditors has supervised the arrangements for the concrete implementation of the rules of corporate governance required by the Self-Regulatory Code drawn up by the Committee for the Corporate Governance of Borsa Italiana, to which the

Company adheres. The Board of Auditors reports that analyses and further in-depth surveys by the management of the Company, with the intervention of the Vice Chairman of the Board of Directors, are also underway, given the changes to the internal governance arrangements introduced by the amendments made in December 2011.

As for the Board of Directors of the Company (currently composed of 15 directors), there are 13 non-executive directors, 6 of whom (Elio Cosimo Catania, Lucia Calvosa, Massimo Egidi, Jean Paul Fitoussi, Mauro Sentinelli and Luigi Zingales) qualify as independent Directors, based on their declarations. In this respect, it should be noted that Telecom Italia has adopted the criteria established by the Self-Regulatory Code of Borsa Italiana for qualifying Directors as independent. Based on the information available to the Company and provided by the Directors themselves, the Board of Directors evaluated the subsistence of the requisites for independence during its meeting on 29 March 2012, and then informed the market; these ascertainment activities were also monitored by the Board of Auditors, which made its own assessments, confirming that the requisites for the composition of the administrative body for collective decision making (the presence of at least two independent Directors satisfying the legally established criteria for Auditors) had been respected

The Board of Auditors also verified that its members possess the independence requirements pursuant to article 148, subsection three of the CFL.

The Board of Auditors supervised the independence of Statutory Auditor PricewaterhouseCoopers, in accordance with the provisions of article 19, subsection 1, lett. d) of legislative decree no. 39 of 27 January 2010, also acquiring from the Statutory Auditor the declaration specified in article 17, subsection 9, lett. a) of said decree.

In accordance with the recommendations of the Self-Regulatory Code of Borsa Italiana, the Board of Directors has instituted a Committee for Internal Control and Corporate Governance and a Nomination and Remuneration Committee from among its own members.

The Committee for Internal Control and Corporate Governance is composed of independent non-executive directors (of whom at least one is drawn from a minority slate) who all have experience of accounting and financial matters. The Committee is responsible for providing advice and recommendations. In particular, it assists the Board of Directors in carrying out its duties regarding the internal control system, assesses the work plan prepared by the internal control manager, supervises the efficacy of the audit process and respect of the principles for executing transactions with related parties, and defines the methods and times of board performance evaluation.

The Nomination and Remuneration Committee is composed of four non-executive Directors, the majority of them independent (of whom at least one is drawn from a minority slate, as per the Company's Self-Regulatory Code) all in various capacities in possession of sufficient knowledge and experience in the area of accounting and finance. The Committee is responsible for providing advice and recommendations. In particular, it formulates proposals to the Board of Directors for the remuneration of Directors who hold particular offices and periodically assesses the criteria for the remuneration of the senior management of the Company; as indicated by the managing directors, it formulates proposals and recommendations with particular reference to the adoption of any stock option or share allocation plans; if an independent Director is to be replaced, it proposes candidates for cooption to the Board of Directors.

The Board of Auditors monitored the activities of both Committees during 2011 by the attendance of its Chairman or an Auditor designated by the Chairman at their meetings.

Since 2008 the Board of Directors has had a subcommittee, the Executive Committee, composed of the executive and non-executive Directors, which is responsible for monitoring the operations of the Company and the Group, approving the organisational macrostructures as proposed by the executive Directors, formulating opinions for the Board of Directors on the budget and strategic, industrial and financial plans of the Company and the Group, and finally, performing any additional tasks attributed to it by the Board of Directors that the latter may delegate. In this respect, at its meeting on April 2011, the Board of Directors assigned the Executive Committee the task of expressing an advance opinion on the transactions which, by their nature, their strategic importance, their size or the commitments which they might entail, may have a significant impact on the activities of the Company and the Group.

It should also be noted that some years ago the Company created the role of Lead Independent Director, the point of reference and coordination for the issues and contributions of the independent Directors. This position is currently held by Director Luigi Zingales, who also has the right to convene special meetings only of the Independent Directors (Independent Directors' Executive Sessions) to discuss issues affecting the functioning of the Board of Directors or the management of the business.

See the Report on the corporate governance and share ownership of Telecom Italia S.p.A. for further detailed information on the corporate governance of the Company, which the Board of Auditors evaluates positively.

18. No significant facts that should be mentioned in its Report to the Shareholders' Meeting, or that should be reported to the other supervisory and control bodies have emerged from the supervision and control activities carried out by the Board of Auditors, as described above.

The Board of Auditors also reports that no observations or problems have emerged from its analysis of the information flows received in relation to the activity carried out by the control bodies of the subsidiary companies or the representations the statutory auditor has made in its reports on said subsidiaries.

Equally, no problems have emerged from the review of the reports of the Statutory Auditor and the Board of Auditors of Telecom Italia Media S.p.A. (a subsidiary company with shares listed on the market organised and managed by Borsa Italiana S.p.A.), or Telecom Italia Sparkle or Olivetti S.p.A. pursuant to and for the purposes of article 153 of the CFL, article 2429, second paragraph, of the Italian Civil Code and article 14 of legislative decree no. 39/2010.

Finally, the Board of Auditors examined the statutory auditor's reports on Tim Participações S.A. and Telecom Argentina S.A., which also contained no observations or remarks.

19. The Board of Auditors, having acknowledged the financial statements at 31 December 2011, has no objections to formulate on the proposed resolutions presented by the Board of Directors on the coverage of the operating losses of Telecom Italia S.p.A. and on the size of the dividend to be paid to Shareholders.

After the resignation of Director Ferdinando Beccalli Falco and the termination of the service of Director Francesco Profumo as a consequence of his appointment as a Ministro della Repubblica (Government Minister), the Board of Directors, in its meetings of 4 August and 1 December 2011 respectively, accepted the proposals of the Nomination and Remuneration Committee and co-opted Directors Lucia Calvosa and Massimo Egidi, both independent, who – in accordance with the law - will remain in office until the Shareholders' Meeting called to approve the financial statements as at 31 December 2011. The Board of Auditors therefore invites the Shareholders to resolve on this matter.

The mandate conferred on the Board of Auditors by the Shareholders' Meeting of 8 April 2009 expires with the Shareholders' Meeting called to approve the financial statements as at 31 December 2011. The Board of Auditors therefore invites the Shareholders to make the resolutions reserved to it for the appointment of the Board of Auditors.

It should also be noted that the Board of Directors of the Company considers that the proposal for the Board of Auditors to carry out the functions of the supervisory body pursuant to Legislative Decree no. 231 of 8 June 2001 art. 6, introduced by law no. 183 of 12 November 2011, is appropriate. For its part, the Board of Auditors considers that this solution is achievable for companies such as the Telecom Italia Group, in which the control organ benefits from the support of specific organisational structures dedicated to training and monitoring the implementation of the regulations contained in Legislative Decree no. 231/2011 and their evolution over time.

The Board of Auditors has no comments to make regarding the initiative concerning the incentive plan called the Long Term Incentive Plan 2012, which the Shareholders' Meeting of 15 May 2012 will be called on to resolve.

The Board of Auditors is aware that the proposal to change articles 9 and 17 of the Bylaws of Telecom Italia S.p.A. to comply with the legal provisions that have introduced into national law the principle of gender balance in the Board of Directors and Board of Auditors of listed companies will be submitted to the approval of the Shareholders' Meeting of 15 May 2012.

## **Section Two**

In last year's Report to the Meeting of the Shareholders of Telecom Italia S.p.A. (the "2010 Report"), the Board of Auditors dedicated a special section to reporting the specific supervision and monitoring activities it carried out in relation to the project known as the Greenfield Project, which was a structured internal analysis undertaken by the top management of Telecom Italia with reference to some allegedly unlawful acts committed to the detriment of the Company and the Group in previous years, which involved four separate project streams (Telecom Italia Sparkle, Security, irregular registration of SIM cards, anomalous sales of products or services), and to expressing its views of the results of this Project.

Also referring to the 2010 Report on this matter, an update on the new events that have occurred and on the activities undertaken by the Control Body during 2011 for each topic of investigation is provided below, generally focused on the monitoring of interventions and improvements made to the internal control system and on checking any elements that support the institution of liability proceedings against the executive directors holding office at that time.

It should be noted that in carrying out its activities, the Board of Auditors obtained the legal advice of Professor Paolo Montalenti, for the civil law aspects, and Professor Alberto Alessandri, for the criminal law aspects.

## **1 The Sparkle case**

The Board of Auditors continued to monitor the developments of this case which involved subsidiary Telecom Italia Sparkle S.p.A and the related criminal proceedings.

On this matter, taking account of the status of the latter proceedings and of the fact that no new elements have emerged that might change the assessments formulated in the 2010 Report, the Control Body confirms that, at present, no opinion has been expressed regarding any possible liability proceedings against the executive directors of Telecom Italia who held office at the time.

The Board of Auditors will continue to monitor the developments in this case very closely; in particular, it will ensure that the legal period within which such proceedings may be started (which ends on 3 December 2012) does not expire without having specifically assessed the opportunity of an application to suspend the expiry of the legal period.

## **2 The Security Department**

In its 2010 Report the Board of Auditors had highlighted how the findings of the Deloitte Report confirm the shortcomings in the organisational structure of the Company, in particular in the internal control system and above all in the operational and control procedures of the Security Department and the in-depth analyses carried out in the Greenfield Project had determined that the internal control system had been modified at that time.

Moreover, with reference to the question of the feasibility of a liability action against the previous senior executives of the company, the Board had expressed the following considerations: *“Considering the many shortcomings reported in an area that is intrinsically delicate, the entity of the increase in costs, even if only budgeted costs, and the gravity of the episodes reported, it might be concluded that the preceding senior executives behaved in a negligent way, in the lateness of the start of interventions to correct the shortcomings in the internal control system after the emergence of anomaly indicators; however, given the extremely complex structure of the company, taking the circumstance that the internal control systems in a complex enterprise are subject to an essentially permanent “tuning” process into account, considering that reaction times can never be instantaneous, and that knowledge not so much of the system anomalies but of the underlying unlawful acts has not been proven, then the time that elapsed between the alarm signals and the start of the intervention process might not appear unreasonable. Considering all the elements indicated, and in particular the circumstance that in the light of the criminal proceedings – currently – it has not been proven that the senior executives were aware of the unlawful acts that underlay the organisational shortcomings, it may be hypothesised that non-compliances imputable to the executive directors - i.e. their negligent conduct - subsist, but since the issue is not an absence of corrective action to remedy the shortcomings in the internal control system but rather possible delays in this, then the question is open to considerable debate.*

*Identifying the legal causal nexus between damages and non-compliances is also uncertain, since whether or not prompt corrective actions would have led to the discovery of the unlawful activities is debatable. Furthermore, the analysis of the costs led to the emergence of a not always clearly identifiable linkage between the various “cost” items and the technical concept of the damages payable.*

*Finally, the Board of Auditors again asserts that the absence of information about criminal investigations to determine the positions of the senior executives means that – at present – no relevant elements have been found to demonstrate their involvement in the alleged facts.*

*In conclusion, the Board of Auditors considers that while liability proceedings against the prior senior executives of the company could be based on some elements, such action would be very uncertain in terms of the capacity to impute the shortcomings in the internal control system to them, or in terms of a causal nexus and, to a certain extent, to identify and quantify the damage payable and for these reasons pursuing such action is – at present - inadvisable.*

*Since the criminal proceedings in relation to this affair do not in any event appear to have been concluded, the Board of Auditors will monitor with the greatest attention the developments in the case, as well as the emergence of any relevant finding, so as to be able to promptly review or update its assessment if this should be necessary.*

*In any event, it emphasised that, for those executive directors hypothetically involved, the legal period within which proceedings may be started, five years after the director concerned ceased to hold office, has not yet expired (a period of time emphasised in the detail by the Company in the report on the Greenfield Project) and the Board of Auditors confirmed that it will not allow any period within which proceedings may be started to expire without having carefully evaluated any opportunity to take action that might arise in the meantime that could suspend the expiry of the legal period.”*

As part of its activities to monitor the evolution of this case and the criminal proceedings underway, the Board of Directors examined the specific position of the ex-Chairman of the Board of Directors of the Company, Marco Tronchetti Provera, as the expiry of the period within which a liability action can be started against him approached (15 September 2011). In this matter, since no fact or circumstance that could change the considerations outlined in the 2010 Report had been ascertained, the Control Body decided not to proceed with an initiative to suspend the expiration of the period within which a liability action against the preceding Senior Management of the company could be started.

Moreover, after the press reports that appeared in November 2011 – confirmed by searches conducted at the Company by the Milan Prosecutor’s Office in January 2012 – regarding the inclusion of Mr. Marco Tronchetti Provera in the register of subjects under investigation regarding some events that occurred prior to 2007 (the so-called Kroll affair and relations with the consultant Naji Nahas), the Board of Auditors noted the initiative of the Board of Directors of the Company to start an internal verification of the facts related to these investigations, concerning the part not already investigated in the Greenfield Project. At present the outcome of this verification has not yet been reported by the consultants: furthermore, the Company has announced that it will report the main results of this initiative, where they are already available, at the Shareholders’ Meeting.

The Board of Auditors is supervising the way in which the aforementioned internal verification is being carried out and will in general monitor the developments of the proceedings, and the emergence of any further relevant element, with the greatest attention: it will on the one hand ascertain any new scenarios that might emerge from the criminal investigations, also with reference to the preceding Senior Management, for which - on this specific topic - the terms within which a liability action could be brought could be reopened, and, on the other, it will not allow any deadline to expire without having also carefully assessed if it might still be appropriate to proceed to suspend the prescription period for the executive directors, for whom the period within which a liability action may be brought expires on 3 December 2012.

In coherence with the declarations made in the 2010 Report and at the Shareholders’ Meeting of 12 April 2011, the Board of Auditors has monitored the initiatives undertaken and to be undertaken by the Company against third parties to reimburse the damages caused by activities that were extraneous to the interests of the company.

### **3 Prepaid Cards**

With reference to the matter of the irregular registration of prepaid cards, the Board of Auditors has over time monitored the initiatives taken by the Company to neutralise this phenomenon, or at least contain it within minimum physiological limits (see the Company’s comments in Note 24 to the consolidated financial statements) particularly closely: the number of prepaid cards activated without documentation of the purchaser, which at the date the rectification operations started totalled over 5.5 million, had been reduced to under five thousand at mid-March 2012 (over 183 thousand suspended in the post-sales period awaiting regularisation); for the newly activated cards, the problem has been reduced substantially.

The Board of Auditors has also monitored the evolution and developments in the criminal proceedings pending at the Milan Prosecutor’s Office insofar as it has been able, given that the matter is still being investigated: currently, given the shortage of information obtained so far, the Board does not have elements that might allow it to formulate a definitive assessment of the merit of bringing a liability action against the executive directors of the Company at that time, the period within which such action can be brought expires on 3 December 2012. The Control Body will therefore continue to monitor the evolution of this matter with due attention.

Finally, the Board of Auditors has noted the position expressed by the Company regarding the notification of the notice concluding the preliminary investigations pursuant to article 415-bis of the Code of Criminal Procedure – notified on 21 March 2011, from which it emerged that the Company is being investigated by the Milan Prosecutor’s Office pursuant to legislative decree no. 231/2001, for the offences of handling stolen goods (article 648 c.c.p.) and counterfeiting (art. 491-bis c.c.p.) committed, in the statement of charges, by fourteen employees of the so called “ethnic channel” of Telecom Italia, with the participation of a number of dealers. The Board of Auditors has only just acquired a copy of these charges and, reserving its right to express its views, will monitor the evolution of the situation with attention.

### **4 Anomalous/irregular sales**

After the 2010 Report, the Board was informed of the pending criminal proceedings in the preliminary investigation phase at the Monza Public Prosecutor’s Office against many subjects, including several employees of the Company, concerning some leased supply and/or sale of goods transactions which are alleged to constitute criminal offences committed to the detriment of the Company, among others. The Board of Auditors will monitor how the situation develops with attention.

### Section Three

The merger by incorporation of the limited consortium company TI Audit and Compliance Services S.c.a r.l. ("TI Audit") into Telecom Italia S.p.A. came into effect on 1 January 2012.

Since the financial statements of TI Audit as at 31 December 2011 will be submitted to the Telecom Italia Shareholders' Meeting for approval, the Board of Auditors is called on to draft a Report pursuant to article 2429, subsection 2 of the Italian Civil Code.

Taking account of the principles recommended by the CNDCEC (the Italian board of chartered accountants and accounting consultants), the Board of Auditors has examined the minutes of the corporate bodies, and in particular the audits of the Board of Auditors of TI Audit for the period in question and would emphasise:

- that the Board of Auditors of TI Audit monitored the observance of the law and articles of association and compliance with the principles of correct administration during 2011;
- that the Board of Auditors of TI Audit attended the meetings of the Partners (2 meetings) and of the Board of Directors (7 meetings) that took place in compliance with the company bylaws and legal and regulatory provisions that discipline their functioning, and for which it can be declared, based on the documentation seen, that the actions resolved were compliant with the law and the company bylaws and were not manifestly imprudent or risky, or in conflict of interest or such as to compromise the integrity of the assets of the Company;
- that the Board of Auditors of TI Audit approved the resolution adopted by the Board of Directors in its meeting of 19 July 2011 concerning the replacement of a Director;
- that the Board of Auditors of TI Audit met five times to carry out the legally required audits, with the participation of Auditing Firm PricewaterhouseCoopers S.p.A., the appointed Statutory Auditor, which evidenced no irregularities or relevant information to report;
- that during these meetings, also attended by members of the consortium company, the Board of Auditors obtained an account and found no evidence or critical issues on the adequacy and functioning of the organisational structure or the administrative and accounting system;
- that the Board of Auditors of TI Audit has acknowledged that the Supervisory Body of the company expressed an opinion that the company rules and procedures comply with the prescriptions of the Organisational Model of the company, pursuant to Legislative Decree no. 231/2001;
- that no complaints pursuant to article 2408 of the Italian Civil Code have been received.

Regarding the financial statements for the year at 31 December 2011, since the Control Body is not required to undertake an analytical audit of their content, the Board of Auditors audited the general approach of this document and its overall compliance with the law relating to its preparation and structure and, in this respect, has no special observations to report.

The Board of Auditors has also checked that the rules regarding the preparation of the Report on Operations were complied with.

In drawing up the financial statements, the Directors have not infringed the legal provisions pursuant to article 2423, subsection four, of the Italian Civil Code.

Given the matters reported above, and having noted the results of TI Audit's financial statements for the year at 31 December 2011, which report an operating profit of 201,108 euros, the Board of Auditors has no comments to make and expresses an opinion in favour of its approval.

Milan, 12 April 2012

**The Board of Auditors**