



2004 annual report »

ERRATA CORRIGE

In Telecom Italia 2004 Annual Report, in the table concerning the remuneration to Directors, Statutory Auditors and General Manager the amount indicated in the column "Fees for the post held in the company preparing the financial statements", for the Director Mr. Umberto Colombo should read "51⁽⁷⁾" instead of "34".

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■ CORPORATE BOARDS

| | | | |
|---|--|--|---|
| Board of Directors ⁽¹⁾ | Chairman ⁽²⁾ | Marco Tronchetti Provera (Executive Director) | <p>♦ (1) Appointed by the Shareholders' Meeting held on May 6, 2004.</p> <p>♦ (2) Appointed by the Board of Directors' Meeting held on May 6, 2004.</p> |
| | Deputy Chairman ⁽²⁾ | Gilberto Benetton | |
| | Managing Directors ⁽²⁾ | Carlo Orazio Buora (Executive Director) Riccardo Ruggiero (Executive Director) | |
| | Directors | Paolo Baratta (Independent Director) John Robert Sotheby Boas (Independent Director) Giovanni Consorte Domenico De Sole (Independent Director) Francesco Denozza (Independent Director) Luigi Fausti (Independent Director) Guido Ferrarini (Independent Director) Jean Paul Fitoussi (Independent Director) Gianni Mion Massimo Moratti Marco Onado (Independent Director) Renato Pagliaro Pasquale Pistorio (Independent Director) Carlo Alessandro Puri Negri Luigi Roth (Independent Director) | |
| | Secretary to the Board ⁽²⁾ | Francesco Chiappetta | |
| Remuneration Committee ⁽²⁾ | Chairman | Luigi Fausti | |
| | Members | Paolo Baratta Pasquale Pistorio | |
| Committee for Internal Control and Corporate Governance ⁽²⁾ | Chairman | Guido Ferrarini | |
| | Members | Domenico De Sole Francesco Denozza Marco Onado | |
| General Managers ⁽³⁾ | | Riccardo Ruggiero Giuseppe Sala | ♦ (3) Appointed by the Board of Directors' Meeting held on August 4, 2003. |
| Board of Statutory Auditors ⁽⁴⁾ | Chairman | Ferdinando Superti Furga | ♦ (4) Appointed by the Shareholders' Meeting held on May 26, 2003. |
| | Acting Auditors | Rosalba Casiraghi Paolo Golia Salvatore Spiniello Gianfranco Zanda | |
| | Alternate Auditors | Enrico Bignami Enrico Laghi | |
| Independent Auditors ⁽⁵⁾ | | Reconta Ernst & Young S.p.A. | ♦ (5) Appointment conferred by the Shareholders' Meeting held on May 6, 2004. |

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■ LETTER OF THE CHAIRMAN



To the Shareholders,

When we took over the helm of the Telecom Italia Group towards the end of 2001, we announced that the cornerstones of our industrial plan would involve becoming firmly entrenched in cutting edge technologies and just as firmly oriented towards the market.

The results of 2004, which are, once again, in line with the objectives announced to the financial community, confirm the validity of that plan. Revenues have increased, profitability has improved, operating free cash flows have increased and indebtedness has been further reduced.

An important contribution to the performance of the Group – a performance which continues to rank our Group at the top of the sector in Europe – has come from precisely the more innovative areas: from the vigorous expansion of broadband and from the success of hi-tech services both in wireline and mobile telephone services.

Thus new patterns of consumption are emerging – based on the exchange of data, images, sounds – which are gradually replacing the transportation of the voice as the key element in the development of telecommunications. This trend, which applies to both wireline and mobile telephone services, has found widespread support in the modernization of the networks and services, to which we have devoted a considerable amount of the euro 5 billion we spend on average every year. The Telecom Italia Wireline Network, in particular, has been described by authoritative analysts in the sector as the most technologically sophisticated network in Europe, the most advanced in the transition to the IP protocol, that is, in the carrier techniques that will dominate telecommunications in a future which is literally just around the corner.

It is precisely the technological level reached by the networks, together with the confirmation of new forms of consumption demonstrated by our customers, which have led us to take an important step: the merger between TIM and Telecom Italia. This merger, while in full respect of the restrictions imposed by the Regulator, will enable us to fully exploit the innovative potential that lies within the convergence between the platforms of wireline and

mobile telephone services which the manufacturers of telecommunications systems and equipment have rendered possible, reliable and affordable in the last few months.

We now face the prospect of reaching the point where we can offer consumers and companies, in both wireline and mobile services, broadband services which share the same common base, yet which remain distinct and different in terms of their characteristics and the specific ways they are used, according to the communication tools involved.

The merger between TIM and Telecom Italia will not only ensure the unitary government of business processes which are in continuous and often turbulent evolution, but will make it possible to create considerable synergies in terms of investments and operating costs.

However, the purely industrial nature of the merger has even more far-reaching consequences if we regard it in the light of the consequences of the events which have marked the corporate history of the Group since it was privatized. In fact, the merger with TIM is the end of the complex journey that we have made to streamline and rationalize the corporate structure; a journey which involved us in the recapitalization of Olivetti in the last months of 2001 and, in 2003, in the merger between Olivetti and Telecom Italia.

According to a leading international newspaper, today, the Group has finally achieved a “normal” structure. This is certainly the case: cash flows and debt are now allocated at the same level. This will make it possible to sustain growth with the necessary level of investments and to remunerate our shareholders with an adequate dividend, reabsorbing, with higher cash flows, also the higher level of indebtedness resulting from the merger transaction.

The flattering acclaim given by the market to our reorganization process is indicative of the credibility and trust which we have been able to generate. Credibility and trust have certainly found solid motivations in the strictness and transparency of the decisions taken at managerial level and in the complete sustainability of our conduct.

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Furthermore, the reliability of the Group is confirmed by the fact that it is capable of generating growth in all its main business units.

In the field of wireline telephone services, our company is the only one of all the large European companies which, even leaving aside the persisting decrease in the level of voice traffic, for the second consecutive year, has increased its revenues and profitability. The merit for this must go to the launch of the new terminals (Aladino and the videotelephone), innovative services packages and, more particularly, to an increase in broadband connections that has far exceeded expectations. The number of broadband connections exceeded the 4 million mark, thus doubling the volumes of 2003 and multiplying by a factor of almost 5 those reported in 2002. It should be emphasized that this spread of broadband was accompanied and encouraged by a series of free increases in connection speed for both residential and business customers. At an international level, too, Telecom Italia is beginning to harvest the fruits of the investments made on the broadband markets in France and Germany, with an increase in a single year from 160 thousand to 420 thousand lines.

Despite the fact that TIM has continued to increase its voice traffic in Italy, it has increasingly entrusted its growth to value-added services and the introduction of the new EDGE and UMTS technologies which also constitute the launch-pad for broadband in mobile telephone services. The contribution by the operations in Brazil has been significant: by increasing the total number of lines from 8.3 to 13.6 million, the TIM Brazil Group has become the second-largest mobile telephone services operator in the country, is the only one to have nationwide coverage and is the first to offer GSM technology.

Telecom Italia Media has increased its revenues and has turned the gross operating profit into a positive figure as a result of a boost from the Internet area, with Virgilio, which has become one of Italy's leading portals, and in television, with the LA7 channel which has yet again increased its viewing audience and consolidated the image of a broadcaster of quality oriented towards the higher range of the public. With regard to digital terrestrial television, where it has achieved a coverage of 68% of the population, last January, LA7 launched a pay-per-view package of the home games of nine teams in the Italian Series A soccer championship.

Now that Olivetti Tecnost has completed its restructuring process and redefined its organization around Office products and Systems, it has recovered its technological vitality and innovative enthusiasm by acquiring new international markets for specialized terminals and significantly improved its operating result.

Telecom Italia Lab, which plays an increasingly important role in the innovation of the Group's networks and services, has filed 86 new patents

and has contributed to the launch of new products (such as the Turbo Call service, the Videotelephone and the Alice Mia Access Gateway), thus strengthening its collaboration with Pirelli Labs, on the one hand, and with suppliers, on the other.

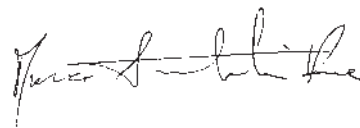
Looking to the future, the priority areas on which we intend to concentrate our efforts and our investments will be the development of innovative services and the strengthening of our international presence.

We want to transform the increasing bandwidth which we are making available on the wireline and mobile networks into concrete opportunities to improve the quality of life for citizens – whether we are talking about new ways for people to interact with the public administrations, contact the national health service, access information and learn, or just have fun – and to increase the productivity of companies – whether it is being used for creating innovation in production processes, new ways of supplying and using services, distributing resources from one place to another or speaking to customers.

As far as international expansion is concerned, we intend to step up our commitment by following a path that is already there for us to take: by focusing very selectively on markets with high development potential. This means France and Germany in the case of broadband; it means Brazil and Turkey because of the size of their markets and also because they offer us the chance to become an integrated operator of wireline and mobile telephone services. We continue to be very interested in Argentina. At the same time, we shall continue to divest non-strategic operations abroad, and intend to devote the resources thus released partly to reduce indebtedness and partly to invest in key markets.

By concentrating on the innovation of networks and services and with an international focus clearly oriented towards the kind of growth that will generate profits, Telecom Italia hopes to succeed in maintaining its position as European leader in a world of telecommunications that is rapidly changing. With fewer and fewer utilities providing voice services (which now constitute less than 40% of traffic) and an increasingly large infrastructure for producing and distributing services, telecommunications have now become a hi-tech sector and, as such, are destined to play a fundamental and driving role in economic and social development.

As far as we are concerned, it is a role for which we feel responsible and which we shall play with the utmost commitment, sustained by the enormous wealth of ability, competence and professional skills of the people who work for our Group. Their intelligence and their enthusiasm have been crucial in making the Telecom Italia Group's industrial plan into a success in such a short time.



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■ HIGHLIGHTS

■ YEAR 2004

■ Improvement in economic results

Revenues: euro 31,237 million, +1.3% compared to 2003; excluding the foreign exchange effect and the change in the scope of consolidation, underlying growth is equal to 4.9%.

Gross operating profit: euro 14,528 million, +1.7% compared to 2003; underlying growth is equal to 4.4%.

Operating income: euro 7,200 million, +6.1% compared to 2003; underlying growth is equal to 9.3%.

Net income - Parent Company interest, pre-amortization of differences on consolidation: euro 2,311 million (euro 2,983 million in 2003). The reduction from last year is partly due to the posting of deferred tax assets in 2003 (euro 1,266 million), which became recoverable thanks to the Olivetti - Telecom Italia merger, countered by higher income taxes as a consequence of the improvement in operations.

Net income - Parent Company interest: euro 781 million (euro 1,192 million in 2003). The reduction from 2003 is due to the effects described above.

■ Reduction of indebtedness

Net financial indebtedness is equal to euro 29,525 million and shows a reduction of euro 3,821 million compared to December 31, 2003, after the distribution of dividends of euro 2,780 million.

■ Growth of industrial investments

Industrial investments are equal to euro 5,335 million and increased by euro 441 million compared to December 31, 2003.

■ Improvement in free cash flows from operations

Free cash flows from operations amount to euro 9,887 million, +7.1% compared to 2003 (euro 9,233 million).

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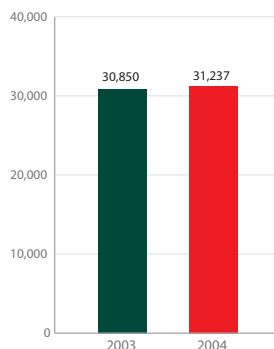
■ SELECTED ECONOMIC AND FINANCIAL DATA - TELECOM ITALIA GROUP

No significant changes in the scope of consolidation occurred in 2004.

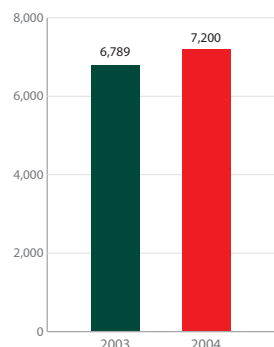
It should be pointed out that Nuova Seat Pagine Gialle was deconsolidated from August 2003; accordingly, the economic data for the year 2003 includes this company's results for only seven months.

The effects of the changes in the scope of consolidation are shown in the section on the economic and financial performance of the Telecom Italia Group, for purposes of comparison.

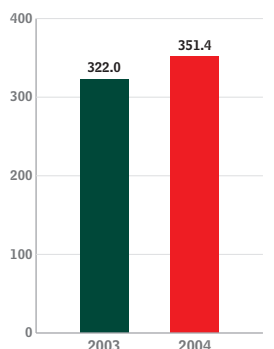
Revenues (millions of euro)



Operating income (millions of euro)



Revenues/Employees (thousand of euro)



| | 2004 | 2003 | 2002 |
|---|--------|--------|---------|
| Economic and Financial Data (millions of euro) | | | |
| Sales and services revenues | 31,237 | 30,850 | 31,408 |
| Gross operating profit | 14,528 | 14,280 | 14,015 |
| Operating income pre-amortization of differences on consolidation | 8,754 | 8,619 | 8,200 |
| Operating income | 7,200 | 6,789 | 6,058 |
| Income (loss) before income taxes | 4,956 | 3,442 | (2,516) |
| Net income - Parent Company interest and minority interest pre-amortization of differences on consolidation | 3,456 | 4,258 | 1,836 |
| Net income - Parent Company interest pre-amortization of differences on consolidation | 2,311 | 2,983 | 838 |
| Net income (loss) before minority interest | 1,902 | 2,428 | (306) |
| Net income (loss) | 781 | 1,192 | (773) |
| Free cash flows from operations | 9,887 | 9,233 | 8,680 |
| Investments: | | | |
| - Industrial | 5,335 | 4,894 | 4,901 |
| - Differences on consolidation | 430 | 5,096 | 346 |
| - Financial | 153 | 1,464 | 1,777 |
| Balance Sheet Data (millions of euro) | | | |
| Total assets | 76,609 | 80,501 | 83,384 |
| Net invested capital | 49,386 | 53,935 | 54,023 |
| Shareholders' equity | 19,861 | 20,589 | 20,624 |
| - Parent company interest | 15,172 | 16,092 | 11,640 |
| - Minority interest | 4,689 | 4,497 | 8,984 |
| Net financial indebtedness | 29,525 | 33,346 | 33,399 |
| Profit and Financial Indexes | | | |
| Gross operating profit/Revenues | 46.5% | 46.3% | 44.6% |
| Operating income pre-amortization of differences on consolidation/Revenues | 28.0% | 27.9% | 26.1% |
| Operating income/Revenues (ROS) | 23.0% | 22.0% | 19.3% |
| Free cash flows from operations/Revenues | 31.7% | 29.9% | 27.6% |
| Debt ratio (Net financial indebtedness/ Net invested capital) | 59.8% | 61.8% | 61.8% |
| Employees | | | |
| Employees (number in Group at year-end) | 91,365 | 93,187 | 106,620 |
| Employees (average number in Group) | 88,892 | 95,804 | 107,079 |
| Revenues/Employees (average number in Group), euro/thousands | 351.4 | 322.0 | 293.3 |

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■ KEY DATA - TELECOM ITALIA GROUP BUSINESS UNITS/CENTRAL FUNCTIONS

Key economic and financial data of the Telecom Italia Group Business Units/Central Functions:

| | | Wireline | Mobile | South America | Internet and Media | Olivetti-Tecnost | IT Market | IT Group | Sub-total | Other activities and eliminations | Total Group |
|--|------------|----------|--------|---------------|--------------------|------------------|-----------|----------|-----------|-----------------------------------|-------------|
| (euro/millions) | | | | (1) | (2) | | | | | (3) | |
| Sales and services revenues | 2004 | 17,571 | 12,900 | 1,076 | 597 | 601 | 729 | 965 | 34,439 | (3,202) | 31,237 |
| | 2003 | 17,216 | 11,782 | 1,111 | 1,297 | 655 | 891 | 1,100 | 34,052 | (3,202) | 30,850 |
| Gross operating profit | 2004 | 8,426 | 6,052 | 396 | 24 | 44 | 65 | 76 | 15,083 | (555) | 14,528 |
| | 2003 | 8,255 | 5,502 | 407 | 322 | 40 | 84 | 96 | 14,706 | (426) | 14,280 |
| Operating income (loss) pre-amortization of differences on consolidation | 2004 | 5,207 | 4,166 | 127 | (60) | 22 | 37 | (67) | 9,432 | (678) | 8,754 |
| | 2003 | 4,972 | 3,885 | 153 | 125 | 4 | 60 | (36) | 9,163 | (544) | 8,619 |
| Operating income | 2004 | 5,199 | 4,073 | 121 | (89) | 21 | 36 | (67) | 9,294 | (2,094) | 7,200 |
| | 2003 | 4,969 | 3,786 | 145 | 63 | 2 | 58 | (36) | 8,987 | (2,198) | 6,789 |
| Industrial investments | 2004 | 2,201 | 2,490 | 157 | 62 | 15 | 25 | 180 | 5,130 | 205 | 5,335 |
| | 2003 | 2,302 | 1,957 | 129 | 102 | 20 | 30 | 174 | 4,714 | 180 | 4,894 |
| Number of employees at end of year | 12/31/2004 | 50,383 | 20,361 | 5,080 | 1,805 | 2,108 | 4,131 | 3,160 | 87,028 | 4,337 | 91,365 |
| | 12/31/2003 | 50,766 | 18,888 | 4,953 | 2,029 | 2,395 | 4,827 | 4,107 | 87,965 | 5,222 | 93,187 |

(1) The data relates to the Entel Chile group and to the Entel Bolivia group. Beginning March 1, 2004, the company Telecom Italia America Latina and the Argentine branch of Telecom Italia have been consolidated in Other Activities. The 2003 data has been restated for purposes of comparison.

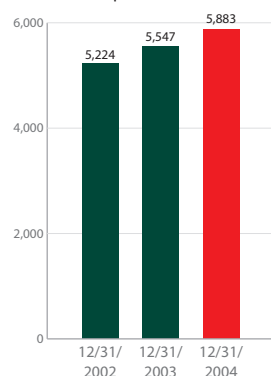
(2) Nuova Seat Pagine Gialle, the beneficiary company of the partial spin-off of Seat Pagine Gialle S.p.A. (now Telecom Italia Media S.p.A.) was sold August 8, 2003. The figures for 2003 include the economic data for the first seven months of the Nuova Seat Pagine Gialle group.

(3) The data presented above includes the activities of International Affairs, TILAB, the centralized group services and the central functions, the financial companies, the company Telecom Italia America Latina and the Argentine branch of Telecom Italia.

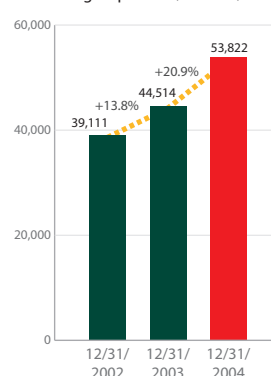
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■ OPERATING HIGHLIGHTS - TELECOM ITALIA GROUP

Voice flat-rate plans (thousands)



Total TIM group lines (thousands)



| | 2004 | 2003 | 2002 |
|---|--------|--------|--------|
| WIRELINE | | | |
| Fixed network connections in Italy (thousands) | 25,957 | 26,596 | 27,142 |
| - of which digital (equivalent ISDN channels) | 5,805 | 6,027 | 5,756 |
| Voice flat-rate plans (thousands) | 5,883 | 5,547 | 5,224 |
| Broadband access (thousands) | 4,430 | 2,200 | 850 |
| Network infrastructure in Italy | | | |
| - access network in copper (millions of km - pair) | 105.2 | 105.2 | 104.3 |
| - access network and transport in optical fibers (millions of km of optical fibers) | 3.7 | 3.6 | 3.6 |
| Network infrastructure abroad | | | |
| - European backbone (km of optical fibers) | 39,500 | 39,500 | 36,600 |
| MOBILE | | | |
| TIM lines in Italy (at year-end, thousands) | 26,259 | 26,076 | 25,302 |
| TIM group foreign lines (at year-end, thousands) ⁽¹⁾ | 27,563 | 18,438 | 13,809 |
| TIM group lines total (Italy + foreign in thousands) ⁽¹⁾ | 53,822 | 44,514 | 39,111 |
| GSM penetration in Italy (% of population) | 99.8 | 99.8 | 99.8 |
| E-TACS penetration in Italy (% of population) | 83.5 | 97.9 | 98.0 |
| INTERNET AND MEDIA | | | |
| Internet: | | | |
| Page Views Virgilio (millions) | 7,902 | 6,612 | 5,267 |
| Active Users ISP (at year-end, thousands) | 3,346 | 2,514 | 2,227 |
| La 7 audience share (average) | 2.4 | 2.2 | 1.8 |
| La 7 audience share (month of December) | 2.6 | 2.2 | 1.8 |

(1) Foreign lines include those of the affiliate Avea I.H.A.S. (Aria-Is TIM in 2003) and the subsidiary T-Mobile CZ (ex-Radiomobil). Avea I.H.A.S.'s lines comprise about 2 million lines that came from Aycell.

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■ SHAREHOLDER INFORMATION

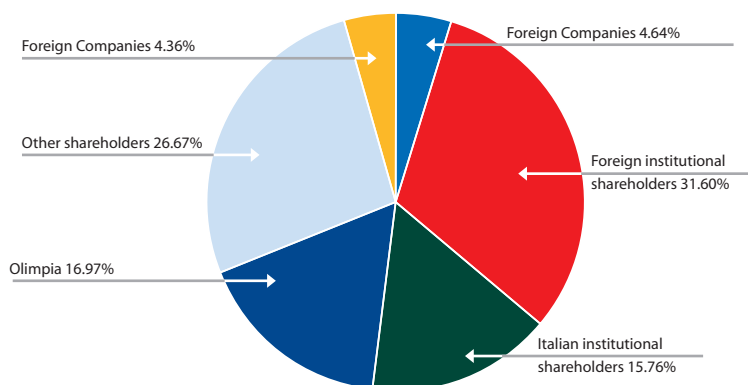
■ Telecom Italia S.p.A. share capital at December 31, 2004

| | |
|---|-----------------------|
| Share capital | euro 8,864,857,175.90 |
| Ordinary shares (par value of euro 0.55 each) | No. 10,322,001,069 |
| Savings shares (par value of euro 0.55 each) | No 5,795,921,069 |
| Telecom Italia treasury stock | No. 1,272,014 |
| Telecom Italia shares held by Telecom Italia Finance | No. 99,936,853 |
| Market capitalization (based on December 2004 average prices) | euro 44,067 million |
| Percentage of Telecom Italia stock | |
| - on Mibtel Index (Telecom Italia - ordinary and savings) | 7.7% (at 12/31/2004) |
| - on DJ Stoxx TLC Index ⁽¹⁾ (Telecom Italia - ordinary) | 5.9% (at 12/31/2004) |
| Percentage of the stocks of companies in the Telecom Italia Group | |
| - on Mibtel Index (Telecom Italia, TIM and Telecom Italia Media - ordinary and savings) | 16.0% (at 12/31/2004) |
| - on DJ Stoxx TLC Index (Telecom Italia, TIM - ordinary) | 10.5% (at 12/31/2004) |

⁽¹⁾ The Index is calculated on a geographical basis that includes all European countries.

■ Shareholders

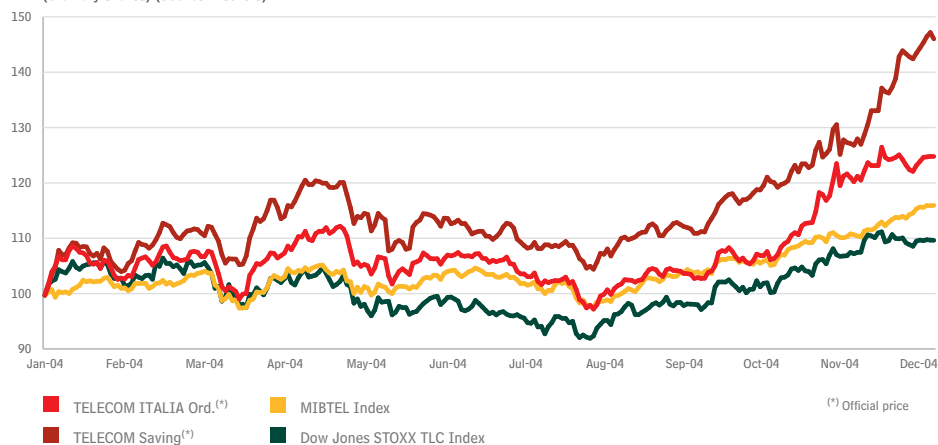
Composition of Telecom Italia S.p.A. shareholders according to the Shareholders Book at December 31, 2004, supplemented by communications received and other sources of information (ordinary)



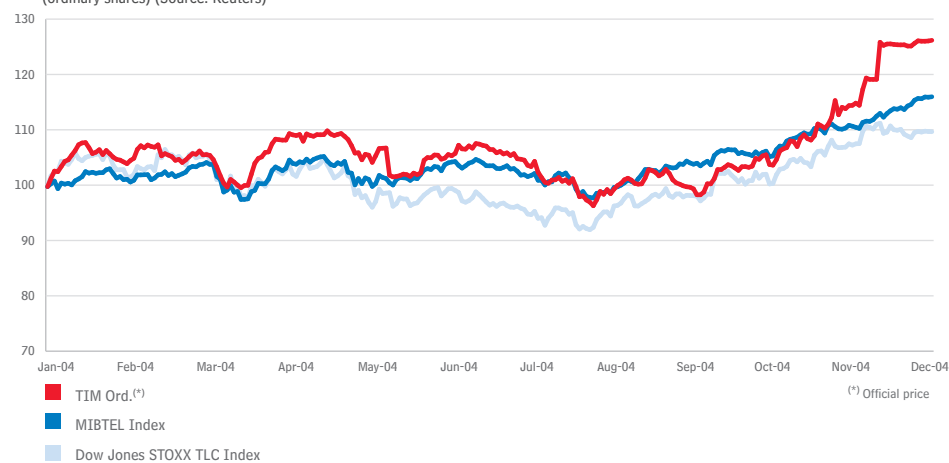
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■ PERFORMANCE OF THE STOCKS OF THE MAJOR COMPANIES IN THE TELECOM ITALIA GROUP

Relative performance Telecom Italia S.p.A. 1/1/2004 - 12/31/2004 vs. MIBTEL and DJ Stoxx TLC Indexes (ordinary shares) (Source: Reuters)



Relative performance TIM S.p.A. 1/1/2004 - 12/31/2004 vs. MIBTEL and DJ Stoxx TLC Indexes (ordinary shares) (Source: Reuters)



Relative performance Telecom Italia Media S.p.A. 1/1/2004 - 12/31/2004 vs. MIBTEL and DJ Stoxx MEDIA Indexes (ordinary shares) (Source: Reuters)



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■ TELECOM ITALIA / TIM MERGER

The Telecom Italia securities referred to herein that will be issued in connection with the merger described herein have not been, and are not intended to be, registered under the U.S. Securities Act of 1933 (the Securities Act) and may not be offered or sold, directly or indirectly, into the United States except pursuant to an applicable exemption. The Telecom Italia securities are intended to be made available within the United States in connection with the merger pursuant to an exemption from the registration requirements of the Securities Act.

On December 7, 2004, the Telecom Italia and TIM Boards of Directors approved a plan for the merger of the two companies. The merger is aimed at streamlining the Group's ownership structure and optimizing the financial and capital structures in view of the rapid technological developments that open the door to significant efficiencies from an industrial standpoint.

The merger calls for:

- a partial voluntary cash tender offer by Telecom Italia for 2,456,534,241 TIM ordinary shares, equal to two-thirds of outstanding ordinary shares, and all 132,069,163 TIM savings shares;
- the integration of TIM and Telecom Italia, after the spin-off of the Mobile Telephone business in Italy to a wholly-owned subsidiary of TIM. This merger will take place after the distribution of dividends.

Following authorization by Consob, on January 3, 2005, Telecom Italia launched a cash tender offer for TIM ordinary and savings shares which ended on January 21, 2005. Telecom Italia's offer price was euro 5.6 per ordinary share and per savings share of TIM. In order to fund the tender offer, corresponding to an outlay of euro 14,496 million, Telecom Italia planned originally to use euro 2,500 million of its own funds and finance the remaining amount of euro 12,000 million with a credit line obtained from a syndicate of Italian and international banks, divided into three tranches (the first for euro 3,000 million, the second for euro 6,000 million and the third for 3,000 million).

The final results submitted by the agents charged with coordinating receipt of the shares tendered showed the following: a total of 2,639,154,665 ordinary shares tendered (equal to approx. 31.2% of TIM ordinary share capital and approx. 107.4% of the ordinary shares targeted in the offer) and 8,463,127 savings shares tendered (equal to approx. 6.4% of TIM savings share capital and, thus, the same percentage of TIM savings shares targeted in the offer).

Although not all the conditions to render the cash tender offer effective were met, in particular, the number of savings shares tendered was less than the minimum quantity of 88,046,109 TIM savings shares, taking into account the overall number of shares tendered and the purpose of the restructuring plan, the aforesaid conditions were waived by the Board of Directors of Telecom Italia which, on January 23, 2005, confirmed the effectiveness of the cash tender offer and accepted the offer to purchase the TIM savings shares tendered.

Since the number of TIM ordinary shares exceeded the maximum number of ordinary shares targeted in the cash tender offer, Telecom Italia prorated acceptance of the shares tendered on a proportional basis at 93.0803440%. As a result, Telecom Italia acquired from each shareholder a quantity of TIM ordinary shares equal to the prorated percentage of the ordinary shares tendered, rounded down to the nearest whole number.

Any ordinary shares not acquired by Telecom Italia following the allotment have been released and returned to the tendering shareholders on January 26, 2005.

The transfer to Telecom Italia of the ownership of the TIM ordinary shares (2,456,501,605) and TIM savings shares (8,463,127), tendered and accepted, took place on January 28, 2005, the date set for payment of the offer price. Telecom Italia's total outlay for the purchase of TIM shares was

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equal to euro 13,804 million, of which euro 2,504 was paid from Telecom Italia's cash resources and euro 11,300 was drawn from the credit line obtained from a syndicate of Italian and foreign banks in December (the residual amount of the first tranche of the line of credit, equal to euro 700 million, was cancelled). On February 11, 2005, the drawdown was rolled-over for euro 9,000 million only; therefore the first tranche of the line of credit was cancelled for the residual amount of euro 2,300 million.

Therefore, at the expiration of the cash tender offer, Telecom Italia holds a total of 7,190,583,124 ordinary shares and 8,463,127 savings shares of TIM, equal, respectively, to approx. 84.8% of TIM ordinary share capital and approx. 6.4% of TIM savings share capital.

On December 21, 2004, Telecom Italia concluded an agreement called "Confirmation of Share Basket Option Transaction" for the purchase of call options and the sale of put options, both up to a maximum of 25 million, each having an underlying basket of shares composed of two TIM ordinary shares and one TIM savings share. All the options, expiring January 31, 2005, carried an exercise price of euro 5.57 per each ordinary share and per each savings shares.

On February 3, 2005, Telecom Italia exercised the call options on 21 million TIM savings shares for a total outlay of approx. euro 117 million.

On the same date, Telecom Italia borrowed 37 million TIM savings shares (divided into two groups, the first for 15 million shares and the second for 22 million shares) for total consideration of approx. euro 225 million (of which about 211 million was cash collateral) through the execution of a stock lending agreement called "Confirmation of a Securities Lending Transaction" negotiated on January 19, 2005.

Consequently, on the basis of the number of the savings shares acquired through the cash tender offer described above, the exercise of the option agreement and the execution of the stock lending agreement, Telecom Italia will be in a position to exercise approximately 50.3% of the votes for this class of shares at the special Savings Shareholders' Meeting which will be called to approve the merger resolution.

On February 8, 2005, the counterpart of the put option contract called "Confirmation of Share Basket Option Transaction", negotiated in December 2004, exercised the put option rights and, therefore, on February 11, 2005 Telecom Italia purchased 42 million TIM ordinary shares for total consideration of approx. euro 234 million.

On January 23, 2005, the Telecom Italia and TIM Boards of Directors approved the project for the merger of TIM in Telecom Italia and confirmed the share exchange ratios that were announced at the Board meeting held December 7, 2004: (i) 1.73 Telecom Italia ordinary shares of par value euro 0.55 each for every TIM ordinary share of par value euro 0.06 each; (ii) 2.36 Telecom Italia savings shares of par value euro 0.55 each for every TIM savings share of par value euro 0.06 each, and no cash adjustments.

The merger will be implemented through:

- cancellation of TIM ordinary shares held by TIM on the effective date of merger, without share exchange;
- cancellation of the TIM ordinary and savings shares held by Telecom Italia on the effective date of merger, without share exchange;
- cancellation of the TIM ordinary and savings shares outstanding on the effective date of merger, with share exchanges as indicated above. The share exchange will be serviced by a capital increase by Telecom Italia for a maximum of euro 1,421 million through the issue of 2,291,344,587 new Telecom Italia ordinary shares and a maximum of 291,729,714 new Telecom Italia savings shares, all with a par value of 0.55 each.

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As mentioned earlier, before the merger becomes effective TIM will spin-off the domestic mobile communications business to TIM Italia S.p.A., a wholly-owned subsidiary of TIM; the spin-off will become effective by the end of February 2005. As to completion of the merger, the intention of both Telecom Italia and TIM is to take steps to ensure its effectiveness by the end of June 2005.

For accounting purposes, transactions carried out by TIM are expected to be booked by Telecom Italia starting from January 1, 2005; the merger will also be effective for tax purposes as of the same date. On completion of the merger, Telecom Italia ordinary and savings shares will continue to be listed on Borsa Italia S.p.A. screen-based trading market and on the New York Stock Exchange as American Depositary Shares (ADS).

With regard to the shareholders' approval of the merger, Telecom Italia's Board of Directors has voted to convene the ordinary shareholders to an extraordinary session of the Shareholders' Meeting to be held on April 5, 6 and 7, 2005, in first, second and third call, respectively. TIM's Board of Directors has voted to convene the ordinary shareholders to an extraordinary session of the Shareholders' Meeting to be held on April 5 and 6, 2005, in first and second call, respectively. Moreover, a special Savings Shareholders' Meeting is expected to be called by TIM on April 6, 7 and 8, 2005, in first, second and third call, respectively.

■ FINANCIAL INDICATORS (*)

| (euro) | 2004 | 2003 | |
|---|-------------|-------------|-----------------|
| Telecom Italia S.p.A. | | | |
| Market price (December average) | | | |
| - Ordinary share | 2.98 | 2.41 | |
| - Savings share | 2.29 | 1.63 | |
| Dividends per share | | | |
| - Ordinary share | 0.1093 | 0.1041 | |
| - Savings share | 0.1203 | 0.1151 | |
| Pay-Out Ratio | 90% | 66% | |
| Market to Book Value | 2.62 | 2.10 | |
| Dividend Yield (on December average market prices) | | | |
| - Ordinary share | 3.67% | 4.32% | |
| - Savings share | 5.25% | 7.06% | |
| | 2004 | 2003 | 2002 (*) |
| Gruppo Telecom Italia (**) | | | |
| Earnings/(loss) per ordinary share | 0.0448 | 0.0705 | (0.1614) |
| Earnings/(loss) per savings share (***) | 0.0558 | 0.0815 | (0.1504) |
| Operating free cash flow per share | 0.6173 | 0.5772 | 0.5435 |
| Equity per share | 0.9473 | 1.0059 | 0.8914 |

(*) Telecom Italia S.p.A. financial indicators for 2002 are not shown as they are not comparable with those of 2003 and 2004 owing to the Olivetti/Telecom Italia merger.

(*) Olivetti Group restated data for 2002.

(**) Such indicators are determined by reference to the number of shares at December 31 of each year, net of treasury stock.

(***) Such indicator is calculated by taking into consideration the bylaws which provide for the assignment of dividends to savings shares that are higher than the dividends of ordinary shares by 2% of the par value of the shares (euro 0.0110).

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■ RATINGS AT DECEMBER 31, 2004

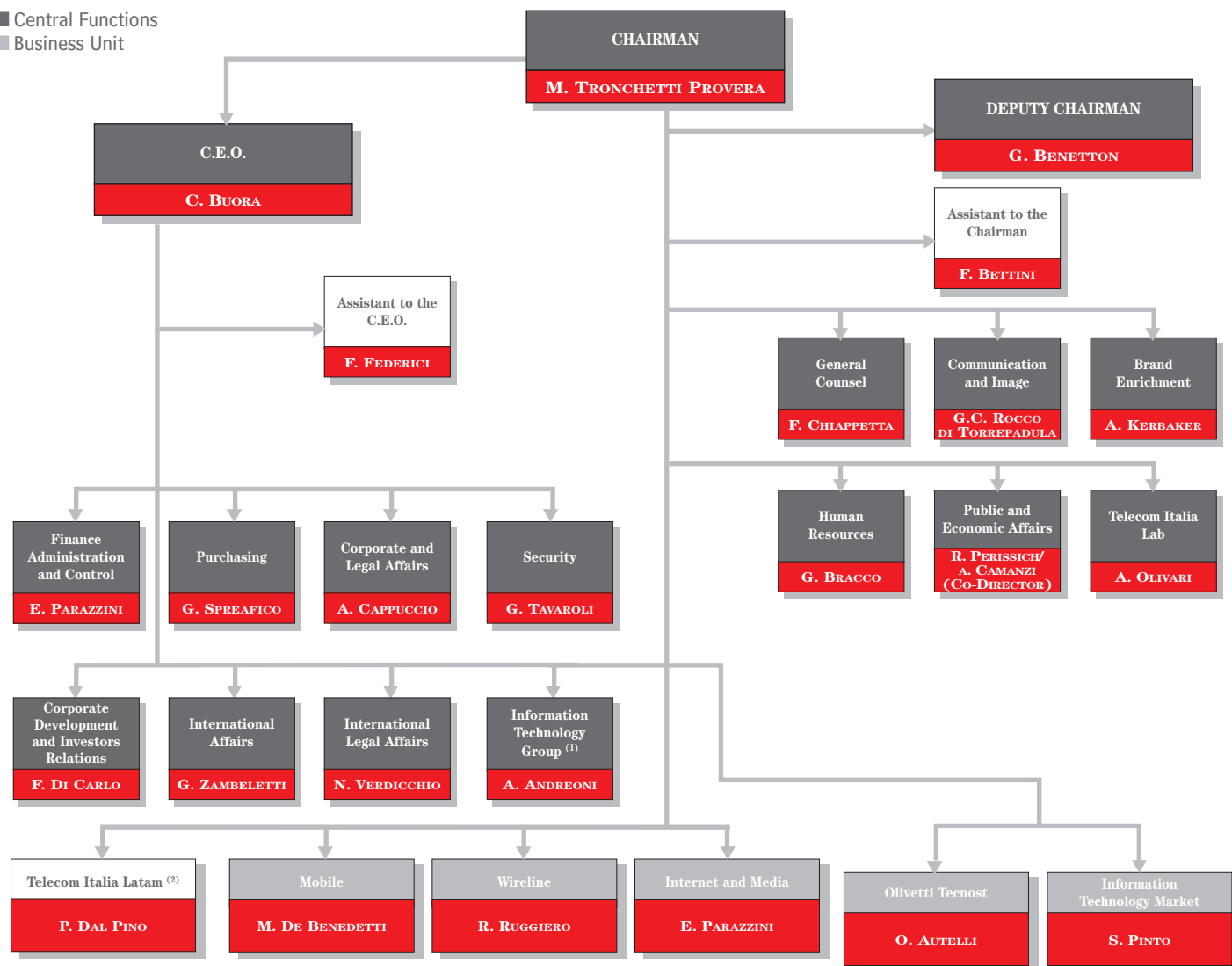
| | | Outlook |
|-----------------|-------|----------|
| STANDARD&POOR'S | BBB + | Stable |
| MOODY'S | Baa2 | Stable |
| FITCH IBCA | A- | Negative |

During the course of 2004, the ratings assigned to Telecom Italia by S&P, Moody's and Fitch remained unchanged, respectively, at BBB+ positive outlook, Baa2 stable outlook and A- stable outlook, in line with the ratings at December 31, 2003. After the announcement of the Telecom Italia/TIM merger on December 7, 2004, the agencies decided to keep the same ratings (S&P and Fitch changed only the outlook, respectively, from positive to stable and from stable to negative).

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■ MACRO-ORGANIZATION CHART - TELECOM ITALIA GROUP AT DECEMBER 31, 2004

■ Central Functions
■ Business Unit



(1) As from January 1, 2005, Marco Forneris is in charge of Information Technology Group.

(2) Telecom Italia Latam has the role of the "delocalized" Corporate function in Latin America. The Business Units – with their present corporate organization structure – are nevertheless responsible for the results of the subsidiaries in Latin America under their control.

Internal Auditing of the Group is entrusted to the consortium company Telecom Italia Audit; the Chairman is Armando Focaroli.

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The organizational Committees of the Group are listed below:

- **Management Committee**, which guarantees coordination of the Group's activities and ensures unitariness in the development and implementation of business strategies;
- **Investments Committee**, which approves investments exceeding specific authorized limits;
- **Purchases Committee**, which promotes coordination of the Group's purchasing processes, monitoring their performance and maximizing synergies among the Business Units/Companies;
- **Business Reviews**, which control the results of each Business Unit, analyze forecasts and operational progress reports and decide on the resulting action plans;
- **Steering Committee "Telecom 2007"**, which guides and approves the Group's initiatives in terms of innovation, development and efficiency, and also controls their progress, for purposes of ensuring the implementation of the merger project voted on December 7, 2004 by the Telecom Italia S.p.A. and TIM S.p.A. Boards of Directors;
- **Steering Committee**, which implements Project 404, aimed at guaranteeing the timely completion of the preliminary steps necessary, at a Group level, for Telecom Italia to fulfill the disclosure requirements on internal control issues, as set forth in Sector 404 of the Sarbanes-Oxley Act of 2002;
- **IT Governance Committee**, which defines the guidelines for the information technology strategies of the Group, directs the relative plans and monitors their progress;
- **Publishing Committee**, which establishes strategic guidelines relating to the publishing lines of reference for the Group. Reporting to the Publishing Committee is the Operating Content Acquisition Committee which purpose is to ensure a unitary vision of the initiatives developed by the Business Units, to leverage the contents present in the Group's plans and packages and to define a synergic approach with outside suppliers;
- **Technological Committee**, which guarantees integrated safeguarding of the innovation and technological development processes;
- **IT Security Committee**, which ensures integrated security in the management of the information and computer security of the Telecom Italia Group;
- **Latin America Purchases Committee** which promotes coordination of the purchasing processes in Latin America, monitoring their performance and maximizing synergies among the operating companies;
- **Latin America Image Awareness and Advertising Committee**, which ensures the comprehensive uniformity of advertising and image awareness initiatives of the Group in Latin America;
- **Latin America Regional Coordination Committee**, which guarantees overall consistency of the Group's activities in Latin America, ensuring unitariness in the development and implementation of business strategies.

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INTERNATIONAL PRESENCE OF TELECOM ITALIA GROUP AT DECEMBER 31, 2004



- Presence through subsidiaries
- Presence through affiliated companies

EUROPE

Major subsidiaries

WIRELINE

- Telecom Italia Sparkle Group *
- Telecom Italia Deutschland GmbH
- HanseNet Telekommunikation GmbH *
- Telecom Italia France
- Group BBNed (Holland)

OTHER ACTIVITIES

- Telecom Italia Finance (Luxembourg)
- Telecom Italia Capital (Luxembourg)

MEDITERRANEAN BASIN

Major subsidiaries

WIRELINE

- Mediterranean Nautilus Group (Mediterranean Basin) *
- Med-1 Group (Mediterranean Basin) *

MOBILE

- TIM Hellas Telecommunications S.A. (Greece) *

Major affiliated companies

MOBILE

- Avea I.H.A.S. (Turkey)



SOUTH AMERICA

Major subsidiaries

WIRELINE

- Latin American Nautilus Group (Latin America) *
- Entel Chile Group (Chile) *
- Entel Bolivia Group (Bolivia) *

MOBILE

- TIM Participações Group (Brazil) *
- Maxitel S.A. (Brazil) *
- TIM Celular S.A (Brazil) *
- Starcel Ltda (Brazil)
- TIM Perú S.A.C. (Peru) *
- Corporacion Digitel C.A. (Venezuela) *
- Blah ! (ex TimNet Com S.A.) (Brazil)
- Entel Chile Group (Chile) *
- Entel Bolivia Group (Bolivia) *

Major affiliated companies

WIRELINE

- Telecom Argentina Group *

MOBILE

- Telecom Argentina Group *

* Comments on the main economic and financial performance of these Companies are provided in the report.

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■ ECONOMIC AND FINANCIAL PERFORMANCE - TELECOM ITALIA GROUP



RESULTS OF OPERATIONS

The **consolidated net income of the Group** in 2004 is euro 781 million (euro 1,902 million before minority interest). In 2003, the consolidated net income of the Group was euro 1,192 million (euro 2,428 million before minority interest).

The change in the consolidated net income of the Group (– euro 411 million) is due to the following factors:

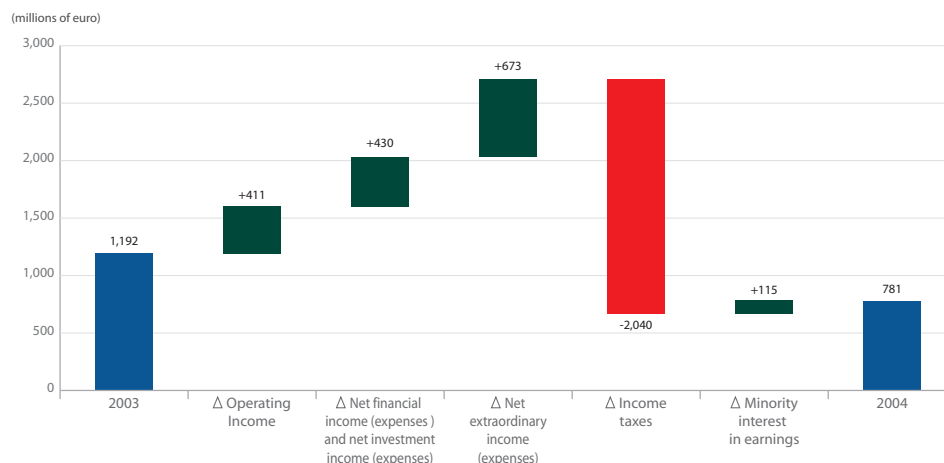
- increase in *operating income* (+ euro 411 million);
- improvement in *net financial income (expenses)* and *net investment income (expenses)* (+ euro 430 million);
- improvement in *net extraordinary income (expenses)* (+ euro 673 million) principally due to lower writedowns and other extraordinary expenses (euro 1,587 million in 2004 compared to euro 2,934 million in 2003), offset in part by lower extraordinary income (euro 1,177 million compared to euro 1,851 million in 2003).

In particular, the year 2004 benefited from prior period income of euro 621 million relating to the TLC fee paid in 1999 as a result of the decision handed down by the TAR of Lazio No. 47/2005 of January 4, 2005 which upheld the appeal filed by Telecom Italia and cancelled the Ministerial Decree dated March 21, 2000 regarding the TLC fee instituted by Law 448/1998 declaring it to be illegal. The year 2003 had included prior period income for non-existent liabilities and reserves relating to the TLC fee (euro 1,465 million) as a result of the verdict returned by the European Court of Justice on September 18, 2003;

- higher *income taxes* of euro 2,040 million, due principally to the posting of deferred tax assets in 2003 (euro 1,266 million), which became recoverable thanks to the merger of Olivetti and Telecom Italia, offset by higher income taxes connected with an improvement in operations;
- lower *minority interest in earnings* (euro 115 million).

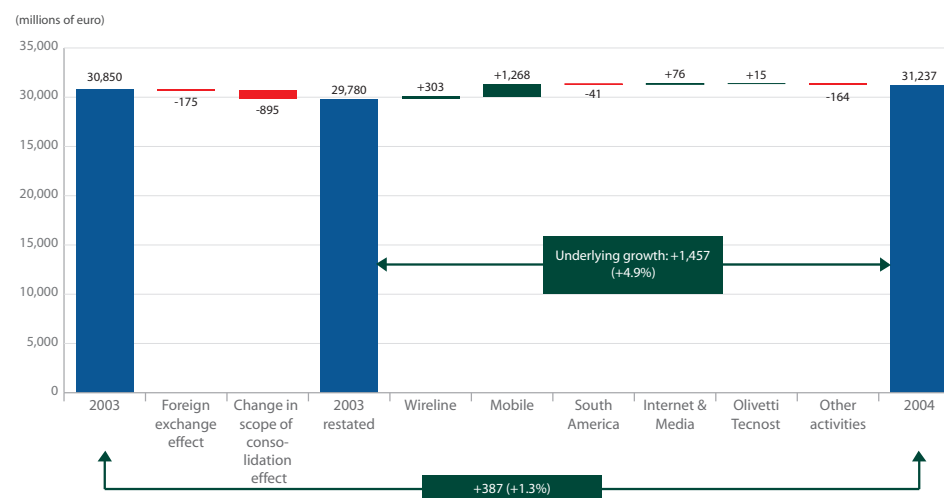
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The following chart summarizes the major items which had an impact on the consolidated net income of the Group in 2004:



Sales and service revenues amount to euro 31,237 million, with an increase of 1.3% compared to euro 30,850 million in 2003. Excluding the negative foreign exchange effect (– euro 175 million, of which euro 150 million relates to the South American companies of the Mobile Business Unit) and the change in the scope of consolidation (euro 895 million, of which euro 703 million relates to the sale of Nuova Seat Pagine Gialle in August 2003), underlying growth is 4.9% (euro 1,457 million).

The following chart summarizes the major items which had an impact on the sales and service revenues in 2004:



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Underlying growth particularly reflects:

- a significant contribution by the Mobile Business Unit (+ euro 1,268 million), mainly due to the good performance of the domestic market (+ euro 474 million) and a positive input by international operations;
- an increase in the revenues of the Wireline Business Unit (+ euro 303 million), achieved thanks to the success of development initiatives in the Broadband market and innovative services, particularly Web services, combined with a stable core Telephone market and enhanced offerings for wholesale services;
- an increase in the revenues of the Internet (+ euro 76 million) and Olivetti Tecnost (+ euro 15 million) Business Units;
- a reduction in the sales of the IT Market Business Unit (– euro 99 million, as a result of booking nonrecurring sales last year on the important contract relating to the Telcal project) and the wireline and integrated telecommunications companies in Latin America (– euro 41 million, mainly in respect of the Entel Chile group).

Revenues from telecommunications services are shown gross of the portion due to third-party operators of euro 4,623 million (euro 4,534 million in 2003).

Foreign sales and service revenues amount to euro 6,629 million (euro 6,039 million in 2003); 47% of the total is localized in the area of South America (42% in 2003). The breakdown of sales and service revenues by customer geographic location is the following:

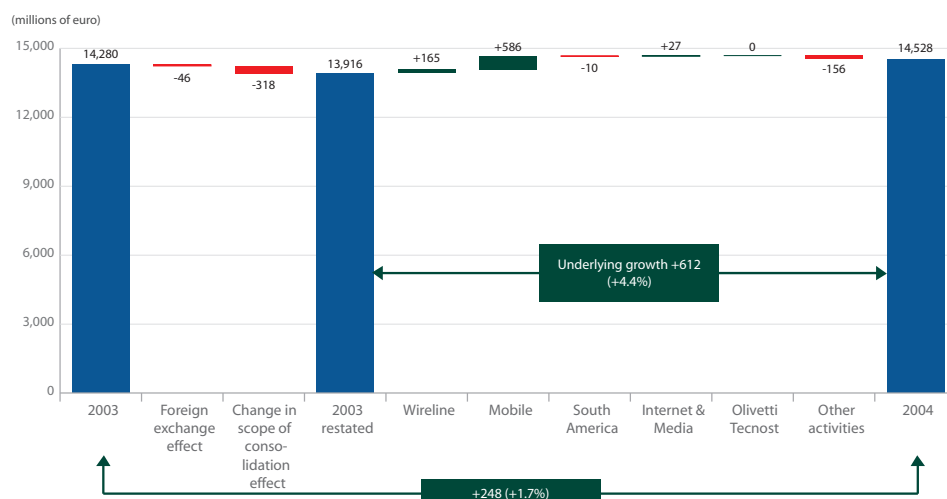
| Geographical area (millions of euro) | 2004 | | 2003 | |
|---|---------------|---------------|---------------|---------------|
| Italy | 24,608 | 78.8% | 24,811 | 80.5% |
| Rest of Europe | 2,588 | 8.3% | 2,478 | 8.0% |
| North America | 537 | 1.7% | 589 | 1.9% |
| Central and South America | 3,118 | 10.0% | 2,566 | 8.3% |
| Australia, Africa and Asia | 386 | 1.2% | 406 | 1.3% |
| Total | 31,237 | 100.0% | 30,850 | 100.0% |

Gross operating profit amounts to euro 14,528 million and grew compared to 2003 by euro 248 million (+1.7%). As a percentage of revenues, gross operating profit represents 46.5% (46.3% in 2003).

Excluding the foreign exchange effect (– euro 46 million) and the impact due to the change in the scope of consolidation (– euro 318 million, mainly as a result of the sale of Nuova Seat Pagine Gialle), underlying growth is 4.4% (+ euro 612 million). Such growth mostly took place in the Mobile Business Unit (+ euro 586 million, of which euro 312 million refers to the domestic market), the Wireline Business Unit (+ euro 165 million) and the Internet & Media Business Unit (+ euro 27 million).

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The following chart summarizes the major items which had an impact on the gross operating profit in 2004:



In greater detail, gross operating profit is impacted by:

- **raw materials and outside services**, equal to euro 13,414 million, up 3.0% compared to 2003 (euro 396 million). The percentage of raw materials and outside services to revenues is 42.9% (42.2% in 2003).
- **labor costs**, equal to euro 4,037 million, are euro 260 million lower than in 2003 (– 6.1%). Besides the change in the scope of consolidation, the decrease is due to a reduction in the average workforce of the Parent Company. The percentage of labor costs to revenues is 12.9% compared to 13.9% in 2003.

Employees at December 31, 2004 number 91,365 (93,187 at December 31, 2003). A breakdown is presented below:

| | 12/31/2004 (a) | 12/31/2003 (b) | Change (a - b) |
|------------------------|-------------------|-------------------|-------------------|
| Italy | 75,034 | 78,069 | (3,035) |
| Outside Italy | 16,331 | 15,118 | 1,213 |
| Total employees | 91,365 | 93,187 | (1,822) |

Compared to December 31, 2003, the reduction of 1,822 employees is due to:

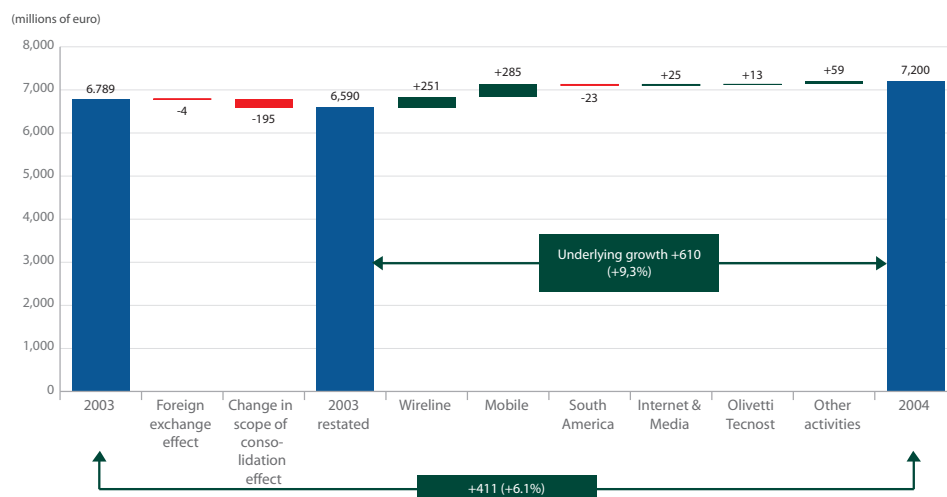
- an increase of 290 persons reflecting turnover (balance between 6,818 persons hired and 6,528 resigned). In Italy this mainly regarded persons hired at Telecontact (+ 882) and, outside Italy, the higher number of employees at the Brazilian mobile telephone companies;
- a decrease of 2,112 persons due to the change in the scope of consolidation, mainly referring to the outsourcing of the "Document Management" business (– 257 at Telecom Italia S.p.A. and Emsa Servizi), "Maintenance and Environmental Services" (– 437 at Telecom Italia S.p.A. and Emsa Servizi), and "Industries & Services" (– 201 at IT Telecom S.p.A.) and the sales of the Webegg group (– 662), Atesia (– 99), CIPI and the GPP group (– 311).

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Operating income pre-amortization of differences on consolidation, equal to euro 8,754 million, increases, compared to 2003, by euro 135 million (1.6%). The percentage of operating income pre-amortization of differences on consolidation to revenues represents 28.0% (27.9% in 2003).

Operating income, equal to euro 7,200 million, increases, compared to 2003, by euro 411 million (+6.1%). As a percentage of revenues, operating income rose from 22.0% in 2003 to 23.0% in 2004. Excluding the foreign exchange effect and the impact of the change in the scope of consolidation, underlying growth is 9.3% (+ euro 610 million). Such growth mostly took place in the Mobile Business Unit (+ euro 285 million), the Wireline Business Unit (+ euro 251 million) and the Internet & Media Business Unit (+ euro 25 million).

The following chart summarizes the major items which had an impact on the operating income in 2004:



In greater detail, operating income is impacted by the following factors:

- the **amortization of the differences on consolidation**, equal to euro 1,554 million (euro 1,830 million in 2003), with a reduction of euro 276 million, principally in connection with the sale of Nuova Seat Pagine Gialle and the writedowns made in 2003;
- the **amortization of other intangibles and the depreciation of fixed assets**, equal to euro 5,092 million (euro 4,949 million in 2003), with an increase of euro 143 million, mainly attributable to the amortization of TIM's UMTS license (euro 134 million).

The breakdown is as follows:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|--|--------------|--------------|-------------------|
| Other intangibles | 1,562 | 1,279 | 283 |
| Fixed assets | 3,530 | 3,670 | (140) |
| Total amortization and depreciation | 5,092 | 4,949 | 143 |

The percentage of the amortization of other intangibles and the depreciation of fixed assets to revenues is 16.3% (16.0% in 2003);

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- **other valuation adjustments**, equal to euro 280 million, chiefly regard writedowns to reduce trade accounts receivable to estimated realizable value. They mainly refer to Telecom Italia (euro 101 million), the Entel Chile group (euro 56 million), TIM (euro 42 million), foreign mobile telephone companies (euro 26 million) and Telecom Italia Sparkle (euro 27 million). Other valuation adjustments show a reduction of euro 197 million compared to 2003 due mainly to lower provisions made by the Parent Company (euro 98 million) in addition to the change in the scope of consolidation following the sale of Nuova Seat Pagine Gialle (euro 28 million);
- **provisions to reserves for risks and charges**, amounting to euro 81 million, present a reduction of euro 13 million compared to 2003;
- **net other income (expenses)** show an expense balance of euro 321 million (an expense balance of euro 141 million in 2003). Details are as follows:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|--|--------------|--------------|-------------------|
| Indirect duties and taxes | (145) | (128) | (17) |
| Losses on sale of fixed assets and intangibles | (23) | (18) | (5) |
| Expenses connected with credit management | (141) | (91) | (50) |
| Late payment fees charged by TLC companies to customers | 85 | 91 | (6) |
| Portion of capital grants credited to income during the year | 53 | 64 | (11) |
| Sundry other income and expenses | (150) | (59) | (91) |
| Total | (321) | (141) | (180) |

The increase in sundry other income and expenses is primarily connected with dealings between Telecom Italia and other telephone operators.

Net financial income (expenses) show an expense balance of euro 1,952 million, an improvement of euro 240 million compared to 2003. Details are as follows:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|--|----------------|----------------|-------------------|
| Net financial income (expenses) | (1,951) | (2,171) | 220 |
| Value adjustments to financial assets, other than equity investments | (1) | (21) | 20 |
| Total | (1,952) | (2,192) | 240 |

The contraction in net financial expenses, compared to 2003, is due to the absence of expenses relating to the JP Morgan put/call options on Seat Pagine Gialle shares (euro 236 million) and the fees sustained for credit lines to fund the Olivetti - Telecom merger (euro 98 million). The improvement is partly offset by the increase in other expenses not directly correlated to debt exposure.

Net investment income (expenses) show an income balance of euro 118 million (an expense balance of euro 72 million in 2003), with an improvement of euro 190 million compared to 2003. Details are as follows:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|---|-------------|-------------|-------------------|
| Income from investments, net | 116 | 17 | 99 |
| Net revaluations (writedowns) of equity investments | 14 | (76) | 90 |
| Amortization of differences on consolidation, regarding investments accounted for using the equity method | (12) | (13) | 1 |
| Total | 118 | (72) | 190 |

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In particular, income from investments, net, includes euro 62 million of gains on the sale, in January 2004, of the remaining stake in Telekom Austria and euro 24 million from the release to income of the remaining portion of the gain on the sale, in 2002, of Mobilkom Austria to the same Telekom Austria. This caption also includes dividends on TIM shares recorded in current assets (euro 10 million).

Net revaluations (writedowns) of equity investments in 2004 include:

- the writeback of TIM shares in current assets to the market value at the beginning of December 2004 (euro 32 million, euro 2 million in 2003). Starting from December 2004, following the announcement of the cash tender offer for TIM shares and the merger of TIM in the Parent Company Telecom Italia, such shares have been consolidated.
- the Group's equity in the earnings (losses) of the other companies (losses of euro 18 million, euro 15 million in 2003). The year 2003 had included the writedown of Sky Italia (euro 96 million) and the Group's equity in the earnings of Etec S.A. Cuba for euro 33 million. In 2004, the adjustment of the investment in Etec S.A. Cuba to equity was compensated by a writedown of goodwill for the same amount.

Net extraordinary income (expenses) show an expense balance of euro 410 million (an expense balance of euro 1,083 million in 2003), with an improvement of euro 673 million.

In particular:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|--|--------------|----------------|-------------------|
| Gains from divestitures of long-term investments and business segments | 190 | 105 | 85 |
| Prior period income relating to the TLC license fee | 621 | 1,465 | (844) |
| Other extraordinary income | 366 | 281 | 85 |
| Total extraordinary income | 1,177 | 1,851 | (674) |
| Extraordinary expenses | (1,587) | (2,934) | 1,347 |
| Total net extraordinary income (expenses) | (410) | (1,083) | 673 |

Gains from divestitures of long-term investments include euro 24 million from the sale of the entire stake held in Mirror International Holding Sarl as well as euro 61 million relating to the release of the remaining part of the gain on the sale, in 2001, of 70% of Mirror International Holding, the company to which the investments in the satellite consortia had previously been transferred.

Other extraordinary income, equal to euro 366 million, increased by euro 85 million compared to 2003, and includes:

- euro 177 million for the release of the reserves for risks, of which euro 109 million was set aside for the Brazilian subsidiary TIM Celular;
- euro 189 million for prior period income and other extraordinary income.

Extraordinary expenses amount to euro 1,587 million and include:

- euro 282 million relating to the settlement with De Agostini, which ended with the purchase 40% of Webfin for euro 325 million (of which euro 287 million refers to the price and euro 38 million to the reimbursement of the expenses incurred by De Agostini Invest to cover the losses and recapitalize Webfin starting from July 2001) compared to a value established by independent valuers of euro 43 million;
- euro 182 million (euro 273 million in 2003) of expenses and provisions for employee cutbacks and layoffs (of which euro 146 million is borne by the Parent Company, euro 196 million in 2003);

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- euro 169 million (euro 406 million in 2003) to write down the differences on consolidation relating to consolidated companies: euro 162 million for Entel Chile following the decision to dispose of the subsidiary and euro 7 million for the South American mobile telephone company Blah! to downsize operations. In 2003, the writedowns of the differences on consolidation had included euro 195 million for Entel Chile, euro 132 million for Digitel Corporation, euro 42 million for EPIClink and euro 37 million for other minor companies;
- euro 158 million for the reorganization of the investments held by the Telecom Italia Group in the Mediterranean Nautilus group and in the Med 1 group, after reaching a preliminary agreement in December 2004 with the minority shareholders of Med SA, Med Ltd and Med 1 to resolve certain conflicting situations referring to MED SA's and Telecom Italia's put, respectively, on 49% of Med Ltd and Med 1 shares, also to resolve the arbitration proceedings set into motion in Luxembourg by the Fishman group (FTT) aimed at the restitution of the sums paid to the Telecom Italia Group in 2000 for the purchase of 30% of MED SA; The transactions negotiated, which call for the buyback of all the minority shares in Med Ltd and in Med 1, allow Telecom Italia to strengthen its presence in the IP services and "wholesale" data sector in the eastern Mediterranean area.
- euro 152 million relating to provisions to reserves for extraordinary risks for the sanction levied on the Parent Company by the Antitrust Authority for the alleged abuse of a dominant position;
- euro 100 million (euro 295 million in 2003) for provisions and writedowns of fixed assets and intangibles, made by the Latin American Nautilus group (euro 56 million) under reorganization programs, by the Entel Chile group (euro 11 million) and by other minor companies (euro 33 million). In 2003, the provisions and writedowns of fixed assets and intangibles had been made by the Latin American Nautilus group (euro 235 million), by Telecom Italia Learning Service (euro 27 million), by EPIClink (euro 15 million) and by other minor companies (euro 18 million);
- euro 66 million for expenses under ex Law 58/1992 to cover employees under the former "Telephone Employees Pension Fund" (FPT) (euro 387 million in 2003, inclusive of euro 315 million for the recalculation of the debt in view of the progress on the dispute with INPS);
- euro 27 million for the provision to adjust the investment in Finsiel to its estimated sales value;
- euro 451 million for other extraordinary expenses and prior period expenses. Details are as follows:
 - euro 121 million to writeoff prior years' receivables balances carried out by the Parent Company and other Group companies;
 - euro 42 million of expenses connected with the tender offer for TIM shares and the announced merger of TIM and the Parent Company Telecom Italia;
 - euro 37 million of expenses booked by the Parent Company for damages caused to the company's assets as a result of natural events or brought about by third parties (euro 33 million in 2003);
 - euro 31 million of prior years' indirect duties and taxes (euro 48 million in 2003, inclusive of the portion of the cost of the tax amnesty not covered by the reserve for income taxes);
 - euro 27 million for the Parent Company's booking of liabilities relating to prior years, principally in respect of matters concerning interconnection (euro 35 million in 2003);
 - euro 19 million relating to provisions for corporate-related transactions;
 - euro 16 million for losses on the sale of intangibles, fixed assets and long-term investments (euro 42 million in 2003),
 - euro 2 million (euro 139 million in 2003) for provisions for risks and charges on equity investments. In 2003, the provisions for risks and charges on equity investments had included euro 59 million relating to the Digitel dispute and euro 30 million to expenses to be paid to Mirror in reference to the lower price on the sale of Inmarsat compared to the reference value used in 2001 when Inmarsat was transferred by Telecom Italia to Mirror;
 - euro 156 million of prior period expenses and other extraordinary expenses (euro 238 million in 2003).

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Extraordinary expenses in 2003 had included, in addition to the above:

- losses and expenses relating to the spin-off and sale of Nuova Seat Pagine Gialle (euro 269 million) and the writedown of the differences on consolidation of TI Media (euro 348 million);
- expenses referring to the Telecom Italia and Olivetti merger (euro 118 million) and the settlement with Pagine Italia (euro 55 million).

Income taxes amount to euro 3,054 million (euro 1,014 million in 2003) and include euro 230 million of income taxes relating to prior period income booked as a result of the cancellation of the TLC license fee (euro 621 million). The year 2003 had benefited from deferred tax assets of euro 1,266 million which became recoverable thanks to the Olivetti/Telecom Italia merger, countered by euro 562 million of income taxes relating to the cancellation of the TLC license fee (euro 1,465 million).

FINANCIAL CONDITION

Intangibles, fixed assets and long-term investments, amounting to euro 52,457 million, decreased by euro 2,116 million compared to the end of 2003.

In detail:

- **intangibles** decreased from euro 33,853 million at the end of 2003 to euro 32,874 million at December 31, 2004. The reduction is due to the difference between investments (euro 2,445 million), amortization and writedowns of the differences on consolidation during the year (euro 3,577 million) and the change in the scope of consolidation, the foreign exchange effect and other movements (+ euro 153 million);
- **fixed assets** decreased from euro 18,324 million at the end of 2003 to euro 17,717 million at December 31, 2004. The reduction is due to the difference between investments (euro 3,320 million), depreciation for the year (euro 3,530 million) and disposals, the change in the scope of consolidation, the foreign exchange effect and other movements (– euro 397 million);
- **long-term investments** decreased from euro 2,396 million at the end of 2003 to euro 1,866 million at December 31, 2004. The reduction is due to the difference between investments (euro 153 million), disposals and reimbursements of long-term receivables (euro 595 million) and the equity method of valuation and other movements (– euro 88 million). The carrying value of the investment in the affiliated company Avea I.H.A.S. (ex-TT&TIM I.H.A.S., the company resulting from the merger of Is TIM with the operator Aycell) is maintained at a zero balance and the receivables due TIM International from Is TIM, also completely written off, were converted to the share capital of the affiliated company Is TIM as part of the merger with Aycell.

Investments total euro 5,918 million (euro 11,454 million in 2003). Details are as follows:

| (millions of euro) | 2004 (a) | 2003 (b) | Change (a - b) |
|------------------------------|--------------|---------------|-------------------|
| Industrial investments | 5,335 | 4,894 | 441 |
| Differences on consolidation | 430 | 5,096 | (4,666) |
| Financial investments | 153 | 1,464 | (1,311) |
| Total investments | 5,918 | 11,454 | (5,536) |

Industrial investments, equal to euro 5,335 million, increased by euro 441 million compared to December 31, 2003. The increase mainly refers to the Mobile Business Unit (+ euro 533 million) against a reduction in investments by other Group companies (– euro 92 million).

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Investments in differences on consolidation in 2004 essentially refer to the settlement with De Agostini which ended with the purchase of 40% of Webfin for euro 325 million (euro 38 million for the reimbursement of the absorption of losses and the recapitalization of Webfin beginning from July 2001) compared to a value established by independent valuers of euro 43 million and a share of net equity of euro 1 million, as well as the purchase of the remaining stake of the Venezuelan subsidiary Digitel (euro 95 million). Investments in 2003 had chiefly referred to the difference (euro 4,551 million) between the payment of the tender offer for Telecom Italia shares by Olivetti (euro 5,274 million) and the share of net equity acquired (euro 723 million) as well as the exercise of the JP Morgan put option on Seat Pagine Gialle shares (euro 428 million).

Financial investments in 2004 mainly relate to equity investments, in particular for the investment in the share capital of Etec S.A. Cuba (euro 26 million), Sky Italia (euro 55 million) and other financial investments (euro 72 million).

Financial investments in 2003 had mainly related to the share of the net equity of the merged company acquired under the tender offer (euro 723 million), the purchase of treasury stock by the acquired company, cancelled at the time of the merger (euro 47 million), the purchase of the equity interest in LI.SIT. (euro 54 million), increases in the share capital of Sky Italia (euro 332 million), the purchase of the call options on the share capital of Sofora - Argentina (euro 49 million) and other financial investments (euro 259 million).

Working capital shows a negative balance of euro 3,071 million (a negative balance of euro 638 million at December 31, 2003). The change of euro 2,433 million is due to the sale of Telekom Austria (euro 708 million), the tax charge for the year less payments made (euro 1,538 million) and the changes in trade accounts receivable/payable and other items (euro 187 million).

Shareholders' equity amounts to euro 19,861 million (euro 20,589 million at the end of 2003), of which the Parent Company interest is euro 15,172 million (euro 16,092 million at December 31, 2003) and the minority interest is euro 4,689 million (euro 4,497 million at December 31, 2003).

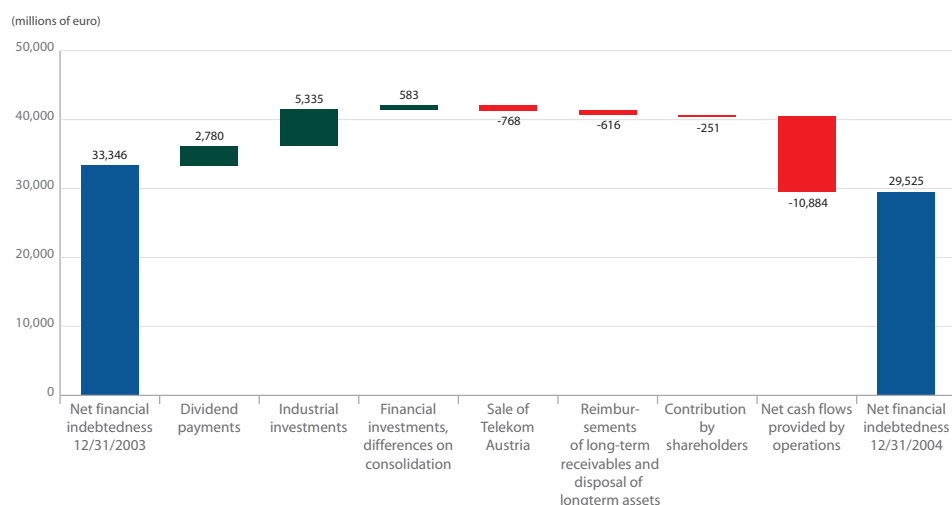
The changes in shareholders' equity are the following:

| (millions of euro) | 2004 | 2003 |
|---|---------------|---------------|
| At beginning of year | 20,589 | 20,624 |
| Contribution by shareholders, conversion of bonds and stock options | 251 | 33 |
| Net income of the Parent Company and minority interest | 1,902 | 2,428 |
| Dividends and reserves distributed to third parties paid by: | (2,780) | (1,049) |
| - Telecom Italia S.p.A. | (1,730) | (794) |
| - TIM S.p.A. | (991) | (185) |
| - Other Group companies | (59) | (70) |
| Shares subscribed on capital increases in progress | 41 | - |
| Consolidation of TIM S.p.A. shares previously recorded in current assets | (20) | - |
| Effects of the share withdrawals, the tender offer, the cancellation of both treasury stock bought back by the merged company and Telecom Italia shares held by Olivetti and reclassified from working capital to long-term investments | - | (1,117) |
| Deconsolidation of Nuova Seat Pagine Gialle | - | (126) |
| Translation adjustments and other changes | (122) | (204) |
| At end of year | 19,861 | 20,589 |

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Net financial indebtedness amounts to euro 29,525 million at December 31, 2004, with a decrease of euro 3,821 million compared to euro 33,346 million at the end of 2003.

The following chart summarizes the major items which had an impact on the change in net indebtedness during the course of 2004:



In particular:

- financial investments and differences on consolidation, equal to euro 583 million, refer to financial investments for transactions involving subsidiaries and affiliated companies and long-term receivables (euro 153 million), and investments for differences on consolidation (euro 430 million), as described in detail earlier;
- reimbursements of long-term receivables and disposals of long-term assets, equal to euro 616 million, refer to:
 - sales of quotas/shares of Sky (euro 88 million), Euskaltel (euro 14 million), Cipi (euro 10 million), Cirsà (euro 31 million), Mirror (euro 73 million for the sale and euro 2 million for the loan repayment), Netco Redes (euro 30 million) and Pirelli & C. Real Estate (euro 24 million);
 - receipts, from Tiglio I as a reimbursement for the loan from shareholders and as a distribution of reserves (euro 104 million);
 - other sales and reimbursements of long-term receivables and sales of fixed assets and intangibles (euro 240 million).

Transactions for the securitization and factoring of trade accounts receivable in 2004 led to a reduction in net financial indebtedness at December 31, 2004 of euro 1,824 million (euro 1,201 million at the end of 2003), of which euro 786 million relates to securitization and euro 1,038 million to factoring transactions, including euro 71 million executed in December 2003.

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Net financial indebtedness is detailed in the following table:

| (millions of euro) | Within 12 months | Beyond 12 months | Total 12/31/2004 | Total 12/31/2003 |
|--|---------------------|---------------------|---------------------|---------------------|
| Debentures | 3 | 29,637 | 29,640 | 30,053 |
| Convertible debentures | 803 | 4,789 | 5,592 | 7,312 |
| Total debentures | 806 | 34,426 | 35,232 | 37,365 |
| Due to banks | 800 | 1,030 | 1,830 | 2,460 |
| Due to other lenders | 318 | 1,305 | 1,623 | 1,012 |
| Other liabilities | 91 | 40 | 131 | 519 |
| Payables to subsidiaries and affiliated companies | 9 | 15 | 24 | 42 |
| Trade accounts payable | 3 | 1 | 4 | 9 |
| Taxes payable | | | | 58 |
| Total other financial payables | 1,221 | 2,391 | 3,612 | 4,100 |
| Total gross financial indebtedness | 2,027 | 36,817 | 38,844 | 41,465 |
| Liquid assets | (8,562) | | (8,562) | (4,877) |
| Other securities in current assets | (932) | | (932) | (2,719) |
| Other accounts receivable | (375) | | (375) | (796) |
| Receivables from subsidiaries and affiliated companies | (7) | | (7) | (30) |
| Receivables for the sale of securities | (2) | | (2) | (60) |
| Total financial receivables in current assets and liquid assets | (9,878) | | (9,878) | (8,482) |
| Accrued expenses and deferred income | 1,351 | 29 | 1,380 | 1,330 |
| Accrued income and prepaid expenses | (510) | (311) | (821) | (967) |
| Balance of financial accruals and deferrals | 841 | (282) | 559 | 363 |
| Net financial indebtedness at December 31, 2004 | (7,010) | 36,535 | 29,525 | 33,346 |

Gross indebtedness due beyond one year amounting to euro 36,817 million (not taking into account a net asset balance of euro 282 million relating to medium/long-term accruals, deferrals and prepayments), corresponds to 95% of total gross indebtedness, euro 30,852 million at the end of 2003 (74%). At December 31, 2004, short-term borrowings include the current portion of medium/long-term debt totaling euro 1,364 million (euro 9,289 million at December 31, 2003).

During 2004, Telecom Italia S.p.A. issued four new notes falling under the Euro Medium Term Note Program for a total of euro 10 billion, approved by the Board of Directors' meeting held October 10, 2003:

- On January 29, 2004, euro 3,000 million was issued divided into three tranches:
 - euro 1,000 million, interest at the 3-month Euribor + 0.33%, issue price of 99.927, maturing October 29, 2007;
 - euro 750 million, 4.50%, coupon, issue price of 99.56, maturing January 28, 2011;
 - euro 1,250 million, 5.375% coupon, issue price of 99.07, maturing January 29, 2019;
- On April 8, 2004, floating rate notes were issued for euro 110 million under a private placement, interest at the 3-month Euribor + 0.60%, issue price of 100, maturing on March 30, 2009;
- On June 24, 2004, fixed rate notes were issued for GBP 850 million, 6.375% coupon, issue price of 98.85, maturing June 24, 2019;
- On November 23, 2004, under a private placement, notes were issued for euro 120 million, interest at the 3-month Euribor + 0.66%, issue price of 100, maturing November 23, 2015.

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On October 6, 2004, Telecom Italia Capital S.A. issued notes for a total of USD 3,500 million guaranteed by Telecom Italia S.p.A., divided into three issues:

- USD 1,250 million, at an annual 4% fixed rate, issue price of 99.732, maturing January 15, 2010;
- USD 1,250 million, at an annual 4.5% fixed rate, issue price of 99.651, maturing September 30, 2014;
- USD 1,000 million, at an annual 6% fixed rate, issue price of 99.081, maturing September 30, 2034.

Moreover, the Telecom Italia Board of Directors' Meeting held on November 9, 2004 authorized the issue of non-convertible notes for a maximum amount of euro 4.9 billion to be issued by December 31, 2006 and granted a full guarantee to Telecom Italia Capital S.A. for any further note issues up to a maximum of USD 5 billion.

During 2004, Telecom Italia also sold bonds under the 2002-2022 issue set aside for subscription by the employees of the Group for a face value of euro 0.7 million. According to the bond indenture, the Company must be the counterpart for the purchases made by the holders of this category of securities.

All issues of notes and new medium/long-term debt secured were aimed at refinancing all the debt maturing in the years 2005 and 2006, consistently with the Group's objective of financing in advance all debt maturities for the following 12-18 months, thus giving the Group a sufficient margin of liquidity. The above bond issues have made it possible to take advantage of favorable interest rates and credit spreads, also allowing a diversification among markets, instruments and maturities, mainly in the Group's three markets of reference (Euro, British pound and U.S. dollar)

The notes directed to third parties issued by companies of the Group do not contain either financial covenants or clauses that provide for the notes to be called in advance on account of events other than the insolvency of the Telecom Italia Group. Furthermore, the redemption of notes and the payment of interest are neither covered by specific guarantees nor are there any commitments for assuming guarantees, except for the guarantees granted by Telecom Italia for the notes issued by Telecom Italia Finance S.A. and by Telecom Italia Capital S.A..

On October 14, 2004, Telecom Italia Capital S.A. finalized the exchange offer between:

- the notes issued on October 29, 2003 (not registered with the Securities and Exchange Commission - SEC) for a total of USD 4 billion, divided into three groups (Series A, Series B and Series C); and
- the notes in a new issue registered with the SEC.

The notes in the new issue have been registered under the United States Securities Act of 1933 and carry the same terms and conditions as those of the notes which were not registered. Both notes are unconditionally guaranteed by Telecom Italia S.p.A..

The amount actually exchanged at the conclusion of the offer, after confirmation of the offers tendered under the guaranteed delivery procedure was USD 3,957,588,000: Series A notes for USD 985,926,000, Series B notes for USD 1,972,460,000 and Series C notes for USD 999,202,000.

Such amount represents about 98.94% of the total equivalent amount of the notes issued in October 2003.

In 2004, notes were repaid for a total of euro 7,800 million, of which:

- euro 1,331 million on January 1, 2004 relating to convertible bonds issued by Telecom Italia S.p.A.;

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- euro 385 million on March 19, 2004 relating to convertible bonds issued by Olivetti Finance N.V. and guaranteed by Telecom Italia S.p.A.;
- euro 1,500 million on March 22, 2004 relating to notes issued by Telecom Italia S.p.A., original maturity date of June 21, 2005, called in advance by exercising the right stated in the bond indenture;
- euro 1,000 million on April 20, 2004 relating to notes issued by Telecom Italia Finance S.A. (originally Sogerim) and guaranteed by Telecom Italia S.p.A.;
- euro 3,550 million on July 30, 2004 relating to notes issued by Telecom Italia Finance S.A. (originally Olivetti Finance N.V) and guaranteed by Telecom Italia S.p.A.;
- euro 30 million relating to notes issued by Entel Chile.

Moreover, it should be mentioned that the notes 2002-2005 equal to euro 500 million issued by Telecom Italia Finance S.A. with a quarterly coupon indexed to the 3-month Euribor +130 basis points provided for the extension of the maturity date, as elected by the noteholders. Each extension in the maturity date is for successive periods of 21 months with the final maturity date not to extend beyond March 14, 2012.

In accordance with the terms and conditions of the notes, noteholders in possession of notes totaling euro 283,000 chose not to extend the notes. For those, instead, that decided to extend the maturity date, for notes totaling euro 499,717,000, Telecom Italia Finance S.A. issued new notes on December 14, 2004 denominated "Telecom Italia Finance S.A. euro 499,717,000 Guaranteed Floating Rate Extendable Notes Due 2006" with a new maturity date of December 14, 2006.

On March 26, 2004, a total of euro 850 million of securities, repurchased in prior years, issued by Olivetti Finance N.V., were cancelled. These securities referred to notes of euro 650 million under the total note issue of euro 4,200 million (the residual amount of euro 3,550 million was repaid in July 2004) and to notes of euro 200 million maturing in February 2005 which have thus been completely cancelled.

Beginning in July 2004, Telecom Italia Finance S.A. repurchased notes for a face value of euro 255 million under the note issue of euro 3,000 million issued by Sogerim (company merged by Telecom Italia Finance in 2002) maturing April 20, 2006 with coupon interest at 6.375%. After repurchasing the notes, the residual face value of the debt is therefore equal to euro 2,745 million.

On March 30, 2004, the new 3-year credit line was signed for euro 6.5 billion. This new line replaces the syndicated credit line of the same amount arranged by the acquiring company Olivetti as part of the merger in 2003. The first tranche (euro 4.5 billion) was due in April 2004. The borrower is not required to abide by specific financial statement ratios and the type of commitment undertaken by the banks guarantees unconditional availability of credit for the line in question.

On December 8, 2004, Telecom Italia signed a loan contract, governed by British law, for an amount of up to a maximum of euro 12,000 million, with a syndicate composed of national and international banks. This loan will be used to service the payment of the part of the price not paid using own resources under the partial voluntary cash tender offer launched by Telecom Italia for the purchase of ordinary shares and all savings shares issued by Telecom Italia Mobile. Repayment of the loan is divided into three parts, having different maturity dates and giving Telecom Italia the possibility of extending the maturity dates of the first two tranches:

- first tranche of euro 3,000 million with maturity at 12 months, extendable for a further 12 months;
- second tranche of euro 6,000 million with maturity at 36 months, extendable for a further 9 months;
- third tranche of euro 3,000 million with maturity at 60 months.

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The following table shows the composition of gross financial indebtedness:

| Composition | At 12/31/2004 | | | | At 12/31/2003 | | | |
|-----------------------|---------------|------------|------------------|------------|---------------|------------|---------------|------------|
| | euro | % | Foreign currency | % | Total | % | Total | % |
| (millions of euro) | | | | | | | | |
| Medium/long-term debt | 28,985 | 95 | 7,832 | 95 | 36,817 | 95 | 30,852 | 74 |
| Short-term borrowings | 1,608 | 5 | 419 | 5 | 2,027 | 5 | 10,613 | 26 |
| Total | 30,593 | 100 | 8,251 | 100 | 38,844 | 100 | 41,465 | 100 |

The maturities of gross financial indebtedness are presented in the following table:

| Maturities of gross financial indebtedness (millions of euro) | Notes | Medium/long-term | | Short-term | Total |
|--|---------------|----------------------|---------------|------------|---------------|
| | | Loans and other debt | Sub total | | |
| by December 2005 | 806 | 558 | 1,364 | 663 | 2,027 |
| by December 2006 | 6,311 | 395 | 6,706 | | 6,706 |
| by December 2007 | 4,100 | 853 | 4,953 | | 4,953 |
| by December 2008 | 2,487 | 167 | 2,654 | | 2,654 |
| by December 2009 | 3,964 | 43 | 4,007 | | 4,007 |
| beyond December 2009 | 17,564 | 933 | 18,497 | | 18,497 |
| Total | 35,232 | 2,949 | 38,181 | 663 | 38,844 |

At the end of December 2004, liquid assets and financial receivables amount to euro 9,878 million (euro 8,482 million at the end of 2003). Details are as follows:

LIQUID RESOURCES AND FINANCIAL RECEIVABLES

(millions of euro)

| | | | |
|---|-------------|-------|--------------|
| Liquid resources (classified by technical form) | | | |
| - Deposits | | 8,114 | |
| - Current accounts | | 448 | |
| Total | (A) | | 8,562 |
| Other securities in current assets | | | |
| - euro commercial paper | | 328 | |
| - Own notes | | 163 | |
| - Notes | | 399 | |
| - Other securities | | 42 | |
| Total | (B) | | 932 |
| | (C = A + B) | | 9,494 |
| Other financial receivables | | | (D) |
| | | | 384 |
| Total liquid resources and financial receivables | (C + D) | | 9,878 |

The different technical forms used for the investment of liquid resources at December 31, 2004 can be further analyzed as follows:

Deposits (euro 8,114 million):

- Maturities. euro 7,957 million has a maximum maturity date of two months (euro 7,852 million is due by the end of January 2005), while the remaining amount, represented by certificates of deposit which are highly liquid, refer to the investment of cash resources by the subsidiaries in Brazil and Bolivia;
- Counterpart risk. Deposits were made with primary banking and financial institutions with a high credit rating. In particular, euro 7,885 million refers to deposits with counterparts with at least an A rating.

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- Country risk. The geographic location of deposits is as follows: euro 7,664 million in Europe (mainly London), euro 148 million in the United States and euro 302 million in South America (referring to investments made by the subsidiaries located in Brazil, Chile and Bolivia). Euro Commercial Paper (euro 328 million): all commercial paper has a maximum maturity date of one month. The issuers all have AAA and AA ratings and headquarters in Europe. Notes and other securities totaling euro 441 million (of which euro 431 million has been invested by the Luxembourg subsidiary Telecom Italia Finance S.A.) refer to notes issued by counterparties with at least an A rating with different maturities over the years, but all are actively traded and therefore can easily be converted to liquidity.

This financial structure will enable the Group to meet maturities, particularly in reference to:

MEDIUM/LONG-TERM DEBT MATURING IN 2005-2006

| (millions of euro) | Notes | Loans and other | Total |
|---|--------------|-----------------|--------------|
| Year 2005 | 806 | 558 | 1,364 |
| Year 2006 | 6,311 | 395 | 6,706 |
| Total | 7,117 | 953 | 8,070 |
| Financed by: | | | |
| Liquid assets and securities in current asset at 12/31/2004 | | | 9,494 |

Moreover, it should be mentioned that at December 31, 2004, unused committed credit lines maturing March 2007 amount to euro 6,500 million, in addition to the previously-described loan of euro 12,000 million to service the cash tender offer for TIM shares.

Telecom Italia Group financial risk management objectives and policy

The Telecom Italia Group, with regard to financial risk management, has put into place guidelines for the control and management of such risks. In particular, the stages and the principles which govern such activity call for, under the established guidelines, the existence of an internal committee to monitor the level of exposure to market risks (interest rate risks and foreign exchange risks) consistently with the defined objectives, the management of risks using derivative financial instruments, the ongoing valuation of the credit risks of the counterparties of the derivative contracts. As to these counterparties, which are banks and financial institutions with a high rating, they are constantly monitored for purposes of minimizing the credit risk.

The Telecom Italia Group tends to diversify market risks connected with its operational and financial activities in order to minimize exposure to interest rates through the diversification of the portfolio. Bearing this in mind, the Group puts into place derivative financial instruments on a selective basis. Exposure of debt to variations in the exchange rates is also hedged so as to avoid any undesirable impact on the statement of income and cash flows.

Telecom Italia Group is exposed to market risks arising from variations in interest rates, mainly in Europe, the United States, the United Kingdom and Latin America. The Group decides on an optimal composition between fixed-rate debt and floating-rate debt and utilizes derivative financial instruments in order to arrive at the composition of the pre-established debt. Interest Rate Swaps (IRS) and Interest Rate Options (IRO) are therefore used to reduce the exposure of both fixed and floating rate loans and bonds to interest rate risk.

Cross Currency and Interest Rate Swaps (CCIRS) and Currency Forwards are used to covert foreign currency loans and bonds – principally in U.S. dollars and British pounds – to the currencies of the financial statements of the subsidiaries.

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As a result of the above hedging activities, at December 31, 2004, the financial debt of the Telecom Italia Group is not subject to foreign exchange risk.

In order to determine the fair value of derivative instruments, the Telecom Italia Group uses various valuation models. The market value of IRSs and CCIRSs reflects the difference between the fixed rate which should be paid/received and the market interest rate (having the same maturity as the swap) at the valuation date. With reference to IRSs, the notional value does not represent the amount exchanged between the parties and thus does not constitute a measure of the exposure to credit risk, which, instead, is limited to the value of the differential of the interest rates to be paid/received.

The fair value of CCIRSs, on the other hand, also depends on the differential between the exchange rate of reference at the date of inception and the exchange rate at the valuation date, since CCIRSs imply the exchange of the capital of reference, in the respective currencies of denomination, in addition to the exchange of interest flows at the maturity date and at any intermediate payment dates.

QUARTERLY HIGHLIGHTS - TELECOM ITALIA GROUP

| (millions of euro) | 2004 | | | | | 2003 (*) | | | | |
|---|-------------|-------------|-------------|-------------|-----------|-------------|-------------|-------------|-------------|-----------|
| | 1st Quarter | 2nd Quarter | 3rd Quarter | 4th Quarter | Year 2004 | 1st Quarter | 2nd Quarter | 3rd Quarter | 4th Quarter | Year 2003 |
| Sales and service revenues | 7,418 | 7,804 | 7,690 | 8,325 | 31,237 | 7,291 | 7,858 | 7,533 | 8,168 | 30,850 |
| <i>Change over same quarter prior year</i> | 1.7% | -0.7% | 2.1% | 1.9% | 1.3% | -3.2% | -1.9% | -1.7% | -0.5% | -1.8% |
| Gross operating profit | 3,494 | 3,595 | 3,699 | 3,740 | 14,528 | 3,374 | 3,666 | 3,608 | 3,632 | 14,280 |
| <i>Change over same quarter prior year</i> | 3.6% | -1.9% | 2.5% | 3.0% | 1.7% | -0.2% | 0.7% | -3.0% | 0.1% | -0.6% |
| % Gross operating profit to Revenues | 47.1% | 46.1% | 48.1% | 44.9% | 46.5% | 46.3% | 46.7% | 47.9% | 44.5% | 46.3% |
| Operating income pre-amortization of differences on consolidation | 2,173 | 2,200 | 2,234 | 2,147 | 8,754 | 2,093 | 2,313 | 2,233 | 1,980 | 8,619 |
| <i>Change over same quarter prior year</i> | 3.8% | -4.9% | 0.0% | 8.4% | 1.6% | 3.0% | 3.9% | -5.8% | 0.7% | 0.3% |
| % Operating income pre-amortization of differences on consolidation to Revenues | 29.3% | 28.2% | 29.1% | 25.8% | 28.0% | 28.7% | 29.4% | 29.6% | 24.2% | 27.9% |
| Operating income | 1,788 | 1,808 | 1,846 | 1,758 | 7,200 | 1,602 | 1,822 | 1,790 | 1,575 | 6,789 |
| <i>Change over same quarter prior year</i> | 11.6% | -0.8% | 3.1% | 11.6% | 6.1% | 7.1% | 8.1% | -2.6% | 9.8% | 5.2% |
| % Operating income to Revenues | 24.1% | 23.2% | 24.0% | 21.1% | 23.0% | 22.0% | 23.2% | 23.8% | 19.3% | 22.0% |
| Industrial investments | 826 | 1,167 | 1,201 | 2,141 | 5,335 | 697 | 1,026 | 1,148 | 2,023 | 4,894 |
| Net financial indebtedness | 30,786 | 33,217 | 31,421 | 29,525 | 29,525 | 31,891 | 37,444 | 34,253 | 33,346 | 33,346 |

(*) The third and fourth quarter of 2003 had benefited from the cancellation of the TLC license fee, which had impacted the first two quarters of 2003. The figures for the four quarters of 2003 presented above have been rendered comparable to those of 2004.

In particular, net financial indebtedness, equal to euro 31,421 million at September 30, 2004, decreased to euro 29,525 million at December 31, 2004. The reduction of euro 1,896 million is essentially due to free cash flows from operations generated in the fourth quarter (euro 3,302 million) that were partly reduced by the payment of net financial expenses of euro 487 million and direct taxes of euro 880 million.

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TELECOM ITALIA GROUP

CONSOLIDATED STATEMENTS OF INCOME

| | 2004 | 2003 | Change (a - b) | |
|---|---------------|---------------|-------------------|---------------|
| (in millions of euro) | (a) | (b) | amount | % |
| A. Sales and service revenues | 31,237 | 30,850 | 387 | 1.3 |
| Changes in inventories of work in progress, semifinished and finished goods | (6) | 13 | (19) | (146.2) |
| Changes in inventory of contract work in process | (6) | (87) | 81 | (93.1) |
| Increases in capitalized internal construction costs | 742 | 805 | (63) | (7.8) |
| Operating grants | 12 | 14 | (2) | (14.3) |
| B. Standard production value | 31,979 | 31,595 | 384 | 1.2 |
| Raw materials and outside services ⁽¹⁾ | (13,414) | (13,018) | (396) | 3.0 |
| C. Value added | 18,565 | 18,577 | (12) | (0.1) |
| Labor costs ⁽¹⁾ | (4,037) | (4,297) | 260 | (6.1) |
| D. Gross operating profit | 14,528 | 14,280 | 248 | 1.7 |
| Amortization of other intangibles and depreciation of fixed assets | (5,092) | (4,949) | (143) | 2.9 |
| Other valuation adjustments | (280) | (477) | 197 | (41.3) |
| Provisions to reserves for risks and charges | (81) | (94) | 13 | (13.8) |
| Net other income (expense) | (321) | (141) | (180) | 127.7 |
| E. Operating income pre-amortization of differences on consolidation | 8,754 | 8,619 | 135 | 1.6 |
| Amortization of differences on consolidation | (1,554) | (1,830) | 276 | (15.1) |
| F. Operating income | 7,200 | 6,789 | 411 | 6.1 |
| Net financial income (expenses) ⁽²⁾ | (1,952) | (2,192) | 240 | (10.9) |
| Net investment income (expenses) | 118 | (72) | 190 | (263.9) |
| G. Income before extraordinary items and taxes | 5,366 | 4,525 | 841 | 18.6 |
| Net extraordinary income (expenses) | (410) | (1,083) | 673 | (62.1) |
| H. Income before taxes | 4,956 | 3,442 | 1,514 | 44.0 |
| Income taxes | (3,054) | (1,014) | (2,040) | 201.2 |
| I. Net income for the year before minority interest | 1,902 | 2,428 | (526) | (21.7) |
| Minority interest - net income | (1,121) | (1,236) | 115 | (9.3) |
| L. Net income for the year parent company interest | 781 | 1,192 | (411) | (34.5) |

(1) Reduced by related cost recoveries.

(2) Includes value adjustments to financial assets, other than equity investments.

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CONSOLIDATED BALANCE SHEETS

| | At 12/31/2004 (a) | At 12/31/2003 (b) | Change (a - b) |
|--|-------------------------|-------------------------|-------------------|
| (in millions of euro) | | | |
| A. Intangibles, fixed assets and long-term investments | | | |
| Intangible assets: | | | |
| • differences on consolidation | 25,637 | 27,137 | (1,500) |
| • other intangible assets | 7,237 | 6,716 | 521 |
| Fixed assets | 17,717 | 18,324 | (607) |
| Long-term investments: | | | |
| • equity investments and advances on future capital contributions | 1,064 | 1,470 | (406) |
| • other | 802 | 926 | (124) |
| | 52,457 | 54,573 | (2,116) |
| B. Working capital | | | |
| Inventories | 435 | 426 | 9 |
| Trade accounts receivable, net | 6,666 | 7,080 | (414) |
| Other assets | 2,646 | 3,960 | (1,314) |
| Trade accounts payable | (7,057) | (5,964) | (1,093) |
| Other liabilities | (5,436) | (6,671) | 1,235 |
| Reserves for employee termination indemnities and pensions and similar obligations | (1,364) | (1,338) | (26) |
| Capital and/or investment grants | (209) | (263) | 54 |
| Deferred tax assets net of reserve for income taxes | 3,246 | 4,609 | (1,363) |
| Other reserves for risks and charges | (1,998) | (2,477) | 479 |
| | (3,071) | (638) | (2,433) |
| C. Net invested capital (A + B) | 49,386 | 53,935 | (4,549) |
| Financed by: | | | |
| D. Shareholders' equity | | | |
| Parent company interest | 15,172 | 16,092 | (920) |
| Minority interest | 4,689 | 4,497 | 192 |
| | 19,861 | 20,589 | (728) |
| E. Medium/long-term debt | 36,535 | 30,545 | 5,990 |
| F. Net short-term financial borrowings (liquidity) | | | |
| Short-term borrowings | 2,027 | 10,613 | (8,586) |
| Liquid assets and short-term financial receivables | (9,878) | (8,482) | (1,396) |
| Financial accrued expenses (income) and deferred expenses (income), net | 841 | 670 | 171 |
| | (7,010) | 2,801 | (9,811) |
| G. Total net financial indebtedness (E + F) | 29,525 | 33,346 | (3,821) |
| H. Total net financing (D + G) | 49,386 | 53,935 | (4,549) |

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CONSOLIDATED STATEMENTS OF CASH FLOWS

| (in millions of euro) | 2004 | 2003 |
|--|-----------------|-----------------|
| A. Net financial indebtedness, at beginning of year | (33,346) | (33,399) |
| Operating income | 7,200 | 6,789 |
| Depreciation of fixed assets and amortization of intangible assets | 6,646 | 6,779 |
| Investments in fixed assets and intangible assets ⁽¹⁾ | (5,335) | (4,894) |
| Proceeds from disposal of fixed assets and intangible assets | 21 | 27 |
| Change in operating working capital and other changes | 1,355 | 532 |
| B. Free Cash Flow from operations | 9,887 | 9,233 |
| Investments in long-term investments and differences on consolidation ⁽¹⁾ | (583) | (6,560) |
| Proceeds from sale/redemption value of other intangible assets, fixed assets and long-term investments | 595 | 741 |
| Spin-off and sale of nuova seat pagine gialle | | 3,681 |
| Change in non-operating working capital and other changes ⁽²⁾ | (3,549) | (6,026) |
| C. | (3,537) | (8,164) |
| D. Net Cash fFlows before distribution of income/reserves and contributions by shareholders (B + C) | 6,350 | 1,069 |
| E. Distribution of income/reserves | (2,780) | (1,049) |
| F. Contributions by shareholders/withdrawals | 251 | 33 |
| G. Change in net financial indebtedness (D + E + F) | 3,821 | 53 |
| H. Net financial indebtedness, at end of year (A + G) | (29,525) | (33,346) |

The change in net financial indebtedness is the result of the following:

| (in millions of euro) | | |
|--|----------------|-------------|
| Increase (decrease) in medium/long-term debt | 5,990 | (2,747) |
| Increase (decrease) in short-term borrowings | (9,811) | 2,694 |
| Total | (3,821) | (53) |

(1) Total cash used for investments can be analyzed as follows:

| (in millions of euro) | | |
|-------------------------------------|--------------|---------------|
| Industrial investments: | 5,335 | 4,894 |
| - <i>other intangible assets</i> | 2,015 | 1,783 |
| - <i>fixed assets</i> | 3,320 | 3,111 |
| Differences on consolidation | 430 | 5,096 |
| Investment in long-term investments | 153 | 1,464 |
| Cash used for investments | 5,918 | 11,454 |

(2) The caption can be analyzed as follows:

| (in millions of euro) | | |
|--|----------------|----------------|
| Net financial income (expenses) | (1,952) | (2,192) |
| Utilization of risk reserve for early exercise of JP Morgan put option | | (1,942) |
| Payment of income taxes | (1,326) | (771) |
| Payment of other taxes (amnesty and withholding tax) | (190) | (186) |
| Extraordinary items and other | (81) | (935) |
| Change in non-operating working capital and other changes | (3,549) | (6,026) |

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■ MAJOR TRANSACTIONS INVOLVING EQUITY INVESTMENTS

■ Acquisition

Purchase of a 40% stake in Finanziaria Web by Telecom Italia Media

At the end of June 2004, an agreement was reached to settle the dispute concerning the framework agreement signed September 20, 2000 between Seat Pagine Gialle S.p.A. (now Telecom Italia Media) and its subsidiaries and the companies in the De Agostini group, regarding, among other things, the purchase of 40% of Finanziaria Webfin (which holds a 66% stake in Matrix, owner of the Virgilio portal).

In particular, based on the agreement – which supersedes that of September 20, 2000 – De Agostini Invest transferred the entire investment held in Finanziaria Webfin to Telecom Italia Media (which already had control of the company with a 60% holding) for consideration of euro 287 million, in lieu of the originally agreed price of euro 700 million. In addition to this amount, euro 38 million was added to reimburse De Agostini Invest for the expenses sustained to cover the loss and recapitalize Finanziaria Webfin starting from July 2001.

On the financial front, the agreement led to an immediate and temporary increase of euro 325 million in Telecom Italia Media's indebtedness. Telecom Italia – in keeping with the commitments undertaken last year when control was relinquished in Nuova Seat Pagine Gialle (the beneficiary company of the partial spin-off of Seat Pagine Gialle S.p.A., now Telecom Italia Media), so that Telecom Italia Media would have the resources necessary to meet the liabilities and commitments existing at the date the spin-off took effect – made a loan of euro 280 million at market rates to the company on June 28, 2004.

Another two transactions were entered into by Telecom Italia Media that are related to this transaction in order to improve its financial and equity position:

- sale of the investment in Finanziaria Webfin purchased from De Agostini Invest, carried out on July 9, 2004, to Vertico (a wholly-owned subsidiary of Telecom Italia, indirectly, and a shareholder of Matrix with a 33.3% holding) for a price of euro 42.6 million.
This sale has allowed Telecom Italia Media to reduce its financial exposure with Telecom Italia while maintaining the control over Matrix unchanged and, on the other hand, to consolidate its commercial cooperation relationships in the Internet area that already exist between Telecom Italia and Matrix/Virgilio;
- share capital increase against payment with option rights for a total equivalent amount (including additional paid-in capital) of euro 120 million approved by the Extraordinary Shareholders' Meeting on September 10, 2004 and entirely subscribed to during the rights offer period (October 11 – 29, 2004) and during the offer period on the stock market for the remaining unopted rights (November 8 – 12, 2004).

Telecom Italia subscribed to its share of the capital increase equal to 352,692,582 new ordinary shares, for a total equivalent amount of approx. Euro 74 million, equal to 62.50% of all ordinary shares offered, and 30,239 new savings shares, for a total equivalent amount of approx. Euro 0.5 million, equal to 0.32% of all savings shares offered.

The economic impact of the above transactions is a loss, net of the tax effect, of euro 130 million for Telecom Italia Media S.p.A. and euro 112 million for Telecom Italia S.p.A.. The net loss of the Telecom Italia Group on consolidation is euro 116 million.

Purchase of Digitel shares by TIM International N.V.

With regard to the numerous disputes pending between TIM International and the other shareholders in Digitel, in relation to the absorption of the loss for the year 2002, a settlement agreement was reached in April 2004 wherein TIM International agreed to purchase the holdings of all the other shareholders (corresponding to 32.88% of Digitel's share capital).

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According to the agreement, executed on July 1, 2004, TIM International purchased 1,480,562 shares held by the minority shareholders of the Venezuelan company for USD 109.6 million. The closing took place after verification of the contractual conditions put into place to protect TIM International and Digitel. As from the date of July 1, 2004, TIM, through TIM International, holds 100% of the shares of the Venezuelan mobile operator.

In November, moreover, an agreement was signed with CANTV (Compañía Anónima Nacional Teléfonos de Venezuela) for the sale of 100% of the share capital of the company. The total value of the transaction is equal to USD 450 million, from which the net financial position will be deducted when the transaction is executed.

Execution of the agreement, presumably scheduled to take place in the first half of 2005, is subject to the signing of the final agreements and obtaining the necessary authorizations from the pertinent Venezuelan authorities. Since CANTV is a regional operator, TIM decided to accept its offer for the purchase of the investment so that it can focus on initiatives where it has national coverage.

Purchase of IAK - Informatica Avanzata per il Credito

On July 14, 2004, Banksiel signed a contract for the purchase of 100% of the share capital of IAK – INFORMATICA AVANZATA PER IL CREDITO S.r.l. for euro 3 million. The contract was executed on October 11, 2004 after the relative approvals were obtained from the Antitrust Authority.

Purchase of a stake in YMINDS S.A.

On September 30, 2004, following receipt of approval from the Antitrust Authority, Olivetti I-Jet S.p.A. in the Office Products Division, finalized the merger of 100% of the Swiss company YMINDS S.A. (in which Olivetti I-Jet already held a 27.2% interest) after purchasing a 61.4% stake from third parties and an 11.4% interest from Olivetti Tecnost International BV. The company is engaged in research and development of products using Ink-jet technology.

Capital increases by Etec S.A. - Cuba

During the first half of 2004, the Shareholders' Meeting of the Cuban company voted three increases in share capital in order to fund the extraordinary financial requirements for the payment of the new license granted by MIC (the Ministry of Cuban Telecommunications). The share capital increases have the following characteristics:

- on March 4, 2004, USD 23.8 million through the issue of 165 new shares for a unit price of USD 144.190;
- on May 20, 2004, USD 31.6 million through the issue of 219 new shares for a unit price of USD 144.190;
- on June 14, 2004, USD 61.9 million through the issue of 429 new shares for a unit price of USD 144.190.

Telecom Italia International N.V. subscribed to such increases based on its investment (27%) paying, respectively, USD 6.3 million, USD 8.5 million and USD 16.7 million, and receiving in exchange, respectively, 44, 59, and 116 new shares.

Telecom Italia International N.V.'s interest has remained unchanged.

■ Divestitures

Sale of Euskaltel S.A.

On January 16, 2004, Telecom Italia International N.V. signed a contract with Araba Gertu S.A. for the sale of a 3.1% stake in Euskaltel to Araba Gertu S.A. for an total price of euro 13.6 million. This sale was conditional upon the pre-emptive right procedure provided by Euskaltel's bylaws.

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The closing took place on February 19, 2004. After the pre-emption right was exercised by Iberdrola S.A., an Euskaltel shareholder, the sale of the above stake occurred through the signing of two separate contracts under which Telecom Italia International N.V. sold 149,231 shares to Araba Gertu for consideration of euro 12.1 million and 18,719 shares to Iberdrola for consideration of euro 1.5 million).

Upon completion of the transaction, Telecom Italia International retains a 3% share in Euskaltel.

Sale of Telekom Austria A.G.

On January 21, 2004, Telecom Italia International N.V. signed a Private Placement agreement under which it sold, on January 27, 2004, its entire remaining 14.78% investment in the share capital of Telekom Austria for a total net value of euro 768 million. A net gain was realized on consolidation for euro 62 million.

Sale of Netco Redes S.A.

On March 4, 2004, Telecom Italia International N.V. signed a contract with Auna for the sale of its entire 30% investment in the Spanish company Netco Redes S.A. for consideration of euro 30 million. On June 24, 2004, following the fulfillment of the suspensive conditions stated in the contract (including the receipt of authorization from the competent Spanish authorities), Telecom Italia International N.V. transferred 301,404 Netco Redes S.A. shares to Auna, receiving the entire agreed amount of consideration of euro 30 million, including interest accrued up to the closing date, on June 30, 2004. After this sale, the only equity interest currently held by Telecom Italia International N.V. in Spain is represented by the 3% holding in Euskaltel.

A net gain was realized on consolidation for euro 6 million.

Sale of Webegg S.p.A.

On June 3, 2004, IT Telecom S.p.A., 100% - controlled by Telecom Italia, signed an agreement with Value Partners S.p.A. for the sale of the 69.8% stake held in Webegg S.p.A. at a price of euro 43 million. The remaining 30.2% interest is held by Finsiel. The transaction calls for Finsiel to keep its investment in Webegg and reciprocal sale and purchase options will be recognized between Finsiel and Value Partners.

On July 15, 2004, after approval by the Antitrust Authority, the agreement with Value Partners was executed with the payment of the agreed price.

Sale of Atesia S.p.A.

Effective July 1, 2004, Atesia sold the wireline customer care business segment to Telecontact S.p.A..

On July 2, 2004, Telecom Italia signed an agreement with the company COS Communication Services S.p.A. (part of the COS Group and the Italian leader in outsourcing for Contact Centers and CRM - Customer Relationship Management services) for the sale of the 80.1% stake in Atesia. Therefore, the sale only covers the activities conducted for TIM and the external market. The deal was executed on November 12, 2004 after approval was obtained from the Antitrust Authority on October 28, 2004.

Sale of Pirelli & C. Real Estate S.p.A. shares

During the period June-August 2004, Telecom Italia S.p.A. sold all the Pirelli & C. Real Estate S.p.A. in portfolio (812,086) for total cash proceeds of euro 24 million.

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Sale of SKY Italia S.r.l.

On September 28, 2004, Telecom Italia sold its 19.9% interest in Sky Italia to the NewsCorp group. The consideration on the transaction was euro 88 million. The transaction gave rise to a gain, compared to the carrying value at June 30, 2004, of euro 31.4 million. This makes it possible to cancel the effects of the writedowns made during the first half of the year so that the transaction had an almost nil economic impact on Telecom Italia's financial statements this year.

Sale of Mirror International Holding S.a.r.l.

On December 21, 2004, Mirror International Holding S.a.r.l. purchased, through a buyback, 30% of its capital held by Telecom Italia. Consideration on the transaction was euro 75 million, euro 73 million for the sale and euro 2 million for the loan repayment. The deal gave rise to a gain on consolidation of euro 24 million for the above sale and euro 61 million for the release of the remaining part of the gain on the sale, in 2001, of 70% of Mirror International Holding, the company to which the investments in the satellite consortium had previously been transferred.

Reduction of Solpart Participações share capital - Brazil

The Extraordinary Shareholders' Meeting of Solpart, held April 26, 2004, voted to reduce share capital by BRL 173,350,000.00. After deducting BRL 1,980,319,91 from that amount to cover the accumulated losses of prior years, BRL 41,898,263,09 will be reimbursed in cash and the remaining amount will be paid through the distribution of 3,474,342,842 ordinary shares and 3,491,253,373 preferred shares of the subsidiary Brasil Telecom Participações S.A.. The valuation of the part of the capital reimbursed in shares was made on the basis of the weighted average price of the shares at the close of trading on the San Paolo stock exchange on April 23, 2004, equal to BRL 17.65 for ordinary shares (1,000 share lots) and BRL 19.52 for preferred shares (1,000 share lots). As a result of this resolution, Telecom Italia International has received BRL 15,917,669,18 in cash and 1,319,945,886 ordinary shares and 1,326,370,406 preferred shares. The reduction in Solpart's share capital did not involve a change in the number of ordinary and preferred shares owned by each shareholder, whereas the value per share was reduced.

■ Other transactions

Is TIM/Aycell merger

On February 19, 2004, the merger of Is TIM and Aycell was finalized. The transaction was effected by conferring the assets and liabilities of Is TIM and Aycell to TT&TIM (owned 40% by TIM International, 40% by Turk Telekom and 20% by the Is Bank group) and then by later canceling Is TIM and Aycell from the Companies Register.

Restructuring of the TIM subsidiaries in Brazil

On July 19, 2004, the Boards of Directors of Tele Celular Sul Participações S.A. and Tele Nordeste Celular Participações S.A., both controlled by TIM Brasil, approved the plan for the merger of Tele Nordeste Celular Participações S.A. in Tele Celular Sul Participações S.A. (a transaction that had already begun on May 28, 2004).

On August 19, and August 30, 2004, Tele Nordeste Celular Participações and Tele Celular Participações, respectively, held their Extraordinary General Shareholders' Meetings which approved the above merger. At the same time, Tele Celular Sul Participações changed its company name to TIM Participações S.A..

October 4, 2004, lastly, marked the deadline for exercising the withdrawal rights on the part of the minority shareholders. In all, 15 shareholders exercised that right for a total of 158,567 ordinary shares equal to 0.0001%.

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At the conclusion of this transaction, TIM, through TIM Brasil, holds 23.73% of the capital of TIM Participações S.A..

Contribution of Maxitel S.A. by TIM International N.V.

As part of the process to streamline the Group's structure, TIM International contributed its investment in Maxitel to TIM Brasil. The transaction was approved by the Board of Directors of TIM Brasil on September 29, 2004 after approval was obtained from the competent authorities. On October 28, 2004, TIM Brasil contributed the same investment in Maxitel to TIM Celular in the form of a capital increase.

Merger of IT Telecom S.p.A. and EPIClink S.p.A. in Telecom Italia S.p.A.

On September 9, 2004, the Board of Directors of Telecom Italia S.p.A. examined and approved the plan for the merger of the wholly-owned subsidiaries IT Telecom S.p.A. and EPIClink S.p.A in Telecom Italia. This plan falls under a broader reorganization of the Information Technology Group area.

Bringing the activities of these two subsidiaries inside Telecom Italia will make it possible to rationalize the use of resources and technological expertise and will lead to an important simplification of the operational, administrative and corporate management processes.

As provided by the respective bylaws, the merger was approved on October 11, 2004 by the Boards of Directors of the three companies, according to the conditions and terms indicated in article 2505, last paragraph of the Italian Civil Code.

The merger is effective from December 31, 2004 and for accounting and tax purposes from January 1, 2004. On December 30, 2004, IT Telecom S.p.A. conferred its Data Center business segment to IT Telecom S.r.l., a new company set up on November 12, 2004.

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■ ECONOMIC AND FINANCIAL PERFORMANCE TELECOM ITALIA S.p.A.



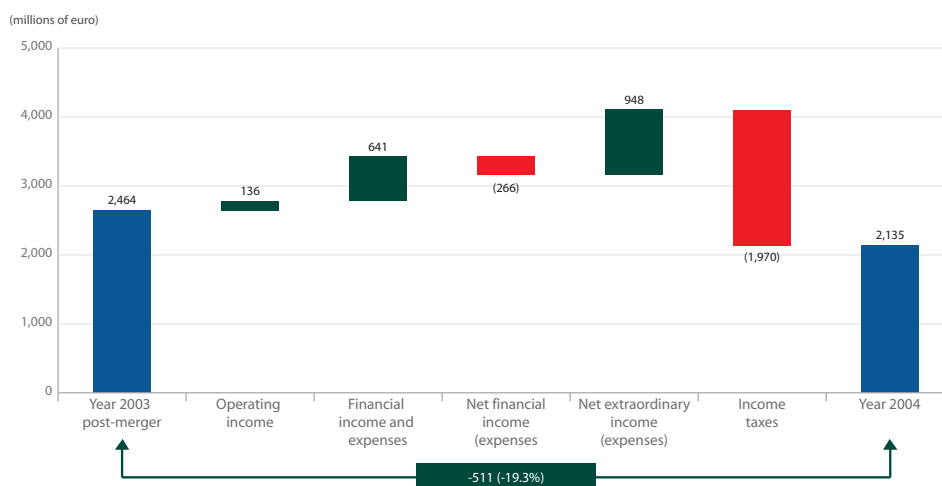
The results of operations and the financial condition of Telecom Italia S.p.A. for the year 2004 reflect the impact of the merger by absorption of the subsidiaries IT Telecom S.p.A. and EPIClink S.p.A.. The agreement was executed on December 17, 2004 and the merger is effective from December 31, 2004 and for accounting and tax purposes from January 1, 2004.

The financial statements show the results for the year 2004 compared to those of the year 2003 "post-merger" restated, by giving effect to the merger as from January 1, 2003, for purposes of comparison.

RESULTS OF OPERATIONS

The Parent Company, **Telecom Italia S.p.A.**, shows a net income of euro 2,135 million in 2004, euro 511 million less than 2003 post-merger.

The following chart shows the components which had an impact on net income during the year:



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In particular, the increase in *income taxes* (+euro 1,970 million) is due both to a better economic result in 2004 and the fact that in 2003 deferred tax assets were booked (euro 1,266 million) which became recoverable thanks to the Olivetti/Telecom Italia merger.

Sales and service revenues, gross of the portion due to other TLC operators, amount to euro 16,126 million and decreased by euro 104 million (– 0.6%) compared to 2003 post-merger. *Excluding, from 2003, the effects deriving from the change in the scope of consolidation of the merged company IT Telecom – mainly with respect to the contribution of the “Development” business segment to TIM – revenues in 2004 record an underlying growth of euro 48 million (+0.3%).*

The decrease in revenues in 2004 compared to 2003 post-merger was caused by a reduction in the revenues of the merged company IT Telecom as a result of the disposals of business segments in 2004 (– euro 152 million) as well as the absence of revenues from the resale of satellite capacity (– euro 79 million) after Telespazio directly took over contacts with the satellite consortia. Such effects were partly compensated by the increase in the revenues by Telecom Italia’s Wireline business (+euro 128 million).

The trend in retail revenues can specifically be ascribed to the following factors:

- increase in Internet revenues (+euro 251 million) due to the growth of *Adsl Alice* and *Smart* plans;
- increase in Data Business revenues (+euro 30 million) specifically due to the growth of innovative data transmission services, which was partly offset by the decrease in traditional data transmission revenues;
- decrease in telephony revenues (– euro 66 million) chiefly as a result of the decline in traffic revenues, which was partly absorbed by the increase in product sales (principally the Aladino cordless phone);
- decrease in VAS - Value Added Services revenues (– euro 57 million) on account of the contraction in premium services, which was partly compensated by the growth of revenues from innovative services;
- decrease in revenues from the national Wholesale area (– euro 30 million).

In 2004, sales and service revenues, net of the portion due to other telecommunications operators, are equal to euro 13,102 million. Such revenues decreased by euro 48 million compared to 2003 post-merger.

Gross operating profit, equal to euro 7,540 million, increased by euro 19 million compared to 2003 post-merger (+0.3%). *Excluding, from 2003, the effects deriving from the change in the scope of consolidation of the merged company IT Telecom – mainly with respect to the contribution of the “Development” business segment to TIM – gross operating profit in 2004 records an underlying growth of euro 63 million (+0.8%).*

As a percentage of revenues, gross operating profit is 46.8% (46.3% in 2003 post-merger).

The growth of gross operating profit compared to 2003 post-merger is principally the result of the reduction in labor costs (– euro 127 million) and the increase in capitalized internal construction costs (+euro 52 million) that were absorbed in part by higher costs for raw materials and outside services (+euro 19 million), by the negative changes in inventory of contract work in process (– euro 36 million) and the aforementioned reduction in revenues.

The decrease in labor costs is mainly due to the reduction in the average headcount (– 3,803 persons compared to 2003; – 6.6%).

The increase in capitalized internal construction costs is due to work performed internally that was previously carried out by external suppliers and the reclassification from “contract work in

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process” – after the merger of IT Telecom and EPIClink – of contracts in the process of completion by IT Telecom for Telecom Italia.

Operating income, equal to euro 4,234 million, increased by euro 136 million compared to 2003 post-merger (+ 3.3%). *Excluding, from 2003, the effects deriving from the change in the scope of consolidation of the merged company IT Telecom – mainly with respect to the contribution of the “Development” business segment to TIM – operating income in 2004 records an underlying growth of euro 179 million (+ 4.4%).*

As a percentage of revenues, operating income is 26.3%, compared to 25.2% in 2003 post-merger.

The increase in operating income compared to 2003 post-merger is due to lower amortization of intangibles and depreciation of fixed assets (– euro 159 million) and lower provisions to the allowance for doubtful accounts (– euro 100 million).

Such positive effects are partly offset by higher expenses for the sale of receivables, higher provisions to the reserves for risks and charges and higher expenses connected with the management of relationships with other telephone operators.

Net financial income (expenses) show an expense balance of euro 1,772 million (– euro 2,413 million in 2003 post-merger), with an improvement of euro 641 million. This reduction is due to the fact that 2003 had included the expenses relating to the JP Morgan put option on Seat Pagine Gialle shares (euro 236 million) and expenses (euro 394 million) referring to the repurchase of the bonds subscribed by Telecom Italia Finance, as well as the expenses incurred in conjunction with obtaining credit lines to fund the Olivetti S.p.A./Telecom Italia S.p.A. merger (euro 98 million). Such positive effects are partly offset by the expenses relating to the increase in average debt exposure in 2004.

Net investment income (expenses) is composed of the following:

| | 2004 | 2003 restated | Change |
|---|--------------|------------------|--------------|
| (millions of euro) | (a) | (b) | (a-b) |
| Income from investments, net | 1,407 | 2,007 | (600) |
| Net revaluations (writedowns) of equity investments | 54 | (280) | 346 |
| Total | 1,461 | 1,727 | (266) |

In particular, the following can be said:

- the decrease in income from investments, net (– euro 600 million) is almost entirely due to the receipt, in 2003, of both pre-merger dividends from the merged company Telecom Italia (euro 511 million) and reserves from the subsidiary TIM (euro 81 million) and tax credits no longer recognized on dividends (euro 81 million) following the tax reform introduced by Legislative Decree No. 344/2003. In 2004, higher dividends were received from TIM (+ euro 132 million) and lower dividends were received from Telecom Italia Sparkle (– euro 51 million);
- net revaluations (writedowns) of equity investments show a positive balance of euro 54 million. The balance consists of revaluations of equity investments (euro 84 million) and writedowns of equity investments (euro 30 million). The revaluations mainly refer to the writeback of the value of the investment in Olivetti Tecnost (euro 49 million), booked in view of the fact that the reasons which gave rise to the writedown in prior years were no longer applicable and, in particular, the possibility of posting, in the financial statements of the subsidiary, tax assets following the introduction of the consolidated national tax return of the Group, as well as the revaluation of TIM shares in current assets (later reclassified to long-term investments) booked to adjust the value of the investment to market (euro 32 million). Writedowns mainly refer to investments in Telecom Italia Learning Services (euro 16 million), LI.SIT (euro 6 million), Telbios (euro 3 million) and TILAB S.A. (euro 3 million).

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The reduction (– euro 327 million) compared to 2003 post-merger is principally the result of writedowns made in 2003 to the equity investments in Sky Italia (euro 96 million), Olivetti International (euro 80 million), Telecom Italia Learning Services (+ euro 48 million), Olivetti Tecnost (euro 54 million) and Webegg (euro 34 million).

Net extraordinary income (expenses) show an expense balance of euro 726 million (– euro 1,674 million in 2003), with an improvement of euro 948 million.

Extraordinary income, totaling euro 567 million, decreased by euro 490 million compared to 2003 post-merger. This reduction is largely attributable to the difference between prior period income on non-existent liabilities which arose in 2003 as a result of the cancellation of the TLC license fee relating to 2000, 2001 and 2002 (euro 922 million) and the prior period income relating to the same TLC license fee paid in 1999 (euro 411 million) which arose in 2004 following the decision handed down by the TAR of Lazio No. 47/2005 of January 4, 2005 which upheld the appeal filed by Telecom Italia and cancelled the Ministerial Decree dated March 21, 2000 regarding the TLC fee instituted by Law 448/1998 declaring it to be illegal.

Extraordinary income includes:

- the aforementioned prior period income relating to the TLC license fee paid for 1999 (euro 411 million);
- the gains (euro 58 million) realized mainly on the sale of the equity investments in Pirelli & C. Real Estate (euro 9 million) and Mirror International Holding (euro 18 million), the sale of the 80.1% stake in Atesia (euro 2 million), the sale of the “Maintenance” and “Environmental Services” (euro 4 million) and “Document Management” (euro 1 million) business segments and the sale of the “Development” business segment by the merged company IT Telecom (euro 23 million);
- the recovery of income taxes (ILOR) paid in 1991 (euro 25 million) relating to the reinvestment of earnings in the south of Italy for which the exemption was requested in the 1992 tax return, pursuant to art. 102 of D.P.R. No. 218 dated March 6, 1978;
- the recovery of expenses from companies of the Group relating to Law 58/1992 (euro 2 million) and from third parties for damage compensation (euro 9 million);
- the elimination of prior period tax interference (euro 1 million), pursuant to Legislative Decree No. 6 dated January 17, 2003, introducing the Corporate Law Reform, following accelerated depreciation taken in prior years by the acquiring company Olivetti as allowed by tax laws;
- other prior period income of euro 61 million.

Extraordinary expenses, totaling euro 1,293 million, decreased by euro 1,438 million compared to 2003 post-merger in which the following items had been booked:

- loss on the sale of Nuova Seat Pagine Gialle (euro 348 million);
- expenses connected with the Olivetti - Telecom Italia merger and the sale of the company Nuova Seat Pagine Gialle (euro 181 million);
- writedowns of the equity investments in Telecom Italia Media (+ euro 378 million), Telecom Italia International (+ euro 146 million), Latin American Nautilus (+ euro 172 million), EPIClink (euro 110 million) and Loquendo (euro 8 million) and provisions for guarantees provided upon the sale of the satellite consortia (euro 30 million);
- expenses relating to the settlement with Pagine Italia (euro 55 million).

Extraordinary expenses include:

- writedowns of the equity investments in Telecom Italia International (euro 257 million) to adjust the investments in Entel Chile and Etec S.A. to market value, Telecom Italia Media (euro 112 million) for the loss of value following the settlement with the De Agostini group,

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Finsiel (euro 139 million) to adjust the investment to its estimated sales value, Latin American Nautilus (euro 65 million), Mediterranean Nautilus (euro 47 million) and Med 1 (euro 13 million);

- provision for the sanction levied on the Parent Company by the Antitrust Authority for the alleged abuse of a dominant position (euro 152 million);
- expenses under ex Law 58/1992 (euro 149 million) to cover employees under the former "Telephone Employees Pension Fund" (FPT), which became part of the "Employees Pension Fund", in accordance with the 2000 Finance Bill;
- expenses (euro 146 million) for corporate restructuring measures relating to employee cutbacks and layoffs;
- prior period expenses relating to the writeoff of prior years' receivables balances (euro 46 million), made necessary by the actions verifying credit transactions with customers;
- expenses for damages caused to the company's assets as a result of natural events or brought about by third parties (euro 37 million);
- expenses for the booking of liabilities relating to prior years (euro 27 million), principally in respect of matters concerning interconnection as a result of tests conducted with the interested operators;
- provisions (euro 25 million) connected with corporate-related transactions;
- expenses connected with the Telecom Italia - TIM merger (euro 19 million);
- other prior period expenses and extraordinary expenses (euro 59 million).

Income taxes totaling euro 1,062 million (a tax benefit of euro 908 million in 2003 post-merger) increased by euro 1,970 million compared to 2003 due to a better economic result and because the previous year had benefited from deferred tax assets (euro 1,266 million) which became recoverable thanks to the Olivetti/Telecom Italia merger, countered by euro 353 million of income taxes on the prior period income which arose as a result of the cancellation of the TLC license fee for 2000, 2001 and 2002.

Income taxes in 2004 include euro 152 million of income taxes relating to the prior period income booked during the year as a result of the cancellation of the TLC license fee for the year 1999.

FINANCIAL CONDITION

Intangibles, fixed assets and long-term investments at December 31, 2004, amounting to euro 47,682 million, decreased by euro 1,099 million compared to December 31, 2003 post-merger. In particular:

- **intangibles**, equal to euro 1,845 million, increased by euro 262 million compared to December 31, 2003 post-merger. The increase is due to the difference between investments (euro 1,031 million), amortization (euro 671 million), the contribution of the Data Center business segment Center to IT Telecom S.r.l. by the merged company IT Telecom S.p.A. (euro 88 million), eliminations (euro 12 million) and reclassifications from fixed assets (euro 2 million);
- **fixed assets**, equal to euro 11,020 million, decreased by euro 1,023 million compared to December 31, 2003 post-merger. The reduction is due to the difference between investments (euro 1,299 million), depreciation (euro 2,221 million), the contribution of the Data Center business segment to IT Telecom S.r.l. by the merged company IT Telecom S.p.A. (euro 80 million) and disposals (euro 21 million);
- **long-term investments**, amounting to euro 34,817 million, decreased by euro 338 million compared to December 31, 2003 post-merger. The reduction is due to the difference between

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investments (euro 1,722 million), adjustments of value (– euro 531 million), distribution of reserves (euro 1,902 million, of which euro 1,800 million relates to Telecom Italia International), disposals (euro 308 million), purchase of the investment in IT Telecom S.r.l. following the aforementioned contribution by IT Telecom S.p.A. (euro 133 million), reclassification of the TIM shares in current assets (euro 198 million), receivables from subsidiaries, mainly TIM – following the introduction of the consolidated national tax return procedure (+ euro 378 million) – and other movements (– euro 28 million).

Investments total euro 4,052 million (euro 9,661 million in 2003 post-merger).

Details are as follows:

| | 2004 | 2003 restated | Change |
|--------------------------|--------------|------------------|----------------|
| (millions of euro) | | | |
| Industrial investments | 2,330 | 2,740 | (410) |
| Financial investments | 1,722 | 6,921 | (5,199) |
| - of which tender offer | - | 5,274 | (5,274) |
| Total investments | 4,052 | 9,661 | (5,609) |

Working capital, totaling euro 386 million (euro 3,176 million at December 31, 2003 post-merger), decreased by euro 2,790 million. The change is due mainly to the reduction of “trade accounts receivable” (– euro 862 million) – above all on account of the sale of receivables to factoring companies at December 31, 2004 – of “other assets” (– euro 842 million) – for the booking, in 2003, of a tax credit sold to TIM (euro 1,294 million) – and of “deferred tax assets net of the reserve for income taxes” (– euro 888 million). Increases in working capital captions refer to “other liabilities” (+ euro 375 million), “reserves for risks and charges” (+ euro 98 million) and the “reserve for employee termination indemnities” (+ euro 13 million).

The above effects were partly compensated by the reduction in “trade accounts payable” (– euro 234 million).

Transactions for the securitization and factoring of trade accounts receivable in 2004 led to a reduction in trade accounts receivable and other assets at December 31, 2004 for a total of euro 1,717 million, of which euro 809 million relates to securitization and euro 908 million to factoring transactions (euro 1,254 million at December 31, 2003, of which euro 874 million had related to securitization and euro 380 million to factoring transactions).

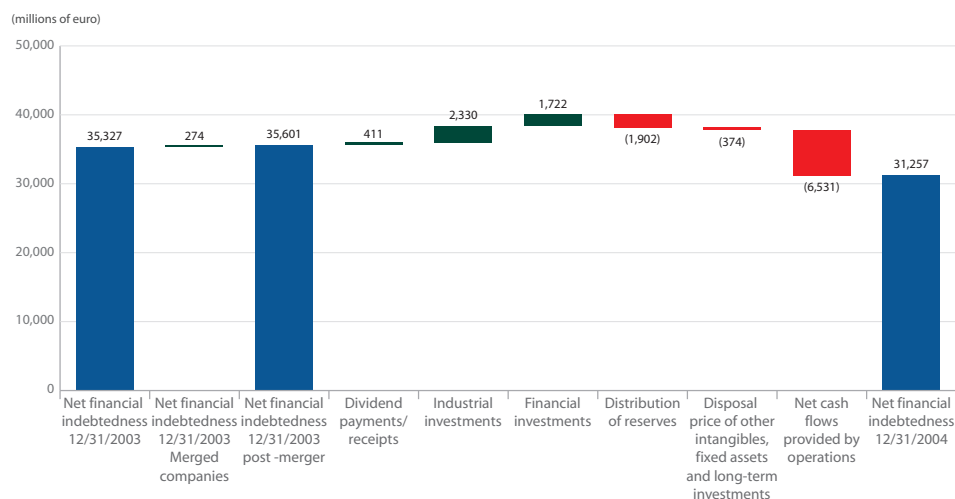
Net invested capital, amounting to euro 48,068 million (euro 51,957 million at December 31, 2003 post-merger), is financed by shareholders’ equity for 35% and net financial indebtedness for 65%.

Shareholders’ equity at December 31, 2004, equal to euro 16,811 million (euro 16,356 million at December 31, 2003 post-merger), increased by euro 455 million. Additional details on the changes in shareholders’ equity during the year are presented in the notes to the Telecom Italia S.p.A. financial statements under “Liabilities and shareholders’ equity”.

Net financial indebtedness (euro 31,257 million) decreased by euro 4,344 million compared to December 31, 2003 post-merger (euro 35,601 million).

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The following chart summarizes the major components which had an impact on the change in net financial indebtedness during 2004:



Financial investments include the payment of advances on future capital contributions of euro 1,500 million relating to Edotel S.p.A., a company contributed by Telecom Italia to Telecom Italia Finance S.A. in October 2004. This advance follows the distribution of a part of additional paid-in capital by Telecom Italia International B.V. for an amount of euro 1,800 million.

The above transactions were entered into for purposes of bringing Telecom Italia Finance's financial position into equilibrium, by transferring liquidity from Telecom Italia International.

Net financial indebtedness benefited from the effects of the securitization and sale of receivables to factoring companies for a total amount of euro 1,698 million at December 31, 2004, of which euro 786 million relates to securitization and euro 912 million to factoring transactions (euro 1,186 million at December 31, 2003, of which euro 851 million had related to securitization and euro 335 million to factoring transactions).

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Net financial indebtedness is detailed in the following table:

| (millions of euro) | Within 12 months | Beyond 12 months | Total 12/31/2004 | Total 12/31/2003 post-merger |
|--|------------------------|------------------------|---------------------|------------------------------------|
| Debentures | - | 12,701 | 12,701 | 9,765 |
| Convertible debentures | - | 2,825 | 2,825 | 4,160 |
| Total debentures | - | 15,526 | 15,526 | 13,925 |
| Payables to subsidiaries and affiliated companies | 2,978 | 16,573 | 19,551 | 19,310 |
| Due to banks | 416 | 490 | 906 | 1,193 |
| Due to other lenders | 260 | 785 | 1,045 | 783 |
| Other liabilities | 46 | - | 46 | 62 |
| Taxes payable | - | - | - | 23 |
| Total other financial payables | 3,700 | 17,848 | 21,548 | 21,371 |
| Total gross financial indebtedness | 3,700 | 33,374 | 37,074 | 35,296 |
| Liquid assets | (5,424) | - | (5,424) | (205) |
| Receivables from subsidiaries and affiliated companies | (707) | - | (707) | (572) |
| Other accounts receivable | (346) | - | (346) | (367) |
| Other securities in current assets | - | - | - | (16) |
| Total financial receivables in current assets and liquid assets | (6,477) | - | (6,477) | (1,160) |
| Accrued expenses and deferred income | 1,032 | - | 1,032 | 1,832 |
| Accrued income and prepaid expenses | (120) | (252) | (372) | (367) |
| Balance of financial accruals and deferrals | 912 | (251) | 661 | 1,465 |
| Net financial indebtedness at december 31, 2004 | (1,865) | 33,122 | 31,257 | 35,601 |

The percentage of gross indebtedness due beyond one year of euro 33,374 million to total gross indebtedness went from 59% at December 31, 2003 post-merger to 90% at December 31, 2004.

During 2004, Telecom Italia S.p.A. issued four new notes falling under the Euro Medium Term Note Program for a total of euro 10 billion, approved by the Board of Directors' meeting held October 10, 2003:

- on January 29, 2004, notes were issued for euro 3,000 million divided into three tranches:
 - euro 1,000 million, interest at the 3-month Euribor + 0.33%, issue price of 99.927, maturing October 29, 2007;
 - euro 750 million, 4.50% interest, issue price of 99.56, maturing January 28, 2011;
 - euro 1,250 million, 5.375% interest, issue price of 99.07, maturing January 29, 2019;
- on April 8, 2004, floating rate notes were issued for euro 110 million under a private placement, interest at the 3-month Euribor + 0.60%, issue price of 100, maturing on March 30, 2009;
- on June 24, 2004, fixed rate notes were issued for GBP 850 million, equal to euro 1,289 million, 6.375% interest, issue price of 98.85, maturing June 24, 2019;
- on November 23, 2004, notes were issued for euro 120 million, interest at the 3-month Euribor + 0.66%, issue price of 100, maturing November 23, 2015.

Telecom Italia redeemed bonds for euro 2,831 million, of which:

- euro 1,331 million, on January 1 2004, relating to convertibles bonds 2001-2004;
- euro 1,500 million, on March 22, 2004, relating to bonds maturing June 21, 2005, called in advance by exercising the right stated in the bond indenture.

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On March 30, 2004, the new 3-year credit line was signed for euro 6.5 billion. This new line replaces the syndicated credit line of the same amount arranged by the acquiring company Olivetti as part of the merger in 2003. The first tranche (euro 4.5 billion) was due in April 2004. The borrower is not required to abide by specific financial statement ratios and the type of commitment undertaken by the banks guarantees unconditional availability of credit for the line in question.

During the course of 2004, Telecom Italia also sold 2002-2022 bonds set aside for subscription by the employees of the Group for a face value of euro 0.7 million. According to the bond indenture, the Company must be the counterpart for the purchases made by the holders of this category of securities.

On December 8, 2004, Telecom Italia signed a loan contract, governed by British law, for an amount of up to a maximum of euro 12,000 million, with a syndicate composed of national and international banks. This loan will be used to service the payment of the part of the price not paid using own resources under the partial voluntary cash tender offer launched by Telecom Italia for the purchase of ordinary shares and all savings shares issued by Telecom Italia Mobile. Repayment of the loan is divided into three parts, having different maturity dates and giving Telecom Italia the possibility of extending the maturity dates of the first two tranches:

- first tranche of euro 3,000 million with maturity at 12 months, extendable for a further 12 months;
- second tranche of euro 6,000 million with maturity at 36 months, extendable for a further 9 months;
- third tranche of euro 3,000 million with maturity at 60 months

The following table shows the composition of gross financial indebtedness:

| | At 12/31/2004 | | | | | | At 12/31/2003 post-merger | |
|-----------------------|---------------|------------|---------------------|------------|---------------|------------|------------------------------|------------|
| | euro | % | Foreign currency | % | Total | % | Total | % |
| (millions of euro) | | | | | | | | |
| Medium/long-term debt | 28,813 | 89 | 4,561 | 100 | 33,374 | 90 | 20,920 | 59 |
| Short-term borrowings | 3,699 | 11 | 1 | | 3,700 | 10 | 14,376 | 41 |
| Total | 32,512 | 100 | 4,562 | 100 | 37,074 | 100 | 35,296 | 100 |

In particular, at December 31, 2004, short-term borrowings of euro 3,700 million include the current portion of medium/long-term debt due within one year amounting to euro 2,238 million (euro 5,760 million at December 31, 2003 post-merger).

Debt positions with Group companies total euro 25,095 million (euro 22,119 million falls due beyond one year) and with third parties euro 11,979 million (euro 11,255 million falls due beyond one year).

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TELECOM ITALIA

STATEMENTS OF INCOME

| | 2004 | 2003 post- merger ⁽¹⁾ | Merger effect | 2003 historical data | Change (a - b) | |
|---|---------------|--|------------------|----------------------------|-------------------|---------------|
| (in millions of euro) | (a) | (b = c + d) | (c) | (d) | amount | % |
| A. Sales and service revenues | 16,126 | 16,230 | 197 | 16,033 | (104) | (0.6) |
| Changes in inventory of contract work in process | (18) | 18 | 12 | 6 | (36) | - |
| Increases in capitalized internal construction costs | 601 | 549 | 489 | 60 | 52 | 9.5 |
| Operating grants | 8 | 9 | - | 9 | (1) | (11.1) |
| B. Standard production value | 16,717 | 16,806 | 698 | 16,108 | (89) | (0.5) |
| Raw materials and outside services ⁽²⁾ | (6,587) | (6,568) | (359) | (6,209) | (19) | 0.3 |
| C. Value added | 10,130 | 10,238 | 339 | 9,899 | (108) | (1.1) |
| Labor costs ⁽²⁾ | (2,590) | (2,717) | (251) | (2,466) | 127 | (4.7) |
| D. Gross operating profit | 7,540 | 7,521 | 88 | 7,433 | 19 | 0.3 |
| Depreciation and amortization | (2,892) | (3,051) | (132) | (2,919) | 159 | (5.2) |
| Other valuation adjustments | (101) | (201) | (2) | (199) | 100 | (49.8) |
| Provisions to reserves for risks and charges | (49) | (17) | (2) | (15) | (32) | ° |
| Net other income (expense) | (264) | (154) | 7 | (161) | (110) | 71.4 |
| E. Operating income | 4,234 | 4,098 | (41) | 4,139 | 136 | 3.3 |
| Net financial income (expenses) ⁽³⁾ | (1,772) | (2,413) | (9) | (2,404) | 641 | (26.6) |
| Net investment income (expenses) | 1,461 | 1,727 | 82 | 1,645 | (266) | (15.4) |
| F. Income before extraordinary items and taxes | 3,923 | 3,412 | 32 | 3,380 | 511 | 15.0 |
| Net extraordinary income (expenses) | (726) | (1,674) | (22) | (1,652) | 948 | (56.6) |
| G. Income before taxes | 3,197 | 1,738 | 10 | 1,728 | 1,459 | 83.9 |
| Income taxes | (1,062) | 908 | (10) | 918 | (1,970) | ° |
| H. Net income for the year | 2,135 | 2,646 | - | 2,646 | (511) | (19.3) |

(1) The post-merger values have been restated by giving effect, as from January 1, 2003, to the merger of IT Telecom and EPIClink in Telecom Italia executed on December 31, 2004 and effective for accounting and tax purposes as from January 1, 2004.

(2) Reduced by related cost recoveries.

(3) Includes value adjustments to financial assets, other than equity investments.

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BALANCE SHEETS

| | 12/31/2004 | 12/31/2003 post-merger | 12/31/2003 historical data | Change |
|--|----------------|---------------------------|----------------------------------|-----------------|
| (in millions of euro) | (a) | (b) (*) | | (a - b) |
| A. Intangibles, fixed assets and long-term investments | | | | |
| Intangible assets | 1,845 | 1,583 | 1,485 | 262 |
| Fixed assets | 11,020 | 12,043 | 11,843 | (1,023) |
| Long-term investments: | | | | |
| • equity investments and advances on future capital contributions | 34,233 | 34,865 | 34,995 | (632) |
| • other | 584 | 290 | 281 | 294 |
| (A) | 47,682 | 48,781 | 48,604 | (1,099) |
| B. Working capital | | | | |
| Inventories | 145 | 124 | 88 | 21 |
| Trade accounts receivable, net | 3,807 | 4,669 | 4,542 | (862) |
| Other assets | 2,854 | 3,696 | 3,693 | (842) |
| Trade accounts payable | (2,804) | (3,038) | (3,138) | 234 |
| Other liabilities | (3,926) | (3,551) | (3,476) | (375) |
| Reserves for employee termination indemnities and pensions and similar obligations | (1,043) | (1,030) | (973) | (13) |
| Capital and/or investment grants | (168) | (201) | (199) | 33 |
| Deferred tax assets net of reserve for income taxes | 2,223 | 3,111 | 3,111 | (888) |
| Other reserves for risks and charges | (702) | (604) | (569) | (98) |
| (B) | 386 | 3,176 | 3,079 | (2,790) |
| C. Net invested capital (A + B) | 48,068 | 51,957 | 51,683 | (3,889) |
| Financed by: | | | | |
| D. Shareholders' equity | | | | |
| Share capital | 8,865 | 8,854 | 8,854 | 11 |
| Retained earnings and reserves | 5,811 | 4,856 | 4,856 | 955 |
| Net income for the year | 2,135 | 2,646 | 2,646 | (511) |
| | 16,811 | 16,356 | 16,356 | 455 |
| E. Medium/long-term debt | 33,122 | 20,697 | 20,692 | 12,425 |
| F. Net short-term financial borrowings (liquidity) | | | | |
| Short-term borrowings | 3,700 | 14,376 | 14,373 | (10,676) |
| Liquid assets and short-term financial receivables | (6,477) | (1,160) | (1,426) | (5,317) |
| Financial accrued expenses (income) and deferred expenses (income), net | 912 | 1,688 | 1,688 | (776) |
| | (1,865) | 14,904 | 14,635 | (16,769) |
| G. Total net financial indebtedness (E + F + G) | 31,257 | 35,601 | 35,327 | (4,344) |
| H. Total net financing (D + H = C) | 48,068 | 51,957 | 51,683 | (3,889) |

(*) The post-merger values have been restated by giving effect, as from January 1, 2003, to the merger of IT Telecom and EPIClink in Telecom Italia executed on December 31, 2004 and effective for accounting and tax purposes as from January 1, 2004.

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STATEMENTS OF CASH FLOWS

| | 2004 | 2003 Historical data |
|---|-----------------|----------------------------|
| (in millions of euro) | | |
| A. Net financial indebtedness, at beginning of the year | (35,327) | (30,622) |
| Net financial indebtedness, at beginning of year of merged company TILAB | - | (169) |
| Net financial indebtedness, at beginning of year of merged companies IT TELECOM and EPIClink | (274) | - |
| B. Adjusted net financial indebtedness, at beginning of period | (35,601) | (30,791) |
| Operating income | 4,234 | 4,139 |
| Depreciation of fixed assets and amortization of intangible assets | 2,892 | 2,919 |
| Investments in fixed assets and intangible assets ⁽¹⁾ | (2,330) | (2,534) |
| Proceeds from capital and/or investment grants | - | 5 |
| Proceeds from disposal of intangible assets and fixed assets | 8 | 314 |
| Change in operating working capital and other changes | 769 | (141) |
| C. Free Cash Flow operations | 5,573 | 4,702 |
| Investments in long-term investments ⁽¹⁾ | (1,722) | (6,918) |
| Proceeds from sale/redemption value of other intangible assets, fixed assets and long-term investments | 2,276 | 3,102 |
| Change in non-operating working capital and other changes ⁽²⁾ | (87) | (4,661) |
| D. | 467 | (8,477) |
| E. Net Cash Flows before distribution of income/reserves and contributions by shareholders (C + D) | 6,040 | (3,775) |
| F. Distribution of income/reserves | (1,740) | (794) |
| G. Contributions by shareholders/withdrawals | 44 | 33 |
| H. Change in net financial indebtedness (E + F + G) | 4,344 | (4,536) |
| I. Net financial indebtedness, at end of the year (A + H) | (31,257) | (35,327) |

The change in net financial indebtedness is the result of the following:

| | | |
|--|----------------|--------------|
| (in millions of euro) | | |
| Increase (decrease) in medium/long-term debt | 12,425 | (3,014) |
| Increase (decrease) in short-term borrowings | (16,769) | 7,719 |
| Total | (4,344) | 4,705 |

(1) Total cash used for investments can be analyzed as follows:

| | | |
|-------------------------------------|--------------|--------------|
| (in millions of euro) | | |
| Industrial investments: | 2,330 | 2,534 |
| - <i>intangible assets</i> | 1,031 | 767 |
| - <i>fixed assets</i> | 1,299 | 1,767 |
| Investment in long-term investments | 1,722 | 6,918 |
| Cash used for investments | 4,052 | 9,452 |

(2) The caption can be analyzed as follows:

| | | |
|--|-------------|----------------|
| (in millions of euro) | | |
| Net financial income (expenses) | (1,772) | (2,404) |
| Receipt of dividends | 1,329 | 428 |
| Utilization of risk reserve for early exercise of JP Morgan put option | - | (1,942) |
| Payment of income taxes ⁽³⁾ | 934 | (246) |
| Extraordinary items and other | (578) | (497) |
| Change in non-operating working capital and other changes | (87) | (4,661) |

(3) The amount in 2004 is a positive figure as a result of the collection of a tax credit sold to TIM (euro 1,294 million).

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■ SUBSEQUENT EVENTS

Besides the cash tender offer relating to the Telecom Italia/TIM merger, described in detail under "Shareholder Information", other principal subsequent events which occurred after December 31, 2004 are listed below:

Bond buyback

On January 26, 2005 and February 3, 2005, Telecom Italia Finance S.A. bought back part of its own issue of bonds on the market (originally euro 3,000 million, 6.125% coupon, maturing April 20, 2006, with a residual value of euro 2,745 million) for, respectively, euro 26 million and euro 30 million. After the buyback of the bonds, the residual face value of the debt is now equal to euro 2,689 million.

Convertible bonds 2001-2010

Subsequent to December 31, 2004 and consistent with the suspensive periods provided by the bonds, requests were received, within February 24, 2005, for the conversion of 1,406,391,362 convertible bonds 2001-2010 issued by Telecom Italia S.p.A. (formerly Olivetti S.p.A.) corresponding to 663,188,066 Telecom Italia ordinary shares. This conversion led to a reduction in debt of about euro 1.5 billion.

Agreement for the sale of Entel Chile S.A.

On January 24, 2005, Telecom Italia, through its subsidiary Telecom Italia International N.V., signed an agreement with Almendral S.A. (an investment holding company listed on the stock exchange in Santiago, Chile, which represents local businesses including the Hurtado Vicuna group and the Matte group) for the sale of its investment in the Chilean company Entel Chile S.A., representing 54.76% of share capital. The sales price amounts to USD 934 million.

Closing of the transaction, scheduled to take place within the next three months, is subject to receipt of the necessary authorizations from the pertinent authorities.

This transaction fall under the Telecom Italia Group's strategy to rationalize its international portfolio and focus on areas of strategic interest with growth potential.

Preliminary contract for the sale of Finsiel S.p.A. to the Cos Group

With regard to the procedure for the sale of the controlling stake held by Telecom Italia in Finsiel S.p.A., on February 24, 2005, as approved by the Board of Directors on the same date, Telecom Italia signed a preliminary sales agreement with the COS group submitted for review. The sale, which covers the entire stake held by Telecom Italia in Finsiel (79.5%), is based upon an Enterprise Value fixed at approx. euro 164 million.

Following this offer, Telecom Italia decided to adjust Finsiel's carrying value, both in the 2004 statutory financial statements and in the consolidated financial statements, to its estimated sales value. Therefore, a writedown was made in the statutory financial statements for a total amount of euro 139 million that adjusted the carrying value of the investment to the estimated sales price (euro 111 million represented by our share of the Enterprise Value net of the estimated average indebtedness of the Finsiel group in the 12 months previous to the sale); in the consolidated financial statements, a provision of euro 27 million was set aside in a specific reserve.

This transaction also makes it possible to book, in the 2004 financial statements, deferred tax assets of euro 38 million, arising from the writedown of Finsiel's carrying value, euro 115 million, made by the parent company in fiscal 2002.

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■ BUSINESS OUTLOOK FOR THE CURRENT YEAR

The results of the current year will be influenced by the merger between Telecom Italia and TIM which will be presented to the next respective Shareholders' Meetings for approval. It is believed that the higher financial charges deriving from the higher debt associated with the cash tender offer, in terms of results, will be more than compensated by the impact of the acquisition of the additional stake in the subsidiary. As far as the trend in operating activities is concerned, the 2005-2007 targets are in the process of being defined and will take into account the effects of the merger. Therefore, for the current year, the Group confirms that the evolution of the result and the operating cash flows will at least be in line with those of the preceding year. In the international sphere, the Group affirms its commitment in areas of strategic interest.

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■ ADOPTION OF IAS/IFRS

■ Evolution of the benchmark regulatory framework

The principal phases which characterized the process of accounting harmonization within the European Union, and in Italy in particular, are:

- the adoption of Regulation No. 1606 issued by the European Parliament and by the Council of the European Union in July 2002 which provides for the mandatory application of IAS/IFRS, beginning from 2005, for the consolidated financial statements of companies listed in regulated markets of the European Union; moreover, this Regulation accorded to the Member States the authority to permit or to require the application of IAS/IFRS also for the preparation of the annual statutory accounts of listed companies and the annual statutory accounts and consolidated financial statements of unlisted companies;
- the European Commission's adoption of Regulation No. 1725 dated September 29, 2003 which approved the international accounting standards, and related interpretations, existing at September 14, 2002; IAS 32 and IAS 39, relating to the disclosure and measurement of financial instruments, respectively, and the related interpretations (SIC 5, 16 and 17) were excluded from that approval process;
- the issue, by Italian legislators, of Law No. 306 dated October 31, 2003 (2003 EU Law) by which the Italian legislators exercised (Art. 25) the option permitted by the above-cited EU Regulation No. 1606/2002, and, accordingly, delegating the Government to adopt one or more legislative decrees implementing the authority provided by the above-mentioned EU Regulation within one year of the law coming into force (i.e. within November 30, 2004). On November 26, 2004, the Council of Ministers approved the draft of the implementing decree provided by Art. 25 of the above-cited Law 306/2003. That document (which was approved by the competent Parliamentary Commissions in the first half of February 2005) provides that listed companies required by EU Regulation No. 1606/2002 to prepare their consolidated financial statements in accordance with IAS/IFRS may, from 2005, also draw up their annual statutory financial statements in accordance with those standards (obligatory from 2006). The possibility to apply IAS/IFRS is also conceded to the unlisted subsidiaries of listed companies. In this regard, Telecom Italia and its Italian subsidiaries intend to apply IAS/IFRS for their annual statutory financial statements beginning from 2006;
- the recommendations of CESR (Committee of European Securities Regulators) published on December 30, 2003 and containing guidelines for companies listed within the EU regarding the transition to IAS/IFRS;
- the European Commission's adoption of Regulations No. 707 dated April 6, 2004, which approved IFRS 1 "First-time adoption of International Financial Reporting Standards", No. 2086 dated November 19, 2004, which approved, with certain limitations, IAS 39, and No. 2236, No. 2237 and No. 2238 dated December 29, 2004 which approved IAS 32 and the other accounting standards reviewed by the IASB in December 2003 and March 2004, the new IFRSs issued in March 2004 (with the exception of IFRS 2, approved by the European commission with Regulation No. 211 dated February 4, 2005), and the interpretation document IFRIC 1 "Changes in Existing Decommissioning, Restoration and Similar Liabilities", thereby achieving a stable system of accounting standards.

However, the version of IAS 39 approved by the EU in the above-cited Regulation No. 2086 differs from the text approved by the IASB with regard to certain aspects of the valuation of liabilities at fair value and of the macro-hedging of the interest rate risk associated with portfolios of assets and liabilities. The Telecom Italia Group intends to apply the unabridged version of IAS 39 (i.e. the version published by the IASB).

■ Telecom Italia Group's process of conversion to IAS/IFRS

During 2003, Telecom Italia commenced a specific project relating to the implementation of IAS/IFRS (through the establishment of a dedicated working group involved the principal

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companies of the Telecom Italia Group) with the final objective being the restatement, in accordance with IAS/IFRS, of:

- the opening consolidated balance sheet at January 1, 2004 (date of transition to the new accounting standards);
- the consolidated financial statements for the year ended December 31, 2004 prepared for comparative purposes only (limited to the statements only);
- the 2004 interim data (quarterly and first-half data) prepared for comparative purposes only.

At present, the first two steps are substantially completed while the restatement of the 2004 interim data is in progress.

Moreover, the restatement of the opening consolidated balance sheet at January 1, 2004 and of the statements of the consolidated financial statements for the year ended December 31, 2004 required the following preliminary decisions by Telecom Italia among the options provided by IAS/IFRS:

- **financial statement presentation:**
 - **Balance sheet:** IAS 1 requires the classification of assets and liabilities as “current/non-current” or in terms of the “liquidity of the assets and liabilities”. The Telecom Italia Group uses the “current/non-current” classification which is generally applied by industrial and commercial enterprises;
 - **Statement of income:** in accordance with IAS 1, the statement of income may be presented with expenses classified by function or by nature. The Telecom Italia Group has chosen to adopt the classification of expenses by nature;
- **principal optional exemptions provided by IFRS 1 upon first-time application of IAS/IFRS (January 1, 2004):**
 - **valuations of property, plant and equipment, investment property and intangible assets at fair value or, alternatively, at revalued cost as the deemed cost:** for property, plant and equipment the Group can take advantage of the following optional exemptions:
 - to adopt the fair value of the asset at January 1, 2004, instead of the original cost, as the deemed cost;
 - to adopt, in the presence of certain conditions, the revalued cost of the asset, instead of the original cost, as the deemed cost.

These exemptions are applicable also to investment property valued at cost (IAS 40) and to intangible assets valued at cost provided that they meet the criteria required by IAS 38 for their recording. The Telecom Italia Group is taking advantage of these exemptions that is, for some asset adopts the revalued cost;
 - **share-based payments:** IFRS 2 is applicable to financial statements for periods beginning on or after January 1, 2005. However, earlier application of this standard is encouraged. The Telecom Italia Group intends to apply IFRS 2 prospectively beginning from January 1, 2004;
 - **business combinations:** should be accounted for by applying the purchase method provided by IFRS 3. For purposes of the first-time adoption of IAS/IFRS, IFRS 1 allows a company/group not to apply IFRS 3 retrospectively to any business combinations which occurred before the date of transition to IAS/IFRS (January 1, 2004). However, if any business combination which occurred before the date of transition is restated to comply with IFRS 3, all subsequent business combinations should be restated in accordance with the purchase method set out in IFRS 3. The Telecom Italia Group has chosen to adopt IFRS 3 prospectively beginning from January 1, 2004;
 - **reserve for net exchange differences deriving from the translation of the financial statements of foreign operations:** in accordance with IAS 21, net exchange differences resulting from the translation of the financial statements of a foreign operation

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(subsidiary, affiliate, joint venture, branch) should be classified as a separate component of equity which, upon disposal of the foreign operation, will be reclassified to the statement of income when the gain/loss on disposal is recognized. IFRS 1 allows first-time adopters of IAS/IFRS to apply IAS 21 prospectively and therefore to not record at the date of transition the cumulative net exchange differences deriving from previous translations of the financial statements of foreign operations. The Telecom Italia Group is taking advantage of this optional exemption;

- **financial instruments recorded in accordance with previous principles:** a company/group should apply IAS 39 to financial statements for periods beginning on or after January 1, 2005. Earlier application is permitted. The Telecom Italia Group has chosen to adopt IAS 32 (Financial Instruments: Disclosures and Presentation) and IAS 39 (Financial Instruments: Recognition and Measurement) from January 1, 2004;
- **designation date of financial instruments as instruments at fair value through the statement of income or as available for sale:** in accordance with IAS 39 a company/group should designate, at the time of initial recognition, a financial instrument as a financial asset or financial liability at fair value through the statement of income or as a financial asset available for sale. IAS 39 allows the possibility to make that designation at the date of transition to IAS/IFRS, and thus at January 1, 2004. The Telecom Italia Group is taking advantage of this optional exemption by making the designation at the date of transition;
- **derecognition of financial assets and liabilities:** in accordance with IAS 39, which amended IFRS 1, a company/group which applies IAS/IFRS for the first time should apply the standard of "derecognition of non-derivative financial assets/liabilities" prospectively for financial years beginning on or after January 1, 2004. In other words, if a company/group, in accordance with its previous accounting policies, derecognized certain non-derivative financial assets and/or liabilities pertaining to transactions that occurred before January 1, 2004, it should not recognize those assets and/or liabilities in accordance with IAS/IFRS (unless they satisfy the conditions provided for recognition following a transaction or event occurring after January 1, 2004).
However, a company/group may apply the "derecognition of non-derivative financial assets/liabilities" retrospectively from a date of the company/group's choosing, provided that the information needed to apply IAS 39 to assets and/or liabilities derecognized as a result of past transactions was obtained at the time of initially accounting for those transactions.
The Telecom Italia Group intends to apply the "derecognition of non-derivative financial assets/liabilities" retrospectively from January 1, 2003;

- **accounting treatments chosen from the accounting options provided by IAS/IFRS:**
 - **inventories:** in accordance with IAS 2, the cost of inventories should be determined by using the FIFO method or the weighted average cost method. The Telecom Italia Group has chosen to use the weighted average cost method for each movement;
 - **valuation of fixed assets and intangibles:** subsequent to the initial recording at cost, IAS 16 and IAS 38 provide that these assets may be valued at cost (and depreciated/amortized) or at fair value. The Telecom Italia Group has chosen to adopt the cost method;
 - **valuation of investment property:** in accordance with IAS 40, a property held as an investment property should be initially recorded at cost, including incidental costs. Subsequently, that property may be valued at fair value or at cost. The Telecom Italia Group has chosen to adopt the cost method;
 - **borrowing costs:** for the purposes of recording borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset, IAS 23 provides that an entity may apply the benchmark accounting treatment, which provides for

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the immediate expensing of borrowing costs, or the allowed alternative accounting treatment, which provides, in the presence of certain conditions, for the capitalization of borrowing costs. The Telecom Italia Group has chosen to record borrowing costs in the statement of income;

- **valuation of interests in joint ventures in the consolidated financial statements:** in accordance with IAS 31, interests in joint ventures may be accounted for using the equity method or, alternatively, using the proportionate consolidation method. The Telecom Italia Group has chosen to adopt the equity method.

■ Principal differences between IAS/IFRS and Italian accounting principles

The principal differences emerging from the application of IAS/IFRS compared to Italian accounting principles are summarized as follows:

- **extraordinary items:** in accordance with IAS/IFRS items of an extraordinary nature can no longer be shown separately in the statement of income, but should be classified as ordinary items;
- **goodwill and differences on consolidation:** these items may no longer be amortized systematically in the statement of income but should be subject to a valuation, carried out at least annually, in order to identify any impairment in value (impairment test);
- **treasury stock:** in accordance with IAS/IFRS, treasury stock may no longer be recorded as an asset but should be recorded as a reduction of shareholders' equity (for the par value) and additional paid-in capital (for the excess amount);
- **principles of consolidation:** the possibility of excluding companies that are not significant in size, companies in liquidation, and those with dissimilar activities from the scope of consolidation has been eliminated; however, special purpose entities created for specific transactions (including, for example, securitizations) and the shares of consolidated subsidiaries recorded as current assets should be consolidated;
- **assets purchased under finance lease contracts:** for purposes of the consolidated financial statements prepared in accordance with Italian accounting principles, the Telecom Italia Group accounts for finance leases (including sale and leaseback transactions resulting in a finance lease) in which there is an option to purchase in accordance with the finance method, while the other types of finance leases are, instead, accounted for in accordance with the operating method (like operating leases). The operating method provides that fixed assets purchased under lease contracts (operating or finance) be accounted for through the recording of the related lease payments as expenses for the period and the immediate recognition in the statement of income of any gains deriving from the sale of those assets. Instead, the adoption of the finance method, applicable, in accordance with IAS 17, to all types of finance leases, results in the recording in the statement of income of interest on the financed principal and depreciation on the value of the assets purchased by lease, as well as the recognition of these fixed assets as assets and the residual debt as liabilities in the balance sheet. Furthermore, the application of the finance method also results in the deferral and amortization over the lease term of any gains or losses deriving from sale and leaseback transactions where the lease is a finance lease;
- **stock options:** IFRS 2 classifies stock options as "share-based payments" or rather as "goods or services acquired as consideration for equity instruments"; in particular, based on this standard, stock options should be valued at their fair value at the time granted, recording the cost in the statement of income with a contra-entry to increase reserves in shareholders' equity;
- **employee termination indemnities (TFR):** Italian accounting principles require recognition of the liability for employee termination indemnities (TFR) on the basis of the nominal liability matured to the end of the reporting period, in accordance with the statutory regulations in force; under IAS/IFRS, TFR falls under the category of defined benefit plans subject to actuarial valuation (taking into account mortality, foreseeable changes in salaries/wages, etc.)

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to present the current value of the benefit, payable upon termination of employment, that employees have matured up to the balance sheet date;

- **compound financial instruments:** in accordance with IAS 32, the value of compound financial instruments (e.g. convertible notes) should be allocated between financial liabilities and equity instruments (e.g. share purchase options);
- **derivative financial instruments:** in accordance with IAS/IFRS, all derivatives should be reflected in the financial statements at their fair value. The method of accounting for derivative financial instruments varies based on their characteristics (hedging instruments and non-hedging instruments);
- **restoration charges:** as required by IAS 37, the Telecom Italia Group must record liabilities to be incurred at the time fixed assets are abandoned as a result of a legal or constructive obligation assumed upon purchase and construction of the installations. The liabilities will be recorded at fair value, in the period in which they arise, as a balance sheet reserve under reserves for risks and charges, with a contra-entry to the fixed assets to which they refer; recognition in the statement of income occurs through the depreciation of the related asset over its estimated useful life;
- **puts and calls on shares:** in accordance with IAS 39, the irrevocable obligation related to the purchase of shares results in the recording of the shares to be purchased and the corresponding financial liability at the time that obligation arises;
- **discontinued operations:** IFRS 5 requires that the results of discontinued operations (corporate units disposed of or held for sale) be presented in the statement of income separately from those of continuing operations; similarly, the assets and related liabilities of corporate units held for sale should be classified separately in the balance sheet;
- **revenues:** in accordance with IAS 18, the recognition criteria should be applied separately to each transaction or, in certain circumstances, to the separately identifiable components of a single transaction, in order to reflect its economic substance and, with reference to the stage of completion of the transaction, this sometimes involves, compared to the Italian regulations in force, a deferral of revenues over the duration of the contract.

In particular, with regard to revenues from the activation of telephone services and from the recharging of prepaid cards, the connection/activation service is not an independent process of revenue generation realized at the time the service is rendered; accordingly, the related revenue must be recognized over time in line with the supply of the related services. This period should be estimated based on the expected duration of the relationship with the customer. Similarly, also the costs incurred for the activation of the service and the recharging of the prepaid card (mainly direct labor costs) should be deferred and recognized in the statement of income over the expected duration of the relationship with the customer.

■ **Principal impacts on the 2004 consolidated financial statements deriving from the application of IAS/IFRS**

Accordingly, the above-mentioned differences emerging from the application of IAS/IFRS compared to the accounting principals in force in Italy, as well as the choices made by Telecom Italia with respect to the accounting options allowed by IAS/IFRS, result in a restatement of the accounting data prepared in accordance with the current Italian statutory regulations with, in some cases, significant effects on the shareholders' equity and the net financial indebtedness of the Group at December 31, 2004. In particular, the differences emerging from the application of the new standards that have a significant impact on the 2004 consolidated financial statements are summarized as follows:

- **goodwill and differences on consolidation:** these items are no longer amortized systematically in the statement of income but are subject to a valuation, carried out at least annually, in order to identify any impairment in value (impairment test). This different practice causes an improvement in net income for 2004 as a consequence of the writeback of amortization recorded in the year under Italian accounting principles;

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- **scope of consolidation:** all subsidiaries (as well as the related shares previously classified as current assets) should be subject to consolidation. Furthermore, vehicle companies (i.e. Special Purpose Entities, or SPEs) created, for example, for securitization transactions, to which receivables are sold and for whose financial needs securities are issued that are subscribed to by third party investors, are to be included in the scope of consolidation. Accordingly, the consolidation of vehicle companies causes an increase in the net financial indebtedness of the Group;
- **factoring transactions:** the adoption of IAS/IFRS and in particular of the provisions of IAS 39 with regard to the derecognition of financial assets (receivables) results in a more restrictive interpretation of the requirements for the recognition of the final sale of receivables with a consequent negative impact on net financial indebtedness;
- **sale and leaseback transactions:** some transactions for the sale of properties with simultaneous leaseback contracts that were carried out by the Telecom Italia Group in previous periods, and classified as operating leases at that time, are classified as sale and leaseback transactions resulting in a finance lease under IAS/IFRS; accordingly, for the purposes of IAS/IFRS, those transactions are recorded in accordance with the finance method, illustrated above, with a consequent increase in net financial indebtedness;
- **reserves for risks and charges:** the provisions of IAS/IFRS involve a more restrictive valuation of these liabilities. In particular, under IAS/IFRS opening shareholders' equity at January 1, 2004 benefits from a positive adjustment to opening net equity for the reversal of certain reserves for risks and charges recorded in the financial statements prepared in accordance with Italian accounting principles. In the December 31, 2004 financial statements prepared, for comparative purposes, in accordance with IAS/IFRS, this different accounting treatment causes a deterioration of net income as a consequence of the reversal of the releases to the statement of income of the reserves for risks and charges recorded in 2004 in accordance with Italian accounting principles;
- **compound financial instruments:** the allocation of compound financial instruments (e.g. convertible notes) between their liability and equity components causes a decrease in indebtedness and an improvement in shareholders' equity;
- **derivative financial instruments:** the recording in the financial statements of derivative financial instruments at fair value causes an increase in net financial indebtedness at December 31, 2004;
- **TIM share options:** for IAS/IFRS purposes, the irrevocable obligation arising at the end of 2004 to purchase, in the first months of 2005, shares of TIM (as the financial transaction linked to the merger of Telecom Italia and TIM) results in the recording of a financial liability in the December 31, 2004 financial statements with a consequent increase in net financial indebtedness;
- **treasury stock:** the reclassification of treasury stock causes a reduction in shareholders' equity;
- **revenues:** revenues from the activation of telephone services and from the recharge of prepaid cards, as well as the related costs, are deferred over the expected duration of the relationship with the customer, with a consequent negative effect on net income.

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■ RELATED PARTY TRANSACTIONS

Related party transactions, including intragroup transactions, are neither unusual nor exceptional but fall under the normal business operations of the companies of the Group. Such transactions, when not concluded at standard conditions or dictated by specific laws, are in any case conducted at arm's length.

The economic, balance sheet and financial effects of related party transactions on the consolidated financial statements of the Telecom Italia Group at December 31, 2004 are presented in the following table.

The economic, balance sheet and financial transactions between Telecom Italia S.p.A. and subsidiaries and affiliated companies are reported, as a supplement to this disclosure, in the individual notes to the statutory financial statements of Telecom Italia S.p.A.

The following table presents the major economic, balance sheet and financial transactions between companies consolidated line-by-line and unconsolidated subsidiaries and affiliates.

| (millions of euro) | | |
|---|-----|---|
| Sales and service revenues | 333 | These mainly comprise revenues from Teleleasing (euro 200 million), LI.SIT. (euro 40 million), Shared Service Center (euro 32 million), Consorzio Mael (euro 14 million), Sky Italia (euro 8 million), Telecom Argentina (euro 10 million), Golden Lines (euro 10 million) and Etec SA Cuba (euro 9 million) |
| Raw materials and outside services | 446 | These mainly comprise rent payable to Tiglio I (euro 56 million) e Tiglio II (euro 28 million) as well as TLC service costs from Etec SA Cuba (euro 123 million), Telecom Argentina (euro 6 million), and maintenance and assistance contracts from Shared Service Center (euro 106 million), software costs and computer material, as well as maintenance and assistance contracts from Siemens Informatica (euro 63 million), costs for TLC equipment, as well as maintenance and assistance contracts from the Italtel group (euro 23 million), and costs for TLC equipment, as well as operating lease costs from Teleleasing (euro 21 million) |
| Net other income (expenses) | 6 | These mainly relate to cost recoveries for personnel on loan to some subsidiaries and affiliates |
| Financial income | 5 | These include accrued interest income on loans made to some subsidiaries and affiliates |
| Financial expense | 2 | These include accrued interest expenses on loans made to certain subsidiaries and affiliates |
| Loans in long-term investments | 64 | These mainly comprise medium/long-term loans made to Avea I.H.A.S. (euro 29 million), Aree Urbane (euro 20 million), Golden Lines (euro 5 million), Telegono (euro 3 million) and Tiglio I (euro 3 million) |
| Financial receivables | 7 | These mainly comprise short-term loans made to Tin Web (euro 5 million) |
| Financial payables | 24 | These refer mainly to payables to Teleleasing (euro 15 million) and Shared Service Center (euro 6 million) |
| Trade and other accounts receivable | 195 | They mainly regard receivables from LI.SIT. (euro 77 million), Teleleasing (euro 70 million), Tiglio I (euro 9 million), Shared Service Center (euro 7 million) |
| Trade and other accounts payable | 281 | They mainly include supply transactions connected with investment and operational activities: Italtel group (euro 150 million), Siemens Informatica (euro 61 million) ad Shared Service Center (euro 34 million) |
| Guarantees and collateral provided | 661 | These mainly comprise sureties provided on behalf of Avea I.H.A.S. (euro 454 million), Tiglio I (euro 56 million), Aree Urbane (euro 45 million), Consorzio Csia (euro 38 million), Italtel group (euro 35 million) ad Tiglio II (euro 13 million) |
| Purchases and sales commitments | 4 | These refer to commitments with Saturn Venture Partners for future capital increases |
| Investments in fixed assets and intangibles | 395 | These mainly consist of acquisitions of telephone exchanges from the Italtel group (euro 324 million) and computer projects from Shared Service Center (euro 21 million) and Siemens Informatica (euro 50 million) |

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Related party transactions other than those with companies of the Group, during 2004, particularly comprise those by the Telecom Italia Group with the Pirelli group, the Edizione Holding group, the Unipol group, the ST Microelectronics group and the companies affiliated with Mr. Moratti, the company Telepost S.p.A. and the Camfin group.

As for transactions with the Banca Intesa group and the Unicredito group, the data refers to the first quarter of 2004 in that the Directors, through which the companies were considered related parties, ended their term of office on the date of the Shareholders' Meeting of May 6, 2004.

The following table presents the major economic, balance sheet and financial transactions between companies consolidated line-by-line and parties related to Telecom Italia through the Directors and key managers of the Company.

| (millions of euro) | | |
|---|-----|--|
| Sales and service revenues | 40 | These mainly refer to computer services and the supply of energy services to the Pirelli group (euro 3 million), power cable-laying services to the Pirelli group (euro 2 million) and telephone services to the Pirelli group (euro 3 million), to the Edizione Holding (euro 5 million), to the Unipol group (euro 13 million), to the ST Microelectronics group (euro 2 million), to the companies affiliated with Mr. Moratti (euro 1 million), to the Banca Intesa group (euro 3 million) and to the Unicredito group (euro 8 million) |
| Raw materials and outside services | 120 | These essentially refer to R&D expenditures and consulting services in the area of computers, tax and intellectual property rights from the Pirelli group (euro 86 million), Document Management services by Telepost (euro 15 million), insurance services by the Unipol group (euro 11 million), sponsoring and content provider costs in reference to F.C. Internazionale Milano S.p.A. – a related party through Mr. Moratti (euro 5 million), commissions paid to Autogrill S.p.A (Edizione Holding group) for the sale of prepaid telephone cards (euro 2 million) and the purchase of electronic components from ST Microelectronics (euro 1 million) |
| Net other income (expenses) | 1 | These mainly relate to miscellaneous revenues with the Pirelli group |
| Miscellaneous operating costs | 1 | These refer to miscellaneous expenses with the Pirelli group |
| Trade and other accounts receivable | 10 | These mainly refer to the above-mentioned services under sales and service revenues rendered to the Pirelli group (euro 8 million) and to the Edizione Holding group (euro 2 million) |
| Trade and other accounts payable | 65 | These mainly refer to supply transactions connected to the performance of services, investment activities from the Pirelli group (euro 49 million), insurance costs from the Unipol group (euro 11 million), costs for Document Management services rendered by Telepost (euro 3 million) and sponsoring costs in reference to F.C. Internazionale Milano S.p.A – a related company through Mr. Moratti (euro 2 million) |
| Investments in fixed assets and intangibles | 24 | These mainly refer to purchases of telecommunications cables from the Pirelli group |

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■ ECONOMIC AND FINANCIAL PERFORMANCE TELECOM ITALIA GROUP BUSINESS UNITS/ CENTRAL FUNCTIONS



WIRELINE

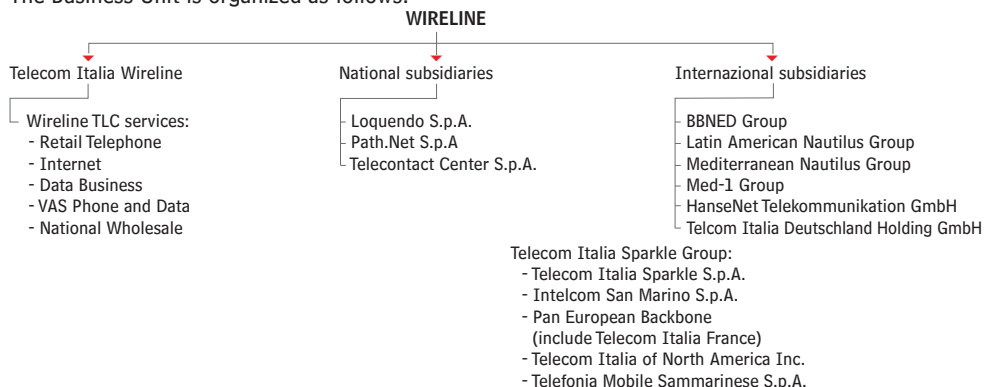
- ▶ Continuing growth of revenues and margins
- ▶ Fortification of traditional core business of Internet access and traffic, while maintaining the market share of traffic
- ▶ Strong growth of the broadband market with more than a 100% increase in the Wireline broadband access portfolio
- ▶ Development of the markets for innovative services (VAS, Phone and Web services) and innovative phones (Aladino and videotelephones)
- ▶ Consolidation of the European Broadband project with growth in revenues and customers in France and Germany

■ THE BUSINESS UNIT

The Wireline Business Unit operates on a national level as the consolidated market leader in wireline telephone and data services and call centers, for final (retail) customers and other (wholesale) providers. On an international level, Wireline develops fiber optic networks for wholesale customers (in Europe and South America), as well as innovative broadband services in key European metropolitan areas. In 2004, the market was again dogged by aggressive competition. This was more accentuated in the case of domestic traffic, and was countered with new plans offered as part of actions to retain customers.

■ THE STRUCTURE OF THE BUSINESS UNIT

The Business Unit is organized as follows:



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■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

In 2004, the scope of consolidation changed as a result of the following corporate-related events:

- consolidation, beginning January 1, 2004, of the company "Telefonia Mobile Sammarinese S.p.A"., 51%-owned by Intelcom San Marino S.p.A.;
- on July 1, 2004, Loquendo S.p.A. sold the "Applications" business segment, which designs projects based on advanced voice technologies, to Citec S.p.A. (a company specialized in planning and developing integrated voice and data systems). At the same time, a contract was also signed to confer the role of Master Distributor to the same Citec for Loquendo technologies in Italy;
- on July 1, 2004, Atesia sold the wireline customer care services business segment to Telecontact Center S.p.A.;
- November 12, 2004 marked the date of the execution of the agreement signed July 2, 2004 between Telecom Italia and the company Communication Services S.p.A. (part of the COS Group and the Italian leader in outsourcing for Contact Centers and CRM - Customer Relationship Management services) for the sale of the 80.1% stake in Atesia. The sale only covers the activities conducted for TIM and the external market.

* * *

Furthermore, the partial spin-off of Atesia to Telecontact Center became effective in February 2004. The transaction involved the transfer of the entire corporate complex consisting of two call centers located in Caltanissetta and Catanzaro. The accounting value of the structures transferred was equal to euro 3.5 million.

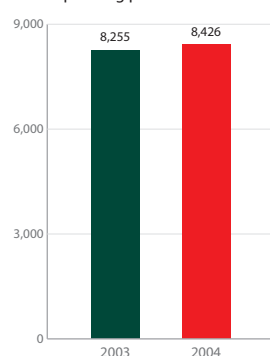
In December 2004, Telecom Italia reached a preliminary agreement with minority shareholders of Med SA, Med Ltd and Med 1 to resolve certain conflicting situations referring to MED SA's and Telecom Italia's put, respectively, on 49% of Med Ltd and Med 1 shares, also to resolve the arbitration proceedings set into motion in Luxembourg by the Fishman group (FTT) aimed at the restitution of the sums paid to Telecom Italia International in 2000 for the purchase of 30% of MED SA.

The transactions negotiated, which call for the buyback of all the minority shares in Med Ltd and in Med 1, allow Telecom Italia to strengthen its presence in the IP services and "wholesale" data sector in the eastern Mediterranean area. At the same time, non-strategic assets referring to certain local Israeli activities now managed by the same MED 1 and Med Ltd will be sold to the counterpart. The execution of the agreement should take place during 2005 and is subject to the approval of the competent regulatory authorities as well as the verification of all the conditions formally agreed and accepted by the parties.

■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003.

Gross operating profit



| | 2004 | 2003 | Change | |
|---|--------|--------|--------|-------|
| (millions of euro) | | | amount | % |
| Sales and service revenues | 17,571 | 17,216 | 355 | 2.1 |
| Gross operating profit | 8,426 | 8,255 | 171 | 2.1 |
| % of revenues | 48.0 | 47.9 | | |
| Operating income pre-amortization of differences on consolidation | 5,207 | 4,972 | 235 | 4.7 |
| Operating income | 5,199 | 4,969 | 230 | 4.6 |
| % of revenues | 29.6 | 28.9 | | |
| Investments: | | | | |
| - industrial | 2,201 | 2,302 | (101) | (4.4) |
| - differences on consolidation | 0 | 43 | (43) | |
| Employees at year-end (number) | 50,383 | 50,766 | (383) | (0.8) |

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Sales and service revenues, totaling euro 17,571 show an increase of 2.1% (+euro 355 million) compared to the prior year, thus confirming the already positive economic performance of 2003. On a comparable consolidation basis, underlying growth was euro 303 million, +1.8%. This positive performance was achieved thanks to the success of efforts to develop the Broadband market and innovative services, particularly Web services. Furthermore, the core telephone market continued to be successful, and the range of wholesale services was enhanced. The contribution to revenues by the individual Strategic Areas of Business is as follows:

Retail Telephone

Retail telephone revenues, equal to euro 10,267 million, show a limited reduction (– euro 67 million, – 0.6%) compared to the prior year. The policy of building customer loyalty continues to be the primary aim of marketing strategy. This takes the form of adding attractive features to the flat rate plans and the new *Tutto 4** and *Chat SMS* packages, which, at December 31, 2004, had reached 7,813,300 customers (of which flat-rate plans total 5,883,300). This was possible thanks partly to the evolution of Innovative Phones, that is, the *Aladino* line of cordless phones equipped with an ever-broader range of options to support innovative services, and videophones. At the end of 2004 the Innovative Phone portfolio arrived at 1,555,000 units.

Retail Internet and Data Business

Revenues from the Internet and the Data Business areas, equal to euro 2,526 million, showed overall growth of approximately 12.5% compared to the prior year (+euro 280 million, of which +euro 251 million referred to Internet Consumers and +euro 29 million to Data Business services). This growth was generated, in particular, by the *ADSL Alice* and *ADSL Smart* packages (+euro 307 million, +108%) and by innovative data transmission services (+euro 104 million, +20%). Conversely, there was a decrease in revenues from traditional data transmission services (including leased lines and data products) and Internet dial-up traffic (respectively, – euro 75 million and – euro 56 million).

At the end of 2004, the overall Telecom Italia Wireline's Broadband portfolio had reached a total of 4,430,000 access lines, an increase of +2,230,000 lines compared to December 31, 2003.

On the domestic market, the number of access lines stood at 4,010,000, an increase of 1,970,000 over December 31, 2003.

On the European market, the number of Broadband access lines totaled 420,000, a growth of 260,000 compared to December 31, 2003. The increase was sustained by the growth of European projects (in France with Telecom Italia France, and in Germany with HanseNet) and by the increment in the clientele of BBNet in Holland.

During 2005, the range of Broadband services, relating to the European projects in France and Germany, will be further enhanced by the launch of new VAS services and innovative phones.

Retail VAS (Value Added Services)

Revenues from VAS services, equal to euro 1,070 million, showed a decrease of euro 60 million (– 5.3%) compared to 2003 following the contraction of premium services (– euro 209 million, – 43.3%). This was partly compensated by the growth of innovative services (+euro 149 million, +23%) achieved thanks especially to the trend of Web services (+euro 102 million, +51.8%).

Wholesale

Revenues from Wholesale services, equal to euro 3,329 million, increased by a total of a euro 61 million (+1.9%), compared to 2003. The growth of revenues from national wholesale services amounted to euro 6 million – with particular emphasis on revenues from Data services (+euro 85 million, +60.7%) – and that of international wholesale operations was euro 55 million (+4.3%).

Gross operating profit, equal to euro 8,426 million, registered an increase of euro 171 million (+2.1%) compared to 2003. As a percentage of revenues, gross operating profit was 48% (47.9% in 2003).

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On a comparable consolidation basis, underlying growth was 2.0%.

The improvement in gross operating profit in 2004 can be attributed not only to the trend of revenues but also to careful management geared to achieving ever-higher levels of efficiency, with a significant improvement in personnel costs and in terms of costs not directly related to business development.

Operating income was euro 5,199 million, and presented an increase of 4.6% (+ euro 230 million) compared to 2003. This was the result of not only the factors already mentioned with regard to gross operating profit, but also lower amortization and depreciation and valuation adjustments. Operating income represented 29.6% of sales (28.9% at the end of 2003).

On a comparable consolidation basis, underlying growth was equal to 5.1%.

Industrial investments amounted to euro 2,201 million and presented a decrease of euro 101 million (– 4.4%), albeit fully respecting the development policies for innovative infrastructures (with particular reference to Broadband activities in the domestic and international spheres), thanks to processes designed to optimize expenditures.

The number of *employees* decreased by 383 compared to December 31, 2003.

The change is due to the hiring of 1,917 persons, including 882 in Telecontact Center (referring to persons taken on under continuous coordinated collaboration contracts, previously employed by Atesia), and about 500 persons by Telecom Italia Wireline (relating to the strengthening of the network operating structure and the improvement in the professional mix) and an increase in the number of employees at the company Telecom Italia France and 2,384 persons who left the company (mainly in Telecom Italia Wireline). There were also organizational changes – mainly regarding the activities performed by the company's telephone exchanges – which brought 226 persons from Telecom Italia's Corporate Central Function to Wireline. In addition, there were intragroup transfers (+9), the consolidation of Telefonía Mobile Sammarinese (+6), the sale of the Loquendo business segment to Citec S.p.A. (– 58) and the sale of Atesia to Communication Services S.p.A (– 99).

■ EVENTS SUBSEQUENT TO DECEMBER 31, 2004

The following events took place:

- on January 19, 2005 the National Regulatory Agency approved the new Telecom Italia rate charges which only affect local calls. The new charges, with effect from January 23, 2005, have increased the price of the answering charge for local calls but have reduced the price per minute of the duration of local calls;
- on January 26, 2005 Telecom Italia signed a protocol agreement with the Consumer Associations which establishes new modes of operation for handling complaints about traffic generated by numbers beginning with 709. In fact, Telecom Italia, has decided to proceed with canceling the amounts owed for 709 traffic prior to September 1, 2003 in the case of residential customers who lodged a regular complaint according to the rules established by the conditions in the phone contract and have reported to or filed a lawsuit against the competent authorities;
- on February 1, 2005 Telecom Italia doubled the speed of broadband connections to 640 Kb/s both for residential customers with ADSL flat-rate plans and business customers. As a result, these customers received a connection upgrade to 1.2 Megabit/s for receiving and to 256 Kb/s for transmitting, without having to request an upgrade or pay any extra charge.

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■ INFORMATION ON OPERATIONS

The main operating highlights at December 31, 2004 compared to December 31, 2003 are reported below, in addition to the principal commercial activities carried out during 2004.

| Operating data | 12/31/2004 | 12/31/2003 |
|--|------------|------------|
| Fixed network connections (thousands) | 25,957 | 26,596 |
| - of which ISDN | 5,805 | 6,027 |
| Minutes of traffic on the fixed network (billions) | 216.8 | 226.6 |
| • national traffic | 203.9 | 215.2 |
| • international traffic | 12.9 | 11.4 |
| TP Terminals using ISDN technology (thousands) | 124.5 | 128.0 |

■ Retail

A brief description follows of the main packages and commercial initiatives in 2004, under the framework of the strategies presiding over the Retail Phone market (Access and Traffic in particular) and the developments keyed to the Internet markets (Adsl Alice and Adsl Smart plans), Data business (Broadband and other Data services) and VAS.

| | | |
|-----------|----------------------|---|
| Telephone | Pricing (rate plans) | <p>Residential customers: in 2004, concurrent with the launch of the Videophone, the Family and Microbusiness segments have the option of making local and long-distance Videocalls at a single rate (euro 6 cents per minute). The range of pricing packages was extended by the launch of <i>Teleconomy Quando Vuoi</i>, the first package which, against payment of a monthly subscription charge, allows customers to choose the time of day during which they can make all fixed-fixed national calls free of charge. In the summer, with the aim of encouraging the growth of new accesses, the <i>Welcome Home</i> package was launched for international calls, directed at customers of ethnic origin.</p> <p>Business customers: March 2004 saw the launch of the <i>Programma Business</i> package, which was enhanced in July 2004 by three new price lists geared to Corporate and SME (Small Medium Enterprise) customers with very high traffic consumption. During 2004, the <i>Teleconomy Aziende Quando Vuoi</i> was also launched, directed at Microbusiness customers who, against payment of a monthly subscription charge, can choose the time of day during which they can make all fixed-fixed national calls free of charge.</p> |
| | Products | <p>2004 saw the launch of the first Videophone, the first corded telephone with a color display offering the Family and Microbusiness segments the possibility of videocommunication on the wireline network. New versions of the family <i>Aladino</i> were also brought out, in particular <i>Aladino micro</i>, the first cordless phone with a modern design giving users the option of downloading ring-tones, <i>Aladino young</i>, the entry level cordless phone in the range of products with a color display, <i>Aladino MMS</i>, an MMS cordless phone with a camera incorporated and, finally, <i>Aladino Flip</i>, the first MMS cordless phone with a shell-shaped design. Other new products included the <i>Raffaello</i>, a low-range fax machine geared to a target of retailers, craftsmen and small businesses, the <i>STARIX</i> switchboard, and the <i>Toshiba PC</i> (only for the Business segment). The last two products can be bought in installments.</p> |
| Internet | Adsl Alice | <p>The September 1 - November 30 promotion in which all new Alice Free customers could surf the Internet free of charge was extended to December 31. A new look&feel and repricing was given to the MPU (the Alice box with modem and activation card) at partner stores and on the e-commerce channel, only for the <i>Alice Free</i> package, in a promotion which ran until January 31, 2005. <i>Alice Mia</i> is the new package incorporating Internet + voice services, enabling customers to have up to five personal telephone numbers and up to three simultaneous conversations, and to take advantage (also in the Wireless mode) of all the potential and benefits of the <i>ADSL Alice</i> packages. The content package of the <i>Rosso Alice</i> portal was enhanced with broadcasting, also live coverage, of the matches played by 15 Serie A and Serie B teams competing in the soccer championship and the reality show "Grande Fratello".</p> |
| | Adsl Smart | <p>Launch of the <i>Smart Free PRO</i> package which completes the range of PRO profiles being marketed. They include the sale in bundles of connectivity and VAS and WEB services provided by the platform (messaging, FAX, SMS, security, videocommunication and websites).</p> |

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| Public Telephone Services | | New types of prepaid telephone cards were launched in 2004, with different rate profiles, to meet the needs of the various targets, both in terms of traffic towards national and international fixed and mobile phones. Also being marketed is a prepaid card valid for two months which gives unlimited access to Internet from public Internet access points. Finally, the <i>InfoTutto "in Città"</i> service was introduced. This makes it possible to obtain various sorts of information (telephone numbers, restaurants, hotels, etc.) by simply using the function keys of the <i>Digito</i> telephone. |
| Data Business | Interbusiness & Hyperway | Launch of new ADSL broadband profiles and revisions in speeds and repricing of already existing packages. Package additions include the new Cisco and TIR (Intelligent Network Termination) wireless technologies for equipment located at customers' premises. Introduction of new access equipment technologies, both for sale and as TIR. Marketing of broadband accesses and applications geared to small and medium-size companies and the introduction of <i>HighBusiness</i> profiles based on copper high-speed connectivity up to 9Mb. Lastly, introduction of so-called "non standard" value-added services and package additions of modes of marketing using temporary accesses. |
| | Public Wi-Fi | Continued extension of the Public Wi-Fi service coverage begun in 2003. At the end of 2004, the service was based at approximately 1,000 locations in Italy: 300 Large Locations, 250 minor locations (available thanks to the <i>Hot Spot in a Box</i> package launched last spring) and the remaining locations through <i>roaming</i> with Tin.it and Megabeam. Outside Italy, on the other hand, the service is available in 44 countries at approximately 17,000 locations available thanks to roaming agreements with leading international operators. Beginning in 2004, prepaid cards can be purchased on line for access to the Wi-Fi service. |
| | Dat@wan | Package additions of modes of marketing that include temporary accesses. Upgrading of technologies and equipment located at customers' premises. |
| | Lambda | Marketing of accesses at 622 Mb and 10 Gb in urban areas and for long-distance. |
| Telephone VAS | Services | <p>Families: During 2004, the new Tutto 4* subscription package was launched, which makes services and information content available to customers. Commercial launch of the fixed network MMS service for sending multimedia messages to all fixed-line telephones, TIM e-mail addresses and mobile phone numbers. Option 3 of the <i>405 service</i> was expanded by means of a new function permitting customers to identify the name of the caller for "missed calls". More SMS numbers were made available for sending SMSs for charity campaigns and important new SMS fund-raising campaigns were organized (Telethon, AIRC, the Tsunami Emergency etc.). Preliminary tests were made with the operator Vodafone on the service which alerts callers making calls from mobile to fixed phones when an engaged number is free, also of the SMS dictation service (Speech2Text). Finally, the <i>4888 Pay for Me</i> service was made available to the mobile telephone services operator WIND.</p> <p>Business: launch of the fixed network MMS service combined with the cordless phone <i>Pico</i>. The numbers of SMSs sent for fund-raising campaigns increased, while testing was carried out on the service which alerts callers making calls from mobile to fixed phones when an engaged number is free. Launch of the SMS dictation service (Speech2Text).</p> |
| Data & Web VAS | Full Business Company (FBC) | The <i>FBC</i> package portfolio was completely renovated. Launch of the <i>Community Portal</i> , an integrated administration portal available to all the <i>FBC</i> clientele. <i>Application hosting</i> and <i>DB hosting</i> services were promoted, based on a platform constructed according to the latest <i>Web Services</i> market standard. Finally, during 2004, marketing began of the new functions of the <i>SAM messaging</i> service, also access by means of the MAPI protocol which offers hi-tech collaboration and integration services with mobile devices. |

■ National Wholesale

In 2004, the growth of the national Wholesale market reflected the trends which had emerged the prior year, with a contraction of interconnection telephone traffic by other operators of 6%. This situation was countered by growth, particularly by Mobile OLO operators, of traffic terminated on the Telecom Italia network (+3% compared to 2003).

With regard to lines supplied to other operators, broadband access lines continued to grow. This was partly encouraged by the launch of Shared Access lines, along with the by now consolidated XDSL and LLU models. Details of the most significant quantitative changes are as follows:

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| Broadband access | XDSL | The number of XDSL Wholesale accesses acquired by other operators (both those with licenses and Internet Service Providers) reached 895,000, with an increase of 67% compared to the prior year. |
| Local Loop Unbundling (LLU) | LLU Lines | The number of lines directly connected to the networks of other operators totaled approximately 760,000, of which 368,500 are qualified for ADSL access. Furthermore, during 2004, approximately 23,000 Shared Access lines were activated to enable other operators to supply ADSL access to the telephone clientele of TI. Including Shared Access lines, the percentage of access lines acquired by other operators to supply the broadband service rises to approximately 52% (compared to 42% at the end of 2003). |
| Carrier PreSelection | CPS Lines | Approx. 2,150,000 carrier preselection requests were handled up to the end of 2004, an increase compared to those handled in 2003. By the end of 2004 approximately 4,017,000 access lines had been configured, with a positive net increase of approximately 300,000 lines compared to 2003. |

■ International Wholesale

In Europe, Telecom Italia Sparkle maintained its leadership position in the Voice market and continued to play an important role in the IP & Data transmission segment.

The Voice business showed a steady growth in volumes, equal to approximately 14%, compared to 2003 (excluding traffic from Telecom Italia Wireline customers). A decisive contribution to this increase was generated by transit traffic which increased by approximately 24%, thanks to the competitiveness of the offering on the international market. This performance also proved possible thanks to the policy of acquiring new customers (57 new interconnections, of which 29 in Voice Over IP - VOIP), a continuous effort to achieve cost efficiencies, based on the development of VOIP carrier technologies (863 million minutes compared to 145 million minutes in 2003), and strategic hubbing policies with customers and suppliers in Africa and the Middle East. With regard to VOIP, synergies set up with Intelcom San Marino, by using their platforms, resulted in approximately 276 million minutes being delivered, proving to be the "best cost" on some routes.

With regard to the IP & Data Transmission market, during 2004, the downward trend of prices was accompanied by a substantial growth of the band sold in the wholesale market, a phenomenon which contributed to an increase in revenues from innovative services of approximately 40% compared to 2003.

■ Domestic network

The domestic network in statistics at December 31, 2004 was as follows.

| | |
|--|--|
| Exchange areas | about 10,340 |
| Switching areas | 615, served by 628 line Urban Group Stages (SGU) |
| Gateway Areas | 33 |
| Copper access network | 105.2 million of kilometers-pair |
| Fiber optic access network | 430,000 kilometers-line |
| Fiber optic carrier network | 3.24 million of kilometers-line |
| Direct dialing circuits | 3.9 million |
| Network for direct digital circuits (PARD) | 435,000 access points with speed up to 2 Mbit/s |
| Network for direct analog circuits (PARD) | 93,000 access points |
| Frame Relay Accesses | 85,000 gates at 2Mbit/s |
| PoP main data networks | 32 |

As far as the domestic network is concerned, the following took place in 2004:

| | |
|--|--|
| National transmissive backbone (fiber optic evolution) | Another 21 Marconi latest-generation high-capacity electronic frames have been installed, bringing the total restoration capabilities to 27 junctions, all located in the largest Italian cities. Work continued to strengthen the DWDM links already in operation, which have an overall capacity of more than 150 systems. |
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| Gigabit Ethernet Access | Work continued to create a network to support the marketing of services based on Gigabit Ethernet technology (<i>Eternity</i> , <i>Hyperway</i> and <i>Genius</i> services based on GBE access). In 2004, 424 new gates with GBE access were installed (up to the end of December, a net increase of 403). In the second half of 2004 the new GBE network for Lodi was completed, bringing the current coverage of GBE technology to 22 locations in Italy. |
| ADSL Access | In 2004, 750 new exchanges were equipped and 1.96 million new lines were added. There are now 3,750 exchanges that can provide ADSL access. At the end of 2004, ADSL coverage of the national territory was approximately 83%. |

■ Foreign Retail Networks

By launching the *"International Broadband"* project, Telecom Italia created access and innovative Broadband service packages in the key European cities by exploiting its know-how and technological assets.

The project, conceived in 2003, currently involves France and Germany through the subsidiaries Telecom Italia France and HanseNet.

| | |
|----------------|--|
| FRANCE | <p>The main achievements by Telecom Italia France (TIF) during 2004 involved the start of the Local Loop Unbundling (LLU) service in the Ile de France (Paris) area and in the cities of Nantes, Strasbourg, Lille and Bordeaux through 79 new exchanges. The total number of exchanges reached by TIF through LLU at December 31, 2004 in the eight cities where the service is active is 208. Work has begun to close the national loop which will protect TIF's traffic and increase its assets. The following sections are involved:</p> <ul style="list-style-type: none"> Bordeaux-Nantes in IRU fiber Second routing Paris-Lille in Lambda@2.5Gb/s Strasbourg-Lyon in IRU fiber Lyon-Marseilles in Lambda@10Gb/s Second routing Marseilles-Nice-Savona in Lambda IRU fiber @10Gb/s in synergy with the supply of a Lambda for the MCI contract <p>The main services offered are as follows:</p> <ul style="list-style-type: none"> launch of the VAS voice services of the 4* services package and the "Rosso Alice" portal creation of ADSL service with 3 Mbit/s of band in December, trials began of the Alice Voice service, the commercial launch of which is scheduled for April 2005. |
| GERMANY | <p>The main achievements by HanseNet in 2004 involved the extension of the service from the Hamburg area to other key areas of Germany (Munich, Berlin, Stuttgart, Frankfurt) and were identified with the acronym of Germany Extension (GE). Achievements include:</p> <ul style="list-style-type: none"> conclusion of the negotiations to acquire, from COLT, the IRU – Indefeasible Right of Use – of the fiber optic connection between the cities of Hamburg, Berlin, Munich, Stuttgart and Frankfurt creation of the long-distance transport infrastructure using the PEB network plus a further 2,000 km of optic fiber in IRU conclusion of the negotiations with LambdaNet to occupy space in the POPs in Berlin, Munich, Stuttgart and Frankfurt IP Backbone: creation of Centro Stella Hubs in the cities of Hamburg and Frankfurt and POPs for transit traffic in Berlin, Munich and Stuttgart requests that Deutsche Telecom should provide space for 251 new exchanges to be distributed between the cities of Berlin, Munich, Stuttgart, Frankfurt and Lübeck, with the aim of providing integrated Voice and Data transmission services based on the solution of Local Loop Unbundling. The service is scheduled to be launched in Berlin at the beginning of February and, subsequently, in the other cities. |

■ International Network

Telecom Italia Sparkle operates international wholesale Voice, Data transmission and IP services and retail Global Corporate Network services for Multinational Customers using an international network consisting of corporate-owned cross-border backbones and bilateral connections. As far as voice telephone services are concerned, during 2004, the switching capacity of international gateways was increased and new services were introduced to accommodate the range of innovative services and new modes of interconnection (Mobile Number Portability, ISUP v2, ITU-ANSI conversion). The ToIP platform was also adapted to support services which

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are establishing themselves as market standards (T.38 Fax Relay, DTMF Out of Band, H.323, SIP, SIP-T) and the billing platform was completely renovated to support the evolution of the business model. In addition, a new PoP was established in Singapore for the collection and direct termination of voice traffic from/to the Asia-Pacific area.

The FreeMoveproject was completed, thus extending interconnection to other European operators with a total coverage of 14 countries, the aim being to support the alliance between European mobile operators, known as TTTO.

With reference to IP & Data Transmission services, work continued to develop the IP backbone by increasing the transmissive capacity of the European backbone and the trans-Atlantic band. Furthermore, in the U.S.A., in the NAPs – Network Access Points – of Newark (NJ), Miami, Palo Alto and Ashburn, approx. 6 Gbit/s of new peerings (IP traffic exchange) were activated. New PoP (Point of Presence) were created in Hamburg (Germany) for synergies with HanseNet, and in Cairo (Egypt), to support the development of IP & Data Transmission business in the Mediterranean area.

In South America the 'Golden Ring' project was completed, in collaboration with LAN, with the creation of IP PoPs in Santiago, Buenos Aires, Lima and San Paolo.

With regard to Global Corporate Network retail services to Multinational Customers, the network was extended for the offering of IP-MPLS and Frame Relay services in South America (Santiago, Buenos Aires, San Paolo) and in the U.S.A. (Miami), whereas, in Europe, a new PoP MNCs was created in Athens.

Solutions for XDSL access services were also developed.

With regard to development of the transmission network, Telecom Italia Sparkle is participating in a consortium to create the new Sea-Me-We 4 submarine cable system which will connect the area of the Mediterranean to the Middle and Far East through 15 landing points including Marseilles, Palermo, Alexandria, Mumbai and Singapore, covering a distance of approximately 20,000 km and with a potential capacity of 1,300 Gbit/s. The system is scheduled to become operational in the second half of 2005.

■ MAJOR SUBSIDIARIES

P.A.thNet

Path. Net S.p.A.

Held by: Telecom Italia 100%

The company is responsible for the development and management of the Single Public Administration (R.U.P.A.) network.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|------|------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 136 | 117 | 16.2 |
| Gross operating profit | 12 | 10 | 20.0 |
| Operating income | 11 | 9 | 22.2 |

Activities during the year:

- Renewal of the RUPA Framework Contract until December 31, 2006
- Expansion of the very high profile broadband services plan at a flat rate.

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Loquendo S.p.A.

Held by: Telecom Italia 99.98%

The company is involved in the research, development and marketing of technologies, equipment and services for voice synthesis, voice recognition and/or voice interaction.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|------|------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 15 | 15 | - |
| Gross operating profit | 3 | 1 | ° |
| Operating income (loss) | 1 | (2) | ° |

Activities during the year:

- Expansion of foreign activities (with Spain, Germany, France, Greece, U.S.A., Canada, South America) and the non-captive market.
- Sale of the "Application" business segment (with effect from July 1, 2004) to Citec S.p.A. (a company specializing in the creation and development of integrated voice and data transmission systems). At the same time, an agreement was signed giving Citec the role of Master Distributor for Loquendo technologies on the Italian market.
- Further development of in-house technologies: so far, 16 languages have been developed, while, at the same time, the company has continued to implement different types of male and female voices (36 at year-end).



Telecontact Center S.p.A.

Held by: Telecom Italia 100%

The company conducts contact center activities and deals with the residential and business clientele of Telecom Italia S.p.A. who contact the "187" and "191" services.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|------|------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 42 | 13 | ° |
| Gross operating profit | 6 | 2 | ° |
| Operating income | 2 | 1 | ° |

Activities during the year:

- Within the framework of the reorganization of the Telecom Italia Group's Customer Care activities, the company acquired the following:
 - on February 4, 2004, as the result of a partial and proportional spin-off from Atesia S.p.A., two new sites at Catanzaro and Caltanissetta, now centers of operations for the "187" and "191" services;
 - on July 1, 2004, as a result of the sale for consideration by Atesia S.p.A., a new site in Rome, now a center of operations for the "187" service.
- Operation of the "191" service continued at the Naples offices.

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Gruppo BBNet

Held by: Telecom Italia International 98.78%

The group operates in the Dutch market providing local broadband access for ISP and business customers.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|------|------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 69 | 39 | 76.9 |
| Gross operating profit | 20 | 1 | ° |
| Operating income (loss) | 6 | (9) | ° |

Activities during the year:

- Completion of development activities of the network and the OSS platform;
- Connection of 329 co-locations to the network of the national operator KPN;
- Marked growth in numbers of customers acquired: 172 thousand by the end of 2004, an increase of 146% compared to the prior year;
- Enhancement of the services portfolio with the launch of Voice over DSL, geared to the SME clientele segment.



Latin American Nautilus Group

Held by: Telecom Italia 100%

The group ensures the transport of traffic and the supply of transmission capacity for wholesale customers in Latin America.

The table shows the key economic highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of USD) | 2003 (millions of USD) | Change in USD % |
|----------------------------|----------------------------|----------------------------|---------------------------|---------------------------|-----------------|
| Sales and service revenues | 25 | 40 | 31 | 46 | (32.6) |
| Gross operating profit | 5 | 4 | 7 | 5 | 40.0 |
| Operating loss | (5) | (13) | (7) | (15) | 53.3 |

Activities during the year:

- Extension of the customer base in the areas under its control and, in particular, consolidation of its presence in Venezuela
- Development and consolidation of the range of IP services in Latin America in synergy with TI Sparkle
- Launch of a plan to reduce operating costs (mainly general and administrative and network costs through renegotiation of contracts with the company's main suppliers).

Mediterranean Nautilus Group

Held by: Telecom Italia 62.51%, Telecom Italia International 7.49%

The group ensures the transport of traffic and the supply of transmission capacity to wholesale customers in the Eastern Mediterranean. The group includes the following companies:

Mediterranean Nautilus S.A., Elettra Tlc S.p.A. and the Mediterranean Nautilus Ltd. group.

The table shows the key economic highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of USD) | 2003 (millions of USD) | Change in USD % |
|----------------------------|----------------------------|----------------------------|---------------------------|---------------------------|-----------------|
| Sales and service revenues | 62 | 63 | 77 | 71 | 8.5 |
| Gross operating profit | 21 | 22 | 26 | 25 | 4.0 |
| Operating loss | (33) | (29) | (41) | (33) | (24.2) |

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Activities during the year:

- On the commercial front, positioning on the Israeli market was consolidated with the finalization of some important contracts
- Continuation of the debt restructuring phase by rescheduling repayments falling due, whereas, on the internal front, the company made particular efforts to reduce operating costs
- Renewal of the MECMA (Mediterranean Cable Maintenance Agreement) contract and extension of cable-laying and survey operations to the power and oil and gas sectors.



Med-1 Group

Held by: Telecom Italia 23.17%, Telecom Italia International 27.83%

The group ensures the operation of the LEV-1 cable (Italy - Cyprus - Israel) and the IC1 domestic Israeli network.

The table shows the key economic highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of USD) | 2003 (millions of USD) | Change in USD % |
|----------------------------|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 15 | 17 | 18 | 20 | (10.0) |
| Gross operating profit | 11 | 11 | 14 | 12 | 16.7 |
| Operating income | 5 | 4 | 6 | 4 | 50.0 |

Activities during the year:

- Supply of maintenance services to the LEV-1 cable customers, operation of the Israeli IC1 domestic network and supply of carrier and connectivity services.



HanseNet Telekommunikation GmbH

Held by: Telecom Italia 100% through Telecom Italia Deutschland Holding GmbH

The company operates in the market of Broadband telecommunications (access developed mainly using local loop unbundling and VAS services) in the Hamburg area.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|------|------|---------------|
| (millions of euro) | | | |
| Sales and service revenues | 161 | 102 | 57.8 |
| Gross operating profit | 35 | 18 | 94.4 |
| Operating loss | (10) | (24) | 58.3 |

Activities during the year:

- Continuation of the development of plans and packages for the residential and business clientele in the Hamburg area
- by December 31, 2004, customers numbered 240 thousand (compared to 105 thousand at the end of the prior year).

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Telecom Italia Sparkle Group

Held by: Telecom Italia 100%

The Group operates in the market for Voice, Data Transmission and Internet Protocol services.

The table shows the key economic highlights:

| | 2004 | 2003 | Change (%) |
|----------------------------|-------|-------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 1,838 | 1,671 | 10.0 |
| Gross operating profit | 285 | 296 | (3.7) |
| Operating income | 130 | 144 | (9.7) |

Activities during the year:

The Group continued to develop the International Wholesale business, where it is ranked one of the best in its class in the world. The trend in results was affected by the start-up of Telecom Italia France launched at the end of 2003.

In particular, activities during 2004 included:

- Creation of new interconnections with carriers to augment business opportunities with a particular focus on the VoIP service;
- With reference to IP services, backbone development activities continued by increasing European transmission capacity and the trans-Atlantic band; in the U.S.A. approximately 6 Gbit/s of new peerings were created for the NAPs of Newark (NJ), Palo Alto, Miami and Ashburn;
- Improvement in the efficiency of traffic delivery with continuous efforts to optimize costs;
- The creation of new PoPs in Hamburg for synergies with Hansenet, and in Cairo to support the development of IP and Data transmission business in the Mediterranean area. In South America, the "Golden Ring" project was completed, in collaboration with LAN, with the creation of IP PoPs in Santiago, Buenos Aires, Lima and San Paolo.

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MOBILE

- ▶ Growth of consolidated revenues and margins, driven by the strong expansion of Brazil and by confirmation of the growth of the domestic business market
- ▶ Continuation of the corporate streamlining process

■ THE BUSINESS UNIT

The Mobile Business Unit (TIM group) operates in the sector of national and international mobile telecommunications. Its international presence is concentrated in South America and in the Mediterranean Basin.

■ THE STRUCTURE OF THE BUSINESS UNIT

The Business Unit is organized as follows:



■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

The following transactions took place during 2004:

- on February 3, 2004, Stet Hellas announced the change of the brand Stet Hellas (now TIM Hellas) from Telestet to TIM. The change was made to reinforce the company's image by using a brand internationally recognized for know-how, technological expertise and a high level of service;
- February 19, 2004 marked the date of the completion of the merger of Is TIM, the mobile operator owned by TIM International (49%) and the Is Bank group (51%), and Aycell, the GSM operator entirely owned by Turk Telecom, Turkey's state-owned wireline operator. The new company resulting from the merger (Avea) is held 40% by TIM International, 40% by Turk Telekom and the remaining 20% by the Is Bank group. The net financial position of Is TIM at the time of the transaction was a borrowings position of USD 1.3 billion and reflected the conversion to share capital of all the loans and advances against future increases in capital received from the shareholders (about USD 2.3 billion).

Furthermore, as presented in the 2002 and 2003 financial statements, the carrying value of the investment in Is TIM and the advances against future increases in capital showed a nil balance. The 2004 financial statements still include, in reference to Avea, reserves for risks and charges of euro 548 million to cover the risks connected with the counter guarantees issued in the interests of Is TIM, now Avea.

At December 31, 2004, the carrying value of the investment in the affiliated company Avea has been maintained at a nil balance, partly in view of the indications contained in International Accounting Standards (IAS 31 and its interpretation) which require that, in the event of the contribution of non-monetary assets to a joint venture, the transaction should be accounted for at the pre-existing carrying values. Furthermore, the TIM group is committed, for the period 2004/2006, to subscribe to capital increases up to a maximum of USD 150 million and issue guarantees to financial entities for a maximum amount of USD 150 million;

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- on March 1, 2004, under the Group's program for information technology, TIM contributed a business segment which develops and maintains software applications in the SAP environment to the company Shared Service Center, a limited liability consortium company, purchasing a 4.55% stake. The value of the business segment was determined at approx. euro 65 thousand by an expert appointed by the Milan Courts;
- on March 31, 2004, under the plan for the reorganization of the Information Technology area of the Telecom Italia Group, TIM purchased, effective on April 1, 2004, the software design and development activities previously carried out by a specialized team of IT Telecom resources. The business segment that was purchased carries out activities that IT Telecom currently provides to TIM in the areas of:
 - innovative services, based on new platforms and IP networks (such as services for e-business or web services) directed at the business and mass-market segments;
 - telecommunications software development and maintenance activities.
 These activities will be integrated with the resources that today already operate in IT development at TIM, making it possible to improve the synergies for the management of the current platforms and the development of their evolution. The sales price, based also upon an external valuation drawn up by Milestone Advisory House S.p.A. in Milan, was agreed between the parties at euro 23 million. 551 resources were transferred to TIM as of April 1, 2004;
- July 1, 2004 marked the date of the execution of the settlement agreements signed in April between TIM International and the then minority shareholders of the Venezuelan subsidiary, Digitel, with the consequent purchase, by TIM International, of shares representing 32.88% of share capital USD 109.6 million. The execution of the agreement brings an end to the dispute with these shareholders that began at the beginning of last year. The closing took place after verification of the contractual conditions put into place to protect TIM International and Digitel. Therefore, as from date July 1, 2004, TIM, through TIM International, holds 100% of the shares of the Venezuelan mobile operator. Moreover, on July 2, 2004, the Digitel Shareholders' Meeting passed a resolution to absorb the losses for the years 2002 and 2003 and TIM International covered the losses by conferring the existing loans receivable from this same company for an amount including interest of USD 58.8 million. In November, moreover, an agreement was signed with CANTV (Compañía Anónima Nacional Teléfonos de Venezuela) for the sale of 100% of the share capital of the company. The total value of the transaction is equal to USD 450 million, from which the net financial position will be deducted when the transaction is executed.

Execution of the agreement, presumably scheduled to take place in the first half of 2005, is subject to the signing of the final agreements and obtaining the necessary authorizations from the pertinent Venezuelan authorities. Since CANTV is a regional operator, TIM decided to accept its offer for the purchase of the investment so that it can focus on initiatives where it has national coverage;
- on July 19, 2004, the Boards of Directors of Tele Celular Sul Participações and Tele Nordeste Celular Participações approved the plan for the merger of Tele Nordeste Celular Participações in Tele Celular Sul Participações. On August 19, and August 30, 2004, Tele Nordeste Celular Participações and Tele Celular Participações, respectively, held their Extraordinary General Shareholders' Meetings which approved the above merger. At the same time, Tele Celular Sul Participações changed its company name to TIM Participações S.A.. At the conclusion of this transaction, TIM, through TIM Brasil, holds 23.73% of the capital of TIM Participações. This operation follows the merger of five operating companies of the Tele Nordeste Celular Participações Group in the subsidiary Telpe Celular (now named TIM Nordeste Telecomunicações S.A.) executed in January which, also in this case, made it possible to simplify the corporate structure of the Group and achieve greater efficiencies in cost management;
- as part of the process to simplify the corporate structure of the Group, TIM International contributed its investment in Maxitel to TIM Brasil in September; in October 2004, TIM Brasil contributed the same investment in Maxitel to TIM Celular.

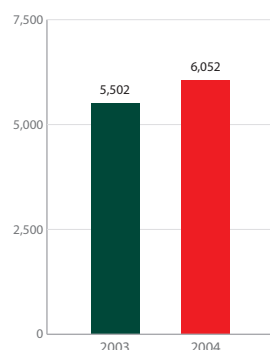
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■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003.

| | 2004 | 2003 | Change amount | % |
|--|--------|--------|------------------|------|
| (millions of euro) | | | | |
| Sales and service revenues | 12,900 | 11,782 | 1,118 | 9.5 |
| Gross operating profit | 6,052 | 5,502 | 550 | 10.0 |
| % of revenues | 46.9 | 46.7 | | |
| Operating income pre-amortization of differences on consolidation | 4,166 | 3,885 | 281 | 7.2 |
| Operating income | 4,073 | 3,786 | 287 | 7.6 |
| % of revenues | 31.6 | 32.1 | | |
| Investments: | | | | |
| - industrial | 2,490 | 1,957 | 533 | 27.2 |
| - differences on consolidation | 95 | 7 | 88 | ° |
| Employees at year-end (number) | 20,361 | 18,888 | 1,473 | 7.8 |

Gross operating profit



Sales and service revenues for the year 2004 amounted to euro 12,900 million, with an increase of 9.5% compared to 2003. Excluding the negative foreign exchange effect, revenues grew by euro 1,268 million (+10.9%). The growth is principally due to the good performance of the domestic market (+5%) and the positive contribution made by the Brazilian activities (+49.9% at a comparable exchange rate).

Gross operating profit in 2004 was euro 6,052 million and increased by 10% compared to 2003 (euro 5,502 million). Excluding the foreign exchange effect, the increase was 10.7%. Gross operating profit as a percentage of total revenues was 46.9% (46.7% in 2003).

Operating income in 2004 was euro 4,073 million and showed an increase of 7.6% compared to 2003 (euro 3,786 million). Operating income as a percentage of total revenues was 31.6% (32.1% in 2003). Beginning January 2004, considering that TIM's UMTS service was already in operation and being used by a pool of test users, the amortization process was started for the relative license. This license had already previously been amortized (beginning from January 2002) exclusively in the TIM S.p.A. statutory financial statements so as not to compromise the benefit of the tax deductibility of the amortization charge. The increase in consolidated operating income in 2004 was thus influenced by the consequent higher amortization charge of euro 134 million.

Industrial investments amounted to euro 2,490 million, of which euro 869 million referred to intangible assets and euro 1,621 million to fixed assets. Investments were designated for technological development and expansion of the network.

The number of *employees*, equal to 20,361, increased by 1,473 compared to December 31, 2003. This increase was due principally to the acquisition of the IT Telecom business segment by TIM S.p.A. and to the increase of employees in Brazil.

* * *

For a description of operating activities, reference should be made to the comments relating to TIM and the individual consolidated companies.

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■ TELECOM ITALIA MOBILE S.p.A.

Held by: Telecom Italia 55.08%, Telecom Italia Finance 0.17%

The table shows the key economic data:

| | 2004 | 2003 | Change amount | % |
|----------------------------|-------|-------|------------------|-----|
| (millions of euro) | | | | |
| Sales and service revenues | 9,943 | 9,469 | 474 | 5.0 |
| Gross operating profit | 5,347 | 5,035 | 312 | 6.2 |
| Operating income | 4,147 | 3,863 | 284 | 7.4 |

Sales and service revenues increased by 5% in 2004, reaching euro 9,943 million (euro 9,469 million in 2003). Traffic revenues, for a total of euro 7,193 million, grew by 1.3%. Revenues from Value-Added Services (which represent 13.4% of revenues from services) amounted to euro 1,256 million, an increase of 22.2% compared to 2003.

Gross operating profit in 2004 amounted to euro 5,347 million, a growth of 6.2% compared to euro 5,035 million in 2003.

Operating income in 2004, equal to euro 4,147 million (euro 3,863 million in 2003), increased by 7.4%.

The main operating highlights at December 31, 2004 compared to December 31, 2003 are reported below, in addition to the principal activities carried out each pertinent sector:

| Operating highlights | 12/31/2004 | 12/31/2003 |
|--------------------------------------|------------|------------|
| TIM lines in Italy (thousands) | 26,259 | 26,076 |
| Mobile traffic (millions of minutes) | 41,225 | 38,420 |
| ARPU (euro/line/month) | 29.0 | 28.2 |

In 2004, TIM stepped up its development of innovative services with the aim of augmenting customer loyalty and increasing opportunities for using mobile phones. The most significant initiatives were:

| | |
|--------------------------------|--|
| Launch of "S.O.S. Ricarica" | The service allows customers to make calls even with zero credit when it is not possible to recharge the phone immediately, by calling the free number 4916, which grants euro 2 credit for immediate use. The next time the phone is recharged, euro 3 is deducted from the total (inclusive of the euro 1 charge to cover the administrative costs of the service). |
| Launch of "MAXXI TIM Messaggi" | The package, directed at prepaid customers, for the sum of euro 10, allows users to send 400 SMS and 100 MMS within 30 days. The offer is automatically renewed for another 30 days if the remaining credit is at least euro 13. |
| Agreement with "3" | The agreement signed with "3" extends the sphere of commercial collaboration and redefines agreements with regard to roaming, sharing sites and interconnection. The agreement also establishes the sharing of the broadcasting rights, via cell phones, of sporting events involving the Serie A TIM and Serie B TIM football teams, owned by the two operators. |
| Launch of "MAXXI TIM Parole" | This is a plan allowing customers to acquire large packages of minutes at highly advantageous prices continuously throughout the year, and the option of choosing the solution best suited to their needs from the many combinations available. |
| Launch of EDGE and "TIM TURBO" | With effect from April, TIM (the first company to do so in Italy) launched EDGE, the Broadband mobile network for high-speed data transmission, a service which complements the UMTS service. TIM customers will be able to use the new line of dual mode "TIM TURBO" phones which can use both the EDGE and UMTS networks, allowing the highest-quality services. At the end of May, TIM launched a new line of third-generation services, marking the commercial launch of the combined Edge-UMTS network for TIM customers. In November, the first dual mode EDGE/UMTS handset was presented to the Italian market. |

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| Launch of the FreeMove brand | On March 29, 2004 the members of the Alliance (Orange, Telefonica Moviles, TIM and T-Mobile) presented the new brand FreeMove, illustrating the first tangible results of the Alliance. These include the conclusion of preferential supply agreements with Siemens and Motorola and the joint acquisition of 6 million handsets for 2004, with an average reduction in cost of 10%. November saw the launch of the FreeMove Alliance, a new, simple and easy-to-calculate rate plan for multinational companies, regardless which network the phone is connected to, with no fixed costs, regardless of use, with a simple system based on geographical subdivisions. |
| Open Mobile Terminal Platform | TIM and other major mobile telephone operators (mm02, NTT DoCoMo, Orange, SMART Communications, Telefonica Moviles, T-Mobile and Vodafone) founded the Open Mobile Terminal Platform (OMTP) association, with the aim of promoting various projects in relation to the creation of a new open reference framework for manufacturers of mobile terminals and suppliers of associated hardware and software. The aim is to develop the Open Mobile Terminal Platform, that is, standard open interfaces which ensure that users have a more effective, broader "user experience" when using different handsets. At the same time, this will enable individual operators and suppliers to differentiate and customize their offering. During the year, many other operators joined the initiative, such as Amena, Hutchinson 3G, KPN, SFR Cegetel and Telenor. |
| Protocol agreement for the online conciliation procedure | On July 23, 2004, TIM and the leading Italian Consumer Associations signed the Protocol Agreement for the online conciliation procedure regarding the settlement of disputes between the company and its customers. The Protocol is representative of the continuity of the commitments made in previous agreements between the company and the consumer associations. |
| Healthcare Information Services via SMS | Health Telematic Network (HTN), a leading company in the field of remote healthcare services, and TIM, have launched the first services for healthcare information on the Italian market to be dispensed via mobile phones. |
| Launch of "Talks" | This revolutionary software enables the blind, the partially sighted and the elderly to use all the functions of a mobile phone and be completely independent, thanks to an electronic voice which reads the display to the user. Blind persons will now be able to read and write SMS and e-mails, compose and download multimedia messages (MMS), call and edit a number in the memory, change the way the phone is used and modify other settings, organize the engagements diary, and write and read text documents. |
| Launch of the "video sharing" service | In collaboration with Nokia, this multimedia service enables customers to introduce visual elements to telephone conversations. |

■ ECONOMIC AND FINANCIAL DATA FOR MOBILE OPERATIONS IN SOUTH AMERICA

The key highlights of the Mobile Business Unit operations in Latin America are presented in the following table.

| Gross operating profit | 2004 | 2003 | Change | |
|--|--------------------|--------|--------|-------|
| | (millions of euro) | | amount | % |
| Sales and service revenues | 2,157 | 1,547 | 610 | 39.4 |
| Gross operating profit | 447 | 196 | 251 | 128.1 |
| % of revenues | 20.7 | 12.7 | | |
| Operating income (loss) pre-amortization of differences on consolidation | (91) | (237) | 146 | 61.6 |
| Operating income (loss) | (102) | (248) | 146 | 58.9 |
| % of revenues | (4.7) | (16.0) | | |
| Investments: | | | | |
| - industrial | 880 | 641 | 239 | 37.3 |
| Employees at year-end (number) | 8,447 | 7,502 | 945 | 12.6 |

In 2004, the operations of the Mobile Business Unit in Latin America generated *revenues* of euro 2,157 million, an increase of 39.4% compared to 2003, despite the impact of the negative foreign exchange effect. Excluding the foreign exchange effect, *revenues* increased by approx. euro 760 million.

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Gross operating profit amounted to 447 million with an increase of euro 251 million compared to 2003. Excluding the foreign exchange effect, gross operating profit rose by approx. euro 287 million, thanks to a better performance by the start-up activities in Brazil (GSM). The *operating result* was a loss of euro 102 million and was impacted by higher amortization and depreciation associated with investments to develop technical and services infrastructures, particularly for the GSM networks in Brazil. *Industrial investments* amounted to euro 880 million, of which euro 146 million referred to intangible assets and euro 734 million to fixed assets. The number of employees grew by 945 compared to December 31, 2003, mainly as a result of increases recorded by Brazilian activities in the start-up phase.

■ MAJOR SUBSIDIARIES

■ Europe



TIM Hellas

TIM Hellas Held by: TIM International N.V. 80.74%, TI Finance 0.13%

The company operates the GSM service in Greece.

The table shows the main economic and operating data:

| (millions of euro) | 2004 | 2003 | Change (%) |
|---|-------|-------|------------|
| Sales and service revenues | 838 | 805 | 4.1 |
| Gross operating profit | 264 | 287 | (8.0) |
| Operating income | 127 | 166 | (23.5) |
| Number of lines at year-end (thousands) | 2,324 | 2,403 | (3.3) |

Activities during the year:

- on January 27, 2004 TIM Hellas was the first company in Greece to debut in the new era of mobile telephone services with the launch of the UMTS service, thus reconfirming its aim to position the company at the forefront in terms of technological leadership and rate plans;
- on April 6, 2004 TIM Hellas offered an innovative service called "2 in 1" which gives subscribers the option of using 2 mobile telephone numbers with a single SIM Card;
- on July 20, 2004, TIM Hellas announced the launch of two new hi-tech services: "TIM Mobile TV", an innovative service offering customers the possibility of seeing TV channels on their mobile handsets, and "TIM Twin Card", another service which is again the only one of its kind on the Greek market, enabling customers to have 2 SIM cards with the same number;
- on November 11, 2004, TIM Hellas offered a new SIM card, permitting all of its customers to access an integrated portfolio of information, entertainment and communication services which are fast and user-friendly. The new TIM SIM card is the only one on the Greek market with a memory capacity of 128K, through which customers can access 58 value-added services based on SMS, MMS, Voice Recognition and video technologies, and also customize their menu by adding up to 10 new services;
- on December 6, 2004 TIM Hellas offered its customers the new "TIM Click" service which makes it possible to transform MMS into photos and postcards to send to friends.

■ Latin America



TIM Participações S.A. Group

Held by: TIM Brasil Serviços e Participações S.A. 23.73%

In 2004, the Tele Celular Sul Participações Group merged the Tele Nordeste Celular Participações Group and changed the company name to TIM Participações. The figures of the two pre-existing groups have been aggregated, for purposes of comparison. The Group operates mobile network

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services based on TDMA and GSM technology in the north-east of Brazil (States of Piauí, Ceará, Rio Grande do Norte, Paraíba, Pernambuco and Alagoas) through the operator TIM Nordeste Telecomunicações and in the south of Brazil (States of Paraná, Santa Catarina and the town of Pelotas), through the operator TIM Sul.

The new company is one of the three leading mobile telephone companies listed on the Brazilian stock market in terms of capitalization. Since October 11, 2004, TIM Participações is listed on the BOVESPA and since October 15, 2004 on the NYSE.

The following table gives the main economic and operating data:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of BRL) | 2003 (millions of BRL) | Change in BRL % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 744 | 657 | 2,706 | 2,281 | 18.6 |
| Gross operating profit | 316 | 286 | 1,150 | 995 | 15.6 |
| Operating income | 163 | 151 | 594 | 524 | 13.4 |
| Number of lines at year-end (thousands) | | | 5,657 | 4,229 | 33.8 |

Activities during the year:

- launch of new VAS services, such as Tons, Image and Video, "TIM Click", "TIM Fotomensagem" and "TIM Videomensagem";
- launch of "Business Control", a prepaid plan which enables Corporate customers to monitor the costs of calls made by employees using mobile phone services;
- strengthening and development of partnerships with numerous dealers;
- launch of commercial plans aimed at migration from TDMA to GSM technology;
- expansion of the GSM network which has reached the same level of coverage as the TDMA network;
- offering of long-distance services;
- implementation of Number portability to speed up migration from TDMA to GSM;
- launch of "GSM broadband" which makes it possible to create a mobile office with benefits in terms of data connection (e-mail, access to corporate applications, etc.).



Maxitel S.A.

Held by: TIM Celular S.A. 100%

The group operates mobile network services using TDMA and GSM technology in Brazil in the states of Minas Gerais, Bahia and Sergipe.

The table shows the main economic and operating data:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of BRL) | 2003 (millions of BRL) | Change in BRL % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 296 | 256 | 1,076 | 890 | 20.9 |
| Gross operating profit | 74 | 91 | 270 | 316 | (14.6) |
| Operating income (loss) | (7) | 18 | (26) | 62 | (141.9) |
| Number of lines at year-end (thousands) | | | 2,418 | 1,606 | 50.6 |

Activities during the year:

- intensification of retention and loyalty programs for high-profile customers;
- promotional packages for prepaid service customers;
- development of VAS services;
- offering of long-distance services;
- acquisition of a new 900 MHz license.

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TIM Celular S.A.

Held by: TIM Brasil Serviços e Participações S.A. 100%

The company operates mobile network services using GSM technology in the north, center and south (Rio Grande do Sul) of Brazil and in the states of San Paolo, Rio de Janeiro, Espirito Santo as well as in the Federal District.

The table shows the main economic and operating data:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of BRL) | 2003 (millions of BRL) | Change in BRL % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 784 | 362 | 2,854 | 1,258 | 126.9 |
| Gross operating loss | (32) | (240) | (115) | (833) | 86.2 |
| Operating loss | (250) | (368) | (912) | (1,278) | 28.6 |
| Number of lines at year-end (thousands) | | | 5,513 | 2,469 | 123.3 |

Activities during the year:

- launch of numerous marketing campaigns aimed at increasing the customer base;
- promotions focusing on the younger clientele, such as "TIM Cartoon" and "Super Troca TIM";
- launch of "TIM Light" and "Mega TIM" to develop the subscriber and prepaid clientele segments, respectively;
- development of VAS services.



TIM Perù S.A.C.

Held by: TIM International N.V. 100%

The company operates mobile telephone services in Perù.

The table shows the main economic and operating data:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of PEN) | 2003 (millions of PEN) | Change in PEN % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 165 | 128 | 701 | 502 | 39.6 |
| Gross operating profit | 37 | 6 | 156 | 26 | ° |
| Operating loss | (5) | (32) | (22) | (128) | 82.8 |
| Number of lines at year-end (thousands) | | | 1.102 | 623 | 76.9 |

Activities during the year:

- launch of new marketing campaigns and strengthening of the commercial network with the aim of reinforcing the company's position on the market;
- policies geared to augmenting the loyalty of high-profile customers;
- development of the GPRS service which enables customers to access WAP, WEB and data transmission services;
- commercial launch of Mobile TV in August;
- expansion of the coverage of EDGE in Lima.

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Corporacion Digitel C.A.

Held by: TIM International N.V. 100%

The company operates mobile telephone services in Venezuela.

The table shows the main economic and operating data:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of VEB) | 2003 (millions of VEB) | Change in VEB % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 174 | 148 | 453,786 | 298,681 | 51.9 |
| Gross operating profit | 54 | 45 | 141,599 | 90,207 | 57.0 |
| Operating income (loss) | 11 | (10) | 30,046 | (19,702) | ° |
| Number of lines at year-end (thousands) | | | 1,368 | 1,153 | 18.6 |

Activities during the year:

- introduction of innovative VAS services such as "TIM Click" and "TV Movil";
- launch of the "Controlame" service which warns customers when they reach a certain level of credit;
- implementation of new ways of electronically recharging phones using POSs, ATMs and the Internet.

■ AFFILIATED COMPANIES

■ Mediterranean Basin

Avea I.H.A.S.

Held by: TIM International N.V. 40%

The company operates mobile telephone services in Turkey. It is the company resulting from the merger between Is TIM and Aycell, which took place on February 19, 2004; 40% of the share capital is held by TIM International and Turk Telekom each and 20% by the Is Bank Group.

Activities during the year:

- during 2004, the performance of Avea focused on the launch of the newbrand, on new commercial initiatives and on improving the coverage of the service. The customer base reached 4.8 million compared to 4 million on the date of the merger with an increase of 20%; the commercial performance achieved its objectives of increasing and improving the quality of the customer base, by means of acquisition policies;
- on July 1, 2004, Avea announced the launch of the first three new rate plans under the AVEA brand name;
- on July 13, 2004, Avea offered its prepaid customers a new service called "Sharecounter" which permits them to recharge the credit of another AVEA customer by sending an SMS;
- in August, agreements were signed to sponsor Turkey's leading soccer teams: Fenerbahçe, Galatasaray and Trabzon;
- on August 24, 2004, the company was the first in the country to announce the launch of a new application geared to corporate customers which enables them to receive and send e-mails through a wireless connection using Blackberry;
- on September 22, 2004, Avea launched a special rate plan called "Okidoki" geared to students and the younger clientele;
- on November 4, 2004, Avea was the first company to introduce a new service called "Push-to-talk" that can link up several people in a conversation within a closed group of users;
- on December 14, 2004, Avea was the first company to introduce the "Ringa" service to the Turkish market, whereby customers can customize the call-wait ringtones.

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SOUTH AMERICA

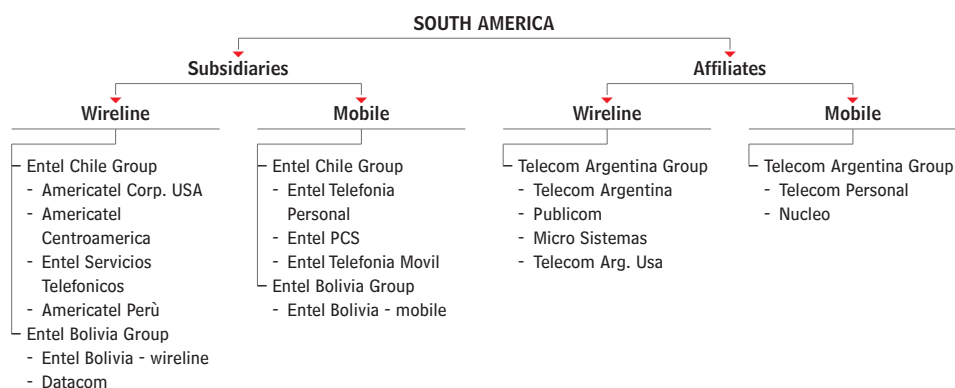
■ STRUCTURE

With effect from March 1, 2004, the former Latin America Operations structure has been disbanded and the Telecom Italia Latam structure took over the role of the “delocalized” Corporate function, in keeping with the strategic policies of the Group to consolidate and develop its presence in Latin America.

Paolo Dal Pino, effective March 1, 2004, was appointed the representative of the Telecom Italia Group in Latin America, reporting directly to the Chairman.

At the same time, the Wireline and Mobile Business Units, with no change in the corporate control structure, are responsible for the results of the subsidiaries in Latin America.

The Latin American structure is organized as follows:



■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

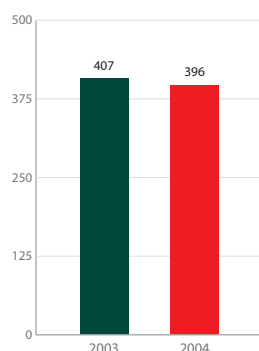
In 2004, the company Telecom Italia America Latina and the Argentine Branch of Telecom Italia have been deconsolidated from South America and are now part of the Corporate structure.

■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of the Entel Chile group and the Entel Bolivia group for 2004, compared to those of 2003, restated for purposes of comparison.

| | 2004 | 2003 | Change | |
|---|-------|-------|--------|--------|
| (millions of euro) | | | amount | % |
| Gross operating profit | | | | |
| Sales and service revenues | 1,076 | 1,111 | (35) | (3.2) |
| Gross operating profit | 396 | 407 | (11) | (2.7) |
| % of revenues | 36.8% | 36.6% | | |
| Operating income pre-amortization of differences on consolidation | 127 | 153 | (26) | (17.0) |
| Operating income | 121 | 145 | (24) | (16.6) |
| % of revenues | 11.2% | 13.1% | | |
| Investments: | | | | |
| - industrial | 157 | 129 | 28 | 21.7 |
| Employees at year-end (number) | 5,080 | 4,953 | 127 | 2.6 |

Gross operating profit



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Sales and service revenues amounted to euro 1,076 million, with a reduction of euro 35 million (– 3.2%) compared to 2003. The reduction can mainly be attributed to a contraction of the revenues of the Entel Chile group from long-distance wireline business in North America. Excluding the foreign exchange effect (+ euro 6 million, of which + euro 26 million refers to the CLP and – euro 20 million to the BOB), consolidated revenues showed a reduction of euro 41 million (Entel Chile group –euro 63 million, Entel Bolivia group +euro 21 million), equal to – 3.7% compared to 2003.

Gross operating profit in 2004, equal to euro 396 million, decreased by euro 11 million (– 2.7%) compared to the prior year (Entel Chile group – euro 10 million, Entel Bolivia group – euro 1 million). Gross operating profit represented 36.8% of sales (36.6% in 2003).

Operating income, equal to euro 121 million, decreased by euro 24 million (– 16.6%), compared to the prior year (Entel Chile group – euro 36 million, Entel Bolivia group +euro 12 million). Operating income represented 11.2% of revenues (13.1% in 2003).

Industrial investments of euro 157 million showed an increase of euro 28 million compared to 2003.

At December 31, 2004 *employees* numbered 5,080, an increase of 127 (+ 2.6%) compared to December 31, 2003. The increase can be attributed to a rise in the number of employees of the Entel Chile group.

The following table shows the key results of the wireline and mobile telephone businesses in 2004, compared to those of 2003.

| | 2004 | | | | 2003 | | | |
|---|----------|--------|-------------------|-------|----------|--------|-------------------|-------|
| | Wireline | Mobile | Elimina- tions | Total | Wireline | Mobile | Elimina- tions | Total |
| (millions of euro) | | | | | | | | |
| Sales and service revenues | 658 | 551 | (133) | 1,076 | 733 | 502 | (124) | 1,111 |
| Gross operating profit | 169 | 227 | | 396 | 183 | 224 | | 407 |
| % of revenues | 25.7% | 41.2% | | 36.8% | 25.0% | 44.6% | | 36.6% |
| Operating income (loss) pre-amortization of differences on consolidation | (9) | 136 | | 127 | 20 | 133 | | 153 |
| Operating income (loss) | (9) | 136 | (6) | 121 | 18 | 132 | (5) | 145 |
| % of revenues | (1.4%) | 24.7% | | 11.2% | 2.5% | 26.3% | | 13.1% |
| Investments: | | | | | | | | |
| - Industrial | 59 | 98 | | 157 | 73 | 56 | | 129 |
| Employees at year-end (number) | 3,166 | 1,914 | | 5,080 | 3,244 | 1,709 | | 4,953 |

■ EVENTS SUBSEQUENT TO DECEMBER 31, 2004

On January 24, 2005, Telecom Italia, through its subsidiary Telecom Italia International N.V., signed an agreement with Almendral S.A. (an investment holding company listed on the stock exchange in Santiago, Chile, which represents local businesses including the Hurtado Vicuna group and the Matte group) for the sale of its investment in the Chilean company Entel Chile S.A., equal to 54.76% of share capital. The sales price paid to Telecom Italia International amounts to USD 934 million.

Closing of the transaction, scheduled to take place within the next three months, is subject to receipt of the necessary authorizations from the pertinent authorities.

This transaction fall under the Telecom Italia Group's strategy to rationalize its international portfolio and focus on areas of strategic interest with growth potential.

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SUBSIDIARIES



Entel Chile Group

Held by: Telecom Italia International 54.76%

The group operates in the sectors of fixed and mobile telephone services, data transmission and Internet access services in Chile. The group's wireline business is focused on national and international long-distance service while its presence in the local domestic telephone segment is limited partly because it has not occupied a historical place as an operator in this market.

The table shows the key economic and operating highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of CLP) | 2003 (millions of CLP) | Change in CLP % |
|---|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 925 | 962 | 701,446 | 750,980 | (6.6) |
| Gross operating profit | 326 | 336 | 247,320 | 262,344 | (5.7) |
| Operating income | 98 | 134 | 74,525 | 104,289 | (28.5) |
| No. of fixed lines at year-end (thousands) | | | 99 | 103 | (3.9) |
| No. of mobile customers at year-end (thousands) | | | 3,265 | 2,684 | 21.6 |
| No. of Internet customers at year-end (thousands) | | | 225 | 250 | (10.0) |

The table shows the key results of the wireline and mobile businesses of the Entel Chile group in 2004 compared to those of 2003.

| | 2004 | | | | 2003 | | | |
|--------------------------------|----------------------------|--------------------------|-------------------|-------|----------------------------|--------------------------|-------------------|-------|
| | Entel Chile Wireline | Entel Chile Mobile | Elimi- nations | Total | Entel Chile Wireline | Entel Chile Mobile | Elimi- nations | Total |
| (millions of euro) | | | | | | | | |
| Sales and service revenues | 578 | 480 | (133) | 925 | 639 | 443 | (120) | 962 |
| Gross operating profit | 133 | 193 | | 326 | 141 | 195 | | 336 |
| % of revenues | 23.0% | 40.2% | | 35.2% | 22.1% | 44.0% | | 34.9% |
| Operating income (loss) | (14) | 118 | (6) | 98 | 15 | 124 | (5) | 134 |
| % of revenues | (2.4%) | 24.6% | | 10.6% | 2.3% | 28.0% | | 13.9% |
| Employees at year-end (number) | 2,573 | 1,643 | | 4,216 | 2,632 | 1,440 | | 4,072 |

Activities during the year in the wireline business:

- promotion of commercial Broadband packages based on competitive prices was stepped up with the launch of "Promoción Banda Ancha" (first month free of charge) in January and "Promoción Banda Ancha Full 128 kbs" for the residential market and "Super ADSL" (local telephone services bundling and ADSL Internet) for the business segment; doubling of the speed of all the packages;
- re-launch of voice services: "Promoción cobro revertido automático", "Autocontrol 500 minutos" and "Entelticket";
- sealing of the agreements to send SMSs via the Internet with mobile operators which cover the whole of the Chilean mobile market;
- important service integration projects were acquired with the Public Administration (MOP, "Ministerio de Obras Publicas" and FONASA, Chile's most important Social Security Department);
- the corporate reorganization of the subsidiary Americatel U.S.A. was begun.

Activities during the year in the mobile business:

- marketing began of VAS services based on EDGE technology;
- re-launch of the SMS roaming service for prepaid customers;
- launch of the "TV Móvil" service and the GPRS/MMS roaming service for all customers;
- GSM 1900 coverage for Easter Island. The company is the only one to offer this service.

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Entel Bolivia Group

Held by: Telecom Italia International through ICH/ETI 50%

The group operates in the sectors of wireline (particularly in the segment of long-distance national and international telephone services, as already mentioned for the Entel Chile group) and mobile telephone services, Internet, data transmission, telex and telegraphy services in Bolivia.

The table shows the key economic and operating highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of BOB) | 2003 (millions of BOB) | Change in BOB % |
|--|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 152 | 151 | 1,495 | 1,312 | 13.9 |
| Gross operating profit | 70 | 71 | 684 | 615 | 11.2 |
| Operating income | 23 | 11 | 225 | 97 | 132.0 |
| No. of fixed lines at 12/31 (thousands) | | | 50 | 49 | 2.0 |
| No. of mobile customers at 12/31 (thousands) | | | 1,146 | 783 | 46.4 |
| No. of Internet customers at 12/31 (thousands) | | | 18 | 15 | 20.0 |

The following table shows the key results of the wireline (*) and mobile businesses of the Entel Bolivia Group in 2004 and those of 2003:

(*) Includes the results of Datacom S.A.

| | 2004 | | | 2003 | | | |
|--------------------------------|-------------------------------|----------------------------|-------------------|-------|-------------------------------|----------------------------|-------------------|
| (millions of euro) | Entel Bolivia Wireline* | Entel Bolivia Mobile | Elimi- nations | Total | Entel Bolivia Wireline* | Entel Bolivia Mobile | Elimi- nations |
| Sales and service revenues | 81 | 71 | | 152 | 93 | 58 | 151 |
| Gross operating profit | 36 | 34 | | 70 | 43 | 28 | 71 |
| % of revenues | 44.4% | 47.9% | | 46.1% | 46.2% | 48.3% | 47.0% |
| Operating income | 5 | 18 | | 23 | 3 | 8 | 11 |
| % of revenues | 6.2% | 25.4% | | 15.1% | 3.2% | 13.8% | 7.3% |
| Employees at year-end (number) | 593 | 271 | | 864 | 612 | 269 | 881 |

Activities during the year in the wireline business:

- consolidation of the Wi-Fi service in Bolivia's three largest cities (La Paz, Santa Cruz and Cochabamba);
- a dynamic commercial boost was given to sales of telephone services through price reviews, the re-launch of the prepaid "UNICA" card and the launch of the new product "Aquí Entel-Telefonía Pública".

Activities during the year in the mobile business:

- the company's position as absolute market leader was confirmed with a market share of 67% at the end of 2004;
- launch of the GPRS and SMS services;
- extension of GSM network coverage;
- international roaming agreements with more than 100 operators in the five continents.

Corporate reorganization was begun with the aim of achieving a greater level of integration of fixed-mobile activities, replacing the present structure of business units, and concentrating greater emphasis on customer care.

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■ AFFILIATED COMPANIES

Telecom Argentina Group

Held by: Telecom Italia and Telecom Italia International through Nortel

Inversora/Sofora 13.97%

The group operates in the sector of fixed and mobile telephone services, data transmission and Internet access services in Argentina.

The table shows the key economic and operating highlights:

| | 2004 (millions of euro) | 2003 (millions of euro) | 2004 (millions of ARS) | 2003 (millions of ARS) | Change in ARS % |
|--|-------------------------------|-------------------------------|------------------------------|------------------------------|-----------------------|
| Sales and service revenues | 1,228 | 1,123 | 4,495 | 3,746 | 20.0 |
| Gross operating profit | 628 | 665 | 2,297 | 2,218 | 3.6 |
| Operating income | 177 | 84 | 648 | 281 | 130.6 |
| No. of fixed lines at 12/31 (thousands) | | | 3,484 | 3,361 | 3.7 |
| No. of mobile customers at 12/31 (thousands) | | | 4,338 | 3,130 | 38.6 |
| No. of Internet customers at 12/31 (thousands) | | | 233 | 200 | 16.5 |

On the operations front, in a macroeconomic scenario that was still dogged by uncertainty and frozen wireline telephone rates, the group continued the policy of optimizing costs and investments and, at the same time, exploited the growth opportunities emerging in the mobile telephone services sector. The measures implemented made it possible to achieve a 51% gross operating margin.

By the year-end, the company reported a significant increase in revenues, to which the following achievements in the wireline business contributed:

in the wireline business:

- launch of semi-flat rate plans for national long-distance services which made it possible to maintain market share and improve the ARPU;
- new packages for Internet services (doubling the speed of ADSL at no extra charge and the launch of "Arnet HW Surf");
- commercial launch of the Wi-Fi package;
- extension of the Broadband customer base;

in the mobile business:

- development of the range of innovative services: EDGE, national and international roaming for data, multiplayer games, "Personal Click", "Me Llamás?", "TV Personal", "Quién Llamó";
- new packages for prepaid customers: "Recarga Delivery" (enables customers to transfer credit from a subscriber) and "Recarga SOS" (enables customers to recharge without credit);
- reorganization of the indirect sales channel and redefinition of market segments based on customers' economic value;
- positive evolution of GSM and the start of retention programs for top customers with replacement of terminals (from TDMA to GSM);
- commercial launch of GSM in Paraguay through the subsidiary Núcleo S.A.

On June 22, 2004, Telecom Argentina S.A. launched an appeal to obtain proxies from among its creditors for the approval and signing of an Acuerdo Preventivo Extrajudicial ("APE"), regulated by Argentine law, which is a necessary part of the process to restructure the company's financial debt.

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On July 2, 2004, Telecom Personal, a subsidiary of Telecom Argentina presented its creditors with a proposal to restructure its debt, similar to the conditions adopted by the parent company.

On August 6, 2004, Telecom Argentina concluded its appeal to obtain proxies from among its creditors necessary for the approval and signing of an Acuerdo Preventivo Extrajudicial ("APE") which will allow the company to restructure its debt (appeal launched June 22, 2004).

94.4% of the creditors expressed their agreement with the proposal for the restructuring of the debt put forward by the company. The percentage thus exceeded the legal threshold of consent (67%), allowing the company to proceed with its debt restructuring.

On August 23, 2004, Telecom Argentina S.A. announced that 94.4% of the creditors had answered the appeal.

On October 21, 2004, the APE was presented for legal approval in Argentina and the company expects to bring the restructuring to completion by carrying out the exchange with new securities during the first half of 2005.

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INTERNET AND MEDIA

- ▶ **TIN.IT:** one of Italy's top WI-FI networks with 730 hot spots, 603 of which are active;
- ▶ **Virgilio:** its position as the leading Italian portal is confirmed with 14.3 million individual visitors and 7.9 billion page views;
- ▶ **La7:** audience share in December 2004 at 2.6% (2.2% in December 2003);
- ▶ **MTV:** market share up by 17% 2.1% in 2004 compared to 1.8% in 2003;
- ▶ **Office Products:** positive inversion of the trend with improved profitability (gross operating profit at +45%).

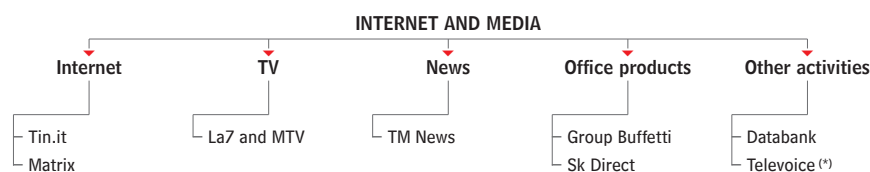
■ LA BUSINESS UNIT

The Internet and Media Business Unit operates in the following segments:

- Internet: in the management of access services (ISP) with Tin.it, in the management and development of the Virgilio portals with Matrix, and in web services, where it occupies a leadership position in the Italian market;
- Television: with La7 and MTV, in the production and broadcasting of editorial content through the television transmission networks entrusted under concession and in the marketing of advertising space in TV programming; in September, La7 Televisioni S.p.A. acquired the rights to broadcast the home matches of eight Serie A soccer teams using digital terrestrial technology;
- Office Products and Services: in the distribution of products, services and solutions for the office through the Buffetti retail network.

■ THE STRUCTURE OF THE BUSINESS UNIT

The Business Unit is organized as follows (the main consolidated companies/business areas are shown below):



(*) On December 16, 2004, Telecom Italia Media signed an agreement with Comdata (Altair Group) for the sale of 100% of Televoice S.p.A., a company which operates in the call center and telemarketing and teleselling sector. The transaction will be finalized on January 3, 2005.

■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

The following transactions took place during 2004:

- on January 29, 2004, as part of the process of rationalizing the business portfolio, the 60% investment in CIPI S.p.A. was sold to Promoinvestments S.r.l. for euro 6.5 million;
- on February 3, 2004, the City of Pesaro and La7 Televisioni S.p.A. signed a memorandum of understanding for the experimentation of digital terrestrial television (DTT) directed to the development and broadcasting of publicly-useful interactive services for the City of Pesaro;

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- on February 11, 2004, Telecom Italia Media S.p.A., Sun Microsystems Italia, a leader in network systems, and CSP Innovation in ICT (Centro per la ricerca e la sperimentazione di tecnologie informatiche e telematiche avanzate) signed an agreement for the experimentation of innovative services for digital terrestrial television in the Province of Turin;
- on June 15, 2004, as part of the rationalization of its business portfolio, the 100% investment in GPP Group was sold to Wise Venture Sgr for euro 10.5 million;
- on June 28, 2004, Telecom Italia Media reached an agreement with the De Agostini Group for the settlement of the dispute, under arbitration, relating to the contract signed on September 20, 2000 which covered, among other things, the purchase of the 40% holding in Finanziaria Webfin (which holds a 66% stake in Matrix, owner of the Virgilio portal).
The economic and balance sheet effects of this transaction, which were illustrated in the first-half report 2004, consist of a loss, net of the tax effect, of euro 130 million for Telecom Italia Media S.p.A.. The net loss on consolidation was euro 189 million and the net financial outlay was equal to 282 million.
As a result of this transaction and in order to bring its capital and financial situation back into equilibrium, Telecom Italia Media carried out a share capital increase, approved by the Shareholders' Meeting held on September 10, 2004, for a gross amount of euro 120 million. This capital increase was entirely subscribed to and led to the issue of 573,796,619 shares of par value euro 0.03 each, equal to 15.49% of new share capital, of which 564,333,957 were ordinary shares at a price of euro 0.21 each and 9,462,662 savings shares at a price of euro 0.17 each.
Consequently, the new share capital of Telecom Italia Media S.p.A. at December 31, 2004 amounts to euro 111,107,893.71 and consists of 3,642,519,221 ordinary shares and 61,077,236 savings shares of par value euro 0.03 each;
- on September 1, 2004, La7 Televisioni S.p.A. conferred the business relating to the technical services of TV signal broadcasting to its subsidiary Telecom Italia Media Broadcasting S.r.l.. This transaction is in line with the provisions of Law 66/01 and the National Regulatory Agency Resolution 435/01/CONS, which provides that the party which intends to ask for a license as a "Network Operator" must be a separate company from the content operator;
- under the projects for the development of digital terrestrial television, La7 Televisioni S.p.A. purchased in September 2004 the rights to "pay TV" for soccer games with Bologna, Palermo, Cagliari, Reggina, Fiorentina, Lecce, Chievo, Brescia and Parma. The total amount of the deal was approx. euro 32 million for the three years 2004-2005, 2005-2006 and 2006-2007. The service began on January 22, 2005 in conjunction with the start of the second round games. The service calls for the purchase of a rechargeable smart card and the sale of pay-per-view events without a subscription fee;
- on October 11, 2004, the Board of Directors of the companies Gruppo Buffetti S.p.A. and PBS S.r.l. voted to merge the latter in the first company.

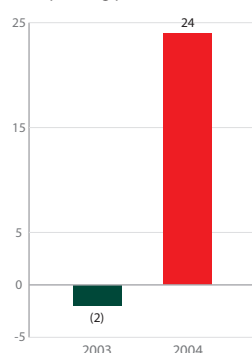
■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003. The figures for 2003 are presented as "Historical" values, "Restated total" figures determined by highlighting the income components typical of the Telecom Italia Media Group post-merger and "restated figures on a comparable consolidation basis" which exclude the change in the scope of consolidation in both 2004 and 2003. All percentages are calculated on the basis of data expressed in thousands of euro.

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TELECOM ITALIA MEDIA GROUPP

Gross operating profit



| | 2004 | 2003 | | Change % |
|---|---------|--------------------------------|------------|-------------------|
| | | Restated | Historical | |
| | | Comparable consolidation basis | Total | |
| (millions of euro) | (a) | (b) | (c) | (a/b) (a/c) |
| Sales and service revenues | 597 | 521 | 595 | 1,297 14.6 0.3 |
| Gross operating profit | 24 | (2) | 12 | 322 |
| % on revenues | 4.1% | (0.5%) | 1.9% | 24.8% |
| Operating income pre-amortization of differences on consolidation | (60) | (85) | (72) | 125 29.1 16.5 |
| Operating income | (89) | (114) | (103) | 63 22.1 13.9 |
| % on revenues | (14.9%) | (21.9%) | (17.3%) | 4.9% |
| Investments: | | | | |
| - industrial | 62 | 84 | 85 | 102 (26.5) (27.2) |
| - differences on consolidation | 6 | 10 | 11 | 61 (37.9) (44.3) |
| Employees at year-end (number) | 1,805 | 1,719 | 2,029 | 2,029 5.0 (11.0) |

In 2004, *sales and service revenues* amounted to euro 597 million, with an increase of 14.6% on a comparable consolidation basis, compared to euro 521 million in 2003.

In particular:

- revenues from the *Internet* area totaled euro 303 million compared to euro 251 million in 2003, with an increase of 20.6%. The increase in revenues is attributable to the positive performance of both business sectors (Internet access and Portal) and particularly the growth of revenues connected with the sale of ADSL products which rose by 69%. In greater detail (gross of intragroup eliminations):
 - in 2004, the TIN.IT Division reported revenues of euro 265 million, an increase of 19.5% compared to the prior year (euro 222 million);
 - in 2004, Matrix S.p.A. reported revenues of euro 44 million, an increase of 23.2% compared to 2003 (euro 36 million).
- revenues from the *Television* area showed a growth of euro 25 million (+ 22.4%), from euro 113 million in 2003 to euro 138 million in 2004, confirming the reputation for editorial content in the programming of the two TV networks. In particular:
 - in 2004, La7 Televisioni S.p.A. posted revenues of euro 62 million, an increase of 14.7% compared to 2003 (euro 54 million);
 - in 2004, MTV reported revenues of euro 80 million, an increase of 25.3% compared to 2003 (euro 64 million).
- revenues from the *Office Products & Services* area were euro 127 million, on a comparable consolidation basis (that is, net of the effects of the deconsolidation in April 2003 of Incas Production S.r.l. and IS Products S.p.A., both companies operating in the field of consumable products), an increase of euro 1 million (equal to 0.5%).

Gross operating profit in 2004 was euro 24 million, an improvement of euro 26 million compared to the gross operating loss of euro 2 million reported in 2003.

The improvement was attributable not only to the increase in sales volumes mentioned earlier, but also to measures taken during the year to improve the efficiency of operating structures. In particular:

- the gross operating profit of the *Internet* area increased from euro 48 million in 2003 to euro 67 million in 2004, an improvement of euro 19 million;

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- the *Television* area improved its gross operating profit (excluding the costs incurred for testing of digital terrestrial TV) by euro 10million, with an increase of 35% compared to the prior year(gross operating loss of euro 28 million net of the costs incurred for digital terrestrial TV);
- the *Office Products* area showed an increase in gross operating profit of euro 3 million (+ 45.2% on a comparable consolidation basis).

The *operating result* in 2004 was a loss of euro 89 million, an improvement of euro 25 million (+ 22.1%) compared to 2003, on a comparable consolidation basis (operating loss of – euro 114 million).

Industrial investments in 2004 amounted to euro 62 million (euro 84 million in 2003, on a comparable consolidation basis) and referred principally to:

- the Television BU, digital terrestrial TV (acquisition of digital frequencies and infrastructure for testing), purchase of TV rights and increasing the power of the plants used to distribute the TV signal;
- the Internet BU, for investments connected with the development Wi-Fi and the growth and use of the Virgilio portal.

The number of *employees* of the Business Unit at December 31, 2004 was1,805, an increase of 86 compared to December 31, 2003, on a comparable consolidation basis.

This increase refers to the sectors which recorded the most growth in terms of revenues (Internet + 20.6% and Television + 22.4%). In particular, the number of employees of the Television BU increased by 68 compared to December 31, 2003. The growth refers to the MTV group where 30 employees were added (principally for the expansion of areas with interactive content, the new satellite channels for Sky and the highly dynamic changes to programs and scheduling) and to the La7 group with the addition of 38 persons (principally in connection with the development of digital terrestrial TV and greater activities associated with changes in the programming and the launching of new TV shows).



■ TELECOM ITALIA MEDIA S.p.A.

Held by: Telecom Italia 59.44%, Telecom Italia Finance 2.03%

The following table shows the key economic highlights compared to restated data (relating only the results of the businesses that were not sold) and historical data. All the percentages are calculated on the basis of data expressed in thousands of euro.

| RESTATED | | | |
|----------------------------|------|------|------------|
| (millions of euro) | 2004 | 2003 | Change (%) |
| Sales and service revenues | 265 | 223 | 19.0 |
| Gross operating profit | 38 | 20 | 88.8 |
| Operating loss | (1) | (25) | 95.1 |
| HISTORICAL | | | |
| (millions of euro) | 2004 | 2003 | Change (%) |
| Sales and service revenues | 265 | 743 | (64.3) |
| Gross operating profit | 38 | 300 | (87.3) |
| Operating loss | (1) | 158 | ° |

Sales and service revenues, equal to euro 265 million in 2004, increased by euro 42 million, + 19.0%, compared to 2003 (euro 223 million). The increase is entirely attributable to the TIN.IT Division, thanks to the positive trend of both traffic revenues and subscription charges.

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Gross operating profit, equal to euro 38 million in 2004, increased by euro 18 million, +88.8%, compared to 2003 (euro 20 million) and represents 14.4% of total sales and service revenues (9.1% in 2003).

The operating result was a loss of euro 1 million and showed an improvement of euro 24 million compared to 2003.

Activities during 2004:

| | | |
|----------------|---|---|
| Internet Users | Dial Up (Tin.it Free and Premium) | At December 31, 2004, Internet users numbered 1.3 million, a reduction (– 0.3 million) compared to December 31, 2003 following the migration of customers towards Broadband products. |
| | ADSL Tin.it | At December 31, 2004, users numbered 296 thousand (148 thousand at December 31, 2003). |
| | ADSL Alice (Telecom Italia customers with services distributed by Tin.it) | At December 31, 2004, users numbered 1.7 million (771 thousand at December 31, 2003). |

■ MAJOR SUBSIDIARIES

MATRIX

Matrix S.p.A

Held by: Finanziaria WEB 66%, ISM 33.3%, Telecom Italia Media 0.7%

The company operates in the Internet sector with the Virgilio portal.

The table shows the key economic highlights.

| (millions of euro) | 2004 | 2003 | Change (%) |
|----------------------------|------|------|------------|
| Sales and service revenues | 44 | 36 | 23.2 |
| Gross operating profit | 9 | 3 | 174 |
| Operating income (loss) | 1 | (5) | ° |

Activities during the year:

in March 2004, the new home page of Virgilio was launched marking a decisive turning-point in the name of innovation and uniqueness.

Virgilio has invested and continues to invest in the Search Engine, with the aim of offering custom-made results to its Italian users through vertical research and hi-tech features. In 2004, in order to meet the requirements of the most demanding customers, Virgilio launched the first integrated Products Research in Italy and an engine was created to search and acquire tracks of music (in collaboration with Alice Music Box).

With regard to content, the new Style channel was launched and dedicated to fashion and everything that is, or will become trendy; Virgilio Sport was the first benchmark on the Internet for the main sporting events during the summer (the European Football Championship, the Olympics, and the Players Market). Furthermore, on the wave of continuous growth of e-commerce, the Shoppingchannel was renovated and enhanced, by integrating it with the Virgilio search engine.

There was a highly positive response from customers to the new formats of advertising space and new publishing initiatives, as shown by the increase in advertising from institutional customers (excluding dialers and intragroup companies).

With regard to Web services, the Rosso Alice portal, operated and implemented by Matrix, was released online in mid-March.

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Holding Media e Comunicazione Group

Held by: Telecom Italia Media 100%

The group operates in the radio and television broadcasting sector.

The table shows the key economic highlights.

| | 2004 | 2003 | Change (%) |
|---|------|------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 138 | 113 | 22.4 |
| Gross operating loss | (29) | (29) | (0.5) |
| Operating loss pre-amortization of differences on consolidation | (57) | (48) | (18.0) |
| Operating loss | (80) | (71) | (12.3) |

Activities during the year:



- **La7** - with the fall just ended and the new program schedule designed following a change in publishing management, La7 has made a real step forward. Despite maintaining its distinctive positioning with regard to general television and targeting an audience interested in probing news in depth and with a fairly high level of education, the network nevertheless succeeded in significantly increasing its market share and attracting new viewers (an increase of 10% compared to the prior year; +22% in fall 2004 compared to fall 2003).



- **MTV** - confirmed its leadership position in the youth television segment and strengthened its position in the Italian advertising market. In particular, growth in advertising was driven by the significant contribution of new customers, the increase in the average investment per customer and the increase in the average revenues per spot. The positive evolution of the MTV Network continued: the publishing success achieved by the Italian edition of the Europe Music Award 2004 was complemented by the gradual growth in the number of viewers.



Buffetti Group

Held by: Telecom Italia Media 100%

The group operates in the office products and services sector.

The table shows the key economic highlights.

| | 2004 | 2003 (*) | Change (%) |
|----------------------------|------|----------|------------|
| (millions of euro) | | | |
| Sales and service revenues | 127 | 126 | 0.5 |
| Gross operating profit | 10 | 7 | 45.2 |
| Operating income (loss) | 1 | (2) | ° |

(*) Figures are on a comparable consolidation basis, excluding, from 2003, the consumables activities, sold in March 2003 and the CIPI S.p.A. activities sold in January 2004.

Activities during the year:

- during 2004, sales in the technological sectors (office automation, telephone products and accessories) increased, the operating software sector remained stable and the traditional product sectors recorded a slight fall. Sales of new products increased by 5% compared to 2003, whereas sales of traditional products showed a slight reduction compared to the prior year, despite the stagnation in the consumption of office products (the annual trend of retail sales of office products recorded by the I+C Institute at the end of 2004 was - 3%).

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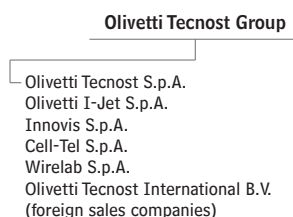
OLIVETTI TECNOST

■ INTRODUCTION

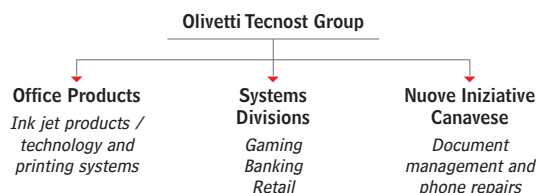
The Olivetti Tecnost group Business Unit operates through the Office Products Division in the sector of ink-jet products for the office, digital printing systems and the development and production of products associated with silicon technology (ink-jet print-heads and MEMS). Through the Systems Division it provides specialized applications for the banking field and commerce and information systems for gaming and lottery management. In addition, the group collaborates with Nuove Iniziative Canavese in document management services and fixed and cell phone repairs. The reference market of the BU is focused mainly in Europe and Asia.

■ THE STRUCTURE OF THE BUSINESS UNIT

The Business Unit comprises the following (the main companies are indicated):



and operates with the following organizational structure:



During 2004, the operating structure has changed: activities for developing and producing ink-jet print-heads and MEMS (Olivetti I-Jet) were incorporated within the Office Products division; the remaining part of the Industrial Operations division (document management and the repair of fixed and cell phones through the companies Innovis, Cell-Tel and WireLab) constitutes the Nuove Iniziative Canavese division.

Furthermore, the North and Central American division is no longer operating following the sale of the stake in Royal Consumer Information Products Inc. and the Olivetti Mexicana SA corporate complex, described further below.

The South America division, which is also no longer operating, is completing the process of winding up its operations.

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■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

The following transactions took place:

- effective January 1, 2004, as part of an operation to rationalize and reorganize the help-desk and customer care activities, the CRM business segment (comprising 14 staff) of Olivetti Tecnost S.p.A. was sold to the Comdata group and an outsourcing contract was negotiated with this company;
- a decision was taken to wind-up the following companies, which, accordingly, have been deconsolidated:
 - Olivetti de Venezuela C.A. (January 30, 2004); the wind-up was concluded on June 11, 2004;
 - Olitecno S.A. de C.V., 50%-owned (February 17, 2004);
 - Olivetti Peruana S.A. (February 20, 2004);
 - Diaspron do Brasil S.A. (March 5, 2004);
 - Multidata S.A. Eletronica Industria e Comercio (March 5, 2004);
 - Olivetti Argentina S.A.C.e.I. (April 14, 2004);
 - Olivetti Colombiana S.A. (May 3, 2004);
 - Olivetti Servicios y Soluciones Integrales S.A. de C.V., Mexico (May 20, 2004).
- on July 26, 2004, the Extraordinary Shareholders' Meeting voted to put the company Dedita S.p.A. into a wind-up;
- on September 23, 2004, the sale was executed for 100% of the United States subsidiary Royal Consumer Information Products Inc. (U.S.A.) and its Mexican subsidiary Royal Consumer Information Products de Mexico S.de R.L. de C.V. (which had been especially set up for the acquisition of the Olivetti Mexicana S.A. business on May 26, 2004) as well as the Olivetti Mexicana S.A. business complex composed of all the employees and part the assets. The holdings in question were part of the North and Central America division;
- on September 27, 2004, the company Olivetti Lexikon Benelux S.A. was put into a wind-up;
- on September 30, 2004, following receipt of approval from the Antitrust Authority, Olivetti I-Jet S.p.A. finalized the merger of 100% of the Swiss company YMINDS S.A. (in which Olivetti I-Jet already held a 27.2% interest) after purchasing a 61.4% stake from third parties and a 11.4% holding from Olivetti Tecnost International BV. The company is engaged in research and development of products using Ink-jet technology. The transaction took place in the Office Products division;
- in December 2004, the following companies were put into a wind-up:
 - Olivetti Servicios Y Soluciones Integrales de C.V. (December 3, 2004);
 - Dedita S.p.A. (December 30, 2004);
 - OLAT Associates S.A. (December 30, 2004);
- on December 29, 2004, the company Triumph Adler Wohnungsbau GmbH was merged by absorption in Olivetti Tecnost Deutschland.

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■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003.

| Gross operating profit | (millions of euro) | 2004 | 2003 | Change | |
|------------------------|---|-------|-------|--------|--------|
| | | | | amount | % |
| | Sales and service revenues | 601 | 655 | (54) | (8.2) |
| | Gross operating profit | 44 | 40 | 4 | 10.0 |
| | % of revenues | 7.3 | 6.1 | | |
| | Operating income pre-amortization of differences on consolidation | 22 | 4 | 18 | ° |
| | Operating income | 21 | 2 | 19 | ° |
| | % of revenues | 3.5 | 0.3 | | |
| | Investments: | | | | |
| | - industrial | 15 | 20 | (5) | (25.0) |
| | Employees at year-end (number) | 2,108 | 2,395 | (287) | (12.0) |

Sales and service revenues amounted to euro 601 million in 2004, of which euro 337 million referred to the Office Products Division, euro 186 million to the Systems Division, euro 26 million to Nuove Iniziative Canavese and euro 52 million to other operations. Revenues by product were as follows: euro 323 million for hardware, euro 128 million for accessories, euro 150 million for services and other revenues.

Compared to 2003, revenues in 2004 showed a reduction of euro 54 million (– 8.2%).

Excluding the foreign exchange effect and the impact of the change in the scope of consolidation (with particular reference to the closing of operations in Latin America and the sale of activities in the U.S.A. and Mexico) foreuro 96 million, and the revenues on the sale of intellectual properties to TI LAB for euro 27 million, underlying growth was equal to euro 15 million (+ 2.7%).

Gross operating profit amounted to euro 44 million with an improvement of euro 4 million (+ 10%) compared to the prior year. Excluding the foreign exchange effect and the impact of the change in the scope of consolidation, underlying growth was nil mainly on account of the incremental costs for the new projects of the Office Division.

Operating income in 2004 was euro 21 million and showed an improvement of euro 19 million compared to 2003. Underlying growth was euro 13 million, mainly on account of the restructuring measures put into place in the past years which led to a reduction in fixed overheads.

Industrial investments amounted to euro 15 million, a reduction of euro 5 million compared to 2003.

At December 31, 2004, *employees* numbered 2,108, of whom 1,916 were employed in Italy and 192 abroad. The reduction of 287 persons compared to December 31, 2003 involved 148 employees in Italy and 139 abroad. The reduction in the number of employees outside Italy was the result of the deconsolidation of the company Royal Consumer Information Products Inc. (U.S.A.) and the operational business segment in Mexico, which was only partly compensated by the acquisition of the Swiss company YMINDS (34 resources).

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■ EVENTS SUBSEQUENT TO DECEMBER 31, 2004

The following events took place:

- on January 14, 2005, the deed was signed for the sale of 60% of the share capital of Innovis S.p.A. by Olivetti Tecnost S.p.A. to the shareholder Comdata S.p.A.; after this transaction, the investment holdings in Innovis S.p.A. are as follows: 80% Comdata S.p.A. and 20% Olivetti Tecnost S.p.A.. At December 31, 2004, the employees of the company Innovis numbered 222;
- negotiations are underway for the sale of 65% of share capital of Cell-Tel S.p.A. to the shareholder Telis S.p.A.; after this operation the investments of Olivetti Tecnost will be to 15%. The sale will be completed by the end of March 2005.

■ INFORMATION ON OPERATIONS

The main activities carried out during 2004 are the following:

Office Products

In 2004 the Office Products division, including Olivetti I-Jet, confirmed the positive trend begun in 2003.

Growth was confirmed along with the division's European leadership in the sphere of fax machines with ink-jet technology. The numbers of fax machines sold during the year increased by approximately 150,000 (+34%) compared to the prior year.

Sales of digital photocopiers, another important segment of the office business, increased by 38% over 2003.

Investment plans are being implemented to support activities for the development and manufacture of new fax machine models and other new products in the sector of ink-jet technology on an industrial scale.

With reference to the process of rationalizing the European network, the back-office activities of foreign affiliates were outsourced and concentrated in the services center of the Accenture group in Prague.

Systems Division

As far as this division is concerned, net of the foreign exchange effect, the results of 2004 confirm growth compared to the prior year, both from the point of view of revenues and margins, and from the standpoint of business initiatives to promote geographical and product diversification.

In particular, in the *Gaming* sector, an important contract was signed and completed in 2004 for the supply of about 25,000 terminals for operating the electronic voting system in Venezuela. In addition, the division began to supply terminals for video-games to the Czech Republic and won an order worth more than US \$2 million for a total supply of 2,000 terminals for automated gaming in China (the Shanghai Welfare Lottery). As far as the Italian market is concerned, terminals for the videolottery have begun to be sold.

In the *Banking* sector, in 2004, Olivetti Tecnost succeeded in maintaining its 2003 market share in Western countries, where there was a generalized downturn. Sales volumes increased on Eastern markets, where approximately 134,000 special printers were sold (of which about 100,000 in China).

In the *Retail* sector, the performance of the Shop Automation business remained steady with regard to volumes of conventional fiscal Cash Registers, of which more than 48,000 were sold.

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Nuove Iniziative Canavese

The activities of this Division increased significantly compared to the prior year.

In particular, the subsidiary Cell-Tel acquired new customers and extended its line of service to repairing and regenerating fixed telephone equipment. However, the increase in volumes was not enough to guarantee positive economic results for most of the year, with the first results only becoming tangible in the last months of 2004.

The subsidiaries Innovis (back-office activities) and Wirelab (repair and regeneration of telephone exchanges) increased both their businesses and, consequently, their number of employees.

* * *

In 2004, a contract was signed between Olivetti Tecnost and the TILAB function of Telecom Italia, for the sale of intellectual property through the acquisition by Telecom Italia of research and development projects and activities carried on by Olivetti Tecnost and authorized by TILAB.

A contract was also signed for the payment of royalties by Olivetti Tecnost to Telecom Italia for use of the Olivetti brand and another was signed for the utilization of patents and the same intellectual properties.

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INFORMATION TECHNOLOGY MARKET

- ▶ Excellent performance of Finsiel S.p.A. in the Government market
- ▶ Strong increase in the volumes of Tele Sistemi Ferroviari (+18%) as a result of consolidating its position with the national railway group, Ferrovie dello Stato.
- ▶ Decline of the Finance market
- ▶ Preliminary contract between Telecom Italia and the COS group for the sale of Finsiel S.p.A.

■ INTRODUCTION

The Telecom Italia IT Market Business Unit brings together all the information technology companies and activities of the Group directed to the external market. The BU, as a whole, is among the ICT – Information Communication Technology – leaders at national level, the largest Italian-owned ICT group, the foremost in providing solutions for the public administrations and transportation companies, and one of the top five supplying solutions for banks.

The customers of the ITM BU include some of the largest central public administrations, the leading Italian banking groups, companies belonging to the national railway group Ferrovie dello Stato, more than 1,000 local organizations, health and transportation authorities, social security agencies and insurance groups.

The activities of the IT Market BU in 2004 can be summarized as follows:

- with reference to the companies in the Government market, thanks partly to measures to improve cost efficiency undertaken during the last two years, there was an increase in volumes and an improvement in profitability margins, particularly in the case of Finsiel S.p.A. which achieved a positive gross operating profit and basically a breakeven in terms of the net result;
- in the Transportation and Industry market, and particularly in the case of Tele Sistemi Ferroviari, there was a considerable increase in revenues, but, on the other hand, strong pressure on prices had a significant impact on profitability;
- in the case of the Finance market, and particularly for Banksiel, there was a contraction of revenues and profitability indicators due to the discontinuation of some activities and price reductions.

■ THE STRUCTURE OF THE BUSINESS UNIT

The Business Unit is currently organized as follows (the main consolidated companies are shown):



The Structure of the Business Unit has changed since 2003 due to the deconsolidation of the Webegg group following the sale of the stake held by IT Telecom in Webegg to Value Partners as from July 1, 2004. Webegg group had been controlled by Telecom Italia through IT Telecom, which held a 69.8% stake, and through Finsiel, which held a 30.2% stake and had been consolidated in the IT Market Business Unit because, operationally, it reported to Finsiel. Under the transaction for the sale of Webegg to Value Partners, Finsiel will keep its investment in Webegg and reciprocal sale and purchase options will be recognized between Finsiel and Value Partners.

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On October 4, 2004, upon purchase of 100% of the company Software Factory, which was already held by the subsidiary Winner Project B.V., the Extraordinary Shareholders' Meeting of Webegg voted to approve the merger by absorption of the companies V.P. Web S.p.A., V.P. Technologies S.r.l., Teleap S.p.A. and Software Factory S.p.A. in Webegg S.p.A. with effect, pursuant to art. 2504 of the Italian Civil Code, on December 31, 2004.

The above Shareholders' Meeting also voted to change the name of the company from Webegg S.p.A. to Value Team S.p.A., again effective from the date of December 31, 2004.

■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

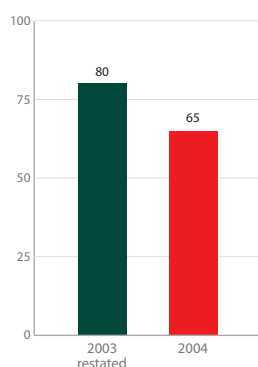
In addition to the deconsolidation of the Webegg group, the following transactions took place:

- the sale, effective January 1, 2004, of the "Facility Management" business to Emsa Servizi S.p.A. by Finsiel S.p.A.;
- on May 4, 2004, Finsiel sold to Finanziaria Ligure per lo Sviluppo Economico - F.I.L.S.E. S.p.A.; the investment in affiliated Datasiel S.p.A. (49%);
- On July 14, 2004, Banksiel signed a contract for the purchase of 100% of the share capital of IAK S.r.l.. The contract was executed on October 11, 2004 after the relative approvals were obtained from the Antitrust Authority. The company was consolidated as from October 1, 2004.

■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003 based on historical and restated data. The data relating to 2003 has been restated, for purposes of comparison, by excluding the data relating to the Netikos Group, Domus Academy and the activities of the Enterprise business segment which was sold to IT Telecom on October 1, 2003, and consolidating the Webegg group only for the first six months of 2003.

Gross operating profit



| | 2004 | 2003 | 2003 historical | Change (a - b) | |
|--|-------|-------|--------------------|-------------------|--------|
| (millions of euro) | (a) | (b) | (c) | Amount | % |
| Sales and service revenues | 729 | 828 | 891 | (99) | (12.0) |
| Gross operating profit | 65 | 80 | 84 | (15) | (18.8) |
| % of revenues | 8.9 | 9.7 | 9.4 | | |
| Operating income pre-amortization of differences on consolidation | 37 | 60 | 60 | (23) | (38.3) |
| Operating income | 36 | 59 | 58 | (23) | (39.0) |
| % of revenues | 4.9 | 7.1 | 6.5 | | |
| Investments: | | | | | |
| - industrial | 25 | 27 | 30 | (2) | (7.4) |
| - differences on consolidation | 2 | - | - | 2 | - |
| Employees at year-end (number) | 4,131 | 4,165 | 4,827 | (34) | (0.8) |

Sales and service revenues in 2004 decreased by euro 99 million compared to the prior year, restated for purposes of comparison. This change was mainly attributable to Intersiel (– euro 112 million) which last year completed and invoiced the activities inherent to the Telcal project, which was treated for the entire duration of the project as work in process, and to Banksiel (– euro 34 million) for the discontinuation of IT services provided on large projects for the migration of information systems of the banks and the effect of the significant reduction in professional price rates although the volumes remained the same. The above negative effects were partly compensated by the increase in activities by Tele Sistemi Ferroviari (+ euro 35 million)

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due to higher volumes associated specifically with activities generating lower margins, by Finsiel (+ euro 9 million) for additional activities in the areas of Culture and Instruction, Welfare and Lombardia Informatica, offset by a deterioration in the Defense and Security area, and by Insiel (+ euro 6 million) for higher sales invoiced to the Friuli Venezia Giulia Region and other minor customers.

Gross operating profit decreased by euro 15 million compared to 2003, restated. This reduction is mainly attributable to the decrease in the gross operating profit of Banksiel (– euro 17 million), Tele Sistemi Ferroviari (– euro 5 million), Carisiel (– euro 2 million) and the Webegg group (– euro 3 million), which were partially offset by an improvement in the performance of Finsiel (+ euro 12 million).

Operating income decreased by euro 23 million compared to 2003, restated. This reduction is mainly attributable to a decline in the operating activities of Banksiel (– euro 18 million), Tele Sistemi Ferroviari (– euro 8 million) and the Webegg group (– euro 2 million), and was partly offset by an improvement in the activities of Finsiel (+ euro 6 million).

Industrial investments amounted to euro 25 million and decreased by euro 2 million compared to 2003, restated, whereas investments referring to differences on consolidation regarded goodwill which arose on the purchase of the subsidiary IAK S.r.l..

At December 31, 2004 *employees* numbered 4,131, with a decrease of 34 compared to December 31, 2003, restated, and 696 compared to historical data (of which 662 employees refer to the Webegg group).

■ EVENTS SUBSEQUENT TO DECEMBER 31, 2004

The following events took place:

- Negotiations continued in 2005 for the sale of shares representing 52% of the share capital of Insiel, owned by Finsiel S.p.A., to the Friuli Venezia Giulia Region.
The sale should take place during the first half of 2005 and would give the Friuli Venezia Giulia Region, which already owns a 46.53% stake in Insiel, control over all Insiel's share capital.

■ INFORMATION ON OPERATIONS

The following important contracts were acquired during 2004:

- **Finsiel**, as part of a temporary association of companies including Hewlett Packard, won the bid announced by the Ministry of Justice to develop and operate a centralized data bank listing information about all assets seized or confiscated from criminal organizations, as part of a series of measures to prevent crimes involving property;
- **Finsiel - Territory and Environment**, in a temporary association of companies with Telespazio and Agriconsulting, won the bid to produce annual agricultural statistics about crops and trees (the AGRIT Project), partly through the use of remote monitoring and partly through on-the-spot observation, on behalf of the Ministry of Agriculture and Forestry;
- **Finsiel** won the bid announced by the Central Criminal Police Headquarters of the Ministry for Home Affairs, of which the Scientific Police Service is part, to supply systems for acquiring digital palm-prints as well as the relative installation, training and support services for Police Headquarters in the southern regions of Italy;

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- **Finsiel** won the contract to create a computer system to manage the securitization of receivables at INPDAP;
- **Tele Sistemi Ferroviari** signed agreements for outsourcing activities with Ferservizi and RFI - Rete Ferroviaria Italiana, extending its Traffic Control Systems and public information announcements to stations in Lombardy, which plan to add this service by the end of 2005, to RFI. Furthermore, outside the state railways system, Tele Sistemi Ferroviari won the bid, in a consortium with MET Sogeda S.p.A., to develop an administration and accounting system based on SAP technology for CTP - Compagnia Trasporti Pubblici S.p.A. in Naples;
- **Banksiel** won contracts with nine of the leading banking groups for projects to develop and update their systems to the new IAS and Basel 2 regulations;
- **Insiel** created an e-business system for Danieli C. S.p.A. so that all the project documentation can be shared between the company's project managers and its customers. Danieli, founded in 1914, is the world's third-largest producer of innovative machinery and plant for the iron and steel industry and exports 99% of its production;
- **Finsiel Romania**, headquartered in Bucharest, created the Global Biodiversity Information Facility portal, the website for collecting data about biodiversity on a worldwide scale, dedicated to the scientific community;
- **Krenesiel**, in a temporary association of companies with Insiel and Dianoema, won the bid announced by Local Health Authority No. 6 of Sanluri (Province of Cagliari) to develop and operate the computer system of the hospital and the Immune-Transfusion Center;
- **Finsiel and TIBCO Software**, one of the world's top suppliers of business integration software, signed a partnership agreement for the resale of user licenses for the Public Administration, Transportation and Finance markets;
- **Tele Sistemi Ferroviari**, in a temporary association of companies with Engineering Ingegneria Informatica (agent), EDS and SIDI, won the bid announced by ENEL S.p.A. for the supply of services to develop SAP projects for the ENEL group;
- **Agrisian** created a website for the Agenzia per le Erogazioni in Agricoltura;
- **Finsiel** won the bid announced by the Marches Region for the study and testing of new technologies to contrast trafficking in synthetic drugs and their chemical precursors". The project will be financed by the European Community and is part of a far-reaching plan to counter organized crime on a European scale. The aim is to identify the critical points in drug trafficking, the traffic of stolen cars, and clandestine immigration;
- **Finsiel** won the bid announced by Poste Italiane for the Service Control Room for the Poste Italiane information system.



Finsiel Group

Held by: Telecom Italia 79.50%

Finsiel Group is one of Italy's leading companies in the field of IT consultancy and services, and the top Italian-owned company. Being part of Italy's leading Information and Communication Technology group ensures that Finsiel's customers are supplied with solutions and services based on the wealth of experience, competence and innovation of all the companies in the Finsiel Group.

Finsiel provides a complete range of services for administrations, leading banks and companies, which covers the whole chain of value of ICT. Its offering is based on the choice of market solutions and platforms, integrated by consultancy on process re-engineering and expert knowledge of the reference markets and the world of legacy systems. It is an offering in which alliances with the best suppliers of products and solutions worldwide are a key factor.

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The table shows the key economic and operating highlights:

| (millions of euro) | 2004 | 2003 restated (*) | Change (%) |
|----------------------------|------|----------------------|---------------|
| Sales and service revenues | 662 | 759 | (12.8) |
| Gross operating profit | 60 | 73 | (17.8) |
| Operating income | 35 | 56 | (37.5) |

◀ (*) The year 2003 has been restated on a comparable consolidation basis with 2004, excluding the share of the Enterprise business segment sold by Finsiel on October 1, 2003.

Activities during the year:

During 2004, the Finsiel group pursued measures to improve overall efficiency and reduce costs. The group also continued, in 2004, the restructuring operations begun in 2003 and sold the Facility Management business of Finsiel S.p.A.. Although performance was positive, in particular by Finsiel, the reduction of revenues from customer banks recorded by Banksiel significantly impacted economic results, with noticeable repercussions on profitability margins.

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INFORMATION TECHNOLOGY GROUP

► Merger of IT Telecom S.p.A. and EPIClink S.p.A. in Telecom Italia S.p.A.

■ THE FUNCTION

The Information Technology Group Function is responsible for coordination, technological innovation and service information technology activities within the Telecom Italia Group. The function focuses on the core business of TLC, pursuing objectives such as the increment, the efficiency and the improvement of quality and innovation, with the aim of implementing economies of scale and achieving advancements in terms of performance.

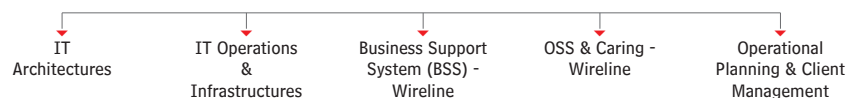
On September 9, 2004, the Board of Directors of Telecom Italia examined and approved the plan for merger of the wholly-owned subsidiaries IT Telecom S.p.A. and Epiclink S.p.A in Telecom Italia. As provided by the respective bylaws, the merger (which will not entail a capital increase by the acquiring company) was approved on October 11, 2004 by the Boards of Directors of the three companies. The merger is effective from December 31, 2004 and for accounting and tax purposes from January 1, 2004. Moreover, on December 15, 2004, effective from December 30, 2004, IT Telecom S.p.A. conferred its Data Center business segment to IT Telecom S.r.l., a new company set up on November 12, 2004.

This plan falls under a broader reorganization of the Information Technology Group area. Bringing the activities of these two subsidiaries inside Telecom Italia will make it possible to rationalize the use of resources and technological expertise and will lead to an important simplification of the operational, administrative and corporate management processes.

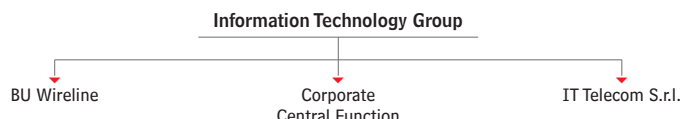
■ THE STRUCTURE OF THE FUNCTION

The Function had comprised the companies IT Telecom and EPIClink dedicated to the information systems of the Group, within the framework of the project to integrate the various areas.

The function was organized as follows:



After the merger, the reorganization of the Information Technology area was completed with a new organizational model which calls for the allocation of IT activities according to the following organization chart:



Wireline - the development and applications of OSS and BSS systems and the development, design, delivery and management of VAS for the Wireline market have been transferred to Telecom Italia's Wireline business segment, the aim being to integrate end-to-end processes so as to maximize the operational synergies between demand management and development activities;

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Central Functions - sthe activities relating to the definition of the reference architectures used in the projects of the BU have been allocated to Telecom Italia's Corporate Central Functions with the aim of making Group IT strategies more uniform;

IT Telecom S.r.l. - the activities of creating and operating Group IT infrastructures (Data Centers) have been allocated to the newly-formed company with the aim of maximizing synergies and encouraging the convergence processes.

■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

The following transactions took place:

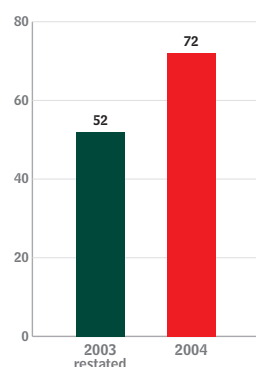
- on March 31, 2004, under the program for the reorganization of Telecom Italia Group's information technology area, the "Development" business segment was sold to TIM S.p.A., effective April 1, 2004.
The "Development" business segment carries out activities currently conducted by IT Telecom S.p.A. for TIM regarding:
 - innovative services, based on IP networks, known also as e-business or web services, directed at the business and mass-market segments;
 - telecommunications software development and maintenance activities.
 These activities are integrated with the resources that today already operate in IT development in the Mobile BU, making it possible to improve the synergies for the management of the current platforms and the development of their evolution.
The sales price, based also upon an outside appraisal by Milestone Advisory House S.p.A. in Milan, was agreed between the parties at euro 23 million. 551 resources were transferred;
- on April 6, 2004, a contract was finalized for the sale of the 75%-investment held in Telesoft Russia ZAO for consideration of USD 24,000;
- on April 6, 2004, Teco Soft Argentina SA, a company controlled 99.99% by IT Telecom S.p.A. was put into a wind-up;
- on June 3, 2004, IT Telecom S.p.A. signed an agreement with Value Partners S.p.A. for the sale of the stock held in Webegg S.p.A., equal to 69.8% of its share capital, at a price of euro 43 million. The agreement was finalized on July 15, 2004 after authorization was obtained from the Antitrust Authority;
- on September 8, 2004, the Board of Directors of IT Telecom S.p.A. voted to confer to Shared Service Center s.c.r.l. (SSC) – in which a 40.91% stake is held – the following business segments: ERP Solutions, engaged in the development and maintenance of ERP systems, and Application Operations - Administration & Finance, which guarantees applications management for the systems in the administration and finance areas.
The ownership interest remained unchanged as the other SSC shareholders (TIM S.p.A., 4,545%, Olivetti Tecnost S.p.A. 4,545% e Pirelli S.p.A. 50,00%) subscribed to their part of the capital increase.

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■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003 based on historical and restated data. The data relating to 2003 has been restated, for purposes of comparison, by excluding the figures relating to the "Development" business segment sold to TIM and those of Telesoft Russia Zao and Tecosoft Argentina but including the figures of the "Enterprise" business segment at September 30, 2003, purchased in October 2003 from Finsiel.

Gross operating profit



| | 2004 | 2003 restated | 2003 historical | Variazioni (a - b) | |
|---|-------|---------------|-----------------|--------------------|-------|
| | (a) | (b) | (c) | absolute | % |
| (millions of euro) | | | | | |
| Sales and service revenues | 965 | 948 | 1,100 | 17 | 1.8 |
| Gross operating profit | 76 | 52 | 96 | 24 | 46.2 |
| % of revenues | 7.9 | 5.5 | 8.7 | | |
| Operating income pre-amortization of differences on consolidation | (67) | (79) | (36) | 12 | 15.2 |
| Operating income | (67) | (79) | (36) | 12 | 15.2 |
| % of revenues | (6.9) | (8.3) | (3.3) | | |
| Investments: | | | | | |
| - industrial | 180 | 175 | 174 | 5 | 2.9 |
| Employees at year-end (number) | 3,160 | 3,216 | 4,107 | (56) | (1.7) |

Consolidated *revenues* showed an increase of euro 17 million compared to 2003, restated. This was both the result of invoicing the work in progress at December 31, 2003 and the increase in activities related to institutional projects for the Corporate business segment of Telecom Italia, such as the SAP Value Program and the development of the Group Portal, and activities conducted on behalf of the Wireline business segment of Telecom Italia on projects such as Usage Collection, Trouble & Job Management and Network Creation. Activities carried out in 2004 include Telecom Italia's new project, begun at the end of 2003, called "International Operators", and outsourcing on behalf of the Wireline network.

Gross operating profit, equal to euro 76 million, showed a growth of euro 24 million compared to 2003. The increase was due to the combined effect of higher production value (+ euro 1 million) – deriving from the aforementioned increase in revenues and the reduction in work in process and capitalized internal construction costs (– euro 16 million) – and the decrease in operating costs (– euro 23 million) – following the increase in external costs (+ euro 9 million) offset by lower labor costs (– euro 32 million) as a result of the restructuring process currently in progress.

The *operating result* was a loss of euro 67 million (– euro 79 million in 2003, restated) and improved by euro 12 million. The improvement can mainly be attributed to the above-mentioned increase in the gross operating profit and the balance of other operating income and expenses (+ euro 4 million). This was partly offset by the increase in amortization and depreciation charges (+ euro 14 million) and provisions to the reserves for pending litigation (euro 2 million).

Industrial investments amounted to euro 180 million and reflected the continuation of infrastructure projects begun at the end of 2003. In particular, work continued on the overhaul and expansion of the Group Network and the refurbishment of the direct interconnections of 48 companies, including 5 foreign companies, while projects relating to the UNICA platform were completed. In addition, new projects were started, relating, in particular, to Griffon, to the development of the Group SAP initiative and to the e-Foundation project.

At December 31, 2004, *employees* numbered 3,160, with a reduction of 56 compared to December 31, 2003, restated. The reduction is mainly due to the continuation of restructuring activities begun during the prior year; the restated figures do not include, in particular, the business segments sold in 2004 to TIM (551 persons) and to SSC (201 persons).

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In 2004, activities continued for the management of the operating systems and in order to rationalize and standardize the architectures and infrastructures of the Parent Company. In particular, work went ahead to develop the "Group Network" and the "Virtual Data Center Network" infrastructure projects, and the new "e-Foundation" project was begun, aimed at the applications integration at the Enterprise level on the different chains of business, and release of the network and safety infrastructures of IT Telecom S.p.A.'s Data Centers for operational implementation.

The release of the International Backbone with the TIM Group is nearing completion. The backbone now connects Brazil, Chile, Venezuela, Peru, Turkey, Greece and Holland. Finally, the center of competence for the operation of development systems at the Naples headquarters became fully operational and the operating systems for the Reporting and Consolidated application were transferred from the Data Center in Turin to the one in Milan.

As far as the BSS and OSS development activities for the Business Unit are concerned, the following events are worthy of note:

for Telecom Italia Wireline:

in the area of BSS

- conclusion of the process of migration of the Business and MicroBusiness clientele to the new CRM - Customer Relationship Management platform which manages the sales, order management, customer care and billing processes;
- start of operation of the new Usage Collection platforms (for managing telephone traffic, data and services) and front-end credit (PACI);
- conclusion of the process of migration from the previous Hansenet platform to the new international CRM platform in Germany. In France, marketing of the Aladino and ADSL plans has been activated and the Alice portal has been launched;
- start of operation of the new e-Commerce platform, also allowing payment by credit card;
- updating of all the information systems in the Business Intelligence areato comply with Resolution No. 180 (concerning consent to release personal data) and completion of datawarehouse systems for analyzing traffic, customers and revenues;

in the area of OSS

- continuation of the integration of the chain of systems supporting the management of complaints and technical failures and elimination of pre-existing legacy environments;
- continuation of the program to expand Broadband in Europe and completion of the second phase of complaint management for the German operator and delivery of Rosso Alice to the French operator;
- completion of the necessary steps, with reference to National Wholesale, to comply with Resolution No. 340/440 of the TLC Authority and completion of the band upgrade for ADSL services;
- completion of work on the projects to technologically update and integrate the UNICA platform (TLC network and services inventory);
- with regard to Local Loop Unbundling, operational implementation of the software developed for the management of the return of the clientele to Telecom Italia and Shared Access;
- introduction of architectural developments to the whole chain of ADSL provisioning to support the increase in customers acquiring ADSL services;
- continuation of the work to improve the efficiency of the Service Delivery platform and the rationalization of the Network Assurance process with the inclusion of further technological domains and the introduction of new functions.

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OTHER ACTIVITIES

The "Other Activities" of the Telecom Italia Group are principally constituted by the TILAB Central Functions, by the companies which provide centralized services to the Group and by the Corporate Functions.

TELECOM ITALIA LAB

■ THE FUNCTION

Telecom Italia Lab is responsible for supervising technological innovation within the Telecom Italia Group. This is achieved by scouting out new technologies, preparing and examining research and feasibility studies and developing prototypes and emulators of new services and products, with a special focus on the main topics of strategic interest to the individual Business Units. It operates to promote the Group's technological leadership and also exploits collaboration with Pirelli Labs.

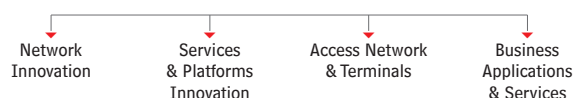
The activities can be broken down into the Group's main innovative areas of interest, such as: developing the access network to cope with the growing demand for band availability, developing the carrier network, with a gradual transition towards optical technologies, developing telephone services, in view of the convergence of the network architecture towards an "all-IP" model, developing third generation hi-tech services and terminals of the new generation for the mobile area and contributing to the evolution of the Internet and multimedia. Telecom Italia Lab relies on the expertise of Telsy, the Telecom Italia Group company which, since 1971, has worked to develop and produce equipment for security in telecommunications with cryptographic functions.

■ THE STRUCTURE

Since April 1, 2004, the structure is organized as follows:



TILAB medium- and long-term research activities are organized as follows:



Network Innovation and Access Network & Terminals: are devoted to short and medium/long-term R&D projects on wireline and mobile network infrastructures, with a focus on the segment of core networking, radio access, broadband access and innovative terminals.

Services & Platforms Innovation and Business Applications & Services: concentrate on the creation of services and the testing of prototypes through innovative platforms, for the consumer and business markets, respectively.

TILAB also has Testing Laboratories which are used to test both equipment acquired from vendors and prototypes developed through research.

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■ MAJOR CORPORATE EVENTS/SCOPE OF CONSOLIDATION

On January 13, 2004, Telecom Italia sold the 40% investment held in the associated company Siosistemi to I.NET S.p.A. for euro 1.6 million. The sale falls under the program for the divestiture of investments that are no longer considered strategic to the core business.

■ ECONOMIC AND FINANCIAL DATA

The following table shows the key results of 2004 compared to those of 2003, restated.

| | 2004 | 2003 restated | Change amount | % |
|--------------------------------|-------------|------------------|------------------|-------------|
| (millions of euro) | | | | |
| Operating costs | 167 | 150 | 17 | 11.3 |
| Amortization and depreciation | 11 | 16 | (5) | (31.3) |
| Operating grants | (5) | (9) | (4) | (44.4) |
| Total Net Costs TILAB | 173 | 157 | 16 | 10.2 |
| Costs recharged to TI BUs | 148 | 128 | 20 | 15.6 |
| Revenues from third parties | 13 | 15 | (2) | (13.3) |
| Total | 161 | 143 | 18 | 12.6 |
| Operating income | (12) | (14) | 2 | 14.3 |
| Investments: | | | | |
| - industrial | 10 | 8 | 2 | 25.0 |
| Employees at year-end (number) | 1,064 | 1,142 | (78) | (6.8) |

During 2004, total net costs, equal to euro 173 million, increased by euro 16 million compared to the prior year (euro 157 million). The increase is due to higher costs (euro 27 million) connected with the contract signed with Olivetti Tecnost toward the end of the year. The contract covered the sale of intellectual property and research and development projects and activities. Net of this change, there would have been a reduction in operating costs in 2004 of euro 11 million.

Mention should also be made of lower depreciation charges following the sale of the owned buildings under the Dedalo project (which was accompanied by an increase in lease costs).

Furthermore, for the purposes of achieving a more meaningful comparison, in 2003, the costs of the research collaboration contract with Pirelli Labs and the contract for consultancy services regarding industrial property that Telecom Italia Group had with the Industrial Properties Function of Pirelli & C. have been taken into account although they were still under Telecom Italia's Corporate Function (euro 19 million for the year 2004 and euro 17 million for the whole of 2003).

The costs recharged to the Business Units rose by euro 20 million as a result of the royalties for the sale of the intellectual property and brands governed by the aforementioned contract with Olivetti Tecnost.

Industrial investments amounted to euro 10 million, an increase of euro 2 million compared to the prior year.

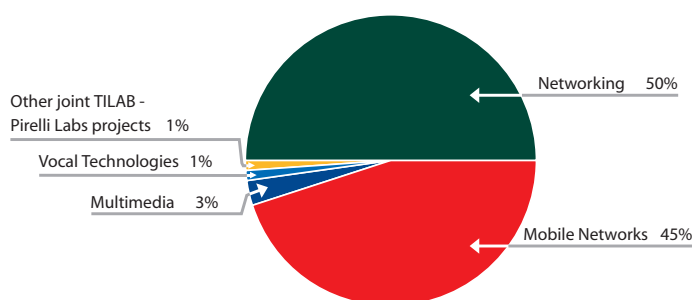
At December 31, 2004, *employees* numbered 78 less than at December 31, 2003.

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■ INFORMATION ON OPERATIONS

The growing emphasis on finding opportunities to generate a competitive advantage and create value for the Telecom Italia Group was partly pursued through the strategic management of the relationships between research, Intellectual Property Right (IPR) and business with the aim of developing the Group's patent portfolio. In this context, in 2004, 86 new patents were filed, of which 5 are joint applications with Pirelli Labs, with an increase of 18 patent filings compared to the prior year.

The patents filed in 2004 were distributed among the various sectors of activity as follows:



The main results achieved by TILAB during 2004 can be summarized as follows.

Innovation of Services

In keeping with the Group's strategy of consolidating the core business of Person to Person communications through ever-more innovative forms of rich call, TILAB supplied two important contributions:

- the **Turbo Call** service is the first service in the world whereby a section of video filmed with the camera incorporated in the cell phone can be combined with a normal UMTS voice call, by simply pressing a button (See What I See). The device was developed by TILAB before the competition thanks to the fact that it already owned two basic technologies (SIP signal and video coding) and by being the first to supply a solution which no vendor yet offers;
- the development in conjunction with URMET of the **second-generation Videotelephone** on the RTG - general telephone network, which offers good-quality video, similar to that of a mobile phone, to any customer. This is helping to change people's perception of wireline telephone services. This development uses the same SIP signal and video coding technologies as the Turbo Call service.

In the strategic product sector now expanding into the business enabled by Convergence and Content-to-Person services, TILAB has made it possible to exploit two important new options:

- encouraging the rapid development of interactive applications which comply with the European MHP (Multimedia Home Platform) standard for Digital Terrestrial Television, by developing the **DTTrun** platform, a software application (Java "middleware") which has been patented and is compatible with every decoder currently available on the national market, and already being used by Telecom Italia Media to create T-government services for Local Public Administrations and "content-related" applications for La 7;
- preparing TIM for entering the newly-emerging "pay-music" market by creating the DRM (Digital Rights Management) component of the **iMusicStore** service, whereby customers can purchase, download and listen to tracks of both high-quality music – in the common MP3 format – and very high quality music in the AAC (Advanced Audio Coding) format which will replace MP3 for young people in the future. This component is not only important but will give rise to a real growth of business.

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Network innovation

With the aim of moving towards both the Triple Play (voice, data and television) offering and enabling the future prospects of Fixed Mobile Convergence, TILAB has defined an innovative **Wireline Network Target Architecture**, consisting of a structure with a fairly low cost, an "All-IP" approach and an innovative solution which exceeds the limits imposed by the best effort policy of IP package carriers while, at the same time, guaranteeing the necessary quality of the individual services.

In this architecture, further enhancement – in terms of simultaneous maximum bit-rate on ADSL, quality and accessibility of the mass clientele – of the existing copper infrastructure continues to play a fundamental role. In 2004, this enhancement made two important steps forward:

- the spread of the **CANTO** system, used by Wireline for the pre-qualification of the wire on 2.5 million active lines. This makes it possible to supply the clientele with an increase in band from 640 kbit/s to 1.2 Mbit/s in the short term, with the prospect of extending it to 4-6 Mbit/s and ADSL2+;
- the creation in conjunction with Pirelli Labs of the new **Access Gateway** (Alice Voice) which enables ADSL customers to use innovative wireless terminals based on VoIP (Voice over IP) technology.

From the point of view of TILAB and the Telecom Italia Group, the network architecture should be structured in such a way as to comprise several levels, each of which supplies a service. This would allow the Operator and its Partners to gradually dominate those functions SEE (Service Execution Environment) and SCE (Service Creation Environment) which are important from the point of view of introducing new services according to the methods and time-scales dictated by market strategies. Hence the partly strategic importance of the release of **STARSIP**, the SIP-based services control platform, developed by TILAB. This platform has been integrated by Italtel in the first version of the NGN (Next Generation Network) for Wireline and is already being used to create the AliceMia and Videotelephone services.

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CENTRALIZED GROUP SERVICES

Centralized Group Services include the operating activities, at virtually a nil profit margin, of the centralized services performed for the Business Units/Central Functions/Companies of the Group. The following table shows operating costs (outside costs and labor costs) incurred during 2004, compared to 2003, restated for purposes of comparison to take into account the different scope of consolidation.

The data takes into account the internal exchanges among the functions of Telecom Italia S.p.A..

OPERATING COSTS

| | 2004 | 2003 restated | Change amount | % |
|---------------------------------------|------------|------------------|------------------|--------------|
| (millions of euro) | | | | |
| Real Estate Activities and Services | 722 | 732 | (10) | (1.4) |
| Central Administrative Services (CSA) | 49 | 50 | (1) | (2.0) |
| Security | 53 | 45 | 8 | 17.8 |
| Other ⁽¹⁾ | 86 | 91 | (5) | (5.5) |
| Total Centralized Services | 910 | 918 | (8) | (0.9) |

⁽¹⁾ Includes Telecom Italia Audit, Telecom Italia Learning Services, TI Finance and other companies.

Centralized Group Services showed a decrease in costs of euro 8 million compared to 2003. This is mainly in reference to "Real Estate Activities and Services" which, although basically in line with the level of TI S.p.A. internal structures (the higher lease payments associated with the Dedalo real estate transaction are absorbed by analogous savings in operational costs), displayed a reduction of euro 10 million. The reduction is due to a decrease in activities, compared to the prior year, by the subsidiary Olivetti MultiServices S.p.A. which, during the last quarter of 2003 sold some properties which had an economic impact on outside costs and revenues. The increase in Security costs can be ascribed to the adoption of higher security standards by offices and installation sites.

The above-mentioned activities and services relate to the planning of the sites and locations of the Group, the design and construction of civil works, the maintenance of properties and technological installation, and also the performance of real estate and general services. In 2004, these services were provided both through Telecom Italia S.p.A. internal structures – essentially for activities conducted on behalf of the Business Units and Functions of Telecom Italia itself – and through the subsidiary Emsa Servizi S.p.A., which directed its activities toward other companies in the Group, and also through the companies in the ex-Olivetti Group which operate in the real estate sector: Olivetti Multi Services S.p.A. (OMS, a wholly-owned subsidiary of Telecom Italia), O & B Costruzioni S.p.A. (a 50.1% - owned subsidiary of OMS), RUF Gestioni S.a.s. (a wholly-owned subsidiary of OMS Holding BV) and Olivetti Systems Technology (a wholly-owned subsidiary of Telecom Italia Finance).

"Facility Management" transactions (Kings Project)

The project for improving the processes connected with "Facility Management" activities, called "Kings Project", led to the following transactions in 2004:

- January 1, 2004: sale of the "Facility Management" business segment to Emsa Servizi S.p.A. by the company Finsiel. This transaction followed the sale of the "Facility Management" business segments of the companies TIM and IT Telecom to the same Emsa Servizi S.p.A. on December 1, 2003;
- February 27, 2004: sale by Telecom Italia and Emsa Servizi of their respective "Document Management" business segments to Telepost S.p.A., a newly-incorporated company in which stakes are held by TNT Mail, Pirelli & C. Real Estate Facility Management S.p.A. and Comdata.

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The new company specializes in the sector of Document Management activities (management and distribution of incoming and outgoing correspondence, archives management, etc.).

On the same date, Telecom Italia and Emsa Servizi signed a contract with Telepost, effective March 1, 2004, for the performance of services by the latter relating to Document Management activities;

- October 28, 2004: sale by Telecom Italia and Emsa Servizi of their respective company organizations made up of the "Maintenance" and "Environmental Services" business segments to the company MP Facility S.p.A. (50-50 joint venture by Pirelli & C. Real Estate Facility Management S.p.A. and Manutencoop Facility Management S.p.A.). The transaction was concluded at the sales price of euro 70 thousand for Telecom Italia and euro 30 thousand for Emsa Servizi and at the amount of euro 3.5 million for Telecom Italia and euro 1.5 million for Emsa Servizi corresponding to the goodwill of the business segments sold. On the same date, a contract was signed by the companies for the outsourcing of these same services by MP Facility S.p.A.. Effective date for the transactions was November 1, 2004.
- December 21, 2004: sale of the Emsa Servizi S.p.A. company complex to Telecom Italia; the transaction became effective on January 1, 2005 and, consequently, the activities which up to that date were performed by Emsa Servizi will be provided by the Telecom Italia structures which operate the centralized services.

Moreover, in May 2004, the telephone exchange activities conducted by the "Real Estate Activities and Services" structures of Telecom Italia and by Emsa Servizi on behalf of the clients TIM, Telecom Italia Information Technology and Finsiel as well as for the same Telecom Italia and for Emsa Servizi were transferred to the Wireline division of Telecom Italia.

The transfer came about by individually reassigning the resources dedicated to such activities.

Fintecna Project

On January 16, 2004, Telecom Italia S.p.A. and Fintecna S.p.A., as agreed in December 2003, signed the contracts for the lease of seven buildings owned by Fintecna S.p.A., as well as a contract containing reciprocal options for the purchase and sale (put/call) of the buildings themselves at a total price equal to euro 72 million.

On June 22, 2004, Telecom Italia S.p.A., after exercising the option right in April 2004, signed the deed of purchase for the seven buildings owned by Fintecna S.p.A. for the agreed contract amount.

On the same date, Telecom Italia canceled the lease contracts relating to these same buildings.

Tiglio Project (Real Estate Funds)

Under the second phase of the Tiglio Project – which calls for an end to the process of appreciating the real estate assets held by Tiglio I and Tiglio II by contributing the assets to real estate funds or concluding individual sale transactions – the following Real Estate Funds were successfully placed on the market during the course of 2004: "TECLA - FONDO UFFICI" - Closed-end Real Estate Fund, "CLOE FONDO UFFICI" - seeded Real Estate Fund intended for qualified investors, "OLINDA FONDO SHOPS" - seeded Real Estate Fund intended for both qualified investors and the public at large and "CLARICE LIGHT INDUSTRIAL - seeded Real Estate Fund intended for qualified investors, all managed by Pirelli & C Real Estate Società di Gestione del Risparmio S.p.A..

Specifically:

- "TECLA - FONDO UFFICI" - placement closed on March 1, 2004. The Fund was seeded by contribution on the part of Tiglio I (45.70%-owned by Telecom Italia) of a real estate portfolio consisting of 65 properties for a total market value of approx. euro 926 million, to which a 15% discount was applied by virtue of their transfer en masse, in addition to a contribution of euro

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25 million in cash. The total offer, net of an indebtedness equal to 60% of the value contributed, amounted to euro 288 million, of which 10% – as a voluntary gesture – was kept by Tiglio I, 2% was subscribed by Pirelli & C Real Estate Società di Gestione del Risparmio S.p.A. as manager of the fund, while the remaining 88% was entirely placed on the market.

- “CLOE FONDO UFFICI” - placed on the market on June 29, 2004. The Fund was seeded by the company “Tiglio I” which contributed 39 properties for a market value equal to some euro 877 million, to which a 15% discount was applied by virtue of their transfer en masse. The total offer, net of a financial indebtedness equal to 60% of the value contributed, amounted to approx. 298 million, of which 5% was subscribed by Pirelli & C Real Estate Società di Gestione del Risparmio S.p.A. as manager of the fund, while the remaining 95% was entirely placed with Italian investors for approx. 70% and with foreign investors for roughly 30%.
- “OLINDA FONDO SHOPS” - placement offered to both qualified investors and the public at large closed on December 6, 2004. The Fund was officially listed on December 9, 2004. The company “Tiglio II” contributed three properties which did not originate from and were not used by the Telecom Italia Group. A total of 42 properties were contributed to the Fund, all of which have a commercial destination and can be converted to such use, for a market value of over euro 562 million. The offer also called for inflows of financial resources earmarked for the purchase of two entertainment centers which took place in December 2004. After these purchases, the Olinda Fund consists of 44 properties for a market value of roughly euro 742 million. The value of the Fund is approx. euro 261 million.
- “CLARICE LIGHT INDUSTRIAL” - placement with qualified investors on December 16, 2004. The Fund was seeded by the company “Tiglio I”, which contributed 27 properties, and the company “Tiglio II”, which transferred 43 properties, for a total market value of euro 221 million, to which a 9% discount was applied by virtue of their transfer en masse. The contribution value was thus equal to euro 201 million and the value of the Fund, after taking into account a financial indebtedness of approx. 55% of the contribution value, was about euro 90 million. The Fund was entirely placed with European investors.

Subsequent to these transactions, in 2004, Tiglio I and Tiglio II proceeded to distribute cash to the shareholders in the form of a reimbursement of its capital (additional paid-in capital) and the repayment of loans. For the Telecom Italia group, total receipts were approx. euro 104 million, of which euro 79 million from Tiglio I and euro 25 million from Tiglio II.

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CORPORATE

Corporate includes the Central Functions of Telecom Italia S.p.A. (Human Resources, Finance Administration and Control, Purchasing, Corporate and Legal Affairs, International Legal Affairs, Public and Economic Affairs, Corporate Development and Investor Relations, International Affairs and General Counsel), Group Communication, which comprise the Brand Enrichment and Communication and Image Functions (including "Italia Project" costs) and the costs of Corporate and Latin America information systems.

The following table shows operating costs (outside costs and labor costs) incurred during 2004 to conduct the above activities, compared to those of 2003, restated for purposes of comparison to take into account the different scope of consolidation and the absence, beginning in 2004, of the research and development costs transferred to TILAB.

The data includes costs recharged for the activities performed by Centralized Group Services.

| OPERATING COSTS | | | | |
|---------------------|------------|------------------|-----------|-------------|
| (millions of euro) | 2004 | 2003 Proforma | Change | |
| | | | amount | % |
| Central functions | 345 | 343 | 2 | 0.6 |
| Information System | 146 | 88 | 58 | 65.9 |
| Group Communication | 48 | 47 | 1 | 2.1 |
| LATAM | 28 | 22 | 6 | 27.3 |
| Corporate | 567 | 500 | 67 | 13.4 |

Corporate costs rose by euro 67 million due mainly to an increase of euro 58 million for the costs to develop the information systems.

The increase in the costs for the information systems is mainly attributable to the projects begun in 2003 (for the rationalization and standardization of architecture and infrastructure solutions also with the intention of improving computer and data security and the running of the dedicated functional systems, etc.), which will convey their full economic impact in 2004.

The increase in staff function costs can principally be ascribed to labor costs that are partly compensated by the savings on professional and consulting services.

■ OTHER SUBSIDIARIES

Telecom Italia Finance S.A.

Held by: Telecom Italia 100.00%

The company operates as an international treasury function to support the financial needs of the foreign companies of the Telecom Italia Group.

In October 2004, the Extraordinary Shareholders' Meeting of Telecom Italia Finance voted to:

- reduce share capital to absorb the accumulated deficit at June 30, 2004, euro 729,844,921;
- further reduce share capital to set up a non-distributable reserve of euro 390,627,449;
- increase share capital by euro 499,999,996 and set up a reserve for euro 1,005,671,163. This increase was subscribed to by Telecom Italia S.p.A. through the contribution of all the shares held in Edotel S.p.A..

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Furthermore, the following should be mentioned:

- on January 1, 2004, the merger of Olivetti International S.A. (OISA) in Telecom Italia Finance became effective for accounting and tax purposes. This merger was approved by the respective shareholders' meetings of the two companies on February 20, 2004;
- on June 1, 2004, Olivetti Finance NV (OFNV) was merged in Telecom Italia Finance which took over all the assets and liabilities;
- in July 2004, the companies Olivetti International NV and Olivetti International Finance NV, wholly-owned subsidiaries of Telecom Italia Finance, were put into liquidation;
- on December 20, 2004, the wind-up of the subsidiary RAP SA was closed.

Telecom Italia Capital S.A.

Held by: Telecom Italia 99.999%, Telecom Italia Finance 0.001%

The company operates as an international treasury function to support the financial needs of the foreign companies of the Telecom Italia Group.

On October 8, 2004, Telecom Italia Capital floated a new bond issue for a total of USD 3,500 million to fund the financial requirements of the Group companies, including the Parent Company. Moreover, the maturity of the loan made in 2003 to Telecom Italia for USD 4,000 million was changed from short to long term.

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■ DISPUTES, LITIGATION AND LEGAL PROCEEDINGS PENDING

The main legal and arbitration proceedings in which companies of the Telecom Italian Group were involved as of 31 December 2004 are described below. Except where explicitly mentioned, provisions have not been made, either for want of definite and objective grounds for doing so or because a negative outcome of the dispute is considered unlikely.

■ POSTE ITALIANE

Appeals are pending from the Rome Civil Court's ruling in favour of the Company regarding payments for the disputed supply of products and services by Olivetti to Poste Italiane. The actions involve events dating back to the late 1980s and early 1990s; the compensation sought currently amounts to approximately euro 50 million.

■ PERSONAL COMPUTER BUSINESS

In connection with the disposal by Olivetti of its personal computer business in 1997, actions brought by the following parties, among others, are pending:

- Centenary Corporation and Centenary International (purchasers of the business unit) for damages of approximately euro 129.1 million;
- some former employees of OP Computers S.p.A. (the special-purpose entity to which the business was transferred pending the sale), to annul the contracts transferring the business unit and consequently to obtain recognition of the continuity of their employment with Olivetti and the award of pay differences and damages amounting to approximately euro 212 million. In March 2004 the majority of the appellants accepted the settlement proposed by the Company. In June 2004 an initial ruling was made in favour of the Company, whose financial statements continue to include a specific reserve.

■ GALACTICA

In 2001 and 2002 a complex dispute arose with the Internet Service Provider Galactica S.p.A. (now Servinternet S.p.A., in liquidation) over the non-renewal of an agreement for testing a flat-rate Internet access service. Although two precautionary petitions had already been rejected, Servinternet S.p.A. has claimed damages of approximately euro 90 million. The arguments formulated in the trial do not appear to justify making a provision.

■ TELEQUE COMMUNICATIONS

On 6 November 2002 Teleque Communications S.p.A., a company operating in the field of prepaid cards for international telephony services, brought an action against Telecom Italia before the Rome Court of Appeal for unfair trade practices, claiming damages of euro 65 million. In particular, Teleque Communications (which went bankrupt in December 2003) claimed that Telecom Italia had gained a competitive advantage by imposing additional costs for the supply of interconnection services that it did not charge to its own final customers in the field of prepaid international services.

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The action, interrupted following the Olivetti-Telecom merger, has been revived by the trustee in bankruptcy.

Considering the opinion of the Company's lawyers and in view of what has emerged so far in the proceeding, it has not been deemed necessary to make a provision.

■ VODAFONE

In July 2003 Telecom Italia initiated an arbitration proceeding with Vodafone to obtain damages in relation to the radiomobile operator's decision to bar its customers from access to the Company's "12" information services between August 2002 and April 2003.

In particular, Telecom Italia is seeking compensation of approximately euro 38.7 million. Vodafone contends that its conduct was licit and has filed a counterclaim for an identical amount.

■ DE AGOSTINI

On 28 June 2004 a settlement was reached in the dispute concerning the framework agreement executed on 20 September 2000 by Seat Pagine Gialle S.p.A. (now Telecom Italia Media) and its subsidiaries with companies of the De Agostini Group regarding, among other matters, the purchase of 40% of Finanziaria Web (which holds 66% of Matrix, owner of the Virgilio portal). Under the terms of the settlement, which composed all the differences between the parties, De Agostini Invest transferred its entire equity interest in Finanziaria Web to Telecom Italia Media (which already controlled the company) for a consideration of euro 287 million, in place of the price of euro 700 million originally stipulated. In addition to the purchase price, it was agreed that euro 38 million would be paid to De Agostini Invest as reimbursement for expenses incurred in making good the losses and recapitalizing Finanziaria Web from July 2001 on.

The parties have no further claims on each another, having withdrawn the petitions and arguments submitted to the arbitration proceeding that began in 2001.

The effects of the transaction have been included in the 2004 financial statements.

■ CECCHI GORI

In connection with the complex legal dispute initiated by the Cecchi Gori Group against Seat (now Telecom Italia Media), the following cases remain pending in the ordinary courts:

- before the Rome Court of Appeal:
 - appeal from the ruling that rejected the petition for annulment of the resolution approved on 11 August 2000 by the extraordinary shareholders' meeting of Cecchi Gori Communications (now Holding Media Communications, which controls the television broadcaster "La7") concerning some amendments to the company's bylaws;
 - appeal from the ruling that rejected the petitions for annulment of the resolutions approving the annual report and the balance sheet of Cecchi Gori Communications for the year ended 31 December 2000 on the grounds that Seat was not entitled to vote the shares owned by Cecchi Gori Media Holding that it held in pledge and for alleged excess and abuse of power. Considering the losses shown by the balance sheet in question, the shareholders' meeting of 27 April 2001 cancelled and then reconstituted the company's capital, all of which was subscribed by Seat;
- before the Milan Court: an action for damages for a tort resulting in injury to Fin.Ma.Vi, Cecchi Gori Media Holding and Vittorio Cecchi Gori from the supposedly illegitimate conduct of Seat

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and of the directors it designated to the board of Cecchi Gori Communications having the alleged aim of ousting the majority shareholder, Cecchi Gori Media Holding;

- before the Milan Court of Appeal: appeal from the ruling issued by the court of first instance on 21 January 2004 rejecting, on grounds of merit, the petition for annulment or cancellation of the deed under which the Cecchi Gori Communications shares belonging to Cecchi Gori Media Holding were pledged as security.

It is to be noted that so far all the decisions of the ordinary courts, both in precautionary and in trial proceedings, have been favourable to TI Media. Similarly, the arbitration proceeding, which originated from the arbitration clause of the agreements between Seat and the Cecchi Gori Group and examined all the material aspects of the affair and, in particular, the facts adduced for the new trial pending before the Milan Court for breach of contract, rejected all the requests formulated by the parties and, not having been appealed, has become final.

■ FINSIEL - CONTRACT AWARDED BY THE MINISTRY OF EDUCATION AND RESEARCH

In the first quarter of 2003 a temporary consortium formed by IBM Italia (principal), Finsiel, Pirelli & C. Real Estate Facility Management and other firms ("RTI IBM") was awarded the service contract put out to tender by the Ministry of Education and Research for the development and management of the Education Information System. The value of the contract was euro 231 million, with Finsiel's share amounting to approximately euro 85 million.

Following an appeal by a temporary consortium headed by Electronics Data System Italia S.p.A. ("RTI EDS"), which came in second in the tender, the Lazio Administrative Tribunal annulled the contract award.

The State Council subsequently rejected the appeal from the annulment and ruled that the admission of RTI IBM to tender had been illegitimate. Moreover, deciding on an appeal presented by another bidder (EDA - Enterprise Digital Architects S.p.A.), the State Council annulled most of the evaluations made in connection with the tender.

On 7 April 2004 RTI IBM filed an appeal with the Joint Sections of the Court of Cassation, asserting that administrative justice had overstepped its jurisdiction in matters of legitimacy, and the Ministry, agreeing with the objection, joined the appeal by means of the State Solicitor's Office. Nevertheless, and notwithstanding an appeal to the Lazio Administrative Tribunal, the Directorate General for Information Systems of the Ministry annulled the contract award to RTI IBM and the State Council ordered a new evaluation of the bids submitted by EDA and RTI EDS. Upon completion of this procedure, the contract was awarded on 21 December 2004 to RTI EDS, which consequently succeeded to RTI IBM in the service contract.

EDA has petitioned against this decision. RI IBM has also filed a petition in the proceeding before the Administrative Tribunal.

* * *

In the past the Ministry of Finance had entrusted SO.GE.I. - Società Generali Informatica - S.p.A. under a franchise with the development and integration of the tax authorities' central and local IT structures and with running and maintaining them. At the time Finsiel held 100% of SOGEI's capital.

With a contract executed on 1 July 2002 Finsiel transferred the entire capital of SOGEI to the Ministry's Department for Fiscal Policies.

On 13 January 2005 the Department notified Finsiel, in accordance with the contract of 1 July 2002 for the sale of 100% of SOGEI's capital, that the Lazio regional attorney's office of the State

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Audit Office had claimed Finsiel and 142 banks were responsible for an alleged loss of tax revenue in 2000 as a result of non-compliance with ministerial instructions concerning the collection of the government VAT account fees for 1997. SOGEI is requested to pay euro 25,408,295.64 out of a total of euro 83,601,488.27.

In particular, the Department has claimed that under the terms of the sale contract any prior-year liability that arises for SOGEI in the case referred to above should be remitted to the Department by Finsiel, as the party that sold the 100% interest in SOGEI.

Under the terms of the contract Finsiel has until 14 March 2005 to challenge the request for compensation. The Department will then have ninety days in which to commence arbitration proceedings to settle the dispute, as provided for in the contract.

It should be noted that, with reference to the proceeding initiated by the State Audit Office, the matter is not at present the subject of a formal action but is still at the investigative stage, while, with reference to Department's request for indemnification, no court action is pending.

■ UNIVERSAL SERVICE

The following actions remain pending in the complex challenge by some operators to the Communications Authority's decisions concerning the universal service net cost sharing mechanism:

- the petition submitted by Vodafone to the Lazio Administrative Tribunal for annulment of the decision with which the Authority, in renewing the proceeding concerning the application of the universal service net cost-sharing mechanism for 1999, recalculated the amount of Vodafone's contribution;
- the petitions submitted respectively by Vodafone to the Lazio Administrative Tribunal and by Wind to the Head of State for annulment of the decision governing the same cost sharing mechanism for 2000. Vodafone has requested that the issue be referred as a preliminary matter to the European Court of Justice for a ruling on the interpretation of the Community directives;
- The petition by Vodafone to the Lazio Administrative Court for annulment of the note dated 29 April 2003 with which the Ministry of Communications enjoined Vodafone to pay the contribution for the year 2000 for the financing of the universal service, as determined by the Communications Authority.

■ LEVY PURSUANT TO ARTICLE 20.2 OF LAW 448/1998

The decisions of the Lazio Administrative Tribunal granting the petitions submitted by Telecom Italia and TIM and annulling a regulation issued with a ministerial decree of 21 March 2000 were published on 3 January 2005. The regulation, implementing Article 20 of Law 448/1998, provided for a levy to be imposed on telecommunications operators based on their previous year's sales for a period of five years beginning 1 January 1999.

Following the European Court of Justice's decision of 18 September 2003 on similar appeals by Albacom and Infostrada, which declared the levy to be incompatible with Community law, the Telecom Italia Group had already reversed euro 1,465 million of liabilities (payables and reserves for risks and charges) relating to the financial years 2000, 2001 and 2002.

In the light of the ruling by the Lazio Administrative Tribunal annulling the regulation on grounds of illegitimacy, euro 546 million, plus euro 74 million of interest paid by the Group in respect of the levy for the 1999 financial year, have been included in income.

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The ruling of the Lazio Administrative Court confirms that, by definitively sanctioning the levy's incompatibility with Community law, the decision of the European Court of Justice excludes any application of the rule to the contrary, thus affirming the Group's claim for restitution.

* * *

Petitions by Telecom Italia and TIM are still pending before the Lazio Administrative Court for ascertainment of the right not to pay any amount as a licence fee for 1998 and to obtain restitution of the euro 529 million already paid. The request is based on the illegitimacy of the provisions of Article 21 of Presidential Decree 318/1998 that extended the effectiveness of the licence fee even after the entry into force of Directive 97/13/EU and the expiry of the time limit for its transposition into Italian law. Following the Court of Justice's above-mentioned decision of 18 September 2003, additional reasons based on the levy's incompatibility with Community law were submitted on 9 February 2004, to corroborate the arguments set forth in the main proceeding.

* * *

Also pending is the petition submitted by Telecom Italia to the Lazio Administrative Tribunal for annulment of the note dated 9 July 2003 with which the Ministry of Communications challenged the non-inclusion of some items of income in the basis of assessment for the licence fee for 1997 and 1998. The difference deriving from the recalculation would amount to euro 31 million for 1997 and euro 41 million for 1998. The petition follows others the Company had already lodged concerning the licence fee computation method in connection with the gradual liberalization of the telecommunications sector. A provision has been made for the amounts involved in these disputes.

Lastly, an appeal by TIM from the ministerial decisions on the checking of the licence fee for the years 1995, 1996, 1997 and 1998 is pending before the Lazio Administrative Tribunal. The contested amounts have been set aside in a reserve.

■ ALLEGED VIOLATIONS OF ANTITRUST LAW

On 15 November 2004 the Antitrust Authority concluded its proceeding A 351 (opened on 5 June 2003) by finding that Telecom Italia had committed abuses of dominant position in violation of Article 3 of Law 287/1990. Between 2001 and the date of the decision, the Authority determined that Telecom Italia had abused its dominant position by:

- applying contractual conditions to corporate users containing exclusive agency clauses, penalties for failure to fulfil spending targets and clauses having equivalent effects to so-called English clauses; and
- establishing economic and technical conditions for business customers that competitors could not replicate and that constituted discriminatory practices in the relevant markets for intermediate services insofar as Telecom Italia applied economic and technical conditions to its competitors that were disadvantageous compared with those it applied to its own commercial divisions.

Consequently, the Antitrust Authority imposed a euro 152 million fine on Telecom Italia and ordered the Company to desist immediately from the competition-distorting conduct referred to above, and to inform the Authority of the measures taken to put an end to the infractions within 90 days of the notification of the order.

The decision of the Antitrust Authority did not take into account the mandatory opinion issued by the Communications Authority, according to which the remedies that Telecom Italia had proposed to its competitors in the course of the proceeding (and which were already in force for operators who accepted them) were effectively consistent with the objective of significantly accelerating the liberalization of the market.

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On 31 December 2004 Telecom Italia lodged an appeal from the Antitrust Authority's decision with the Lazio Administrative Tribunal, requesting annulment of the measure and interim suspension of its effects. In its appeal, Telecom Italia argues that the Authority's decision was based on an investigation that failed to establish the facts of the Company's responsibility for the alleged abuse of dominant position. In particular, the Company contests the ostensible need to refer to the interconnection price list in preparing offers to large customers, the Authority's failure to identify large customer as a separate relevant market, its failure to consider both the change in the applicable legislation during the investigation and the remedies offered by Telecom Italia. In the hearing of 12 January 2005, the judge adjourned discussion of the petition for suspension until 16 February 2005, deciding that it would be dealt with together with the main proceeding.

Following the latter hearing, the Lazio Administrative Tribunal granted the suspension exclusively in relation to the fine. On 22 February 2005 the Lazio Administrative Tribunal filed the order issued pursuant to the decision. The order simply states that Telecom Italia's appeal is partially granted; it provides no further information for evaluating the practical consequences of the decision. Since it will be possible to assess these only after the decision is filed, an appropriate amount has been set aside in the 2004 financial statements.

* * *

Acting on the complaint filed by competing operators, in 2003 the Communications Authority cited Telecom Italia for pursuing commercial strategies detrimental to the development of the market (Resolution No. 179/01/CONS) and initiated sanction procedures. That provision and the subsequent resolutions have been challenged; the appeals are pending before the Lazio Administrative Tribunal.

■ CHALLENGES TO MEASURES ADOPTED BY THE COMMUNICATIONS AUTHORITY

At the end of December 2004 Telecom Italia appealed to the Lazio Administrative Tribunal for the annulment and interim suspension of Communications Authority Resolution No. 15/04/CIR of 3 November 2004 ("Assignment of the rights to use the numbers reserved to subscriber information services").

The Authority's resolution follows up its Resolution No. 9/03/CIR of 3 July 2003.

The latter updated the Numbering Plan in the telecommunications sector, establishing that the number "12XY" would be assigned to subscriber information services. Accordingly, these services will have a number composed of the digits "12" followed by another two digits, different for each operator. The resolution provided that the implementing timetable, subjective requirements for the rights of use and the procedure for assigning the numbers reserved to subscriber information services would be established in a subsequent resolution.

The Authority has set a very tight timetable for the cessation of all subscriber information services provided with numbers other than "12XY" (including services accessed with the addition of "4" (e.g. "412", recently added to the traditional "12") and has also established the procedures for informing customers about the "migration" of these services to other numbers. Telecom Italia considers these procedures discriminatory, since the Company is not free to use its discretion in advertising the new number the service will migrate to.

According to Telecom Italia, the Authority's decisions also entail substantial economic losses for the Company, including those stemming from the fact that the cessation of services on the number "412", the shutting down of the number "12" and the mechanism for assigning the new numbers (which for Telecom Italia involves the use of totally different numbers from those to which its customers are accustomed) are likely to cause customers to shift to numbers of other operators.

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■ GREECE

The arbitration proceeding initiated in 1996 at the Paris International Chamber of Commerce by Mobitel, former distributor of STET Hellas (now Tim Hellas), concluded in August 2004. Mobitel had requested to be paid fees on the incoming traffic of customers procured by the Greek mobile operator and compensation for alleged violation of the exclusivity clause of the distribution contract.

The arbitration award ordered STET Hellas to pay the opposing party approximately euro 31 million, including reimbursement of costs and legal expenses, of which almost half for interest accrued from the dates to which the claims referred up to the date of the award. The amount was paid in the last quarter of the financial year.

In the first half of 2004 the Greek subsidiary had made a provision against the risk of an unfavourable outcome.

* * *

The arbitration proceeding concerning the cancellation for non-performance of the contract with Delan Cellular Services S.A. for the development of prepaid services remains pending. The proceeding was initiated in Athens in February 1998, with Delan claiming damages of approximately euro 79 million.

During the inquiry STET Hellas contested the merits of the opposing party's claim and requested the Athens Court to review the procedural conduct of the arbitration board, which had initially refused to order an expert opinion on the fairness and reasonableness of the amounts claimed by Delan for damages. STET Hellas also reported the violation of some rules of procedure during the arbitration.

The arbitration board thereupon ordered the expert opinion that STET Hellas had requested; it was filed in April 2003.

The chairman of the arbitration board resigned in the second half of 2004 and the appointment of a replacement is still pending.

Calculating the risk deriving from the dispute, STET Hellas has made appropriate provisions to its reserve for risks and charges.

■ TELEKOM SRBIJA

At the end of May 2003 OTE, a Greek telecommunications company, notified two requests for arbitration to Telecom Italia for alleged breaches of, respectively, the bilateral agreement of 4 June 1997 and the shareholders' agreement of 9 June 1997 in connection with the sale to PTT Serbia of 29% of the capital of Telekom Srbija (the sale was concluded on 7 July 2003).

In particular, OTE claims that Telecom Italia: (i) violated its right of pre-emption under the agreement of 4 June 1997 (the right, which was subject to the consent of the Serbian government, was denied in the case in question); (ii) did not fully pay the management fee percentage owed to it under the technical assistance contract referred to in the agreement of 4 June 1997; and (iii) infringed the shareholders' agreement, as Telecom Italia was not allowed to transfer its holding without the consent of the other shareholders.

OTE also notified two arbitration requests to PTT Serbia, for different reasons.

Under the sale agreements, PTT Serbia relieved Telecom Italia of every responsibility towards OTE deriving from the shareholders' agreement, the technical assistance contract and any other

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related contract. Nevertheless, Telecom Italia International has made a provision as a precautionary measure.

At the present time, further to discussion aimed at reaching a settlement, OTE submitted a request for termination of the arbitration proceedings, to which the other parties have agreed. The closing order by the Arbitral Tribunal is expected to be issued soon.

■ TURKEY

In February 2004 - at the time of the merger between Is-TIM and Aycell, which created the company TT&TIM (now AVEA) - an agreement was reached with the Turkish telecommunications authority to withdraw from the arbitration proceeding that Is-TIM had initiated in March 2003 against the Turkish authority for alleged violation of the terms of the licence to operate radiomobile service obligating the Turkish authority to create and maintain market conditions likely to permit effective competition among operators.

■ MEDITERRANEAN NAUTILUS

In October 2003 FTT Investments (of Israel, minority shareholder of Med Nautilus S.A.) notified a request for international arbitration to obtain annulment of the contract signed in March 2001 with Telecom Italia International, Telecom Italia and Med Nautilus S.A. for the transfer from Telecom Italia International to FTT of 30% of the capital of Med Nautilus S.A.

FTT invoked invalid consent owing to fraud on the part of the Telecom Italian Group or, in any event, owing to its having been misled as to the subject of the contract. It requested restitution of the price paid (approximately \$98 million) plus interest, without detriment to its right to put forward additional claims. In particular, FTT asserts it was induced to make the purchase on the basis of a misrepresentation arising from the omission of information about the existence of a put option written by Med Nautilus S.A. for the shares of Med Nautilus Ltd. held by the minority shareholders.

Telecom Italia asked to be excluded from the arbitration proceeding inasmuch as FTT did not initially make any specific demand in its regards.

In May 2004 FTT filed further arguments, formalizing a request to extend to Telecom Italia and Med Nautilus S.A. the demand for restitution of the purchase price that it had initially made solely vis-à-vis the seller, Telecom Italia International. The arbitration board reserved its right to decide on the procedural admissibility of the request when it decides on the merits of the dispute.

In December 2004 the parties asked the arbitration board to suspend the procedure to allow time for talks aimed at reaching a negotiated settlement.

An amount has been set aside in the 2004 financial statements in relation to the probable effects of the settlement.

■ BRAZIL

In April 2001 Brasil Telecom brought two actions before the Civil Court of Rio de Janeiro against, respectively,

- Telecom Italia and Telecom Italia International, and
 - two directors appointed by Telecom Italia International,
- for alleged injury to Brasil Telecom as a result of the acquisition of Companhia Riograndense de

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Telecomunicações (CRT) and the company's failure to participate in the auction of SMP (Serviço Móvil Pessoal) radiomobile licences.

Brasil Telecom contends it was injured by abusive conduct on the part of Telecom Italia and Telecom Italia International and by impediments created by the directors appointed by Telecom Italia International, who allegedly (i) interfered with the negotiations for the purchase of CRT and with the setting of the purchase price, and (ii) favoured TIM's investee companies in the award of the SMP licences.

Both cases are still in the investigative phase.

* * *

The complex dispute between Telecom Italia International and Techold and Timepart, its partners in Solpart Participações (controller of Brasil Telecom through Brasil Telecom Participações), remains open. The dispute concerns the agreement concluded on 27 August 2002 between Telecom Italian International and Techold and Timepart for the temporary reduction from 37.29% to 19% of the Group's stake in the ordinary capital of Solpart Participações and the temporary suspension of its governance rights, with the aim of overcoming a regulatory impediment to the start of TIM's commercial operations in Brazil.

In detail:

- in December 2003 Techold and Timepart advised Telecom Italia International and Telecom Italia of a request for international arbitration before the Paris International Chamber of Commerce. The aim of the request is essentially to have the clauses of the 2002 agreement regarding the reacquisition of the transferred shares declared "non-operational" and to permit the exercise of the governance powers provided for in the existing Solpart shareholders' agreement. The investigative phase of the proceeding opened in 2004;
- in January 2004, given the refusal by Techold and Timepart to accede to Telecom Italia International's request to exercise its repurchase option and for the restoration of its governance powers (which the Brazilian telecommunications regulatory authority, Anatel, had authorized subject to some conditions), a petition was filed with the Court of Rio de Janeiro for an injunction protecting the right to discharge of the defendants' contractual obligations, which under Brazilian law are also binding on Solpart, Brasil Telecom Participações and Brasil Telecom;
- while the precautionary proceeding was pending, Telecom Italia International petitioned the court to examine the merits of the case and to issue a provisional decree that would anticipate the effects of the final ruling. In November 2004 the court issued the provisional decree, ordering Techold, Timepart, Solpart, Brasil Telecom Participações and Brasil Telecom to make Telecom Italia International's right to exercise its governance powers effective but deferring judgment of the question of the repurchase option until the ruling on the merits of the case. In the event, the decree's effectiveness has been suspended following appeals filed by, respectively, Techold/Timepart/Solpart and Brasil Telecom Participações/Brasil Telecom.

Meanwhile, in July 2004 the association of small shareholders' of listed Brazilian telecommunications companies (Animec) initiated an administrative proceeding in which it requested the precautionary suspension of the antitrust authority's decision of 30 June 2004 approving the repurchase of the shares sold to Techold and Timepart and the restoration of Telecom Italia International's governance rights. The request was rejected both in a first ruling and upon appeal.

* * *

In April 2004 Brasil Telecom brought an action before the Court of Rio de Janeiro claiming abuses of the control power exercised by Telecom Italia International. According to the plaintiff, the abuses in question led in 1999 to the failure to purchase the operator VICOM and to delay in the granting of a loan by BNDES (Banco Nacional de Desenvolvimento Economico e Social), and prevented the issue of debentures in 2001.

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Brasil Telecom neither quantified the damages it sought nor provided elements for such quantification, leaving the matter to the judge's discretion.

* * *

In January 2004 TIM Telecomunicações Instalações e Montagem Ltda, a Brazilian company with registered office in the State of Goiás that supplies and installs telecommunications equipment, cited TIM Brasil Serviços e Participações SA, Tim S.p.A. and Brazil's National Institute for Industrial Property (INPI) before the Federal Court of Rio de Janeiro with a view to securing the annulment of the trademark registrations bearing the name "TIM" that had been granted to the Group between 2000 and 2003 and a prohibition on their use in Brazilian territory. The plaintiff also petitioned for damages equal to 10% of the TIM Group's sales and service revenues in Brazil from the start of its activities there and for a temporary injunction against the use of the trademark.

TIM Telecomunicações Instalações e Montagem Ltda bases its request on its ownership of exclusive rights to the name "TIM", deriving from the fact that its corporate name was registered before the date on which the Group filed for registration of the TIM trademark.

The TIM Group has rejected the plaintiff's claims, observing that there is no risk of confusion as the parties operate in different sectors. It has also pointed to the trademark's established international reputation as refuting the scope-for-confusion argument of the plaintiff, formerly a supplier of the Brazilian parent company TIM Brasil Serviços and Participações SA. and its subsidiaries. Furthermore, it has noted that the plaintiff applied to register the trademark "TIM" under the business sector "telecommunications" only after the same trademark was already being used and had been filed by the Group, without TIM Telecomunicações Instalações e Montagem Ltda even operating in that business sector.

The judge, who has already declared the investigative phase closed, decided against the issue of a temporary injunction.

■ VENEZUELA

In April 2004 TIM International and its partners in Digitel reached a settlement in litigation over the measures making good Digitel's losses for 2002. Under the terms of the agreement, TIM International undertook to purchase the stakes of all the minority shareholders (corresponding to 32.88% of Digitel's capital).

Finalization of the agreement was subject to the withdrawal of all claims and actions against TIM/Digitel, notably the arbitration proceeding initiated by the shareholder Venconsul under the rules of the International Chamber of Commerce.

The agreement was executed on 1 July 2004, ending the complex dispute.

■ ETEC S.A.

In August 2002 Bancomext, an entity controlled by Banco de México, Mexico's central bank, brought an action against the Cuban telecommunications operator EtecSA (in which Telecom Italia International holds a 27% equity interest) and its majority shareholder Telefonica Antillana SA ("Telan"), petitioning the Court of Turin for the precautionary sequestration of assets belonging to Telan and EtecSA. The writ of sequestration was executed on assets amounting to approximately euro 43 million.

Bancomext acted on the basis of agreements (a loan contract and a credit-facility contract) signed with the two Cuban companies under which a part of the dividends belonging to Telan would be held in escrow as security for repayment of a \$350 million loan from Bancomext to Banco Centrale de Cuba ("Bancuba"), Cuba's central bank. The action was lodged after the Cuban

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government, with a decree law issued in April 2002, prohibited EtecSA and Telan from taking any steps to satisfy the above-mentioned claim and assumed, via Bancuba, all the commitments and guarantees vis-à-vis Bancomext.

In response to Bancomext's action, EtecSA and Telan proposed arbitration before the Paris International Chamber of Commerce with a view to establishing: (i) the illegitimacy of Bancomext's claim to hold EtecSA jointly responsible with, or guarantor of, Telan for the restitution of the loan, and (ii) the exempting nature of the above-mentioned decree law with respect to the restitution of the loan. The request for arbitration caused the action brought by Bancomext to be suspended.

The arbitration award of August 2004 determined that EtecSA was neither a debtor of Bancomext nor a guarantor of Telan, but it also established:

- that the Cuban decree law did not constitute valid grounds of *force majeure* relieving EtecSA from the obligations deriving from the loan contract and credit-facility contract with Bancomext and Telan; and consequently
- that EtecSA must restore the mechanism envisaged in the credit-facility contract by transferring the dividends belonging to Telan to the escrow account, with retroactive effect as of April 2002.

In October 2004 the Board of Directors of EtecSA, with the abstention of the directors appointed by Telecom Italia International, decided to appeal the arbitration award before the French courts.

In the meantime Telecom Italia International (in possession of a letter from the Cuban government relieving it of any possible injury arising from the award) has asked the Cuban government, Bancuba and Telan to take every necessary step to avoid harmful consequences for its affiliate EtecSA, reserving its right to take protective action.

■ IRIDIUM

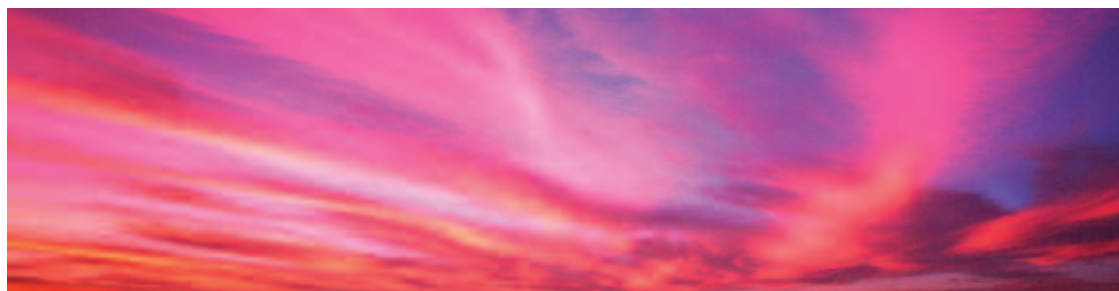
In June 2000 Chase Manhattan Bank (now JP Morgan Chase Bank) filed an action in the US District Court for the District of Delaware against the shareholders of Iridium LLC, seeking discharge of the obligation to proceed with a capital increase that had been entered into to ensure the repayment of a \$800 million loan granted to Iridium Operating LLC, a subsidiary of Iridium LLC. As part of the petition, the plaintiff asked that Telecom Italia be ordered to pay its presumed share of the capital increase (approximately \$7.5 million), even though Telecom Italia had disposed of its corresponding interest in Iridium Italia before the loan was disbursed. The court issued an ordinance that rejected the defences pled by the parties, including Telecom Italia's request to be excluded from the proceeding), considering the case ready for judgment even without a hearing. The judgment has not yet been issued.

Pending the conclusion of the main proceeding, the district court suspended the separate action brought in January 2003 by Chase Manhattan Bank against Iridium Italia (now in liquidation, 30% owned by Telecom Italia, the remainder equally divided between TIM and Telespazio).

Provisions have been made in respect of the plaintiff's claims.

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■ SUSTAINABILITY SECTION



CONTEXT

"Telecom Italia Group proposes Sustainability as a business value, a tool for programming, management and control".

For the past eight years Telecom Italia Group has published a special report to evaluate the satisfaction of the Stakeholders on which the Group depends and, at the same time, influences by its own activities: Customers, Suppliers, Competitors, Institutions, the Environment, the Community, Human Resources and Shareholders.

For the past three years The Annual Report has included the Sustainability section in order to confirm the Group's commitment to report on its financial and non-financial performance.

The paragraph on Shareholders also contains information on Financial Communications and the Safeguarding of Privacy.

■ ACKNOWLEDGEMENTS

- In "The Global Reporters 2004 Survey", which was carried out under the aegis of ONU and the rating agency Standard & Poor's, Telecom Italia SpA was confirmed to be among the 100 best companies in the world in terms of the quality of its reporting on Sustainability.
- Telecom Italia SpA has been selected as an index component for two indexes managed by Dow Jones:
 - Dow Jones Sustainability World Indexes (DJSI World) which include 300 companies from 24 countries, Sustainability leaders at world level.
 - Dow Jones STOXX Sustainability Indexes (DJSI STOXX) which include 167 companies from 13 countries, Sustainability leaders at European level.
 The companies admitted are grouped in clusters according to the registered score. In both indexes, Telecom Italia has been included in the first cluster.
- Telecom Italia and TIM have been confirmed in the following indexes:
 - FTSE4Good Global which includes the first 100 worldwide companies as measured by their market capitalization (FTSE4Good Global 100 - tradeable index);
 - FTSE4Good Europe which includes the first 100 European companies as measured by their market capitalization (FTSE4Good Europe 50 - tradeable index);

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- ESI (Ethibel Sustainability Index): the Global index includes 180 securities, while the European index includes 84 securities;
- E.Capital Partners: the Global index consists of 300 securities, while the European index consists of 150 securities;
- ASPI (Advanced Sustainable Performance Index) Eurozone consists of 120 companies selected by the French agency Vigeo.

■ RESULTS

- The first stage of the study of the Group's intangible assets, carried out in collaboration with Bocconi University, confirmed the link existing between the financial and the non-financial performance. The results of the research were presented to the scientific Community and to financial analysts at the Bocconi University on November 24, 2004.
- The Global Compact Leaders Summit, chaired by Kofi Annan, took place in New York on June 24, 2004 and was attended by 260 corporations, 19 state governments, the European Commission, and 63 company and workers Associations. During this Summit the 10th principle against corruption was introduced. Telecom Italia and TIM undersigned the agreement and produced two proposals of their own which were taken into consideration:
 - the integration of criteria for the evaluation of the so-called "intangibles" between Europe and the USA;
 - the creation of a permanent Forum where "corporate citizenship" can be discussed.
- Telecom Italia Media also adhered to the Global Compact. To date, 1,800 important corporations all over the world have subscribed to the Global Compact.
- The Group, together with 25 TLC European operators, signed the "Sustainability Charter", a document that represents the evolution of the Environmental Charter, launched in 1996, which had already obtained wide recognition at an international level.
- The appointment of Environmental Managers for Wireline, Mobile and Internet & Media Business Units has been formalized. The Environmental Manager supervises the impact of the business processes on the environment and supports the related reporting system.
- From January 1, 2004, all important investment projects proposed by the companies of the Group have been accompanied by a "Sustainability Form" in which the impact of the investment on 12 chosen areas of interest is evaluated. The evaluations have been recorded and studied to bring the 2005-2007 strategic guidelines up to date.
- Specific actions have been carried out to communicate Sustainability outside and inside the Group.
- A specific Training Plan has been implemented within the Group with the aim of making the culture of Sustainability more widely known.
- Among the various international activities in support of Sustainability, the Group Sustainability department actively participated in the following:
 - ETNO (European Telecommunications Network Operators' Association) General Assembly which took place in Sarajevo on November 18-19, supporting the ETNO's adhesion to the Global Compact principles;
 - first European Conference on Telecommunications and Sustainability which took place in Budapest on November 25-26, where the study on the Group's intangible assets was presented;
 - Workshop on the Sustainability Reporting, which took place in London on November 1-2 during which the "Global Reporters 2004 Survey of Corporate Sustainability Reporting" was presented;
 - annual Conference of the European Environmental Bureau on the safeguarding of the environment, which took place in Brussels on September 20 and was attended by the European Commission's and European Parliament's members; during the Conference the new European strategy on sustainable development was presented.

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■ COMMITMENTS

For the year 2005 six objectives have been defined at Group level: Reliability, Sustainability, Cash generation and Profitability, Innovation and Competitiveness, Focus on customers, Strategic and Operational Flexibility.

Among the 2005 focus points, particular attention will be given to the customer's satisfaction and the quality of the service.

The second phase of the collaboration with the Bocconi University on the Group "intangibles" will be started. A project aiming at the evaluation of the Group's intangible assets will be launched, as well as a process review in relation to six macro-areas of interest: Strategic, Financial, Governance & Stakeholders, Customers & Products, Human, Process.

Business Unit Mobile's priority objectives are the recycling and valorization of the waste from technical systems, with particular reference to the abandoning of the analogical system of mobile communications (TACS).

Telecom Italia will take part, together with other important companies, in the advisory body for the development of the Global Marshall Plan, which aims at reaching the objectives set by the United States in the "Millennium Development Goals" that ties the funding directly to the economic development and the improvement of the democratic, social and environmental standards of the poorest countries in the world.

Telecom Italia, together with other companies, will adhere to "The European Manifesto of businesses 2010" on March 3-4 2005 in Brussels. The Manifesto will indicate the European way to Corporate Responsibility, as intended by the European Commission and President Barroso.

"Voluntary business initiatives, in the form of Corporate Responsibility practices, can play a key role in contributing to sustainable development, while enhancing Europe's innovative potential and competitiveness".

José Manuel Barroso

■ REFERENCES

In defining and implementing the strategy and programs for Sustainability, Telecom Italia Group used the guidelines proposed by the main bodies responsible for orienting and standardizing Corporate Responsibility.

Since 2002, Telecom Italia has adhered to the principles of the Global Compact, the key benchmark at world level launched in 2000 by the UN to promote the safeguarding of the environment, respect for human rights and labor standards in companies, practices against corruption.

The model for monitoring and reporting on Sustainability is based on a multi-stakeholder analysis approach and on a set of performance indicators (316). Telecom Italia Group bases its reporting on the guidelines of the Global Reporting Initiative (GRI), according to the principles of Global Compact. These guidelines are intended to harmonize the reporting on economic issues with the data on Sustainability.

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The indicators being monitored are consistent with the information required by the main rating agencies (SAM for the Dow Jones Sustainability Index, EIRIS for the FTSE4Good and SIRI) for admission to the Sustainability indexes and with the guide-lines included in the Social Statement developed by the Ministry of Labor and Social Politics within the framework of the project CSR-SC.

The Sustainability management system also takes into account the main international standards for the various stakeholders:

- the ISO 9000 and ISO 14000 quality certification for systems for managing quality and the environment, to ensure quality of service for customers and respect for the environment;
- the standard of Social Accountability 8000 (SA8000), that aims at encouraging respect for human rights and working conditions on the part of suppliers and sub-suppliers alike;
- the methods suggested by the London Benchmarking Group (LBG) for measuring investments in the Community;
- the principles of the Conventions of the International Labour Organization (ILO) for respect of fundamental workers rights.

In order to protect shareholders, the Group's Corporate Governance system is based on criteria of exactness and transparency and reflects the highest national and international standards. The Organizational Model, ex legislative decree No. 231, dated June 8, 2001, has been adopted by all concerned companies of Telecom Italia Group (about 70).

♦ DJSI (Dow Jones Sustainability Indexes): equity indexes including companies committed to Sustainability, managed by Dow Jones in co-operation with SAM (Sustainable Asset Management).

♦ FTSE4Good (Financial Times Stock Exchange): equity indexes including companies which respect certain standards of responsibility managed by FTSE in association with EIRIS (Ethical Investment Research Service).

♦ SIRI (Sustainable Investment Research International Company): company that works in the SRI (Socially Responsible Investment) sector that supplies research and consultancy service.

■ CHARTERS AND CODES

The codes, procedures and principles supporting the Group's governance system can be consulted in a dedicated section of the corporate website www.telecomitalia.it.

The Group's system is based on the Code of Ethics which constitutes the charter of fundamental values with which the Group identifies.

Telecom Italia has adopted a system of values which constitutes a constant benchmark of conduct for everyone who works for the Group, reinforcing the idea that they belong to one company.

With particular reference to the managerial staff, the Group's values system foresees a Managerial Model which constitutes a synthesis of conduct to which managers in the Group should refer in the pursuit of their business objectives.

| Values | Managerial Model |
|-------------------------|-------------------------------------|
| Customer focus | Central importance of the customers |
| Taking responsibility | Creation of value |
| Innovation | Investing in people |
| Pro-action | Change management |
| Efficiency | Networking and integration |
| Integration | |
| Transparency | |
| Professional excellence | |

The principles of conduct with regard to customers and the commitments made by the main companies in the Group in terms of quality of service, are described in the Charters of Services drawn up accordingly to the requirements coming from the National Regulatory Authority. Telecom Italia's Charter of Services and General Subscription Conditions can be viewed on the company's website (www.187.it).

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■ ADDED VALUE AND STAKEHOLDERS

The following tables show the added value generated by Telecom Italia Group, its distribution among the various stakeholders and the contribution to each of them.

ADDED VALUE

| | 2004 (a) | 2003 (b) | Change % (a-b)/b |
|-------------------------------------|---------------|---------------|---------------------|
| (millions of euro) | | | |
| Standard production value | 31,979 | 31,595 | 1.2% |
| Raw materials and external services | (13,414) | (13,018) | 3.0% |
| Gross added value | 18,565 | 18,577 | (0.1%) |
| Telecommunications license fee | 97 | 56 | - |
| Other Items ⁽¹⁾ | 1,252 | (1,206) | - |
| Corrected added value | 19,914 | 17,427 | - |

◀ (1) The Other Items represent the balance between the various items of the income statement: sundry income/expenses, extraordinary income/expenses, dividends distributed, value adjustments to financial assets, income from equity investments, financial income, loss and profit on exchange rates, end of year result owing to Parent Company or third parties.

DISTRIBUTION OF GROSS ADDED VALUE AMONG STAKEHOLDERS AND OTHER PARTIES

| | 2004 (a) | 2003 (b) | Change % (a-b)/b |
|--|-------------|-------------|---------------------|
| (millions of euro) | | | |
| Employees | 3,165 | 3,376 | (6.3%) |
| Institutions | 4,234 | 2,506 | - |
| of which: | | | |
| • Social security costs | 938 | 1,308 | (28.3)% |
| • Direct taxes | 3,054 | 1,014 | 201.2% |
| • Indirect taxes | 145 | 128 | 13.3% |
| • TLC license fee | 97 | 56 | 73.2% |
| Shareholders | 2,780 | 1,049 | 165.0% |
| Financers | 2,728 | 3,146 | (13.3%) |
| Business (depreciation and amortization, reserve funds for risks and fees, other accruals and adjustments) | 7,007 | 7,350 | (4.7%) |

CONTRIBUTION TO THE STAKEHOLDERS

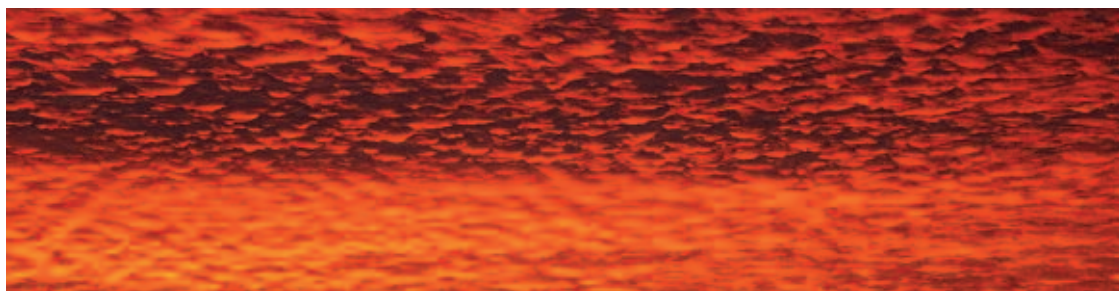
| | | |
|-----------------------------|--------|--|
| (millions of euro) | | |
| Suppliers ⁽¹⁾ | 16,925 | Consumption of raw materials and external services, industrial investments |
| Institutions ⁽²⁾ | 4,234 | Expenses, taxes and state contributions |
| Employees | 3,165 | Cost of labor net of compulsory contributions |
| Shareholders | 2,780 | Dividends distributed |
| Financers | 2,728 | Financial expenses |

◀ (1) The breakdown of the contribution to this stakeholder is described in the paragraph on Suppliers.

◀ (2) The breakdown of the contribution to this stakeholder is described in the paragraph on Institutions.

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CUSTOMERS



■ CUSTOMER FOCUS

Telecom Italia Group's customers are one of its main assets, and so the Group has decided to include customer focus, pro-action and transparency of information among its primary corporate values.

Satisfaction expressed by the customer is a fundamental prerequisite for the creation of value and maintaining market leadership. The Group undertakes several initiatives to pursue full customer satisfaction:

- within the framework of performance related compensation, Telecom Italia SpA has adopted a target linked to customer satisfaction, in fact, alongside the profitability indicator (gross operating profit), a Customer Loyalty indicator has been added that carries a weight of 30% on the performance related compensation. The indicator is an average of customer satisfaction with regard to offered services, Customer Relationship Management (CRM), image and technical quality;
- an Integrated Feedback System is presently being used at Telecom Italia SpA. The main objective of this project is to allow customer's opinions to reach strategic and managing levels. In this way the Group has a better understanding of demands, for the development of new services and the improvement of existing ones. The customer's viewpoints are gathered in two ways:
 - in support of business development, through exploratory research that takes place during the design of new products and services (through focus groups, qualitative analyses leading to evaluation of appeal, satisfaction and potentiality) as well as during the development phase (through qualitative focus to test usability, satisfaction and functionality);
 - through the customers' perception, negative or positive, during the process of supplying the service. The satisfaction/dissatisfaction judgement is precious for the company in terms of improving service quality as well as maintaining customer loyalty. Perceived quality levels are monitored during all phases of the service delivery process and for all customer segments;
- special attention is paid to disadvantaged customers: people who fall below a certain income threshold are granted a 50% reduction on the rental fee, while the hearing/speech impaired do not pay for any rental fee and are granted free SMS services from mobile phones;
- TIM has developed a "New CRM Portfolio" whose segments are related to the socio-demographic features of the customer and his disposition to the use of innovative services. This allows the company to identify actions and services, on a one-to-one relationship with the customer, offering products closer to the clients demands. A personalized caring service was also introduced. All possible channels to contact customers have now begun to be integrated into the client relations activity;

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- an agreement was made between the Civil Protection Department of the Prime Minister's Office and the Mobile Operators, including TIM, for implementing a national emergency information circuit. This project, which is experimental and has a one year term, gives the Civil Protection Department the possibility of asking for an informative SMS to be sent nationwide or to specific areas in order to face emergency situations, natural calamities, disasters or other tragic events that for reasons of intensity and extensity require the use of extraordinary means and powers. These requests are subject to an ordinance, signed by the competent Authority that specifically derogates the regulations relative to privacy in force at the time.

All the companies of the Group conduct surveys on the level of customer satisfaction and work for a constant improvement in their CMR systems. In accordance with the principle of transparency in the relationship with stakeholders, information on the criteria used for measuring the quality of services can be consulted on the websites dedicated to the customers.

■ EFFECTIVENESS OF CRM (Customer Relationship Management)

In order to build a closer relationship with its customers and to identify and satisfy their requirements, the Group has adopted a multi-channel approach to CRM (Customer Relationship Management), by making available to its customers numerous technical support centers, toll-free numbers and websites, specialized according to the segment of services or the country involved.

MAIN CHANNELS OF CRM ACTIVE AT DECEMBER 31, 2004

| | BU Wireline | BU Mobile | LATAM ⁽¹⁾ | BU Internet & Media |
|--|------------------------------------|--|----------------------|------------------------|
| Toll-free numbers | 521 ⁽²⁾ | 91 | 27 | 2 |
| Calls received by toll-free numbers | 82,525,520 | 303,922,458 | 16,783,233 | 4,140,027 |
| Technical support centers | 42 | 5,787 | 111 | 25 |
| Websites | www.187.it | www.119.tim.it | www.entelchile.net | tin.virgilio.it |
| | www.191.biz | www.privati.tim.it | www.entel.bo | help.virgilio.it |
| | www.aliceadsl.it | www.business.tim.it | | |
| | www.info412.it | www.iltelefononline.tim.it | | |
| | www.radiomarittimi.it | www.timbrasil.com.br | | |
| | www.wholesale- telecomitalia.it | www.timnordeste.com.br www.digitel.com.ve | | |
| | www.ti-sparkle.it | www.tim.com.pe | | |
| | www.pathnet.it | www.telestet.gr | | |

◀ (1) Including Entel Chile and Entel Bolivia.

◀ (2) Including customized numbers for top business customers.

Communication with residential customers takes place mainly through call centers, websites, e-mails (for example, the TIMNews newsletters, which had been delivered to almost one million subscribers by December 31, 2004), SMS text messages, or through enclosures sent with the bills.

Communication with business customers takes place through direct (for Corporate customers) and indirect (small/medium-size business and professionals) sales channels.

After-sales support is supplied through call centers, Internet and other direct or indirect channels.

The Group's CRM systems:

- provide information and technical support;
- manage customer requests either directly (one call solution) or activating the appropriate departments for the solution to the problems;

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- update the client's profile by keeping track of the calls received from the call centers;
- manage commercial contacts, selling and activating contracts.

The CRM employees are continuously trained, from a technical and behavioral viewpoint, and have a portal available to supply them with guidelines for solving problems, in One Call/On Line Solution perspective.

The CRM automatic service (Self Caring Options) allows you, through the use of Internet, to modify personal data, check traffic status, configure or activate services, pay bills or recharge, change type of subscription, purchase products, search for sales points, request information, technical and commercial assistance, subscribe to or consult loyalty programs and other services. TIM has made almost all its services available on the web, according to the guidelines of the Web Accessibility Initiative (WAI) established by World Wide Web Consortium. Access to the CRM automatic systems is also possible through the "Individual Voice Responder" (IVR) modality.

Clients' satisfaction with customer care is of a very high level as shown by the results of surveys conducted periodically by external companies into customer satisfaction with the service supplied by the Group's call centers.

CUSTOMER SATISFACTION WITH CUSTOMER CARE IN THE MAIN COMPANIES OF THE GROUP

| Company | Cientelee segment | Customer satisfaction |
|----------------|-----------------------|-----------------------|
| Telecom Italia | Consumer ¹ | 87.5% |
| | Business ² | 76.1% |
| TIM | Consumer ³ | 86.6% |
| | Business ⁴ | 76.4% |
| Tin.it | Consumer ⁵ | 76% |
| | Business ⁵ | 73% |

- 1 Level of satisfaction with customer care supplied by the "187" service; sum of the percentages of customers who described the service positively; average 2004.
- 2 Level of satisfaction with customer care supplied by the "191" service; sum of the percentages of customers who described the service positively; average 2004.
- 3 Level of satisfaction with customer care supplied by the "119" service; sum of the percentages of customers who described the service as excellent, very good, or good; data relates to the last quarter of 2004.
- 4 Level of satisfaction with customer care supplied by the Business toll-free number 800 846 900; sum of the percentages of customers who described the service as excellent, very good, or good; data relates to December 2004.
- 5 Level of satisfaction with customer care supplied by the toll-free number 80 33 80 to Tin.it Pay customers; sum of the percentages of customers who said they were very satisfied or satisfied with the service; annual average.

The range of services and tariff profiles is continuously evolving with a view to fulfilling the needs and expectations of clients. In an endeavor to achieve transparency and provide complete information, all the changes are communicated promptly to the clientele through the various channels available: in the pages accompanying the phone bill, on the website, through direct mailing, call center operators, sales points and agents. In addition, specific announcements about changes in prices, the launch or termination of services, or changes in contracts are communicated to users and consumers – in compliance with the instructions given by the Electronic Communication Code (artt. 25, c. 5, 70, c. 4 and 71). Another channel used to inform customers and help them to choose services in an informed way is advertising campaigns and promotions, to which the Telecom Italia Group applies the principles of transparency in agreement with existing legislation.

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■ LEADERSHIP IN INNOVATION

Telecom Italia Group is in the forefront when it comes to technological innovation of products and services, for fixed and mobile telephone services, as well as Internet access technology, webservices and television. A few innovations, among many introduced by the Group are shown here below.

MAIN INNOVATIONS ON THE ITALIAN MARKET IN 2004

| | | |
|--------------------------------|------------------|---|
| Telecom Italia Wireline | Telephony | <ul style="list-style-type: none"> In 2004 the videophone was launched: the first phone with a color display that allows video calls from fixed line network. Cordless phones with integrated camera which can send MMS were introduced. New tariff offers were introduced for all segments of the clientele. |
| | Internet | <ul style="list-style-type: none"> Integrated offer voice+ internet, "Alice Mia", allowing a client to have up to 5 telephone numbers and up to 3 conversations at the same time (also in wireless mode) in addition to the other features of the "Alice" Internet offer. The speed of all "Alice" services was increased without charge from 256/128 Kbps to 640/256 Kbps. In 2005 other increases will be introduced free of charge. Extension of the public Wi-Fi service. Internet services and band width connection speed for business clients were increased. "Alice Sat" offer was boosted, allowing for ADSL connection by satellite in areas not covered by the fixed broadband service. |
| | Public telephony | <ul style="list-style-type: none"> A prepaid card was launched allowing unlimited Internet access for two months from public booths. "InfoTutto in Città" service which allows you to obtain information on telephone numbers, hotels, restaurants, etc. was introduced. |
| | VAS | <ul style="list-style-type: none"> MMS service from the fixed network which allows to send multimedia messages from fixed phones to e-mail addresses and to mobile phones. Increase of the numbers to which SMSs can be sent during special charity campaigns. Testing of the dictation SMS service (Speech2Text). Increase and strengthening of hosting and web services for business clientele. |
| TIM | Network upgrade | <ul style="list-style-type: none"> Expansion of the coverage based on 3G EDGE/UMTS with completion of the upgrade of the GSM platform supporting the EDGE service. The UMTS coverage has reached more than 100 cities and numerous places of interest. Offers were introduced for returning GPRS kits in exchange of 3G dual mode cell phones with the aim of speeding up the transition to third generation mobile telephony. |
| | 3G services | <ul style="list-style-type: none"> Launch of "TIM Turbo" service: availability of broadband services with national coverage thanks to the EDGE/UMTS integration. TIM "Turbo Call" service allows enrichment in communication during vocal calls with video and images recorded in the moment by the mobile phone, showing the person we are talking to what is happening in the surrounding area. <ul style="list-style-type: none"> Launch of UMTS PC card for data transmission up to 384 Kbps. Launch of EDGE PC card for data transmission up to 200 Kbps. Launch of Dual mode EDGE/UMTS PC card. TIM video calls from WEB: a client who doesn't have a new generation videophone, can through the the use of a PC make video calls and receive video calls from other TIM customers that have a videophone. |
| | Other services | <ul style="list-style-type: none"> The "ChiamaOra" ("Call now") service allows automatic redialing of numbers: it is a new function introduced in 2004 which allows TIM customers to repeat the call automatically (to a number previously busy or unattainable) as soon as the person called can be reached. The Wi-Fi service offer is a data access service through wide band connection, which can be obtained alternative or in addition to data transmission service through radiomobile networks of second and third generation. Data transmission through the public Wi-Fi service offer was integrated with wireless data transmission. New georeferential services (for example "kiss"- georeferred chat through SMS). Control and management of vehicle fleets. |

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|-------------------------------|--|
| Telecom Italia Internet Media | <ul style="list-style-type: none"> TIN.IT consolidated and strengthened broadband wireless connection services for the Internet, increasing the number of locations for "Hot Spot TIN.IT". The "Gettone Virtuale per navigare in Wi-Fi" service was activated for internet connection through the "Hot Spot TIN.IT" using a temporary code of access obtainable on-line or by credit card. This service can also be used by non TIN.IT customers. |
| | <ul style="list-style-type: none"> The "HELPEXpress" project has been strengthened. This service helps TIN.IT ADSL customers to solve any problems linked to internet connection and electronic mail in a simple and automatic way. |
| | <ul style="list-style-type: none"> Increase of internet services (for example photo print services, new mail services, news and so on). |
| | <ul style="list-style-type: none"> Free of charge applications which allow to increase the speed of internet navigation. |
| Television | <ul style="list-style-type: none"> The testing of Digital Terrestrial Television (DTT) which continued throughout 2004 was concluded in December. Among others, conditioned access systems have been tested and introduced. |

■ CARE FOR THE QUALITY OF SERVICE

The Group's commitment to the quality of service is mainly expressed in the Charters of Services and the General Subscription Conditions.

In connection with the evolution of the market, technology, services and regulations, the Group's companies have updated the Charters of Services, the documents regarding the clientele which describe the fundamental principles of conduct and the general commitments undertaken by the companies of the Group in terms of supply of service.

The General Subscription Conditions are specific to the various services involved, which regulate contractual dealings with customers and comply with measures contained in Legislative Decree No. 259 of August 1, 2003. The Charts of Service can be consulted on the corporate website together with the General Subscription Conditions.

All the companies in the Group have implemented end-to-end control systems, which are often extended to the sales networks, to monitor the quality parameters of supplied services.

| AVERAGE TIME FOR SOLVING TECHNICAL PROBLEMS IN THE MAIN COMPANIES OF THE GROUP | | |
|--|--|--|
| Company | Service | Average time |
| Telecom Italia | Residential phone services (public telephony network + ISDN) | 17 hours and 16 minutes |
| | Business phone services (PTN + ISDN) | 7 hours and 51 minutes |
| | Residential ADSL | 13 hours and 53 minutes |
| | Business ADSL | 5 hours and 5 minutes |
| TIM | Business phone services | 1.6 working days |
| Telecom Italia Media (Tin.it) | ADSL | 0.85 (solar day) |
| | Dial-up | Problems solved with customer over the phone |

Note: in the case of Wireline and Tim the data refers to the annual average in 2004, whereas, in the case of TI Media the data refers to the second half of 2004.

In the IT Mercato BU, the average time for maintenance intervention is defined by contract in the Service Level Agreement.

The quality of service, as perceived by customers, is constantly monitored. Among the many monitored aspects of quality, the table shows customer satisfaction level for:

- quality of radiomobile services
 - In Tim, at the end of 2004, the customer satisfaction relating to the quality of the network was over 92%;

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- in TIM Hellas, in June, 92.2% of the clientele said they were satisfied;
 - in Digitel, the annual rate of the satisfaction expressed by residential customers was 4.21, on a scale from 1=low to 5=excellent.
- quality of internet services from fixed line;
- in Wireline, in December 2004, 81% of the residential customers and 86% of small companies said they were satisfied with the ADSL services;
 - in Tin.it, during 2004, on average, 76% of the consumer customers and 75% of the business customers said they were satisfied;
 - in the area LATAM, in December 2004, 76% of the ADSL clients and 63% of the Internet free clients of Entel Chile, as well as and 71% of internet users in Bolivia said they were satisfied.

During 2004, almost all the Business Units added further certification to their Quality Systems.

| BU | Certification | Certified Company/area |
|------------------|------------------------------|---|
| Wireline | ISO 9001/2000 | Wireline, Elettra, Pathnet |
| | ISO 14001 | Wireline (rete) |
| Mobile | ISO 9001 | TIM, TIM Hellas, Maxitel, TIM Peru; 2005 objective for Digitel |
| | ISO 14001 | TIM (network) |
| | QWEB | Websites: Investor Relations, i.tim, company.tim |
| | BSI OHSAS 18001 | TIM's various territorial areas |
| | BS 7799 | TIM |
| Internet & Media | SA8000-Social Accountability | TIM and TIM Hellas's objective 2005 |
| | ISO 9001 | Buffetti, Databank |
| | ISO 14001 | 2005 objective for Buffetti |
| | Audiweb | Matrix |
| ITM | ISO 9001 | 11 companies out of 15 |
| Olivetti Tecnost | ISO 9001 | Office Products Division, Italian Sales Division, System Division, Olivetti I-JET |

All the Group companies have adopted procedures for technical assistance and customer complaint management which have been integrated with or incorporated into the quality management systems.

■ DISPUTES WITH CUSTOMERS

The following table gives a picture of the complaints raised by customers and the case of litigation in 2004 for all the Business Units.

| | Numbers of complaints | | Numbers of cases of pending litigation |
|---------------------|-----------------------|---------------|--|
| | Received | Resolved | |
| Corporate | | | 73 |
| BU Wireline | 995,453 | 1,060,537 (*) | 17,098 (**) |
| BU Mobile | 5,544,225 | 5,324,481 | 744 |
| BU Internet & Media | 24,880 | 24,291 | 38 |
| BU Market IT | 6,275 | 6,265 | 59 |
| BU Olivetti Tecnost | 162 | 140 | 27 |
| LATAM | 705,248 | 691,564 | 31 |

(*) The number of complaints resolved is higher than those received because some complaints received in 2003 were resolved in 2004.

(**) In 2004 a new complaints tendency was registered regarding the legitimacy of the mailing expenses of telephone bills charged to the customer. The value of each complaint is very small.

Telecom Italia and TIM offer their customers the chance to access a free, rapid out-of-court procedure to resolve disputes ("Procedure of Conciliation and Arbitration" whose regulations and

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the application forms can be found on the companies' websites). The procedure was agreed with consumer associations and was reviewed in 2004 to bring it in line with the new European directives on out-of-court settlements. For TIM, the procedure is completely on-line.

■ RELATIONSHIP WITH THE CONSUMER ASSOCIATIONS

Telecom Italia Group began collaborating with the main consumer associations in 1997, when it signed the General Framework Agreement with 12 among the main associations. Meetings aiming at safeguarding consumers' rights continued in 2004. The Consumer Associations were involved in the review of the Charters of Services, contracts, and the Conciliation Rules of the Group.

In general meetings are regularly held with the Associations, to discuss the launch of new services and technologies and the related contract conditions.

The Group takes part, as founder member in the Consumers' Forum, which brings together Consumer Associations, companies and research institutions, and deals with the sphere of consumerism. Within the framework of the Consumers' Forum, topics of customers' interest were examined with the aim to provide the competent Group's departments with strategic feedbacks.

The Group's commitment to the area of consumers' right was also expressed in the following activities:

- information on the possibility of benefiting from special contractual conditions for categories of disadvantaged customers;
- in the same way as the on-line procedure adopted by TIM last July, a procedure for reconciliation on-line to resolve disputes related to Internet services through out-of-court settlements is being set up by TI Media;
- creation, with the collaboration of the Consumer Associations, of a procedure to safeguard users victims of hoaxes played on Internet through services such as 709, including the free permanent disconnection of these services and the freezing of the disputed bills.

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SUPPLIERS



With the aim of quantifying Telecom Italia's contribution towards the stakeholder "suppliers", the following table shows the consumption of external goods and services and industrial investments:

| TELECOM ITALIA GROUP | | |
|--|---------------|---------------|
| (millions of euro) | 2004 | 2003 |
| Expenditure for raw materials and external services (net of basic subscription charge or grants) | 13,317 | 12,962 |
| - of which correlated share | 566 | 454 |
| Industrial Investments | 5,335 | 4,894 |
| - of which correlated shares and internal capital | 1,161 | 1,312 |
| Total contribution | 18,652 | 17,856 |
| - of which correlated shares and internal capital | 1,727 | 1,766 |
| Total net contribution | 16,925 | 16,090 |

■ QUALITY

The management of the quality of the supply process is guaranteed by a special Group procedure, which was set up during the previous year. This procedure regulates the selection of suppliers based on competition amongst "qualified" suppliers, who have been admitted to a special Register of Vendors. The supplier's evaluation leads to the attribution of a vendor rating indicator, which determines the admission or exclusion of the supplier from the Register of Vendors and makes it possible to calibrate the quality controls on supplies.

Constant commitment to quality is confirmed by the following:

- the supply qualification process has been extended to the most important product categories of to the main suppliers of some overseas subsidiary companies (TIM Hellas, TIM Brazil, Entel Chile, Entel Bolivia);
- a process for the control and authorization of subcontracts was defined for the suppliers of the companies that carry out work on the network for Telecom Italia. Telecom Italia involved these companies in the process of defining evaluation criteria for the subcontractors, by listening to their views and often taking into consideration their observations. A similar procedure, although simplified, was implemented for the subcontractor of companies which install radio base stations for TIM;
- communication with suppliers has been made easier due both to a creation of an Internet site, through which the suppliers have been also able to certify their regular administrative position, and to a dedicated helpdesk, dealing with the management of commercial information. About 300 major suppliers have been enabled to give and visualize information relating to their own position in the Register of Vendor, through the access to Telecom Italia's Internet portal (under the dedicated purchasing section).

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Law No. 448/98, art. 20 about the telecommunications licence fees

With the ruling of the European Court of Justice of September 18, 2003, the non-conformity to the European Law of the licence fee required by the law No. 448/98 art. 20, was sanctioned. With reference to this law, the regional administrative court (TAR) in Lazio upheld the appeal lodged by Telecom Italia with ruling No. 47/2005, published on January 4, 2005. On the basis of this ruling, the ministerial decree dated March 21, 2000 regarding the measures for the payment of the fee established by law No. 448 of December 23, 1998, under the second paragraph of the art. 20, has been declared invalid.

Indicators of the quality service and services charter

With Resolution No. 254/04/CSP, dated November 10, 2004, AGCOM approved a directive regarding quality and charters of services for fixed vocal telephone services for the companies supplying electronic communication services available to the public.

Each year AGCOM sets the threshold which must to be respected, in particular, specific quality indicators for universal service are identified. In a similar way, with resolution No. 278/04/CSP dated December 10, 2004, AGCOM issued a policy regarding the quality and charters of the pay television service.

Market Analyses relative to electronic communications

In compliance with Recommendation CE No. 2003/497 and with the Electronic Communication Code (Legislative Decree No. 259 dated August 1, 2003), with the Resolution No. 118/04/CONS dated May 19, 2004, AGCOM started the preliminary consultations concerning analyses of the 18 markets mentioned in the Recommendation and in the articles numbers 18 and 19 of the Electronic Communication Code.

The procedures' objective is "market analysis, evaluation of competitiveness, identification of possible predominant operators, and creation of a proposal regarding the cancellation, maintenance and modification of the existing requirements, that is the introduction of new requirements". AGCOM launched public consultations on the following markets:

- Resolution No. 410/04/CONS, (Official Gazette of December 24, 2004) regarding local, national and fixed/mobile telephone services markets available to the public and supplied through fixed line for residential and non-residential clients (markets No. 3 and 5);
- Resolution No. 411/04/CONS (Official Gazette of January 3, 2005) regarding retail leased lines (market No. 7);
- Resolution No. 414/04/CONS (Official Gazette of January 4, 2005) regarding the international telephone services accessible to the public and supplied through fixed line to residential and non-residential clients (markets No. 4 and 6);
- Resolution No. 415/04/CONS (Official Gazette of January 19, 2005) regarding the market of unbundled access (including shared access) to copper network and sub-network for vocal and broadband services (market No. 11);
- Resolution 465/04/CONS dated December 22, 2004, regarding the market of termination of vocal calls on different mobile networks (market No. 16).

Other resolutions and measures of corporate interest

- Resolution No. 417/04/CONS containing the regulatory measures for the resolution of conflict of interest;
- Resolution No. 406/04/CONS, which published the description and report of conformity of accounting, accounting separation, and regulatory accounting of Telecom Italia, relative to 2001 financial year;
- Resolution No. 253/04/CONS on the access, of suppliers of content of particular value, to the Digital Terrestrial Television networks;
- Communication of 17/11/04 which started the procedure on the analysis and applicability of the sharing and evaluation mechanism of the net cost of the 2003 universal service.

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■ INTERBUSINESS SERVICES

The main accounting principles used to determine the economic values for Interbusiness services are described below. These accounting principles have been verified by the auditors since 1996.

In 2004, this audit was performed by Reconta Ernst & Young SpA.

- **Revenues:** are stated at market prices for services offered in competition and at rates established by law for regulated services and recorded on accrual basis. In the case of services that imply the use of retail dedicated access lines, the revenues also include the income from leasing such lines (valued on the basis of the rates defined in the related resolutions), with the consequent accounting of the same amount among costs.
- **Direct costs:**
 - network utilization costs include the cost to use the regulated carrier services (dedicated circuits) and the cost to use the carrier products/services offered in a competitive framework; they are therefore valued, respectively, using the rates established by the law and the rates applied to all third-party customers, the same as occurs in the cost structure of other carriers in the sector;
 - labor costs represent the cost of personnel who worked to provide such services; the cost includes salary and wages, social security costs, provisions for employee termination indemnities and other sundry costs recorded on the basis of the number of people working in the appropriate structures. Such costs are determined according to accounting standards;
 - other direct costs refer to other typologies of direct costs (marketing, connection fee, operations and maintenance, etc.) and indirect costs (costs of departments supporting the operating functions) valued using unambiguous cost accounting standards and applying specific allocation methods.
- **Depreciation** of fixed assets directly employed in providing the services in question is determined on the basis of the lifecycle of the fixed assets of Telecom Italia.

The economic results of the interbusiness services are reported as follows:

| | 2004 | 2003 | Change amount | % |
|---------------------------|----------|----------|------------------|--------|
| (thousand of euro) | | | | |
| Revenue | 51,053 | 62,822 | (11,769) | (18.7) |
| Direct costs | (29,385) | (46,855) | 17,470 | (37.3) |
| of which: | | | | |
| Labor costs | (4,168) | (2,016) | (2,152) | 106.7 |
| Network utilization costs | (22,100) | (38,548) | 16,448 | (42.7) |
| Other | (3,117) | (6,291) | 3,174 | (50.5) |
| Gross operating profit | 21,668 | 15,967 | 5,701 | 35.7 |
| Depreciation | (15,742) | (16,731) | 989 | (5.9) |
| Operating result | 5,926 | (764) | 6,690 | |

The results for 2004 show an operating result of euro 5,926 thousand compared to a loss of Euro 764 thousand in 2003. Such result is due to the combined effect of the reduction in revenues that was more than offset by the reduction in costs. The impact on revenues (– 18.7%) is mainly on account of a decline in customers who switched to other alternative offers. The reduction of resources absorbed by the service is due to a decline in the clientele and, in some cases, a reduction in the unit cost; in total, therefore, costs decreased by 37.3%. Depreciation shows a reduction of 5.9%.

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■ CONTROLS

During 2004, about 14,000 inspections of the Group's suppliers and sub-suppliers on a random sample basis were carried out. The controls were planned and implemented in accordance with a specific "risk assessment" model for the industrial sectors pertaining to purchasing. In the case of situations potentially at risk, determined by a new supplier or particular supply characteristics, further controls were carried out. The results of the inspections led to the following actions:

- inclusion in/exclusion from the Register of Vendors listing the qualified suppliers of the Group;
- authorization (where appropriate) to sub-contract activities to third-party companies;
- overall assessment of the supplier with regard to specific sectors of purchasing and subsequent assessment of a Vendor Rating;
- acceptance or refusal of the supplies;
- possible contractual implications, such as application of penalties.

■ CARE FOR ETHICS AND THE ENVIRONMENT

The ethical qualification assessment, already implemented for the qualified suppliers included in the Register of Vendors, has been extended to all the Telecom Italia Group's active suppliers. This evaluation, based on the observance of the principles of Global Compact, guarantees a better safeguarding for all the stakeholders involved in the purchasing process and improves, in the mid to long-term period, the relationship with the suppliers.

The contribution given by the Purchasing department to the "Environmental Project" was significant. It helped in defining the "guidelines for the controls on the management of the waste produced by the Group's companies. The guidelines are applied to all Business Units and companies of the Group.

Specific audits were carried out in order to verify if the environmental normatives had been observed by the Group's suppliers and to check the quality of the processes relating to the application of those norms. In some cases, the audits led to requests for improvement.

A procedure for the integration the Vendor Rating requirements has started, in order to include the monitoring and checking of the waste produced by suppliers in the assessment process.

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COMPETITORS



■ RELATIONS

Telecom Italia Group, which joined the TV sector with the acquisition of La7 and MTV, started experimentation of Digital Terrestrial TV on a sample of 4,000 families in the following cities: Turin, Bologna, Modena, Pesaro, Macerata, Rome and Milan. The experimentation was concluded on December 31, 2004.

Telecom Italia took part, in collaboration with its competitors in the TV sector, at conventions, seminars, study days, and round tables regarding the main technical, economical and regulatory topics in the industry, concerning, in particular, to the development of innovative services. Telecom Italia participates in the activities of DGTVi', the Association for the development of the Digital Terrestrial TV in Italy, which was founded by Rai, Mediaset, Bordini Foundation, Radio Television association and D-free. The aim of the Association is to promote the conversion to Digital Terrestrial TV and to keep track of all the problems linked to the interoperability of the networks built by the various television operators.

The Association has been involved in several promotional activities of the Digital Terrestrial TV taking part in important sectorial events, organizing an important meeting at national level with the participation of journalists concerned in digital matters as well as training courses for aerial fitters and installers.

Furthermore, in collaboration with Fastweb and Telefonica, a meeting at European level was organized with the aim of promoting the development of the market of content and copyrights.

Along with other fixed line operators, Telecom Italia has supported numerous meetings in order to create a framework agreement, which is now under development, for the constitution and running of a unique Data Base containing numbers and the necessary elements for the identification of subscribers to the national fixed network operators. The objective is to supply Italian customers with an information service based on a single list of the names of all subscribers to the various operators active in Italy. During the following months, both the mobile network operators, who have already signed an agreement on this matter, and the fixed network operators should sign a protocol of intent in order to harmonize the two different framework agreements and guarantee the interoperability of the related databases.

As from July 1, 2004, an agreement between the mobile network operators has been operative. This agreement, concluded under the aegis of the National Regulatory Agency, aims at creating a database of identification codes for mobile terminals (International Mobile Equipment Identity - IMEI). The database will enable stolen phones to be identified remotely and rendered unusable through connection to the CEIR (Central Equipment Identity Register), a centralized database set up by GSM Association.

The agreement foresees the possible future integration with similar systems existing in other European countries.

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■ ORGANIZATIONS AND ASSOCIATIONS

Collaboration with competitors has continued at Community level within the context of various associations and events:

- BRT (Brussels Round Table) unites various European TLC operators and manufacturing companies. It aims at maintaining a constant dialogue with the European Institutions about major issues relating to the ICT sector at Community level. The BRT is participated by the CEOs of the various companies, and the most senior representatives of the European institutions are invited;
- ETNO (European Telecommunications Network Operators' Association) is the largest association in the sector on the Continent and its objectives include the development of a competitive, efficient European telecommunications market, through the coordination of the various operators and dialogue with the institutions. Telecom Italia is on the Executive Board and chairs the Sustainability working groups;
- EIF (European Internet Foundation), unites the TLC manufacturers and operators, software providers, ISP and content providers. The association aims at creating, within the European Parliament and among the various communications operators in Brussels, a favorable environment for fast development of the internet, broadband, convergence and multi-media technologies and services, benefiting the final customer;
- ERT (European Round Table of Industrialists) is a forum in which 45 European Industry leaders take part. Its aim is to promote the competitiveness and growth of the European economy;
- ESF (European Service Forum), consists of European operators in the service sector aiming at promoting the interests of the industry of European services and the liberalization of the service sector at worldwide level in the framework of the GATS 2000 negotiations;
- ITU (International Telecommunications Union) is part of the United Nations System and aims at promoting the development of the sector on an international level through cooperation between the public and the private sectors;
- BRUEGEL (Brussels European and Global Economic Laboratory) was established in January 18, 2005, and is the new Center for the European Studies, based on a joint collaboration between the European Community Governments and the main companies of the Continent and dedicated to the analysis of international economy and the principal industrial sectors. Telecom Italia is the sole Italian supporting company.

Together with other operators in the sector, Telecom Italia Group participates in the activities of the Ugo Bordoni Foundation which conducts, among other things, research, study and consultancy activities in the field of communications and information technologies, in particular in the digital television sector.

The Ugo Bordoni Foundation has been legally entitled to the technical supervision of the experimental activities relating to digital terrestrial transmissions and interactive services. Telecom Italia's annual contributions to Ugo Bordoni Foundation are included in the calculation of the contribution to the "Community" stakeholder according to a model of the London Benchmarking Group (LBG) (see the dedicated section on the matter).

Work continues in the associational relations and coordination with Confindustria and its members associations. Initiatives at national and local level, which, in some cases, are shared with competitors, consist in actions and meetings to promote business development and the safeguarding of corporate interests on economical, regulatory, unions and labor matters. Telecom Italia Group takes part in 97 regional associations and in the following federations and associations: Federmeccanica, Federcomin, Aitech, Asstel, Assoelettrica and Assografici.

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■ REGULATORY FRAMEWORK

With the coming into force of the new "Code of Electronic Communications" on September 16, 2003, the regulatory framework of the telecommunications sector, in Italy, has now been consolidated. Among other things, it included into the national regulatory framework the EC Directives referred to in the "99 Review" regarding electronic communication services and networks ("Access", "Authorization", "Framework" and "Universal Service" directives). The following is a brief description of the main regulatory issues adopted by the competent authorities in 2004.

Information service on subscribers "12"

When the Code of Electronic Communication came into force, sanctioning the non-applicability of the obligations to provide Universal Service for the subscriber information service "12", Telecom Italia published the new conditions of its service with effect on November 1, 2003, January 1, 2004 and July 1, 2004.

With Resolution No. 15/04/CIR dated November 3, 2004, the Italian Communication Authority (AGCOM) provided for the assignment by the Communication Ministry of the rights to use subscriber information numbers (12xy) to telecommunication operators that request it. The service will come into effect on July 1, 2005.

Universal Service 2002

With Resolution No. 2/04/CIR dated April 8, 2004, AGCOM launched a public consultation regarding the proposal for a resolution concerning the applicability of the mechanism to distribute and to evaluate the net cost for the year 2002. AGCOM calculates a net cost equal to about 37 millions of Euro, with a financial support of about 24 million in favor of Telecom (of which 12 million from TIM, 8 from Vodafone and 4 from WIND).

WLL public consultation service

With Resolution No. 55/04/CONS dated March 11, 2004, the Authority announces a public consultation regarding measures for the assignment of the rights to use frequencies available for broadband point-multipoint radio networks for Wireless Local Loop systems.

With Resolution No. 195/04/CONS, dated June 23, 2004, AGCOM established the modalities for the assignment of these frequencies by the Ministry of Communications.

Interconnection and unbundled access to the local network

With Resolution No. 16/03/CIR dated December 23, 2003, AGCOM announces a public consultation regarding the approval of the interconnection rates for 2004 made public by Telecom Italia on October 31, 2003. On April 14, 2004, with Resolution No. 03/04/CIR, AGCOM approved the offer, substantially confirming the proposal put forward by Telecom Italia which provides for the reduction of interconnection costs compared to last year. This is in line with the network cap system introduced by the same Authority.

Price cap

In the framework of the revision of prices of retail services subject to price cap regulations, applying from January 1, 2004, the price of connection fee for residential clients was increased by 25% (from Euro 100 to 125), the price of line transfer was increased by 20% (from Euro 50 to 60) and the cost of the monthly subscription fee for business clients was increased by 3% (from 16.5 to 17 Euro). The price of calls from fixed line numbers to mobile phones was reduced by 2% as from July 2, 2004.

Regarding the 2005 price cap, subscription fees for business clients was increased by 7.6% (from 17 to 18.30 Euro) as from January 1. A variation of price for local calls has been in force since January 23 (increase of the call set up price and decrease of the tariff per second) which, however, does not affect the customer's average telephone bill.

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Each year AGCOM sets the threshold which must to be respected, in particular, specific quality indicators for universal service are identified. In a similar way, with resolution No. 278/04/CSP dated December 10, 2004, AGCOM issued a policy regarding the quality and charters of the pay television service.

Market Analyses relative to electronic communications

In compliance with Recommendation CE No. 2003/497 and with the Electronic Communication Code (Legislative Decree No. 259 dated August 1, 2003), with the Resolution No. 118/04/CONS dated May 19, 2004, AGCOM started the preliminary consultations concerning analyses of the 18 markets mentioned in the Recommendation and in the articles numbers 18 and 19 of the Electronic Communication Code.

The procedures' objective is "market analysis, evaluation of competitiveness, identification of possible predominant operators, and creation of a proposal regarding the cancellation, maintenance and modification of the existing requirements, that is the introduction of new requirements". AGCOM launched public consultations on the following markets:

- Resolution No. 410/04/CONS, (Official Gazette of December 24, 2004) regarding local, national and fixed/mobile telephone services markets available to the public and supplied through fixed line for residential and non-residential clients (markets No. 3 and 5);
- Resolution No. 411/04/CONS (Official Gazette of January 3, 2005) regarding retail leased lines (market No. 7);
- Resolution No. 414/04/CONS (Official Gazette of January 4, 2005) regarding the international telephone services accessible to the public and supplied through fixed line to residential and non-residential clients (markets No. 4 and 6);
- Resolution No. 415/04/CONS (Official Gazette of January 19, 2005) regarding the market of unbundled access (including shared access) to copper network and sub-network for vocal and broadband services (market No. 11);
- Resolution 465/04/CONS dated December 22, 2004, regarding the market of termination of vocal calls on different mobile networks (market No. 16).

Other resolutions and measures of corporate interest

- Resolution No. 417/04/CONS containing the regulatory measures for the resolution of conflict of interest;
- Resolution No. 406/04/CONS, which published the description and report of conformity of accounting, accounting separation, and regulatory accounting of Telecom Italia, relative to 2001 financial year;
- Resolution No. 253/04/CONS on the access, of suppliers of content of particular value, to the Digital Terrestrial Television networks;
- Communication of 17/11/04 which started the procedure on the analysis and applicability of the sharing and evaluation mechanism of the net cost of the 2003 universal service.

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■ INTERBUSINESS SERVICES

The main accounting principles used to determine the economic values for Interbusiness services are described below. These accounting principles have been verified by the auditors since 1996.

In 2004, this audit was performed by Reconta Ernst & Young SpA.

- **Revenues:** are stated at market prices for services offered in competition and at rates established by law for regulated services and recorded on accrual basis. In the case of services that imply the use of retail dedicated access lines, the revenues also include the income from leasing such lines (valued on the basis of the rates defined in the related resolutions), with the consequent accounting of the same amount among costs.
- **Direct costs:**
 - network utilization costs include the cost to use the regulated carrier services (dedicated circuits) and the cost to use the carrier products/services offered in a competitive framework; they are therefore valued, respectively, using the rates established by the law and the rates applied to all third-party customers, the same as occurs in the cost structure of other carriers in the sector;
 - labor costs represent the cost of personnel who worked to provide such services; the cost includes salary and wages, social security costs, provisions for employee termination indemnities and other sundry costs recorded on the basis of the number of people working in the appropriate structures. Such costs are determined according to accounting standards;
 - other direct costs refer to other typologies of direct costs (marketing, connection fee, operations and maintenance, etc.) and indirect costs (costs of departments supporting the operating functions) valued using unambiguous cost accounting standards and applying specific allocation methods.
- **Depreciation** of fixed assets directly employed in providing the services in question is determined on the basis of the lifecycle of the fixed assets of Telecom Italia.

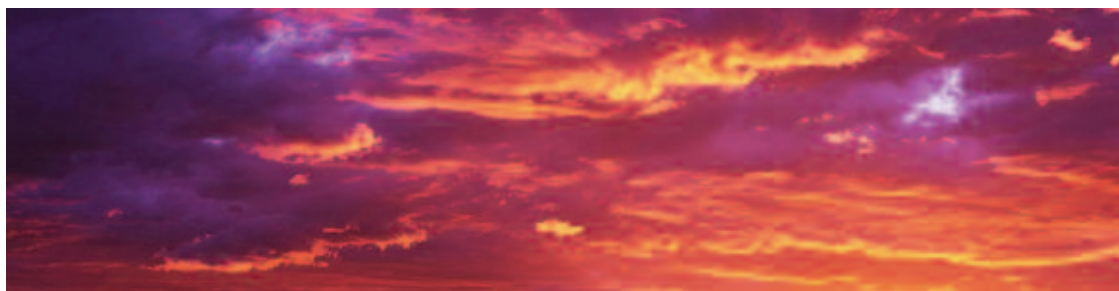
The economic results of the interbusiness services are reported as follows:

| | 2004 | 2003 | Change amount | % |
|---------------------------|----------|----------|------------------|--------|
| (thousand of euro) | | | | |
| Revenue | 51,053 | 62,822 | (11,769) | (18.7) |
| Direct costs | (29,385) | (46,855) | 17,470 | (37.3) |
| of which: | | | | |
| Labor costs | (4,168) | (2,016) | (2,152) | 106.7 |
| Network utilization costs | (22,100) | (38,548) | 16,448 | (42.7) |
| Other | (3,117) | (6,291) | 3,174 | (50.5) |
| Gross operating profit | 21,668 | 15,967 | 5,701 | 35.7 |
| Depreciation | (15,742) | (16,731) | 989 | (5.9) |
| Operating result | 5,926 | (764) | 6,690 | |

The results for 2004 show an operating result of euro 5,926 thousand compared to a loss of Euro 764 thousand in 2003. Such result is due to the combined effect of the reduction in revenues that was more than offset by the reduction in costs. The impact on revenues (– 18.7%) is mainly on account of a decline in customers who switched to other alternative offers. The reduction of resources absorbed by the service is due to a decline in the clientele and, in some cases, a reduction in the unit cost; in total, therefore, costs decreased by 37.3%. Depreciation shows a reduction of 5.9%.

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INSTITUTIONS



In 2004, Telecom Italia Group paid the Italian State 3,650 million euro and foreign states 584 million euro, as shown in the table below. The Group received capital grants from Italian Public Administrations for 12 million euro, of which euro 8 million pertained to Telecom Italia.

| TELECOM ITALIA GROUP | | | | | | |
|------------------------------|--------------|--------------|------------|--------------|--------------|------------|
| (in millions of euro) | 2004 | | | 2003 | | |
| | Total | Italy | Foreign | Total | Italy | Foreign |
| Social security and pensions | 938 | 786 | 152 | 1,308 | 1,267 | 41 |
| Income taxes | 3,054 | 2,757 | 297 | 1,014 | 753 | 261 |
| Indirect taxes | 145 | 107 | 38 | 128 | 110 | 18 |
| TLC license fee | 97 | 0 | 97 | 56 | 0 | 56 |
| Dividends | 0 | 0 | 0 | 0 | 0 | 0 |
| Total | 4,234 | 3,650 | 584 | 2,506 | 2,130 | 376 |

■ LOCAL INSTITUTIONS

The Group continues to keep track of the legislative activities of the Regions and local institutions – regional laws, resolutions, ordinances – and the regulatory activities of the local authorities. The main issues of interest include the work for the installation of network infrastructures, electromagnetic pollution, local finance and regional funding of special projects by the EU. Relations continued with the institutions and Associations of the local governments for representing the Group's position with regard to such organizations.

■ NATIONAL AND INTERNATIONAL INSTITUTIONS

Telecom Italia Group maintains constant, transparent relations with the central national institutions (Parliament, Government and independent sectorial authorities), with the aim of representing the Group's position in areas of specific interest and monitoring the procedure of approval of relative prescriptive acts in those areas. Constant support is given to the competent institutions (Parliamentary commissions, the Ministry of Communications and other government departments) in preparing regulations of interest. Special attention is paid to relations and similar support is given to the authorities of countries in which controlled companies are active.

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■ EUROPEAN INSTITUTIONS

Telecom Italia plays a continuous, interactive role with the European Commission and its Institutions (for example: the Communication Committee and the Radio Spectrum Policy Group regarding the management of spectrum), the Council of the European Union, the European Parliament and the European Regulators Group (ERG) with the aim of monitoring the activities which have significant impact on the Group.

Numerous meetings were held to discuss and initiate various projects, for example:

"Local Loop Unbundling", "Partial circuits", "Recommendation on remedies", "Intellectual Property Rights" (IPR), "eEurope", "2005 Action Plan", "Regulatory policies in the broadband sector", "TV without boundaries", "Services of General Interest" (SIG), "Unsolicited commercial communications" (SPAM), "Digital Rights Management Systems", "Data retention", "eMoney", "Spectrum trading", "VoIP", "Fiber to the home", "Collecting societies", "Software patentability".

■ NATIONAL LEGISLATION

The following legislative provisions are of key interest to the Group:

- law No. 5 dated January 16, 2004 converting Legislative Decree No. 315/2003 contains dispositions concerning authorizations for electronic communication plants;
- law No. 45 dated February 26, 2004 converting Legislation Decree No. 354/2004 contains provisions to modify various articles of Legislation Decree No. 196/2003 "Code of practice for Protection of personal data" regarding the registration of telephone traffic data. Telecom Italia is obliged by law to keep data for 24 months for reasons of control and repression of general offenses, and a further 24 months reasons of control and repression of more serious crimes, including those regarding computer and telematic systems;
- law No. 112 dated May 3, 2004 (the "Gasparri law") identifies the general principles underlying the national, regional and local television broadcasting system and adapts it to the new digital technology and converging process between television and other mass and interpersonal communications sectors such as telecommunications, publishing (including electronic publishing), and Internet in all its applications. As owner of television channel La7 and MTV, the Group has particular interest regarding this law as well as for the aspects concerning antitrust regulations;
- law No. 128 dated May 21, 2004 converting Legislative Decree No. 72/2003 ("Urbani" decree) proposes measures to contrast the illegal telematic diffusion of contents protected by copyright;
- the 2005 financial act has confirmed for the year 2005 contributions for the spreading of Digital Terrestrial Television decoders (contribution of euro 70 per decoder, for a total allocation of 110 million euro) and broadband access to Internet (contribution of euro 50, up to 75 in specific conditions, for a total of 30 million euro). The financial act also established a contribution of 10 million euro for the promotion and realization of "all digital" areas and T-Government services on the Digital Terrestrial Television platform;
- the constitutional bill for the modification of second part of the Constitution. The bill establishes a federal Senate to which it entrusts the examination of the fundamental principles of concurrent legislation matter (regulations regarding communications were included too in the original version of the bill) leaving the Regions to establish the regulation in detail. Telecom Italia has supported the proposal to modify the document which is been considered in the text under examination and aims to bring telecommunications regulations back within the sphere of exclusive competence of State, assigned to the Chamber of Deputies;

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- draft of Legislative Decree bearing a sole text of legislative provisions on radio-television matters, according to art. 16 of Law No. 112 dated May 3, 2004;
- bill regarding the legal ownership of television broadcasting rights in codified form, which entitles the ownership rights to those who are the organizers of the First and Second Division national football league championship and of other sport competitions included in the federal regulations;
- bill giving provision for the introduction of group action to safeguard the rights of consumers and subscribers (class action).

■ INTERNATIONAL LEGISLATION

The Group concentrated on the following measures with regard to international legislation:

- “Proposal for a directive of the European Parliament and of the Council on environmental liability with regard to the prevention and remedying of environmental damage”: proposed by the Environment General Direction and adopted on March 30, 2004. The adoption procedure was followed by the ETNO Sustainability working group.
- “Communication from the Commission to the Council and the European Parliament - Modernizing Company Law and Enhancing Corporate Governance in the European Union - A Plan to Move Forward”. In the framework of this action plan a public consultation is under way concerning the remuneration of the Directors in order to issue a Recommendation.
A brief account of the contributions has been published. Regarding short term actions mentioned in the action plan, the Commission has issued “a proposal of directive for the legal control of accounts in the European Union amended by directives 78/660/EC and 83/349/EC” (COM177)”. The proposal was passed on to the European Parliament and Council in March and the adoption procedures for both measures is under the supervision of the office in Brussels.
- “Proposal for a Directive of the European Parliament and of the Council on the minimum health and safety requirements regarding the exposure of workers to the risks arising from physical agents (electromagnetic fields)”: task force created by ETNO Sustainability working group to deal with electromagnetic fields has issued a Reflection Document - RD171 in collaboration with the GSM Europe e Mobile Manufacturers Forum which has already been sent to the European Commission. The document regarding electromagnetic emissions and directed to European Parliament members, aims to highlight the safeguarding of public health initiatives by the telecommunications operators as well as current status of scientific research and problems regarding the implementation of 3G networks. The proposal was adopted on April 29, 2004 with directive 2004/40/EC and basically acknowledges comments of the telecommunications operators.
- “Proposal for a Directive of the European Parliament and of the Council on establishing a framework for the setting of Eco-design requirements for Energy-Using Products and amending Council Directive 92/42/EEC (COM/2003/0453 final - COD 2003/0172)”: launched by the European Commissions’ DG Enterprise. The ETNO Sustainability working group tracks its development.
- Other measures relating to fixed and mobile telephony of the countries in which the Group is active, for example the regulations regarding the broadband wholesale and retail offers.

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THE ENVIRONMENT



In 2004, Telecom Italia Group launched the "Environmental Project" and started the study of the coordination of the various Environmental Management Systems (EMS) of the Group with the purpose of achieving an EMS at Group level.

The EMS currently adopted within the Group is being assessed in collaboration with DNV (Det Norske Veritas) which uses the evaluation method IERS (International Environment Rating System). IERS is an International Environment Evaluating System, to systematically analyze all the variables.

■ ENVIRONMENTAL PERFORMANCE INDICATORS

The data reported below is related to the environmental performance of the Group assessed in the following areas:

- waste management
- water
- energy consumption
- emissions

Comparing data with the previous years has also been reported.

All the data reported below has been calculated by processing operating data that has been appropriately reclassified.

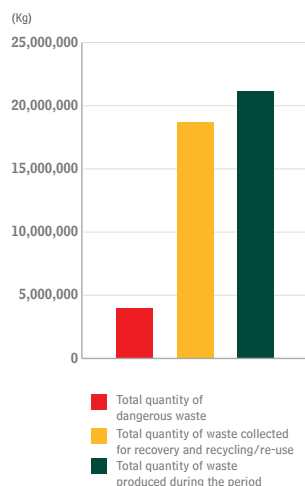
The basic data used for determining corporate performance has been inserted by the reference person of each Business Unit through a special, uniform computerized procedure used by all the subsidiaries in the Group involved in the reporting process.

The percentage pertaining to Wireline compared to Telecom Italia has been highlighted in a special column in the tables relating to the aggregate of Telecom Italia.

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■ WASTE MANAGEMENT

The data relating to waste management shown below is stated in kilograms and refers to the quantity of waste for the most part recorded in accordance with the law.



WASTE PRODUCED

| | | Telecom Italia ^(*) | Percentage change compared to 2003 | Percentage change compared to 2002 | Percentage change compared to TI |
|--|----|-------------------------------|------------------------------------|------------------------------------|----------------------------------|
| Total quantity of dangerous waste | Kg | 3,965,515 | 8.65% | -61.96% | 99.27% |
| Total quantity of waste collected for recovery and recycling/re-use | Kg | 18,677,367 | 16.13% | -12.59% | 97.09% |
| Total quantity of waste produced during the period | Kg | 21,174,311 | 12.64% | -10.81% | 95.77% |
| Ratio between quantity of recovered/recycled waste and total quantity of waste | % | 88.21% | 2.65% | -1.79% | |

(*) In this table and in the following tables of the environmental section, besides Wireline the scope of TI refers to TILab, TIFM/TI Facility Management, TILS (TI Learning Services) and ITG (Information Technology of the Group). To facilitate comparison, the 2003 data has been recalculated accordingly to the same scope.

The data refers to waste recorded in compliance with Legislative Decree No. 22 of February 5, 1997.

Up until 30th of March each year there could be a small adjustment of the situation described on 31st December due to the fact that the source of the data is the registers of acquisition and disposal of waste and is only confirmed with the verification of the real weight at the disposal plant. That information is supplied to the waste producer within three months of consignment and this justifies the possibility of an adjustment of these figures.

Compared to 2002, there was a reduction in the quantity of waste generated by Telecom Italia, while an increase of 12.64% was registered compared to 2003. This increase is due both to the replacement of the wooden telephone poles, in compliance with the Agreement Program with the Ministry of the Environment, the Ministry of Production Activities, the Conference of State and the Regions, and the extra clearing activities of the nationwide telephone exchanges. The percentage of the recovered and recycled waste is higher than 88%, with an increase of 2.65% compared to the previous year.

Compared to 2002, the quantity of dangerous waste was more than 61% lower, while an increase of 8.65% was registered compared to 2003. This increase is due to a clearing of diesel oil contaminated ground (equivalent to 403,080 Kilograms) as a result of a tank leakage.

The table and the chart below show the total quantity of the waste produced by the Group and the data for each Business Unit as a percentage of the Group.

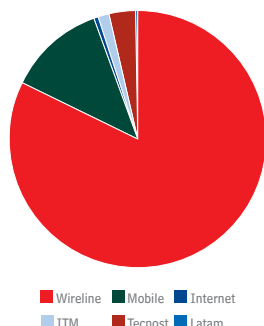
Waste production

| Waste production | | Data of each Business Unit as a percentage of the Group total | | | | | |
|------------------|------------|---|----------------------------|-----------|---------------------|--------|---------------------|
| | | Group | BU Wireline ^(*) | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost |
| Kg | 26,421,977 | 82.42% | 12.13% | 0.66% | 1.28% | 3.47% | 0.04% |

(*) In this table and in the following tables of the environmental section, besides the BU Wireline data, TILab, TIFM (TI Facility Management), TILS (TI Learning Services) and ITG (Group Information Technology) data is included.

(**) Entel Chile and Entel Bolivia data is included.

Data of each Business Unit as a percentage of the total waste produced by the Group

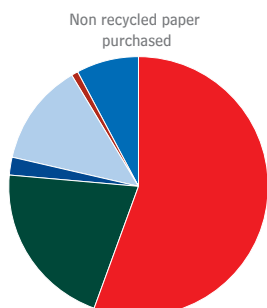


Eco-recovery of wooden telephone poles

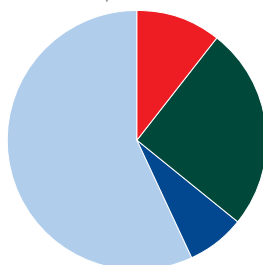
During the year 2004, a Vigilance Committee was created to control the implementation of the Agreement Program on the telephone poles signed on May 27, 2003, with the Ministry of the Environment, the Ministry of Production Activities, the Conference of State and the Regions and recycling companies. The Vigilance and Control Committee, made up of one representative from each signatory party of the agreement, together with representatives from the National Observatory of Waste, APAT and the High Institute of Health, meet periodically and monitor systematically the state of implementation of the agreement.

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Recycled and non-recycled paper purchased as a percentage of the Group total



Recycled paper purchased



Wireline Mobile Internet
ITM Tecnost Latam

Paper

The paper purchased by the Group during the year slightly exceeded 2,100 tons, of which more than half was purchased by the Wireline Business Unit.

The amount of paper purchased compared with the previous year was almost halved, because the production activity of telephone directories and Yellow Pages was sold, with the sale of Seat Pagine Gialle Group, in the second half of August 2003.

| Paper | Group | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | LATAM |
|-----------------------------------|-----------|-------------|-----------|---------------------|--------|---------------------|-------|
| Non-recycled paper purchased (Kg) | 1,992,750 | 55.74% | 20.73% | 2.18% | 12.81% | 0.89% | 7.65% |
| Recycled paper purchased (Kg) | 123,122 | 10.74% | 25.10% | 7.31% | 56.85% | - | - |
| Total paper purchased (Kg) | 2,115,872 | 53.12% | 20.99% | 2.48% | 15.37% | 0.84% | 7.20% |

The monitoring of the procurement activity is defined in the new type of contract with suppliers.

The following charts show each Business Unit's paper purchase as the percentage of the Group's total amount of recycled and non-recycled paper.

■ WATER

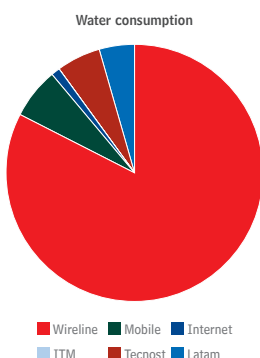
In 2004, Telecom Italia's water consumption increased by 23% compared to the previous year. This increase is due to the fact that when the data was recorded in 2003, the relative end of the year balance had not yet been communicated; therefore data for the year 2003 was underestimated compared to the real consumption.

| Water consumption | Telecom Italia 2004 | Percentage change 2004 compared to 2003 | Percentage change 2004 compared to 2002 | Percentage Wireline compared to TI |
|-------------------|---------------------|---|---|------------------------------------|
| m ³ | 5,582,275 | 23.22% | 9.03% | 85.50% |

Data from the main Business Units in the Group shows that approximately 82% of water consumption is produced by the Wireline Business Unit.

| Water consumption | Group 2004 | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | LATAM |
|-------------------|------------|-------------|-----------|---------------------|--------|---------------------|-------|
| m ³ | 6,976,138 | 81.99% | 6.42% | 0.93% | 0.92% | 5.47% | 4.27% |

The Tecnost Group, despite having only a few sites, has higher water consumption due to industrial processes.



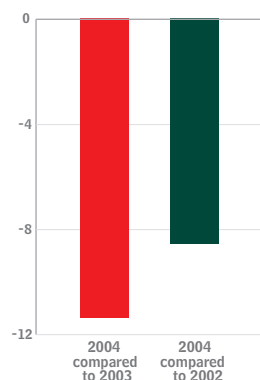
Wireline Mobile Internet
ITM Tecnost Latam

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■ ENERGY

Electricity

Energy purchased or produced



| Energy purchased or produced | Telecom Italia 2004 | Percentage change | | Percentage Wireline compared to TI |
|-------------------------------------|---------------------|-----------------------|-----------------------|------------------------------------|
| | | 2004 compared to 2003 | 2004 compared to 2002 | |
| Total energy from various sources | Kwh 1,555,087,662 | -11.39% | -8.57% | 90.63% |
| Total energy from renewable sources | Kwh 132,000,000 | -32.88% (*) | — | 86.06% |

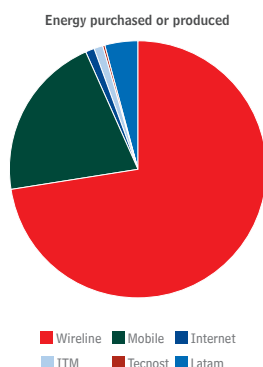
The **electrical energy** used to supply corporate buildings and infrastructures is mainly produced by fossil fuel.

Telecom Italia uses more than 88% of the energy it purchased for its telecommunications network.

Thanks to improvements in the management of electrical energy and to the efficiency of the infrastructures developed during recent years it has proved possible to continue the trend of **reducing** electrical energy consumption (– 11.39% compared to 2003; – 8.57% compared to 2002).

Considering that electrical energy is acquired from different operators, we can estimate that at least 30% of the energy consumed comes from renewable hydroelectric and geothermic sources, solar energy plants and wind-farms, amounting to approximately 450,000,000 kWh.

The table below shows the data relating to the energy purchased and produced by the Group and the percentage change of each Business Unit.



| | | Group | Data of each Business Unit as a percentage of consolidated Group data | | | | | LATAM |
|------------------------------|-----|---------------|---|-----------|---------------------|--------|---------------------|-------|
| | | | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | |
| Energy purchased or produced | Kwh | 2,274,358,278 | 71.48% | 21.59% | 1.17% | 1.36% | 0.15% | 4.24% |

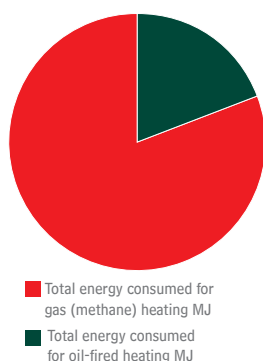
Experiments are continuing with alternative sources of electrical energy production, to supply radio base stations using photovoltaic and wind energy production technology.

The Wireline Business Unit's consumption of electrical energy amounts to approximately 71% of the total consumption of the Group, whereas the consumption of the Mobile Business Unit is more than 21% of the total.

(*) To facilitate comparison between 2004 and 2003 data, the latter has been recalculated and includes the energy purchased abroad, attributed to "green certification".

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Telecom Italia SpA: breakdown of energy for heating divided by type



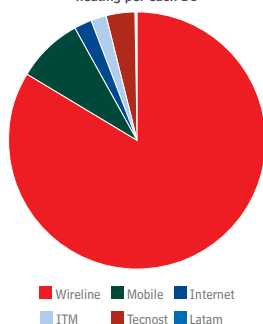
Fuel for heating

The substitution with methane gas of heating oil continues to increase, with a **reduction** of approximately 10% in the use of oil, which produces a higher level of pollution.

| Energy for heating | | Telecom Italia 2004 | Percentage change 2004 compared to 2003 | Percentage change 2004 compared to 2002 | Percentage Wireline compared to TI |
|---|----|---------------------|---|---|------------------------------------|
| Total energy consumed for oil-fired heating | Mj | 177,663,102 | -10.72% | -8.09% | 92.48% |
| Total energy consumed for gas (methane) heating | Mj | 746,431,953 | 13.60% | 9.08% | 78.27% |
| Total energy consumed for heating | Mj | 924,095,055 | 7.95% | 5.30% | 81.00% |

Both the Wireline Business Unit and the Mobile Business Unit have decreased their consumption of natural resources for heating, substituting polluting fuel with low impact sources. Changes in emissions will be described in greater detail in the next section, where different levels of emissions produced by heating, vehicles and electrical energy will be assessed.

TI Group: breakdown of energy for heating per each BU



| | | Data of each Business Unit as a percentage of consolidated Group data | | | | | | |
|--------------------------|----|---|-------------|-----------|---------------------|--------|---------------------|-------|
| | | Group | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | LATAM |
| Total energy for heating | Mj | 1,111,330,984 | 83.86% | 8.28% | 2.08% | 2.12% | 3.67% | - |

The consumption of the Wireline Business Unit as a percentage of the overall consumption of the Telecom Italia Group remains decisive: more than 83% of total energy.

Vehicle fuel

| Vehicle fuel consumption | | Telecom Italia 2004 | Percentage change 2004 compared to 2003 | Percentage change 2004 compared to 2002 | Percentage Wireline compared to TI |
|---------------------------------------|---|---------------------|---|---|------------------------------------|
| Vehicle consumption of lead-free fuel | l | 17,997,336 | -14.11% | -6.47% | 98.91% |
| Vehicle consumption of diesel fuel | l | 8,220,596 | 60.98% | 175.49% | 83.36% |
| Total vehicle consumption | l | 26,217,932 | -0.60% | - | - |

All the cars of the corporate fleet run on lead-free or diesel fuel.

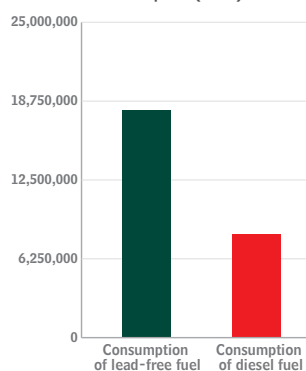
In 2004, consumption of diesel fuel represented 30% of total vehicle fuel consumption.

In 2004, Telecom Italia reduced its vehicle fleet by more than 1,000 units, equivalent to a **reduction** of 4%. At the same time, the percentage of catalytic vehicles increased to about 100% of the total.

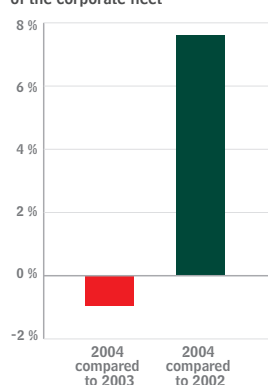
| Number of vehicles and distance travelled | | Telecom Italia 2004 | Percentage change 2004 compared to 2003 | Percentage change 2004 compared to 2002 | Percentage Wireline compared to TI |
|---|-----|---------------------|---|---|------------------------------------|
| Tot. No. of corporate vehicles | No. | 20,949 | -4.64% | -18.82% | 96.46% |
| No. of corporate catalytic vehicles | No. | 20,671 | -3.37% | 5.24% | 96.96% |
| Total distance travelled by vehicles | Km | 308,301,563 | -0.95% | 7.61% | 94.36% |

The overall distance travelled by vehicles of the corporate fleet shows a negative figure of about 1% compared to last year.

Vehicle fuel consumption (liters)



Overall distance travelled by vehicles of the corporate fleet



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Data in the following table shows the different uses of vehicles, according to the specific industrial characteristic of each Business Unit.

| Total No. of vehicles and distance travelled | | Group | Data of individual Business units as a percentage of consolidated Group data | | | | | LATAM |
|--|-------------|-------|--|-----------|---------------------|--------|---------------------|-------|
| | | | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | |
| No. | 25,152 | | 84.03% | 11.35% | 0.81% | 1.17% | 1.05% | 1.59% |
| Km | 391.337.137 | | 79.82% | 13.41% | 1.64% | 1.30% | 2.02% | 1.80% |

The distance travelled per vehicle also depends on the predominant type of clientele and the kind of technological network that has to be maintained.

■ EMISSIONS

Atmospheric emissions

As far as Telecom Italia Group's industrial activity is concerned, the most typical and significant emissions in terms of quantity are carbon dioxide (CO₂) emissions derived from "indirect" emission, due to the purchase of energy from national suppliers (Enel and other companies) and fuel consumption for heating and transportation purposes CO₂, is a typical product of combustion and, as such, is produced almost exclusively by thermoelectric systems.

During the last year, the **decrease** of CO₂ emissions continued thanks to a **reduction** in the consumption of electrical energy and an increase in the use of gas (methane) instead of oil-fired energy for heating, together with a corporate fleet reduction and an increase in the use of green energy. CO₂ emissions have been calculated according to the instructions contained in the guidelines published by UNEP (United Nations Environment Programme) and others recommended by ETNO (European Telecommunications Network Operators' Association) within the framework of the "Climate Change" project.

The amount of CO₂ produced by combustion is calculated by applying specific emissions factors to the consumption of the various kinds of fuel ⁽¹⁾.

In 2004, the data relating to the emissions produced by the use of electrical energy was taken from the parameters published by Enel in the year 2004 (2003 Environmental Report).

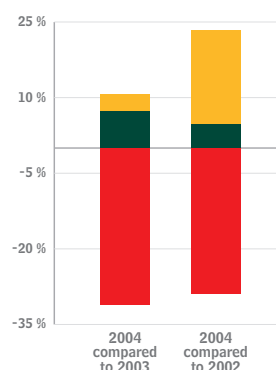
| Atmospheric emissions | Telecom Italia 2004 | Percentage change | | Percentage Wireline compared to TI |
|--|---------------------|-----------------------|-----------------------|------------------------------------|
| | | 2004 compared to 2003 | 2004 compared to 2002 | |
| CO ₂ emissions from electrical energy produced by various sources | Kg 664,737,772 | -31.05% | -28.89% | 90.63% |
| Total emissions of CO ₂ from heating | Kg 61,614,669 | 7.27% | 4.84% | 81.35% |
| Total emissions of CO ₂ produced by vehicles | Kg 61,985,283 | 2.96% | 18.59% | 93.39% |
| Total CO ₂ emissions | Kg 788,337,724 | -27.12% | -3.32% | - |

(1) The factors used in the past (for reasons of uniformity, using criteria adopted at that time by the Ministry of the Environment) were: 4.03 t of CO₂/tep for coal and derivatives; 3.27 for oil products; 2.35 for natural gas.

These factors were replaced with the ones recommended in the 1996 Guidelines published by IPCC (International Panel on Climate Change) for the national inventory of greenhouse gases and have already been used for the second national communication on emissions: fuel oil: 3.24 t of CO₂/tep; orimulsion: 3.38; diesel fuel: 3.10; natural gas: 2.35; coal: 4.02; lignite: 4.24; cokery gas: 2.00. Each one of the above is then multiplied by a correcting coefficient which takes into account the typical fraction of unburnt carbon (solid fuel: 0.980; liquid fuel: 0.990; gas fuel: 0.995).

As in the past, the resulting figure regards burnt carbon – which, however, as just mentioned, is now assumed to be less than 100% – as being completely oxidized to CO₂.

Changes in emissions



■ Total CO₂ emissions due to motor vehicles
■ Total CO₂ emissions due to heating
■ CO₂ emissions from usage of electrical energy produced by mixed sources

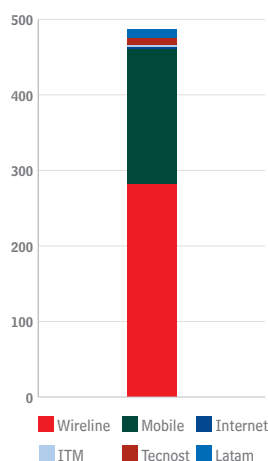
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Telecom Italia helped to **reduce** greenhouse gas emissions by reducing the emissions of CO₂ produced by the energy system of the Group (consumption of natural resources to produce electricity, fuel for the corporate fleet and heating) by more than 27% compared to 2003.

| Atmospheric emissions | | Data of each Business Unit as a percentage of consolidated Group data | | | | | | |
|--|----|---|-------------|-----------|---------------------|--------|---------------------|-------|
| | | Group | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | LATAM |
| Emissions of CO ₂ from the consumption of electrical energy produced by various sources | Kg | 972,019,439 | 71.49% | 21.59% | 1.18% | 1.36% | 0.15% | 4.23% |
| Total emissions of CO ₂ from heating | Kg | 74,259,768 | 83.72% | 8.11% | 2.04% | 2.27% | 3.86% | - |
| Total emissions of CO ₂ produced by vehicles | Kg | 104,988,980 | 80.65% | 13.33% | 1.13% | 0.76% | 1.96% | 2.16% |
| Total CO ₂ emissions | Kg | 1,151,268,188 | 73.12% | 19.97% | 1.23% | 1.37% | 0.55% | 3.77% |

Furthermore, considering the quantity of emissions avoided by purchasing energy from renewable sources, it may be observed that Telecom Italia Group contributes to the sustainable development recommended by the Kyoto Summit with more than 498 million kg of CO₂ which were avoided.

Avoided emissions of Telecom Italia Group (Millions Kg of CO₂)



Avoided atmospheric emissions

| Emissions avoided | | Level of emissions avoided and influence of the BUs as a percentage of the total emissions avoided by the Group | | | | | | |
|-------------------------|----|---|-------------|-------------|---------------------|-----------|---------------------|------------|
| | | Group | BU Wireline | BU Mobile | BU Internet & Media | BU ITM | BU Olivetti Tecnost | LATAM |
| Total emissions avoided | Kg | 498,174,519 | 287,263,102 | 181,041,077 | 3,533,224 | 4,104,446 | 9,480,435 | 12,752,235 |
| | | | 57.66% | 36.34% | 0.71% | 0.82% | 1.90% | 2.56% |

The "emissions avoided" are calculated by considering the quantity of energy consumed from renewable sources (which do not produce emissions) and the quantity of energy with "green certification".

Electromagnetic emissions

Telecom Italia Group's concern for the topic of electromagnetic emissions can be summarized in the following commitments and actions:

1. absolute respect for existing laws in countries in which it operates ⁽¹⁾;
2. careful and scrupulous management of company installations throughout the whole life cycle, in compliance with internal standards concerning efficiency and security;
3. use of, and constant research for, advanced technological tools for monitoring and investigating activities.

⁽¹⁾ It is worth noting that Italian law, in relation to this, is particularly strict. Corporate process foresees a precise management at the design stage, of the choice of locations and installation of equipment. More precisely every transmitting antenna is designed in such a way as to not allow public access in the areas in which levels of exposure could possibly be exceeded.

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Controls

TIM carries out the constant monitoring of the electromagnetic emissions in full observance of the standards set forth by the current law.

This monitoring activity is carried out within the corporation itself through a procedure that ensures the conformity to current limits during the installation of the site and throughout the period of its activity.

TIM likewise fully collaborated in the realization of the National Monitoring Network carried out by the Ministry of Communications with the help of the Ugo Bordoni Foundation. This activity aims to allow the control and supervision of the company systems and promote their periodical monitoring. The control of the systems is pursued through the Regional Offices for the Protection of the Environment (ARPA), which cooperates with the Ministry of Communications in the realization of the project through special protocols.

In 2004, the monitoring of TIM's sites begun in accordance with the agreement contained in the Legambiente/TIM Protocol.

The purpose of the protocol signed in 2003 is to guarantee and give assurance in the environmental field and to give the Legambiente technicians full support in verifying the safety of the base radio stations, particularly concerning electromagnetic emissions.

In most cases, TIM relies on external companies to carry out these measurements, whereas, in others, it directly delegates the responsibility of measuring emissions to the territorial representatives of the Ministry of the Environment and the ARPA (Regional Offices for the Protection of the Environment), especially when specific environmental situations are involved (regional laws, local regulations, and so on).

Even in the absence of any change to its installations, TIM carries out the measurements of electromagnetic emissions in agreement with the landowners and/or local authorities or in compliance with UNI EN ISO 14001 or UNI EN ISO 9001 certifications, for the networks nationwide.

Where it is necessary, modification of the radiant position (tilting) in order to optimize the signal strength is carried out. Surveys of planimetries of radio base stations and of radiant systems are added to the network database and used in order to survey and optimize the electromagnetic emissions parameters.

Last year a total of 2,957 controls were carried out.

Specific projects

– APOGEO Project

The APOGEO (Antennas Procedures On Geographic Enhanced Orientation) procedure aims to calculate radioelectric parameters relating to the three-dimensional positioning of GSM and UMTS transmitters.

The calculation is made on the basis of georeferenced topographic surveys made through the GPS satellite system, the precision of which is increased by using the differential correction technique allowed for by GEOTIM (network of permanent GPS reference stations). The application consists in positioning the "lobe of radiation" of the transmitter accurately, and, at the same time, verifying its electromagnetic compatibility.

Radioelectric parameters have to be measured accurately to optimize the mobile planning process and reduce interference on TIM networks. Furthermore, the accuracy of the data measured is considered essential for evaluating the exclusion zones (TIM can certify its own installation data by guaranteeing transparency and respect for current laws) with the aim of respecting and safeguarding the environment.

In 2004, 25 complete equipment kits were acquired and given to regional network divisions. The kit consists of a GPS satellite receiver and an integrated laser for topographical surveys.

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The use of this equipment according to the APOGEO operating procedure (a TIM patent) aims to give the correct georeference (latitude, longitude and height above sea level) of the radio base stations and accurately measure the Tilt, the Azimuth and the height of the transmitters.

– FORECASTING SYSTEMS

The “Guardian” tool calculates the exclusion zones relating to the areas where base radio stations are located and guarantees that the statutory limits are respected. When so applied, the tool plays a double-role depending on compatibility:

- to optimize the locationing of the stations and the positioning of transmitters in relation to the specific context (houses, streets, meeting-places);
- to provide objective data for the required comparisons (ARPA, population).

The improvement of the TIMPLAN tool used for the network planning contributed to the rational Development of the UMTS and EDGE systems.

The rational use of the radio frequencies (that can be guaranteed only by appropriate instruments) is useful for the operator and at the same time, the amount of electromagnetic energy released into the environment due to networks and services is reduced.

The new procedures for the definition of the electromagnetic propagation models, which was developed during the year, gave rise to guidelines and training courses for network planners. The innovative solutions adopted to model the radio propagation characteristics, gave rise to training courses for the system-planning staff.

These solutions have been tailored to the following radio planning issues:

- frequency-code assignment for mixed GSM-UMTS radio access
- optimization of the UMTS radio parameters
- management of the EDGE carriers within the frequency planning process.

In conclusion, the planning of the radio access network with the use of TIMPLAN tool, in addition to the improved SW process and the procedures developed both during 2004 and the previous years, contribute to the correct working of the mobile communications network of second and third generation, reducing, at the same time, the interference and consequently the superfluous power emission.

– STEREOSPACE

StereoSpace software makes it possible to visualize twin images, acquired digitally and appropriately oriented (SV Master) stereoscopically on a computer screen, and to carry out measurements, make comparison and updates, with the same precision as that produced using classic measuring tools.

StereoSpace contains digital images of areas regarded as being of strategic importance to TIM. These images are of key importance not only because they are aerial photographs with an adequate amount of resolution, but especially because they are georeferred. The tool makes it possible to identify the exact position of the transmission installations, thus providing accurate data for frequency planning and for calculating and seeing the exclusion zones on screen.

In 2004, the sites were increased by 7 units bringing the total to 23.

With regard to the mobile phones marketed through its sales channels, TIM makes a selection based on the level of technical innovation and the measurements of the Standard Absorption Rate (SAR) to guarantee reduced electromagnetic emissions levels.

– EMISSION MAPPING

Within the Business Unit Internet & Media, La7 Television network in cooperation with the University of Turin, carried out the mapping of progressive electromagnetic emissions released by signal transmission systems, proving that the DTT technology (Digital Terrestrial Television) reduces the electromagnetic emissions compared to the traditional analogic technology.

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■ ENVIRONMENTAL MANAGEMENT

The Environmental Management Systems (EMS) represents the operating instrument to plan, implement and manage the production and support processes. The EMS also identifies action plans for prevention and potential improvement, guaranteeing at the same time the conformity to existing legal requirements.

Some of the Group's companies and departments have already obtained both the UNI EN ISO 14001 and ISO 9001 certifications. The actual target is gradually to extend the implementation of the EMS to the whole Group, through a special project studied and coordinated by the Corporate Department. This plan aims to harmonize the existing EMS and provide guidelines for the creation of new ones.

The fundamental objectives of the Management Systems are the following:

- to optimize the use of energy sources, of materials and products;
- to improve waste management by making efforts to re-utilize and re-cycle used materials and residues from processes;
- to minimize the negative impact and maximize the positive impact on the environment due to the dissemination of hi-tech telecommunication services;
- to adopt procurement policies which are sensitive to environmental problems, by involving suppliers;
- to improve the indicators of effectiveness and efficiency relating to corporate processes;
- to promote the cultural propagation of a correct approach to environmental issues;
- to guarantee the commitment to a constant improvement of the environmental performances as a whole, through a periodical evaluation of the actual situation and an operative control procedure which aims to make the management system itself more efficient and effective.

Up to the present time, at Group level, remarkable improvements have been made in the spreading of the adoption of the Environmental Management Systems and obtaining certifications for them.

In 2004, the Wireline Network, which completed the ISO 14001 certification project for all its operative units in June 2003, successfully passed two audits in the North-East and South areas carried out by the Certification Entity. During the audits, 4 building yards were checked to verify the observance with environmental requirements; these areas were managed by external companies that undertake, on contract, enlargement and modernization work of the TLC network. The Management System's control has always been present to guarantee compliance with certifications.

TILAB and Olivetti I-Jet, which obtained the ISO 14001 certification in 2001, saw the certification for the year 2004 reconfirmed.

In March 2004, Elettra TLC completed the process of planning and adoption of the EMS and obtained the certification for the whole company.

In July 2004, TI Sparkle began the process of EMS planning, taking the necessary steps to obtain the certification, expected in December 2005. At the present time, TI Sparkle has already drawn up and published its own environmental policy and also settled all the actions which need to be taken.

During the year 2004, TIM completed the project to extend the integrated Environmental Management System, developed in compliance with the UNI EN ISO 9001 and UNI EN ISO 14001 standards for all the premises of the nationwide Network.

The Environment Management System is related to the activities of "Planning, Realization, and Superintendence of the nationwide network of mobile telecommunication".

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In this regard, an environmental policy based on principles of continuous improvement of the environmental performances as well as pollution prevention has been developed.

Specific plans to monitor the consumption of natural resources and energy have been developed, together with plans to reduce and contain the production of waste, with particular attention to lead accumulators.

The monitoring and checking activities of the electromagnetic emissions continued through precise programmes of measurement and optimization.

The communication activity with the external local communities, in particular with Public Administrations and Institutions continued. Environmental communication programmes were developed for employees with the aim to promote information and awareness on these subject matters to all employees.

The checking and monitoring of activities of environmental efficiency are part of the Environmental Management System process and are carried out with dedicated instruments. Local databases were created to monitor the trend of the main environmental indicators. Periodical reports are made to be distributed and discussed afterwards with managers. The System process includes inspections (carried out both by internal staff of the company and external staff of a CSQ - IMQ certified organization) to verify the efficiency and effectiveness of the environmental processes performed by the company.

THE ENVIRONMENT PROJECT

The project consists of 10 working groups and stretches over a 3 year period, from 2004 to 2006. The project objectives are mainly related to the implementation, harmonization and certification of the Environmental Management Systems, the development of a computerized system to operate the environmental data, training and information programs, the analyses of the life cycle of products and services, control of the environmental aspects that present risk factors.

Particular relevance is given to computerized waste management, prevention of ground pollution, clearing of the materials containing asbestos, and monitoring of both acoustic emissions and electromagnetic fields.

■ ENVIRONMENTAL RESEARCH

In 2004, projects managed by Telecom Italia with a positive environmental impact can be summed up as follows:

Adaptive transmitters

Advanced prototype solutions have been developed for mobile communication (also through cooperation with the constructors) both for adaptive transmitter systems and remote-controlled transmitters.

- adaptability makes it possible to reduce the emissions by just using the power and directions necessary for communication, avoiding, at the same time, the release of unnecessary energy into the environment;
- transmitter remote controlling makes it possible to disengage the transmitter from the location of the related control systems (base station) with obvious advantages at infrastructure level (simplifying building requirements and reducing the visual impact on the environment).

Measurements and safety of the second- and third-generation (2G/3G) radio systems

The main activities of the project are related to the following aspects:

- GSM/GPRS and UMTS access networks;
- definition of technical test standards;

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- Development of automatic tests for GSM and UMTS access networks equipment;
- assessment tests for the definition of radiant systems;
- measurements of performance parameters of termination networks;
- definition of measurements to evaluate the tools used in cell planning;
- creation of hardware/software instruments to evaluate and foresee the electromagnetic field levels irradiated by radio stations.

Evaluation of the quality and qualification of the mobile terminals

Fine-tuning of measurement procedures to assess the mobile terminal performances in relation to the customer's perception of the service in order to prevent malfunctions and other problems. Qualification of the mobile telephones on TIM's catalog in compliance with the SAR standard (Standard Absorption Rate).

Environment, health and safety management of telecommunication materials and processes

The project, which has reached an advanced stage at the Mobile Business Unit, examines how to reduce the impact of telecommunication products and services on the environment with particular reference to the following areas:

- selecting materials;
- substituting dangerous substances;
- using recycled materials;
- employing innovative processes;
- optimizing the management of materials/products/systems with a life cycle assessment;
- supporting the development and usage of alternative energy production techniques.

Evaluation of the electromagnetic impact on the brain

This is a continuous project.

Thermic and energetic effects on the human brain have been investigated through anthropomorphous puppets and sophisticated measurement instruments.

The activity is developed in cooperation with medical institutes and Universities, which help in completing the results with the necessary biological and epidemiological evaluations.

Development of service platforms for transport and info-mobility

Solutions for the optimization of traffic and reduction of the environmental impact due to private traffic in city areas have been studied.

The project, developed within Torino Wireless Project, aims (through the cooperation with FIAT and the local transport company) to make a rational use of motor vehicles, compared to its actual use, integrating the existing transport system with extra transport services supplied by the local community (parking networks, information on traffic and indications of the most convenient routes).

■ 2005 SPECIFIC AIMS

Reducing air pollution

- Analysis of fumes produced by Wirelines Networks Generators' waste pipes located in residential areas.

Reducing electromagnetic pollution

- Defining rules for the co-location of the various operators in Telecom Italia's sites in compliance with the environmental requirements associated with electromagnetic emission fields.

Reducing noise pollution

- Recording noise levels on critical Group's sites.

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Reducing visual and acoustic impact of the Radio Base Stations

- Adoption of solutions to minimize the visual impact on the environment for stations that are already being planned, in cooperation with the authorities involved in the preliminary stage of the project (Superintendency of cultural heritage, Municipal Administrations, Parkland Authority and so on).
- Gradual restyling of the existing plants with strong visual impact according to a program studied in cooperation with the concerned local Institutions (inserting the equipment in false chimnies, colored and camouflaged structures, poles and pylon like false trees, where cables are hidden inside or where transmitters are concealed with radio-transparent material).

Reducing visual impact in company infrastructures

- Utilization of new cable technologies.

Reducing fuel consumption

Increase in clearings of contamination substances

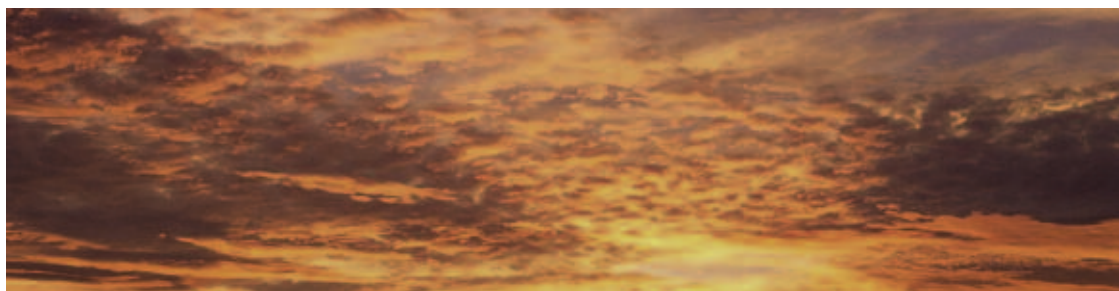
- Removal of transformers still in use containing PCB/PCT.
- Clearing of asbestos substances from the plants of the Generators' structures, there where it is still present.
- Removal of 10 containers containing asbestos.
- Replacement of 200,000 pine wooden telephone poles.
- Implementation of 1,600 capacity measurements of gas-oil tanks used by Generators.

■ GUIDELINES 2005 FOR:

- monitoring Suppliers and drawing up contracts relating to waste management;
- defining performance relating to environmental acoustics by Telecom Italia Group's equipment;
- evaluating and mapping the state of preservation of the materials containing asbestos which can be found on properties or plants belonging to a third party;
- surveying the tanks belonging to Telecom Italia Group and filing a database;
- mapping and evaluation of areas contaminated by substances from leakage in storage tanks;
- checking on waste management produced by contractors;
- defining the procedures for controls and maintenance of all the Telecom Italia Group's tanks;
- implementation of clearing of materials containing asbestos, which are on properties or plants belonging to a third party.

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THE COMMUNITY



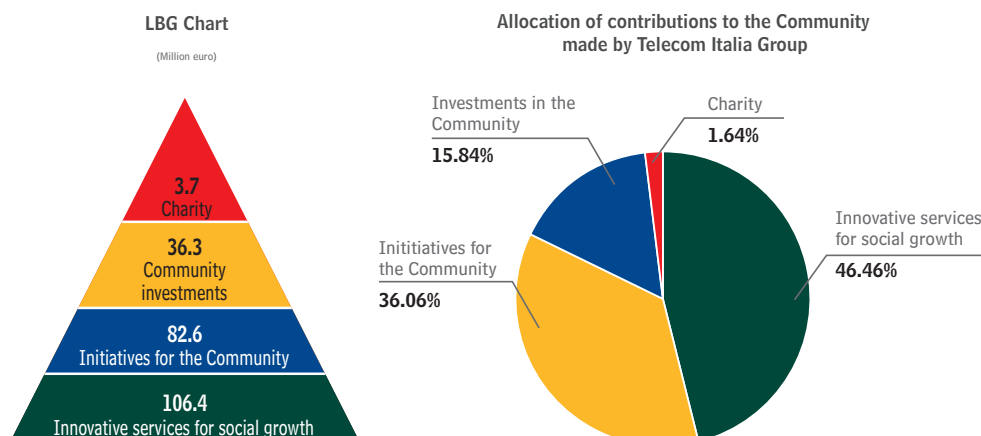
Telecom Italia Group's contribution to the Community, calculated taking into account the guidelines issued from London Benchmarking Group, amounts to 229 million euro in 2004 (203 million euro in 2003), accounting for 3.2% of the Group's Net Operating Profit. This contribution was calculated utilizing management data which had been appropriately reclassified and partially estimated.

■ CLASSIFICATION OF THE CONTRIBUTION IN ACCORDANCE WITH THE LONDON BENCHMARKING GROUP MODEL

The London Benchmarking Group (LBG), established in 1994, is an association comprising more than 90 big international member companies, and it represents the worldwide standard. In order to evaluate and report their commitment to the "Community", the companies adhering to the LBG have formulated a model that reclassifies contributions on the basis of 4 different categories.

The pyramid diagram makes it possible to measure the benefits and returns from business deriving from the various activities:

- activities directly connected with the core business are grouped at the base of the pyramid;
- activities linked more directly to the Group's sense of moral responsibility appear at the top.



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| | |
|---------------------------------------|--|
| Charity | Contributions to associations and liberal grants Donations Contributions to solidarity without business returns |
| Investments in the Community | Amateur cultural and sports events that provide brand exposure Solidarity-related events that provide brand exposure Accessory costs for solidarity that provide brand exposure |
| Initiatives for the Community | Cultural events in support of single products or services Sponsorship of socially-useful products and services Costs of monitoring electromagnetism Energy-saving interventions Initiatives in support of scientific research Costs for communicating sustainable activities Investments in health and safety Financing trainees and scholarships |
| Innovative services for social growth | Costs and investments for projects concerning innovative products and services which have a positive impact on the Community Research and development of projects for innovative products and services which have a positive impact on the Community |

■ CHARITY

■ Wireline

Donation to AMREF

AMREF is the leading non-profit private healthcare organization and is based in Africa. Its multidisciplinary technical staff, 95% of whom are African professionals - doctors, health experts, sociologists and engineers - manages hundreds of development programs every year in 14 West-African countries to support healthcare and social development among the poorest populations, by involving them actively.

■ Mobile

In order to manage its initiatives in favor of the Community efficiently and in a coordinated manner in accordance with the company's targets, TIM launched the program "A World for Everyone", identifying some target areas for developing single projects: disabilities, the family, infancy and childhood, the elderly, legality, the environment, research and medical assistance. Some of the outstanding projects carried out in 2004 are listed below.

Eliminate barriers in sports

In the European Year of Education through Sports, TIM created the project "Eliminate barriers in Sports" jointly managed with Cittadinanzattiva onlus; the project aims at eliminating architectural barriers in sports facilities in order to guarantee disabled people's right to participate in sports activities.

A census of architectural barriers in public sports facilities was carried out, also with the assistance from citizen volunteers, in order to provide a guide to accessibility conditions. A concrete plan of action to remove the barriers was drawn up on the basis of that census.

The plan was carried out in partnership with the Italian Federation Overcoming Handicaps and the Italian Federation Sports for Disabled Persons and it was backed by RAI's Social Secretariat.

Pony Express for Solidarity

The project Pony Express for Solidarity, now in its sixth edition, is a free service to provide home assistance to people over 65.

Liaising with the Departments of Social Politics and Volunteer Associations, TIM contributed to the creation of an articulated network of solidarity. Elderly people can call a phone number,

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provided by their town council or the Associations which participate in the project, and ask for assistance with daily tasks or simply for some companionship. The local council operators, connected to a main switchboard, transfer calls to volunteers' mobile phones, and the volunteers take immediate action, even on public holidays. In 2004 the project Pony for Solidarity involved about 1500 Ponies in six big Italian cities where TIM has territorial headquarters (Bari, Bologna, Naples, Rome, Turin, Palermo).

Libera project

Tim has been working since 1996 with Libera - Abele Group, an association headed by Don Luigi Ciotti. This association operates in social services, with the aim of enhancing and co-ordinating in the effort of civil society against every form of illegal acts.

TIM continues to support the Association with a wide-ranging and articulated project called "Progetto Libera"; its main purpose is to raise social awareness and to use it as a tool to fight crime of all types. The Project is broken up into a series of further initiatives:

- the "School" Project, which educates students about legality using examples from real life;
- the "Libera Sport" project, consisting of sports activities;
- the "Libera Terra" project, which established agricultural and food co-ops with young people from underprivileged backgrounds where they manage property that has been confiscated from the mafia.

Santa Lucia Foundation

TIM has continued to support the Santa Lucia Foundation, an Institution for Hospitalization and Treatment, that, among other things, researches on neuromotor rehabilitation and neurosciences.

In 2004, TIM provided special support to the following projects:

- "Multi-sensorial interactivity in the human brain" to evaluate the possibility of interactivity between attentive factors and the integration of multi-sensorial signals;
- "Listening does not always leave hands free" to study whether acoustic stimuli affect memories of visual and spatial stimuli;
- "An integrated artificial-intelligence system to assist disabled people and help them moving" to evaluate whether to use some of the most recent technologies, for example intelligent software agents and robots, to help disabled people accessing a range of services;
- "Direct, non-invasive brain-computer interfaces" to create a transportable device that acts as interface between the brain and a computer;
- "Experiments with a device to overcome communicative barriers" to overcome the difficulties deaf patients encounter today in the Health Care System, especially in outpatient surgeries and hospital wards.

■ Information Technology Market

National Association for the fight against Aids

The company TSF has promoted fund-raising activities in support of ANLAIDS - Lazio section. Funds raised have contributed to implementing some of the projects the Association promotes, for example an information campaign for high-school students in Lazio; a project for collaborating with the government of Cameroun on maternal-foetal prophylaxis; and a first-aid surgery for outpatient immigrants with this type of pathology.

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■ INVESTMENTS IN THE COMMUNITY

■ Project Italia

In 2004 Project Italia continued its activities. The project, focused on supporting cultural, social and sports undertakings, distinguished itself for its close cooperation with scientific partners, to whom Telecom Italia supplied technical, organizational and communications expertise. Important alliances were thus developed with public and private institutions, local governments, associations and organizations. Progetto Italia's distinguishing feature is its direct organization of projects undertaken, and the quality and uniqueness of events planned.

The following is a list of projects the Group supported in 2004, divided by subject matter.

Culture

- **Telecom journey:** inspired by a leitmotif that illustrates the particular characteristics of each host city, the Journey, which is Progetto Italia's 2004 novelty, is a stimulating three-day cultural experience dedicated to discovering the history and traditions of our country. Art, music, theater, dance, mime are the languages used to express the cultural itinerary. The first two stages of the Telecom Journey took place in Cosenza (May 21-23, the theme was "Utopia and Heresy") and Perugia (June 4-6, the theme was "Spirituality and Poetry").
- **Telecom Award:** the "Telecom Award, Beauty is Infectious" is for projects aiming to enhance art, culture, the environment; in a word: beauty. The jury, with Umberto Eco, Riccardo Chiaberge, Dario Del Corno, Philippe Daverio, Andrea Kerbaker, Marco Magnifico, Renato Mannheimer, Vittorio Sermonti, Andrée Ruth Shammah, Guido Vergani, Massimo Vitta Zelman and Ugo Volli, will award a prize to the most original projects in May 2005.
- **Dial me:** Telecom Italia has provided its know how and technologies to the Milan digital library, located in the Sormani library. On www.digitami.it, therefore, rare texts that are too delicate to be lent out and can only be consulted in the library, may be read, free of charge. The virtual library is different from common search engines because it certifies the quality of the on-line text; that may be personalized, even with notes in the margins, thanks to their conversion to Word format.
- **Lectura Dantis by Vittorio Sermonti in Florence - Purgatory:** the Lectura Dantis has continued with the second part of the poem in Florence, in the Refectory of Santa Croce. Total participants at the 33 evenings: 12,500 people.
- **Strega award:** Telecom Italia, in its role of institutional partner, commissioned Melania Mazzucco (winner of the award for her novel "Vita") to write a book that, together with the books by Domenico Starnone and Margaret Mazzantini (winner of preceding awards) has been included in the "I libri Stregati" series created by Progetto Italia to promote and highlight contemporary literature. The title of Mazzucco's book is: "L'anno marziano o il compleanno della tigre".
- **Digital laboratory for the National School of Cinema:** the new 2003-2004 courses have started at the Experimental Center for Cinematography directed by Francesco Alberoni.
- **Digital Laboratory at the "La Sapienza" university in Rome:** new courses for the academic year have started at the Laboratory directed by Maurizio Costanzo, set up within the faculty of Communication Sciences; at the end of the summer session work done by the students will be publicized.
- **Conversations about History of Art - Rome:** a cycle of conferences on various topics held by well-known experts in the field (university professors and Italian and foreign curators) at the Casino dell'Aurora in Palazzo Pallavicini Rospigliosi.
- **7 Poets for 7 Cities:** in partnership with the Corriere della Sera Foundation, this project has an ambitious target: popularizing poetry. The cycle of 12 appointments, organized in 7 Italian cities during the first half of 2004, brought together Italian literary writers and popular actors known to the general public, who performed as narrators.

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- **FAI - Italian Environmental Fund:** Telecom Italia contributed to the restoration of the Necchi Campiglio home, a historic building in Milan dating to the beginning of the century that is the only remaining example left of an urban villa in the city center in a state of perfect preservation. This initiative was presented by the president of Telecom Italia, Marco Tronchetti Provera, together with the president of FAI, Giulia Maria Mozzoni Crespi.

Social activities

Social activities were organized for the purpose of promoting solidarity and spreading culture.

• Solidarity

- **Dreams mission:** Telecom Italia supports this non-profit association with a project, “Webcam with a view”, for children hospitalized at the Institute of Tumors in Milan. The Group has provided its technology (computer, webcam, adsl connection) to alleviate suffering caused by long-term hospitalization: by connecting to the site www.missionesogni.org, the young patients, using a simple password, can communicate long distance with their families and follow school lessons.
- **The Spirit of Stella:** TIM and Project Italia support a new project for sailing with solidarity: a disabled man, Andrea Stella, organizes a tour of Italy every year in his boat for people with severe spinal-marrow pathologies.
- **Crazy about sailing:** also continuing this year, the initiative for sailing with solidarity for patients with psychological problems which, supported by a team of doctors and volunteers, participate both in important regattas (Millevele Telecom Italia, Settimana dei 3 Golfi, Trofeo Pirelli) and a tour of Italy by sailboat for therapeutic purposes, ending up with the participation in the Barcolana race in Trieste.
- **114 Emergency infancy:** support for the phone number 114, created jointly with the Ministry of the Interior, the Ministry of Equal Opportunities and the Ministry of Communications, continues this year, managed by “Telefono Azzuro”, the entity headed by Prof. Ernesto Caffo, who has fought against the abuse of minors for many years.

• Divulagation

Telecom Italia Future Center (Venice): the center’s activities have become more intensive, with new multi-disciplinary undertakings: the San Salvador Conversations, Wednesdays in the Future Center, Art Experience and the presentation of the album by Gianni Maroccolo, founder of Litfiba, for a total of 26 events. Several celebrities from artistic and cultural milieus participated in the Conversations, which were organized by the art historian Philippe Daverio. The multidisciplinary approach was the common denominator between the Wednesdays and the Conversations and afforded an opportunity to compare experiences of changes in our life styles brought about by new information and communication technologies. Contemporary art was the main topic at Art Experience, a series of workshops lasting a week organized with Domus Academy; thanks to Art Experience, the public from Future Center attended interactive seminars with world-famous artists.

Over 25,000 people took part in activities at the center and 50,000 videostreaming contacts were made.

IDI - Interaction Design Institute Ivrea: established by Senator Franco Debenedetti, IDI graduates the best designers in the world every year. Telecom Italia has been supporting its activities for a few years with tangible contributions in the form of scholarships for students.

Sport

Telecom Alleniamoci alla Vita (Telecom Let’s Train for Life): 15,000 texts prepared by students from schools all over Italy to participate in the second edition of the contest “Hunting for values”, part of “Telecom Let’s Train for Life”. This year the initiative acquired further lustre with its “Direct connection to Athletes”, a series of testimonials given by great sports champions in Italian schools. The purpose of the project, which uses educational material for professors, students and their families, is to acquaint young people with positive values.

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A show by Marco Anelli in Rome: a show by Marco Anelli, a photographer for the Grazia Neri agency, exposed Italy's greatest tennis players in black and white during the 2003 edition of the Telecom Italia Masters. Five thousand people visited the show.

■ Mobile

TIM meets schools

This initiative showed children from Roman middle schools how communicative technologies have evolved, with a guided tour of TIM's control room and machinery.

These meetings, with 25/30 people each time, included an introductory lesson on various forms of communication and their evolution, using illustrated exercise books, followed by an educational game to test how much the participants had learned. At the end a group work shop was organized (for example, a drawing) with which the students could give their opinions on how mobile phones influence socializing, and on possible future developments in the communications sector.

Climate Bank Project

In 2004 TIM continued its support of the "Climate Bank", a project promoted by Cittadinanzattiva and WWF for the purpose of reducing greenhouse emissions into the atmosphere with a wide-ranging communication campaign to encourage individuals, businesses and public administration to adopt energy-saving practices.

TIM participated in organizing a series of information/training seminars held at local institutions (regions, provinces, and municipalities) and a travelling exhibition with events in ten Italian cities.

■ Internet & Media

The Group's TV

During 2004 the Group's television continued to be involved in supporting culturally and socially important topics. La7 included special news programs and debates on current topics of the moment in its schedule; the project "Be Equal", partially funded by the European Community, aired a series of ads against racism; on the world day for the struggle against AIDS, it broadcasted a tv series on the subject.

MTV created, or contributed to the creation of, events and initiatives to safeguard health, education, culture, solidarity and humanitarian aid.

We would particularly like to point out:

- the campaigns "Free your mind - drugs" to raise awareness about using narcotics and "Free your mind - human trafficking" concerning the trade in human beings;
- the book "Clean Cut Kids - Youngsters in a world where you have to have to be" written out of a desire to know its audience, explain its expectations, and intuit its evolution. It's the result of a study of Italian boys and girls carried out by MTV Lab, a monitoring centre for young people in relation to broad social concerns.

The following special programs were also of particular interest:

- "I've good baby mama drama": an episode about undesired or difficult pregnancies in the "True Life" series dealing with current topics, to inform young people and encourage them to think about issues;
- "Drugline": 3 special live programs about narcotics with guests, experts and phone calls from viewers;
- the "World AIDS 2004": a day-long event to raise public awareness of the AIDS problem and help Lila (Italian Organization for the fight against AIDS) raising funds for research, realized by sending SMS.

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■ INITIATIVES FOR THE COMMUNITY

■ Corporate

Telecom Italia Lab

Business Unit Wireline, Mobile, TI Media and the Information Technology Group department contributed considerably in financing scientific research carried out by Telecom Italia Lab. Research activities covered, among other things:

- how the access network has evolved in relation to the diffusion of wide-band services and technology;
- the evolution of the transport and commuting network with low-cost structures that guarantee the required levels of quality as well as transforming it in line with the “all IP” model;
- additional voice services along with the video component and development of wide-band and multimedia services;
- evolution of the mobile network toward the third generation; estimate of its impact on radio, and development of adequate control and planning tools;
- development of third-generation mobile services and their integration with the EDGE package;
- network solutions and the apparatus needed in order to guarantee safety for communications and related computer systems.

Crisis Management

The Group has set up a system to deal with any critical situations that might impact negatively on business, caused by, for example, natural disasters, hacking or other criminal activities in Italy or abroad. The system, formalized with a Group procedure signed by the Chairman, is based on the following bodies:

- the Crisis Management Board, including representatives of the Group’s top management, with strategic and coordinating tasks;
- the Crisis Management Board’s Secretary, in charge of generally managing the system and updating it;
- the Operational Crisis Teams, that carry out the Board’s strategic orders in the field;
- the Incident and Crisis Center, which monitors all signals that might be premonitory of critical situations and channels information flows required by top-management in order to optimize decision making. The Incident and Crisis Center is also the contact and assistance point for all company structures and single employees having specific security needs in connection with possible incidents or transfers in foreign countries that are potentially risky.

CRSA (Control & Risk Self Assessment)

The operative deployment phase of the project continued, providing the Group with a method of structured self-evaluation of risks made by the management, in relation to defined company objectives. This methodology has been integrated within the Group’s planning process.

A web-based application has been set up to support the main phases of the CRSA process: allocating objectives, pointing out and evaluating possible risks associated with them, formalizing action plans and their subsequent controls.

In 2004 training programs were further expanded for CRSA members within the Group and the methodology is being introduced in TIM Peru’ for Latin America, and in the BBNET Group for Europe.

In 2005 the methodology will be extended to other European subsidiaries such as HanseNet Telekomunikation, TI France and TIM Hellas.

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■ Mobile

Elettromagnetism

New radio transmission equipment that was installed and the modification of existing equipment require the electromagnetic emission to be measured in order to ensure they conform to current legislation.

For further details refer to the paragraph "Electromagnetic Emissions" in the stakeholder "Environment" section.

■ BU Olivetti Tecnost

MEMS (Micro-Electro Mechanical Systems)

MEMS measurement and implementation systems were created which are useful for augmenting the quality and safety of people's lives. These developments had two main areas of application:

- a range of differential, absolute and gauge pressure sensors based on a piezoresistant silicone chip that supplies tension in proportion to pressure applied, having the following specific applications:
 - home appliances;
 - measuring tire pressure and temperature;
 - industrial controls.
- optical instruments on silicon for telecommunications, developed in conjunction with Pirelli Labs for use in the field of photonics.

■ INNOVATIVE SERVICES FOR SOCIAL GROWTH

■ Wireline

Wi-Fi (Wireless Fidelity)

The service provides high-speed wireless connection to Internet or company Intranets from public places where it has been installed (hot spots) using laptop computers or palmtops. During 2004 the home page that appears automatically to users who access services in the hot spots was completely renewed both in structure and content, making it simpler and more comfortable to enter and remain in Wi-Fi areas. In the new portal pre-paid Wi-Fi cards may be bought on-line in any denomination.

Thanks to creating many new hot spots and to several new roaming contracts, Telecom Italia has one of the largest Wi-Fi networks in the world.

"Loquendo" platform

This is an advanced interactive voice system that allows the user to access information and transactional data with a simple telephone call. The platform has undergone restructuring in order to improve voice recognition technology so as to provide services that are even more advanced and of increasingly high quality. The platform supports 15 languages and can recognize 50,000 words; it can use voice prints as a biometric feature to verify a person's identity.

There are various possible applications also for the business sector, such as, for example, automation of Call Centers, introducing voice services for Customer Relationship Management applications, creating infomobile services, and dialogue services for company Intranet systems.

Telemedicina

Telecom Italia continues to contribute to the activities of Telbios, a company that operates in the Telemedicine sector to develop added value services for healthcare facilities and for final clients. The following are its main achievements in 2004:

- a specialistic network for treating patients with head injuries which was used by several territorial healthcare structures; because it transfers clinical data and images in real time, patients don't have to be transferred unless it's absolutely necessary;

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- the safe network for the National Center for Transplants allows all data on explanted organs to be checked so they can be immediately and efficiently reimplanted;
- the introduction of Telemedicine services that distance monitor main cardiac parameters of patients released from hospitals and their medical reports; the services can be extended to other branches like for example pneumatology or diabetology;
- development of the technological platform that provides the Teleassistance service for the elderly, chronic patients, people who live alone and who are difficult to reach through traditional channels.

■ Mobile

Talks

TIM launched the Talks software, a revolutionary application that makes it possible for blind, visually-impaired and the elderly to use all the functions on mobile phones by themselves thanks to an electronic voice that reads the display screen and guides the user to the various options offered on the menu.

The Talks software uses the "ETI Eloquence" program, the same one used by other programs that read the screen on personal computers; it is very popular with blind people.

EDGE and UMTS

The update of the GSM platform that supports EDGE (Enhanced Data rates for Global Evolution) was completed in order to provide access to the advantages of third-generation (3G) services to a wider range of clients, including people living in remote areas; this helped to reduce the digital divide.

Meanwhile, planning and realization of the UMTS (Universal Mobile Telecommunications System) network, which guarantees coverage of regional capitals as per contractual obligations stipulated in their licenses, proceeded in several other cities and localities of interest.

In 2004 TIM launched its commercial TIM Turbo service; thanks to integration with EDGE and UMTS it provides broad-band services with significantly better data transmission speed than GPRS, similar to UMTS speed.

In order to support the new broad-band 3G services while ensuring high-quality levels, the Core Network IP platform, which was already used by most of the technologies, has been updated.

■ Olivetti Tecnost

Inkjet technology

A new technological platform was developed to expand inkjet technologies to new products and markets. The development of these new projects allows an important technological and professional relaunch of the Arnad research center; this is the only European active center for research in this field, one of the only four in the world.

Products that use inkjet technology, which uses water-based inks and paper that has not been chemically treated, have less environmental impact than products that use other printing technologies.

■ Information Technology Market

Hypovision kit

The company Venis took part in the "Easier Reading" project presented by the city council of Venice during the FORUM PA 2004, realising a "hypovision kit." It is a mini compact disk which contains a series of easy-to-install programs to help visually-disabled people, like the visually-impaired or the elderly, to use computers more easily by, for example, making it easier to read data and prompts.

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■ Internet & Media

Terrestrial Digital

Investments in 2004 were mainly to acquire frequencies and update technology on the transmission networks, which now cover more than 65% of the Italian population, and operate the service, which served about 4,000 users in some sample cities. Terrestrial Digital represents the technology of the future in the television sector, and beginning in 2006 will be present in all Italian homes. Via interaction with ADSL and third-generation mobile phones, the Group will be able to offer its clients services that are steadily more integrated and highly value enhancing.

■ RESEARCH AND DEVELOPMENT

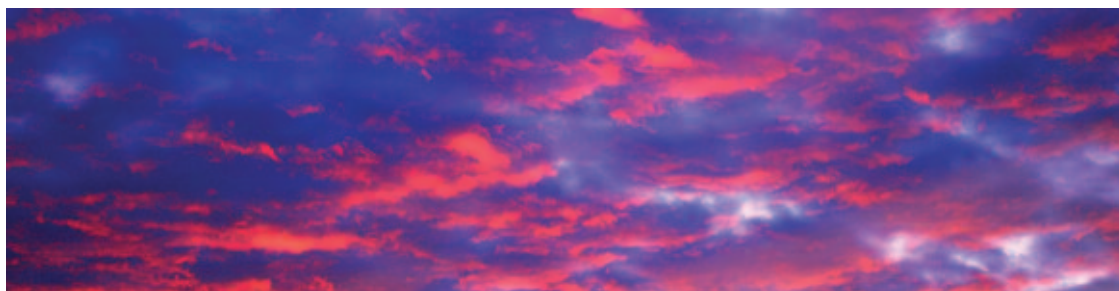
During the year 2004 research and development activities at Telecom Italia Group were mainly carried out by the central department TILAB, also in collaboration with Pirelli Labs. Furthermore, at year-end 2004 the TILAB department signed an agreement for Telecom Italia to acquire projects and research and development activities carried out by Olivetti Tecnost and authorized by TILAB.

Total costs sustained in 2004 amounted to about 144 million euro, of which 5 million euro, covered by and, were collected or are to be collected. The number of employees involved in said activity was 1,209 units.

Research and development activities carried out by Telecom Italia Group appear in detail in the Report on Operations in the section "Performance of Business Units/Central Departments of the Telecom Italia Group" in the comments on the TILAB department and the Olivetti Tecnost business unit (the "Office Products" and "Systems Division").

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HUMAN RESOURCES



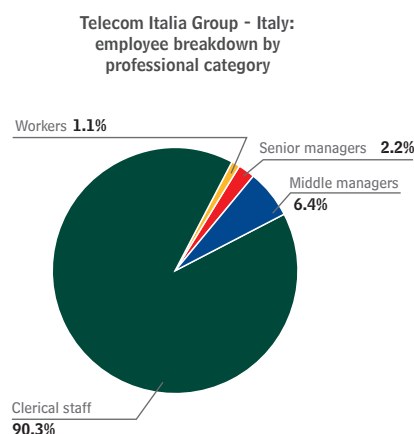
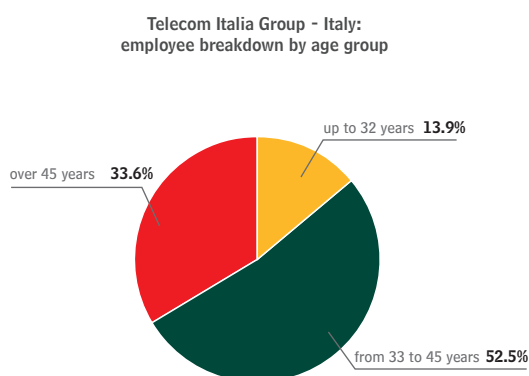
■ HEADCOUNT AND CHANGES IN TELECOM ITALIA GROUP

| Employees at December 31, 2003 | Changes in the year | | | | Employees at December 31, 2004 |
|--------------------------------------|---------------------|------------|-------------------------------------|---------|--------------------------------------|
| | Recruited | Terminated | Changes in consolidation area | Total | |
| 93,187 | 6,818 | (6,528) | (2,112) | (1,822) | 91,365 |

At December 31, 2004 there were 91,365 employees in Telecom Italia Group. The overall difference of 1,822 units compared the 2003 headcount is attributable to 6,528 terminations, 6,818 recruitments (for a global turnover of + 290 units) and 2,112 fewer units due to reshaping. The latter is mainly connected:

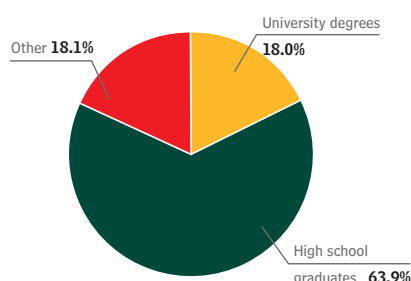
- to the outsourcing of the “Document Management” activities (– 257 units from Telecom Italia SpA and Emsa Servizi), “Maintenance and Environmental Services” (– 437 units from Telecom Italia SpA and Emsa Servizi) and “Industries and Services” (– 201 units from IT Telecom SpA);
- to the sale of Webegg Group (– 622 units), the Atesia company (– 99 units), CIPI and GPP Group (– 311 units).

In Italy personnel in the Group make up 82.1% of the total and has the following characteristics:

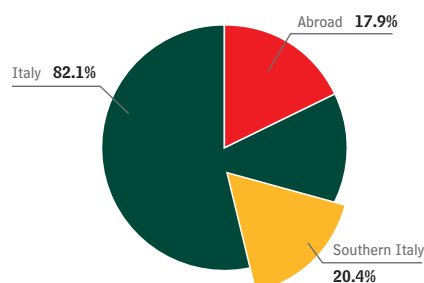


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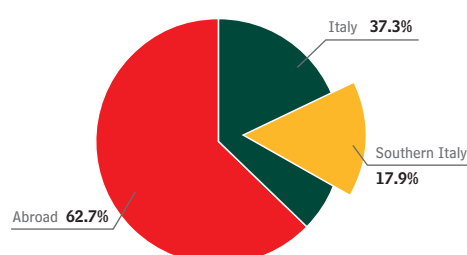
Telecom Italia Group - Italy:
employee breakdown
by academic qualification



Telecom Italia Group:
employee breakdown by geographic area



Telecom Italia Group:
recruitment breakdown by geographic area



■ HEADCOUNT AND CHANGES IN TELECOM ITALIA SPA

| Employees at December 31, 2003 | Changes in the year | | | | | | Employees at December 31, 2004 |
|--------------------------------------|--|-----------|------------|--|--------------------------------------|-------|--------------------------------------|
| | IT Telecom & Epiclink employees at December 31, 2003 | Recruited | Terminated | Transfers among companies in the Group | Transfer of company activities | Total | |
| 52,361 | 4,020 | 696 | (2,399) | (1,112) | (718) | 487 | 52,848 |

The employees at December 31, 2004 include the resources (2,554 units) that joined Telecom Italia following the merger to incorporate IT Telecom and Epiclink on December 31, 2004 fiscally effective as of January 1, 2004.

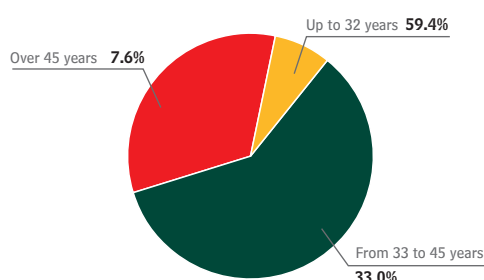
During 2004 staff from the incorporated IT Telecom diminished, especially due to employee departures following transfer of the company's "Sviluppo" activity to TIM (- 551 units) and the company's data center activity to the newly-created IT Telecom S.r.l. (- 606 units).

As for the other changes, it is worth noting that the "transfer of company activities" refers mainly to the outsourcing of the "Document Management" activities (- 189 units), "Maintenance and Environmental Services" (- 334 units), and "Industries and Services" (- 201 units).

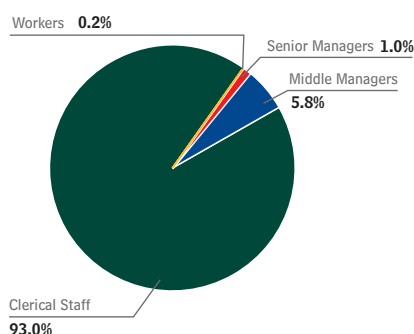
■ FOCUS ON LATIN AMERICA

The data on companies in South America refers to the Business Unit Mobile and the Entel Chile Group, the Entel Bolivia Group, Telecom Italia America Latina and Telecom Italia Audit sa.

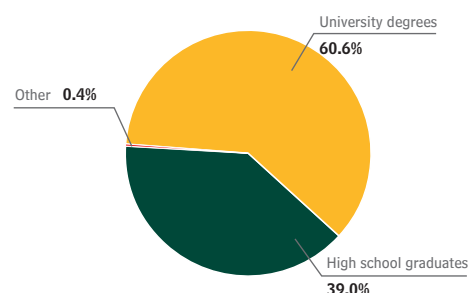
Latin America:
employee breakdown by age group



Latin America:
employee breakdown by professional category



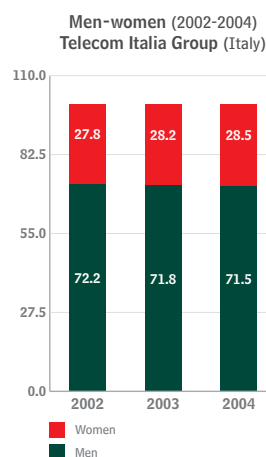
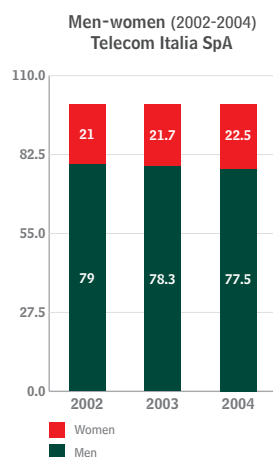
Latin America:
employee breakdown by academic qualification



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■ GENDER BALANCE

Distribution percentages of men and women are shown in the following graphs:



During 2004 the percentage of women holding senior management positions in the Group (in Italy) was around 12%; at middle management level it was around 25%.

Welfare Project and Equal Opportunities

For the purpose of fostering a better balance between work and free time, Telecom Italia is following a company Welfare policy with the goal of developing initiatives to facilitate its employees' wellbeing.

Some of these initiatives are:

- a "Personal affairs" service (by which employees can pay bills, fines, etc.);
- an Easy Free-time service where employees can organize their free time, including conventions with tour operators, railroad companies, car-hire services and hotel chains;
- some company canteens have been renovated and turned into pleasant dining rooms.

In 2004, the Woman Project, an integrated program which was launched on July 1, 2003 to identify initiatives in support of professional development for women and foster equal opportunities within Telecom Italia Group, promoted and carried out the following activities:

- a web portal dedicated to the project, updated with all the activities for employees and offering a wealth of information about maternity/paternity and raising children;
- loans for mothers;
- the introduction of a Children's Day to the company calendar and the organization of several initiatives for the employees' children (summer day camps, refunds for university enrolment fees, scholarships and Master studies);
- the introduction of an on-line shopping service.

Management policies (training, mentoring, coaching, etc.) to help employees resume their jobs after maternity leave, as well as the opening of childcare centers in some company offices, are under consideration.

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■ DEVELOPMENT

During 2004 development activities were characterized by the special attention given to the **talent enhancement**.

In this perspective several initiatives were launched in the various Business Units to implement the Group Professional System, with projects for the purpose of assessing employees' competence portfolio (specialized knowledge and personal ability).

In more detail, during the year a census was made of specialized knowledge for around 60,000 people working in the various Business Units, using a common model that allows the company to estimate the patrimonial value of the know-how present in the Group, to evaluate the best allocation of the resources in terms of business needs and to set up measures of retention and development of core competences.

As regard to talent enhancement within the larger framework of the annual process to identify Key People in the Group, during 2004 a **Knowledge Review** study was carried out according to a common model in all the Business Units. This study identified resources within the various company realities who, due to their competences, represent professional reference points.

In keeping with a policy of continual reinforcement, dissemination and internalization of the System of Group Values, several initiatives were carried out by the Business Units during the year to develop and increase management competences, at all levels, on the theme of **employee enhancement**.

Another specific course of action followed in 2004 was **harmonizing** policies and systems of developing resources at **international level** in the various companies of the Group abroad. In this framework there were numerous initiatives to promulgate the development procedures already in use in the Business Units in Italy, for example by extending the experiences of the Development Center and the Assessment Center to the management of the companies in Latin America.

The Internal Development, Training and Communication activities during 2004 were orientated towards the logic of the reinforcement of the of **Professional Families' system and culture**.

Several surveys (questionnaires and focus groups) were carried out to constantly monitor perception and motivation levels in the various Professional Families; get-togethers and conventions were organized to gather resources from various professional areas; professional families fostered job-rotation following a logic of richer and larger professional development.

Recruiting

In 2004 a program was implemented to recruit, screen and place a considerable number of high-potential new graduates, mainly in engineering and finance.

This project, which began in May, underlined the importance of transferring the Group culture following a common path of recruitment, screening, placement, training and use of tools for professional development. In coherence with the Industrial Plan and the Professional Families' orientation, the project was based on the data on the Group's recruitment requirements as to quality and quantity.

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The placement and professional development path that resulted ensures a good-quality generational turn-over in the intermediate term, while keeping sight of the Group's objectives and culture.

■ TRAINING

During 2004 there were around 1.9 million hours of training activities in Telecom Italia Group (classroom, on-line, training on the job for Italian personnel) and around 33 million euro for basic training costs (excluding the labor costs and logistic expenses).

These activities, largely carried out by Telecom Italia Learning Services, regarded mainly the following areas:

Overall Group Projects

- Completion of the managerial training program for executives aiming at change management in accordance with the managerial model drawn up for the Group ("Tools for Change") and the "Objective: Image" project for all executives in the Group, to foster and spread an organizational culture that defends and reinforces the company image.
- Realization of 5 editions of the placement-training program for new graduates in Telecom Italia Group to acquaint them all with identical knowledge of the organization and the Group's values and teach them the basic "tools of the trade".
- A Learning Tour was held in the USA for 15 managers from various Business Units, with a full immersion in top American corporate realities on the subject of "Business Innovation".
- The training programs for the Professional Families Human Resources and Finance, Administration and Control, and the launch of the training program for professional Buyers (Purchasing Professional Family) were concluded.

Training for the Business Units

Training in the Business Units was mostly to develop competences needed to run the separate businesses.

Specifically:

- In Wireline training projects in client relations and role adjustment for front-end personnel continued (i.e. the Evolution Project for SAT, Coaching Project, Minerva Project) as well as training projects for sales personnel to acquire expertise at high level both in Telecom Italia products, services and offers and in client relationships (i.e. the Negotiation Project, Projects for Organizational Development of Sales to Business Clients, General Management of Public Telephony Clients and General Management of Residential Clients). On the emergent topic of convergence between electronic communication and television services from a technical and regulatory angle (national and European Community regulations on acquiring and defending intellectual property rights to new platforms and in the television sector) the first training sessions mainly directed to managers and professionals in Business Regulations and Legal Department were held. These training sessions also saw the participation of resources from Marketing and Network.
- In TIM the main initiatives have been in "multinationality" to foster integration and networking between TIM Italia and the foreign companies (i.e. First International Business Championship - TIM CUP), "People enhancement" with a training plan for executives and key middle managers in charge of structures for furthering knowledge and modalities of managing the Performance Management process and "Orientation toward the Client" (i.e. the training project involving TIM key people and executives from corporate TIM clients).

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- The "Orienteering" training plan begun in late 2003 continued in IT Telecom, to provide all heads of departments with instruments to develop competences and motivate their employees.
- In TI Media some of the main training programs involved Tin.it departments, and dealt both with managerial and specialist topics; a training activity about Terrestrial Digital was held for technicians from La7 channel.
- Training courses continued for employees' requalification at Olivetti Tecnost S.p.A. according to the reorientation processes required for new industrial initiatives.

As regards training programs for Telecom Italia Group foreign personnel, monitoring of Mobile and South America (Chile, Bolivia), i.e. around 92% of foreign personnel in the Group, recorded about 690,000 hours in 2004.

■ EMPLOYEE SATISFACTION

A study of climate analysis with an on-line questionnaire, named Group Photo 2004, was made in May and June 2004.

It included more than 76,000 employees in the Group in Italy and for the first time employees in Greece participated too.

Participation was around 70% in Italy and 50% in Greece.

Overall satisfaction continued to grow for the third consecutive year and stabilized at about 6.25 (on a scale from 1 to 10) in Italy and 3.77 (on a scale from 1 to 5) in Greece.

During 2004 the study was made in Brazil and Peru as well, where satisfaction stabilized at 3.44 (on a scale from 1 to 5) and 3.45 (also on a scale from 1 to 5).

The results were gradually circulated to all Group employees.

■ INTERNAL COMMUNICATION

During 2004 Internal Communication carried out a series of initiatives for employees at Telecom Italia Group, some of which were:

- A Group 2004 convention: it was held on April 7, 2004 and about 7,000 executives and middle managers of Telecom Italia Group took part at locations in Italy and South America.
- Four issues of the Group *noi.magazine*.
- A questionnaire was sent out to a statistically-representative sample of blue collar workers, clerical staff, middle managers and executives in Telecom Italia Group to assess the efficacy of *noi.magazine* and study how to improve it.
- A questionnaire was sent out to assess the efficacy of the 2004 calendar and agenda and undertake new initiatives for 2005.
- A Human Resources professional family newsletter was launched, intended for the roughly 1000 professionals in the company.
- A quarterly newsletter that periodically informs all Group employees of the Group's financial results.
- Extensive use of emails to all personnel for special events.
- Intranet sites were launched for the Woman Project, Olivetti Tecnost, and Telecom Italia Audit.
- Connectivity between Italy and South America was realized that guarantees access to all contents on intranet site "Open" and the reserved areas.
- Between April and June 2004 the new version of the Group's Intranet Portal *noi.portal* for employees in Telecom Italia Media and Central Departments was launched.

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- A Security Professional Family convention (second session) was held with middle managers and executives in the Group.
- A Human Resources Professional Family convention (third session) was held with middle managers and executives in the Group.
- A plan of specific communication for boardroom managers, executives and all Group employees was held on occasion of the announcement of the merger between Telecom Italia and TIM.
- A calendar, a diary and a badge holder with the logos of all Group Business Units was sent to all employees for the end-of-year holidays.
- The "I am" project in the Wireline Business Unit was consolidated.
- The "Tim People" project for TIM employees was started.

■ REMUNERATION POLICIES

In 2004 the management of interventions on fixed-compensation was consolidated. The interventions are ever more targeted to link it directly with the level of strategic importance and roles filled.

The variable compensation element in compensation packages was increasingly-tightly linked to company/individual performance. In this respect, formalized systems took on particular significance; in 2004 we saw a consolidation of the systems already in place (MBO Managerial Incentives and Long Term Incentive Plan) as well as the introduction of a new formal incentive plan – named Performance Bonus Program (PBP) – destined at resources holding relevant business positions which have more of a professional than a managerial content.

In a Group perspective, the commitment to harmonize policies on benefits continued; furthermore, during 2004 the number of people receiving some type of benefits increased. This was to valorize the overall compensation package.

■ STOCK OPTIONS

During the first quarter of 2004, in conjunction with the Shareholders' Meeting, trading in Telecom Italia SpA shares was suspended from April 24, 2004 (the tenth trading day of the Stock Market prior to the date of the first call of the Shareholders' Meeting) until May 21, 2004, inclusive.

On December 15, 2004 and December 31, 2004, deadlines for the "Stock Option Plan 2002-2004" and the "Stock Option Plan February 2002 - December 2004" came due; consequently, on those dates all options to underwrite assigned shares elapsed, in Olivetti SpA, before the operation to merge by incorporation.

On December 31, 2004 the deadline to underwrite shares in the second and last lot of the "Stock Option 1999 Plan" fell due. The trading lot was entirely bought up except for residual shares with fractional certificates created after the trading which followed the merger by incorporation of Telecom Italia SpA with Olivetti SpA; consequently, these residual shares elapsed on the same date.

In accordance with the recommendation in Consob directive No. 11508 dated February 15, 2000, the following table summarizes the essential elements in the Stock Option Plans effective in FY 2004. Relative to items shown in the tables, please note that stock option holders are entitled to subscribe, at the subscription price, the total number of shares obtained by multiplying the number of options held by the exercise ratio, rounded down to the nearest whole number.

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| (Amount in euro) | | Options existing at 1/1/2004 | New options granted during the year | Options exercised during the year | Options expired and not exercised or forfeited during the year | Options forfeited during the year due to termination of service | Options existing at 12/31/2004 | of which exercisable at 12/31/2004 |
|------------------|------------------------------|------------------------------|-------------------------------------|-----------------------------------|--|---|--------------------------------|------------------------------------|
| 1999 | No. options | 4,511,901.24 | - | 4,511,879.74 | 21.50 | - | - | - |
| Plan | Exercise ratio | 3.300871 | - | 3.300871 | 3.300871 | - | - | - |
| | Subscription price | 2.057033 | - | 2.057033 | 2.057033 | - | - | - |
| | Market price | 2.403 | | 2.764 ^(*) | 3.006 | - | - | - |
| 2000 | No. options | 10,699,996.00 | - | - | - | - | 10,699,996.00 | 10,699,996.00 |
| Plan | Exercise ratio | 3.300871 | - | - | - | - | 3.300871 | 3.300871 |
| | Subscription price | 4.185259 | - | - | - | - | 4.185259 | 4.185259 |
| | Market price | 2.403 | - | - | - | - | 3.006 | 3.006 |
| 2001 | No. options | 32,340,000.00 | - | - | - | 360,000.00 | 31,980,000.00 | 31,980,000.00 |
| Plan | Exercise ratio | 3.300871 | - | - | - | 3.300871 | 3.300871 | 3.300871 |
| | Subscription price | 3.177343 | - | - | - | 3.177343 | 3.177343 | 3.177343 |
| | Market price | 2.403 | - | - | - | 3.177 ^(*) | 3.006 | 3.006 |
| 2002 | No. options | 25,744,700.00 | - | 208,498.91 | - | 1,999,700.00 | 23,536,501.09 | 14,340,901.09 |
| Plan | Exercise ratio | 3.300871 | - | 3.300871 | - | 3.300871 | 3.300871 | 3.300871 |
| | Average subscription price | 2.906507 | - | 2.906507 | - | 2.928015 | 2.905390 | 2.905424 |
| | Market price | 2.403 | - | 2.973 ^(*) | - | 2.654 ^(*) | 3.006 | 3.006 |
| 2002 TOP | No. options | 11,340,000.00 | - | 749,999.02 | - | 90,000.00 | 10,500,000.98 | 6,000,000.98 |
| Plan | Exercise ratio | 3.300871 | - | 3.300871 | - | 3.300871 | 3.300871 | 3.300871 |
| | Subscription price | 2.788052 | - | 2.788052 | - | 2.788052 | 2.788052 | 2.788052 |
| | Market price | 2.403 | - | 2.938 ^(*) | - | 2.537 ^(*) | 3.006 | 3.006 |
| 2002-2004 | No. options ^(**) | 800,000.00 | - | - | 800,000.00 | - | - | - |
| Plan | Exercise ratio | 0.471553 | - | - | 0.471553 | - | - | - |
| | Subscription price | 7.015118 | - | - | 7.015118 | - | - | - |
| | Market price | 2.403 | | | 3.006 | - | - | - |
| Feb. 2002-2004 | No. options ^(***) | 5,940,000.00 | - | | 5,640,000.00 | 300,000.00 | - | - |
| Plan | Exercise ratio | 0.471553 | - | | 0.471553 | 0.471553 | - | - |
| | Subscription price | 5.333441 | - | | 5.333441 | 5.333441 | - | - |
| | Market price | 2.403 | | | 3.006 | 2.531 ^(*) | - | - |

(*) Weighted average price.

(**) Refers to no. 1,330,000 warrants assigned.

(***) Refers to no. 29,000,000 warrants deliberated of which 26,475,000 assigned.

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| Plan | Exercise ratio | Subscription price of shares (euro) | Number of options granted at 12/31/2004 and exercisable from | | | | | Total | Maximum period of options |
|-------------------------|----------------|-------------------------------------|--|---------------|--------------|--------------|--------------|---------------|---------------------------------|
| | | | 2001 | 2002 | 2003 | 2004 | 2005 | | |
| 1999 | 3.300871 | 2.057033 | - | - | - | - | - | - | December 31, 2004 |
| 2000 | 3.300871 | 4.185259 | 5,349,998.00 | 5,349,998.00 | - | - | - | 10,699,996.00 | 5 years starting from each year |
| 2001 | 3.300871 | 3.177343 | - | 31,980,000.00 | - | - | - | 31,980,000.00 | April 15, 2007 |
| 2002 | 3.300871 | 2.928015 | - | - | 6,868,200.70 | 6,908,700.31 | 8,779,600.00 | 22,556,501.01 | 5 years starting from each year |
| | 3.300871 | 2.409061 | - | - | 222,000.04 | 222,000.04 | 336,000.00 | 780,000.08 | |
| | 3.300871 | 2.339080 | - | - | 60,000.00 | 60,000.00 | 80,000.00 | 200,000.00 | |
| 2002 TOP | 3.300871 | 2.788052 | - | - | 3,000,000.49 | 3,000,000.49 | 4,500,000.00 | 10,500,000.98 | 5 years starting from each year |
| 2002-2004 | 0.471553 | 7.015118 | - | - | - | - | - | - | |
| Feb. 2002- Dec. 2004 | 0.471553 | 5.333441 | - | - | - | - | - | - | December 31, 2004 |

■ INDUSTRIAL RELATIONS

During the financial year collective Group bargaining mainly concerned:

Company reorganization

The Group's initiatives to focus on core business activities were carried out in accordance to legal procedures governing transfers of the following company activities:

- Telecom Italia SpA and EMSA Servizi SpA Document Management to Telepost SpA;
- TIM SpA Administrative Services to Shared Service Center S.c.r.l.;
- Loquendo SpA Applications to CITEC SpA;
- Telecom Italia SpA Maintenance and Environmental Services and EMSA Servizi SpA to MP Facility SpA;
- IT Telecom SpA Industries & Services to Shared Service Center S.c.r.l.

Furthermore, during the Group reorganization legal procedures were applied to the following areas:

- Transfer of the Business Solution Mobile activities from IT Telecom SpA to TIM SpA;
- Transfer of the Infrastructures Center activities from IT Telecom SpA to IT Telecom Srl;
- Merger by incorporation of IT Telecom SpA and of Epiclink SpA in Telecom Italia SpA;
- Transfer of EMSA Servizi SpA to Telecom Italia SpA.

An agreement on the reorganization and development plan at Atesia SpA with the Unions was also reached foreseeing the transfer of the Atesia company activities of fixed network telephony to Telecontact Center SpA and the sale of the controlling share of the remaining part of Atesia (concerning TIM and other companies) to an operator in the sector.

The agreement provides for an adjustment to the contractual stipulations with personnel working in these areas in accordance with the "Riforma Biagi" (Biagi Reform law).

Other topics

- Regarding health care, an agreement was made with the unions representing Group executives that allows the Assida's Board of Directors to redefine, with a statutory reform, the system that manages the Fund guaranteeing greater involvement from the adhering companies and a streamlining of company bodies. In this way they are able to act more quickly and efficiently to achieve the Fund's institutional aims.

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- In 2004 early retirement was completed for 20 employees at Gruppo Buffetti as provided for by law No. 416/81.

- On July 14, 2004 a union agreement was signed that ended the resort of CIGS' funds for professional re-training of employees at Olivetti Tecnost Group, according to the two-year reorganizational plan FY 2003-04.

- As regards disabilities and obligations stipulated by law 68/1999, Telecom Italia started a project to guarantee the targeted inclusion of disabled people in the world of work, with innovative use of all the conventional tools provided by this law.

A protocol of understanding was signed with the Labor Unions in which two time periods are set out for the realization of the project; following this the protocol was approved by the Ministry of Labor and Social Policies and associations representing people with disabilities.

The first phase, ending in 2006, foresees the introduction of 200 disabled workers throughout Italy, according to the modalities set out in the protocol, using contractual procedures normally carried out within the company but also telework and remote work.

- On November 12, 2004 two agreements were signed with the Unions for Outsourcing and Training for company workers.

The agreement regarding management of outsourcing processes confirms the use of this tool as an organizational instrument in order to achieve business objectives.

This also allows reinforcing of advanced communication to the Unions of any outsourcing operations as well as strengthening the system of social guarantees for the workers, which Telecom Italia agrees to impose on the companies that take over outsourced activities.

The Training agreement, based on the creation of Fondimpresa, "Interprofessional Fund to boost the continuous training of middle managers, clerical workers and blue collar workers in the companies" will allow companies to benefit from the pertinent funds to realize training courses for employees.

- As regards the Renewal of the Collective National Labor Contract for executives, undersigned by Confindustria and Federmanager on November 2004, an agreement was signed on December 14, 2004 with the coordination the company union representatives of the Group's executives in order to harmonize some of the regulations established in the company with those in the aforementioned Collective National Contract.

■ HEALTH AND SAFETY

During 2004 some important projects began/were consolidated at Group level:

- Research into wellbeing in call centers, managed by a Scientific Committee composed of Italian university professors specialized in Psychology, Ergonomics, and Medicine in the Workplace.
- Assessment of concentration levels of radon gas in some work places by means of scientific collaboration with the Istituto Superiore di Sanita (Superior Health Institute) to develop a working methodology and an accredited laboratory.
- "Environment Project", to guarantee coherent defence of environmental themes within all the

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companies in the Group, in line with the principles and codes set forth in the Sustainability Report and the Code of Ethics.

Furthermore, in order to guarantee and promote health and safety on the job, the following significant activities were carried out in the main companies of the Group:

Telecom Italia SpA

More than 200 specific assessments were carried out to inspect environmental conditions in work places, especially the ones that have been structurally modified;

The physician in charge and the manager of the Servizio di Prevenzione e Protezione (Prevention and Protection service) visited videoterminal workstations 1,541 times;

7,312 videoterminal workers were examined in accordance with the process of health surveillance;

348 company-evacuation tests to test the efficiency of the Plans for Managing Emergencies;

279 specific assessments to check the level of acoustic pollution in the companies;

195 inspections to check the level of exposure to electromagnetic fields for personnel who work on antenna supporting structures;

more than 30,000 training hours were carried out by the Prevention, Protection and Environment Service. Among topics treated were the regulations, the procedures and the related legislation, the managing of emergencies, and also training courses for new recruits.

TIM

The Security Management System

During 2004 two further territorial areas of TIM - Northwest and South 2 - worked to implement the Security Management System in compliance with regulation BSI OHSAS 18001; thanks to a structured path, including training for all personnel involved, the system was activated and inspected in specific Audit cycles. The final certification phase, managed by a third party, will take place within the first months of 2005.

Training

Training courses were constantly held throughout 2004 in the framework of the basic and specialist training programs for all personnel; in particular, in 2004 specific training programs were developed for:

- "Safe Driving", courses for operative personnel aiming at awareness and training of people who frequently use cars for their professional activities.
- "Working at heights" for some Network workers.

Comprehensively, the program involved 2,108 resources for a total of 17,573 hours.

Health

The Campaign of Healthcare Surveillance saw a total of 1,433 resources involved. The examinations covered all video terminal workers.

"Wellbeing in the Call Centers" project:

In agreement with Telecom Italia SpA an experimental project was launched to monitor quality of life of the workers at the TIM Call Center in Torino Rivoli, using subjective, behavioural, physiological and biochemical criteria.

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The following table illustrates data on accidents in Telecom Italia SpA and TIM SpA:

| | Telecom Italia SpA | TIM SpA |
|--|--------------------|---------|
| Total accidents | 732 | 57 |
| Accident severity index ^(*) | 0.37 | 0.2 |
| Frequency rate ^(*) | 9.78 | 3.7 |
| Average duration (in hours) | 154.89 | 155 |
| Unproductiveness rate ^(*) | 1.51 | 0.89 |
| Accidents x 100 workers | 1.48 | 0.54 |

◀ ^(*) The data relating to severity, incidence and unproductiveness refers respectively to:

- the number of conventional days lost per year per thousand hours worked;
- the number of accidents per million hours worked;
- the number of hours lost due to accidents per thousand hours worked.

■ INITIATIVES FOR EMPLOYEES

CRALT

The Telecommunications Workers Company Recreational Club organizes tourist, sports, cultural, recreational and solidarity activities for employees and retired employees from the companies in the Group.

Around 52,000 employees and 8,000 retirees had joined as of December 31, 2004.

ASSILT

At December 31, 2004, more than 217,000 people were enrolled in the Association for Integrative Healthcare for Telecom Italia workers: 68,200 employees, 40,200 retirees and 109,000 family members.

As well as reimbursing healthcare expenses to integrate the National Healthcare Service (561,000 cases in 2004), Assilt created campaigns for preventive medicine and healthcare education, using its mobile diagnostic units and support from public healthcare facilities.

Also in 2004 the programs for multidisciplinary Oncological Prevention to discover breast and skin pathologies continued, as did the program, which began in 2003, for respiratory allergies.

Furthermore, Assilt, in collaboration with OSSFAD, supported Telecom Italia's "No Smoking" initiative for the benefit of its employees.

Initiatives for employees' children

Summer Holiday Camps provided 4,644 children with an opportunity to spend two weeks in one of the 11 camps reserved specifically for them (5 at the seaside, 6 in the mountains).

Activities in the camps are organized around an educational project which is periodically updated with input from university professors and experts in the sector.

Around 300 young people were reimbursed their enrolment fees for the first year at university; 60 adolescents took part in a four-week study holiday abroad to study English and 20 adolescents between the ages of 16 and 17 went away for a school year abroad (13 in the United States and 7 in various European countries).

ALATEL

Association for the Elderly (ALATEL and Gold Pins)

Following the merger between Telecom Italia and Olivetti, the Senior Workers' Association in the Telecom Italia Group (over 26,000 members, of which a third are working employees) started a collaboration with the Olivetti Gold Pins Association (about 6,400 members).

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■ WORK AND HUMAN RIGHTS IN LATIN AMERICA

The following shows the main actions taken by the Group in Latin American countries to implement the Principles of the Global Compact regarding human rights and safeguards for work.

Human Rights

At TIM Peru, as of November 2003 a document called "Internal Manual of Labor" was introduced which defines clear rules for rights and obligations of Company employees.

This document is given out at the moment of employment, listing the person's rights regarding: respect for ideas/personal contributions, privacy, health and safety, equal opportunities, facilities/aids for disabled personnel.

Human Resources' administration and welfare departments ensure the observance and respect of the rules.

In the Company Code of Ethics and yet another document called "TIM Peru Policy for Conduct", the principle of mutual respect between workers without discrimination on the basis of race, religion or nationality is cited. This principle is strictly applied also when recruiting personnel.

TIM Peru, through its activities in the struggle against child poverty, was considered by UNICEF to be a "Friendly UNICEF Enterprise".

In TIM Brazil, where there are specific regulations to guard against discrimination on the basis of race, religion and gender, both in the Federal Constitution (which respects the principles of the International Labour Organization and the Universal Declaration of Rights for Man) and in national legislation, it was not deemed necessary to introduce a specific policy on the subject; it was left to Human Resources to monitor the fundamental processes relating to human resources (recruitment, management and development) making use of its own holding and territorial organizations. The first Company Code of Ethics is being distributed to employees; it cites the general principles of the Group and supplements them according to specific local requirements.

In Chile the government has set up a special body to monitor compliance with guidelines to safeguard relationships between companies and workers. Entel Chile fully respects these regulations.

At Entel Bolivia, the Collective Labor Contract in force between the parties stipulates respect for dignity and human rights of employees and fosters equal opportunities for men and women; it especially promotes female participation in company activities.

Safeguards for Labor

On the subject of freedom to belong to associations, in Group companies in Latin America specific policies that refer to and regulate in detail the general rules of each country are usually not formalized.

The collective contracts of all the operative companies in TIM Brazil were renewed in 2004, with new salaries and contracts (for example fixed-term contracts).

Entel Bolivia actively cooperates with the Unions to guarantee freedom to associate in conformity with local labor laws. The country's constitution stipulates that no-one may be forced to perform any job without proper remuneration and Entel Bolivia monitors observance of this provision.

In Entel Chile there are professional continuing-education programs about labor law for union members; relevant regulations are published on the company Intranet.

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Regarding union representation the following data has been collected:

- TIM Brazil: about 6% of workers are members of collective union organizations; results of negotiations affect the entire employee base, including non members;
- TIM Peru: membership is not high given the traditional weakness of union associations in this country;
- Entel Bolivia: 48% of workers are members of union associations;
- Entel Chile: 39% of personnel are members of union associations and 59% of them benefit from results of negotiations.

When there are company reorganizations, the company's obligations to the workers and union representatives differ from one country to another:

- TIM Brazil: there are no particular formalities to observe with workers and union representatives; the only duties are towards institutional bodies such as ANATEL (regulatory) and CADE (anti-trust);
- TIM Peru: although there are no formalities at legislative level, specific measures to involve employees and listen to them have been adopted, such as open forums, focus groups, meetings to talk directly to top management, etc.;
- Entel Bolivia: developed a series of tools to prevent possible conflicts by means of wide-spread information about company plans and policies.

These tools are:

- Foro Estratégico (Strategic Forum): it meets bi-monthly to discuss industrial policies and strategies, financial and legislative scenarios, market trends, technological innovations and investments.
- Observatorio (Observatory): with representatives of the company and the workers, it aims to analyze and discuss topics of general interest such as markets and competition, action to improve working conditions, action to improve and preserve company profits.
- Sistema de Informaciones (Information System): ENTEL reports information every four months to CEN of FESENTEL (executive committee of the Federation Labor Union) about:
 - developing scenarios in the sector;
 - evolution of internal occupational levels;
 - trends for main economic indicators in the sector;
 - evolution of prospects for production and investment;
 - evolution of technological and organizational aspects and their impact on organization of work;
 - notable programs in training and professional continuing education.
- Entel Chile: there aren't any special obligations, but special operations affecting profits are discussed with union representatives.

On the subject of respecting regulations that protect child labor, all companies in the Group conform to the principles in national and international regulations. To counter exploitation and unfavourable socio-economic conditions, specific initiatives of a social nature were activated at a national level:

- TIM Brazil: projects for social inclusion and to fight discrimination through teaching music (i.e. Tim Musica nas Escolas, Tim Arteducação, etc.), reading and writing projects (i.e. Alfa 100, Pastoral da Criança), humanitarian aid programs (i.e. TIM Ajuda sem Fronteiras).
- TIM Peru: Carabayllo project (fighting child poverty), program to train young people and prepare them for work.

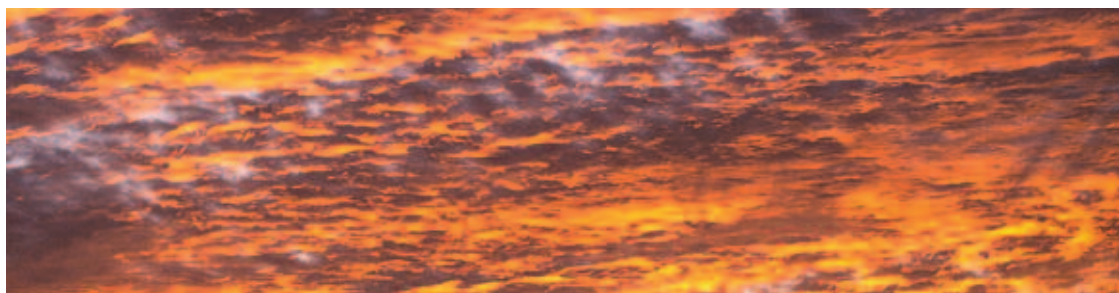
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To create a shared-values base and raise the level of involvement of employees in company management topics, initiatives were undertaken to spread Group values and communicate the company's strategic programs. Results of these efforts were monitored with polls using the questionnaire "Group Photo" that reaches all the employees in the companies every year.

In TIM Brazil and Entel Chile there are active programs talent enhancement by enrolling people in post-graduate Master studies with company contributions towards expenses. In Entel Bolivia there is an internal job-posting system to fill vacancies through an intranet publication or by posting available positions on a company notice board.

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SHAREHOLDERS



■ FINANCIAL COMMUNICATION

In 2004 Telecom Italia Group issued an ever more accurate and fast financial communication in line with preceding years, focussed on fundamental values of its fixed-telephone and mobile businesses.

Investor Relations activities continued to be managed by a Central Department which also managed Merger & Acquisition activities, which in turn reports directly to the chief executive so as to ensure the fastest and most efficient communication possible.

The www.telecomitalia.it website provides comprehensive and accurate information with institutional documents such as the year-end financial statement and the Sustainability Report, and communiqués about company activities and its salient operations in the market, along with on-line quotations for the Group's shares.

At year-end 2004 a project to redesign the website and give ample space to Sustainability began.

During 2004 the company organized over 100 formal encounters with the market (sell side analysts, institutional investors and specialized national and international press) such as quarterly conference calls, road shows, attendance at conventions and press conferences. There were also daily contacts with financial analysts and investors, both direct and by telephone.

On March 25 and 26, 2004 the yearly meeting with the financial community was held in Milan to present the Group's targets for the three-year period 2004-2006.

In December the company announced the merger with its subsidiary, Telecom Italia Mobile following a public bid to acquire 2/3 of ordinary TIM shares on the market and the entire amount of the saving shares. A comprehensive and timely information campaign was provided to the market by conference call to institutional investors and the necessary documentation was published on Telecom Italia's website.

■ SAFEGUARDING PRIVACY AND PROTECTING DATA

In 2004 Telecom Italia Group's concrete commitment to guarantee observance of current regulations concerning the protection of personal data (Legislative Decree 196/03, so called "Privacy Code") continued.

In particular, the "Privacy Project", realized by Telecom Italia's Corporate and Legal Affairs, coordinated and delivered the guidelines and policies to guarantee coherence and the correct

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application of new regulations introduced with the privacy code and the Garantor's regulations to protect personal details (i.e. new notification to the Privacy Authority, methods of getting the information to the people involved, video surveillance) to all the companies in the Group.

Some of the main initiatives undertaken were:

- the setting up of various operational procedures to comply with the law, in Telecom Italia and in the rest of the Group (System for regulation of personal data, internal control activities, assigning the privacy role in contractual relationships with third parties, dealing with client request about privacy, etc.);
- preparation, in accordance with principles established by the Privacy Authority, relative to the handling of personal data in the new telephone books, sent to all Telecom Italia clients in January and February 2005. The briefing includes a form wherein the client can give explicit consent for the use of his data for different purposes;
- spreading awareness of a privacy culture by means of an on-line course for all Group employees on privacy laws, with special mention of security measures and a day-long training course for all the people in charge of privacy in the Group's companies;
- a program to carry out spot checks in Telecom Italia central and territorial facilities and companies that handle personal data belonging to Telecom Italia, to ensure that privacy laws are complied with correctly. Controls were especially careful in regard to compliance when managing personnel, dealing with requests of interested parties (employees and clients), putting in place the required minimal security measures, and giving the management of personal data to third parties;
- ascertaining the extent to which the companies in the Group apply regulations and monitoring action eventually taken to improve it.

Lastly, in accordance with rule 26 of attachment B (Technical Manual about the required minimal security measures) of the Privacy Code, Telecom Italia drew up the Personal Data Security document on Security (DPS) FY 2004. This document describes the technical and organizational criteria adopted to protect common, sensitive and legal personal data handled with information technology tools; the DPS also foresees a training project to inform people responsible of handling personal data about security measures related to identified risks.

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■ CORPORATE GOVERNANCE

INTRODUCTION

As indicated in earlier annual corporate governance reports (see, in particular, the 2003 report), the Company's system of corporate governance is based on the central role of the Board of Directors, the complete transparency of operational decisions, both internal and in relation to the market, efficient and effective internal controls and rigorous rules governing conflicts of interest. The backbone of the system consists of a series of codes, rules and procedures.

In 2004 these documents were carefully reviewed and, where necessary, updated in response to legislative and regulatory developments and changes in international best practices and the Company's operations. Furthermore, some amendments and additions were made to the bylaws, partly to take account of the changes in company law introduced by the "Vietti reform".

This section of the report describes the innovations concerning Telecom Italia's system of corporate governance and how it operated during the year.

■ BOARD OF DIRECTORS

■ Role and tasks

The Board of Directors has the power (and the duty) to lead the Company and pursue the primary objective of creating value for its shareholders. To that end the Self-Regulatory Code reserves several especially important tasks exclusively to the Board, including those of:

- (i) examining and approving strategic, business and financial plans;
- (ii) reviewing and approving the annual budget;
- (iii) examining and approving transactions – including investments and disinvestments – with a substantial impact on the Company's activity in view of their nature, strategic importance or size;
- (iv) the adequacy of the general organizational and administrative structure of the Company and the Group;
- (v) preparing and adopting the Company's corporate governance rules and the Group's governance guidelines;
- (vi) nominating the persons who are to hold the offices of Chairman and Managing Director in strategic subsidiaries;
- (vii) reviewing and approving the periodic financial reports.

■ Meetings

In 2004 the Board of Directors met 12 times. Board meetings were always well attended, with more than 90% of the directors present on average (the independent directors recorded an attendance rate of 94%).

When board meetings were to be held, documentation permitting effective participation in the proceedings was provided in advance.

In October 2004 the Company released the calendar of corporate events scheduled in 2005.

In consideration of the planned merger between Telecom Italia and Tim, a revised version of the calendar was released in December 2004.

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■ Appointment of directors

The bylaws require the members of the Board of Directors to be elected using the slate system. This ensures an adequate representation on the Board of persons not representing the shareholders commanding a majority of votes in shareholders' meetings since they are drawn from slates presented by minority shareholders (in fact slates may be presented by shareholders who, individually or together with others, hold at least 1% of the voting capital).

The present Board was appointed by the shareholders' meeting held on 6 May 2004, on the basis of two slates: one presented by the majority shareholder, Olimpia S.p.A., and the other by a group of Italian institutional investors.

The slates were accompanied by the profiles of the individual candidates to enable shareholders to evaluate their personal and professional qualifications. The curricula submitted when the slates were presented are on the Company's website under Investor Relations.

■ Composition of the Board

Telecom Italia's bylaws provide for the Board of Directors to have not less than 7 and not more than 23 members. The shareholders' meeting of 6 May 2004 fixed the number of directors at 19 and established that they would remain in office until the date of the approval of the 2006 financial statements.

The Board is made up of the following directors:

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| Marco Tronchetti Provera | Chairman |
| Gilberto Benetton | Deputy Chairman |
| Carlo Buora | Managing Director |
| Riccardo Ruggiero | Managing Director and General Manager |
| Paolo Baratta | Member of the Remuneration Committee |
| John Robert Sotheby Boas | |
| Giovanni Consorte | |
| Domenico De Sole | Member of the Internal Control and Corporate Governance Committee and the Strategy Committee |
| Francesco Denozza | Member of the Internal Control and Corporate Governance Committee |
| Luigi Fausti | Chairman of the Remuneration Committee |
| Guido Ferrarini | Chairman of the Internal Control and Corporate Governance Committee (Lead Independent Director) |
| Jean Paul Fitoussi | |
| Gianni Mion | |
| Massimo Moratti | |
| Marco Onado | Member of the Internal Control and Corporate Governance Committee and the Strategy Committee |
| Renato Pagliaro | |
| Pasquale Pistorio | Member of the Remuneration Committee and the Strategy Committee |
| Carlo Alessandro Puri Negri | |
| Luigi Roth | |

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The directors Francesco Denozza, Guido Ferrarini, Jean Paul Fitoussi and Pasquale Pistorio were elected from the slate presented by the group of institutional investors and the others from the slate presented by Olimpia S.p.A., which at present holds 21,8% of the ordinary share capital. The offices held by the directors in other listed companies and other large financial, banking and insurance companies are shown below:

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| Marco Tronchetti Provera | Chairman of Camfin, GPI - Gruppo Partecipazioni Industriali S.p.A., Marco Tronchetti Provera & C. S.p.A., Olimpia S.p.A., Pirelli & C. S.p.A. and Pirelli & C. Real Estate S.p.A. |
| Gilberto Benetton | Chairman of Autogrill S.p.A. and Edizione Holding S.p.A.; Deputy Chairman of Olimpia S.p.A.; Director of Autostrade S.p.A., Banca Antonveneta S.p.A., Benetton Group S.p.A., Lloyd Adriatico S.p.A., Mediobanca S.p.A., Pirelli & C. S.p.A. and Schemaventotto S.p.A. |
| Carlo Buora | Chairman of Telecom Italia Mobile S.p.A.; Managing Director of Pirelli & C. S.p.A.; Director of Mediobanca S.p.A., Olimpia S.p.A., Pirelli & C. Real Estate S.p.A., Ras S.p.A. and Rcs Mediagroup S.p.A. |
| Riccardo Ruggiero | – |
| Paolo Baratta | Director of Banca Finnat Euroamerica |
| John Robert Sotheby Boas | – |
| Giovanni Consorte | Chairman and Managing Director of Unipol Assicurazioni S.p.A.; Deputy Chairman and Managing Director of Unipol Banca S.p.A. and Unipol Merchant Banca per le Imprese S.p.A.; Deputy Chairman of Aurora Assicurazioni S.p.A.; Director of Euresa Holding S.p.A., and Hopa S.p.A. |
| Domenico De Sole | Director of Procter & Gamble and Bausch & Lomb |
| Francesco Denozza | – |
| Luigi Fausti | Chairman of Patrimonio Immobiliare dello Stato S.p.A.; Director of Monrif S.p.A. |
| Guido Ferrarini | Chairman of TLX S.p.A.; Director of Autostrade S.p.A. |
| Jean Paul Fitoussi | – |
| Gianni Mion | Managing Director of Edizione Holding S.p.A. and Schemaventotto S.p.A.; Deputy Chairman of Telecom Italia Mobile S.p.A.; Director of Telecom Italia Media S.p.A., Autogrill S.p.A., Autostrade S.p.A., Banca Antonveneta S.p.A., Benetton Group S.p.A., Cartiere Burgo S.p.A., Luxottica Group S.p.A., Olimpia S.p.A. and 21Investimenti S.p.A. |
| Massimo Moratti | Director of Interbanca S.p.A. and Pirelli & C. S.p.A. |
| Marco Onado | Chairman of Pioneer Global Asset Management S.p.A. (from December 2004); Director of Unicredit Banca Mobiliare (until the 2004 AGM, following the appointment to the Board of Pioneer Global Asset Management); |
| Renato Pagliaro | Director of Cartiere Burgo S.p.A. and RCS Mediagroup S.p.A.; Co-General Manager of Mediobanca S.p.A. |
| Pasquale Pistorio | Chairman and Managing Director of STMicroelectronics S.p.A. |
| Carlo Alessandro Puri Negri | Deputy Chairman and Managing Director of Pirelli & C. Real Estate S.p.A.; Deputy Chairman of Camfin S.p.A. and Pirelli & C. S.p.A.; Director of Capitalia S.p.A. and Olimpia S.p.A. |
| Luigi Roth | Chairman of Fondazione Fiera di Milano; Director of Art'è S.p.A., Intesa Gestione Crediti S.p.A., Banca MB S.p.A. and BPM Private Equity |

■ Independent directors

The Company has adopted criteria conforming with international best practice and the Italian corporate governance code, known as the Preda Code, to qualify directors as “independent”. In the light of the declarations submitted and the annual assessment carried out by the Board of Directors, 10 of the 19 directors qualify as independent, namely: Paolo Baratta, John Robert Sotheby Boas, Domenico De Sole, Francesco Denozza, Luigi Fausti, Guido Ferrarini, Jean Paul Fitoussi, Marco Onado, Pasquale Pistorio and Luigi Roth.

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The directors in question:

- (i) neither have nor have recently had, directly, indirectly or on behalf of third parties, business relationships of a significance able to influence their autonomous judgement with the Company, its subsidiaries, the executive directors or the shareholder or group of shareholders who control the Company;
- (ii) do not hold, directly, indirectly or on behalf of third parties, equity interests allowing them to control the Company or exercise a significant influence over it;
- (iii) do not participate in shareholders' agreements to control the Company or containing clauses regarding the composition of the Board of Directors or its decisions. This requirement is interpreted broadly, with an eye to "substantial" independence. Accordingly, "participation in shareholders' agreements" precludes independence when a director has significant relationships with the natural or legal persons that are parties thereto;
- (iv) are not close relatives of executive directors of the Company or of persons in the situations indicated above.

During the year the Board of Directors of Telecom Italia S.p.A. decided it was desirable to appoint a Lead Independent Director, with the aim of further enhancing the role of the independent directors.

Professor Guido Ferrarini, Chairman of the Internal Control and Corporate Governance Committee, was chosen to be the Lead Independent Director. The position is intended to provide a point of reference and coordination for the needs and inputs of the independent directors and ensure they can decide with the greatest possible autonomy with respect to the management. Among other things, the Lead Independent Director is authorized to call, at his own initiative or at the request of other directors, special meetings of the independent directors (Independent Directors' Executive Sessions) to discuss issues related to the working of the Board or operational activity (with the possibility of requesting the participation of members of the management).

One such Independent Directors' Executive Session was held before the meeting of the Board called on 7 December 2004 to launch the plan for the merger of Tim into Telecom Italia.

The meeting was devoted to examining the terms and conditions of the transaction.

The independent directors were assisted by Goldman Sachs, the advisor selected directly by the Internal Control and Corporate Governance Committee (see below).

■ Executive directors

The authority to grant delegated powers to directors and revoke such mandates is reserved to the Board of Directors, which also establishes their limits, the manner in which they may be exercised and the intervals at which persons with delegated powers must report on their activity. The authority to determine the duties and powers of the general managers is also reserved to the Board of Directors.

On 6 May 2004, in the first meeting following its renewal, the Board of Directors appointed Marco Tronchetti Provera as Chairman, Carlo Orazio Buora and Riccardo Ruggiero as Managing Directors, and Gilberto Benetton as Deputy Chairman.

Looking beyond the system of powers delegated to the executive directors, it is worth noting that in practice decisions concerning transactions of particular significance are taken by the Board, even though they theoretically fall within the scope of the delegated powers. In fact, delegation does not mean the assignment of exclusive powers but is rather the solution adopted by Telecom Italia to ensure, in terms of the Board's organization, a high degree of operational flexibility, both within the Company and in relation to third parties.

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The powers delegated by the Board to the Company's executive directors are as follows:

- Marco Tronchetti Provera (Chairman) is entrusted with the powers needed to carry out every transaction relating to the Company's activity, apart from the issue of guarantees for obligations of Telecom Italia or its subsidiaries where the individual amount exceeds euro 250 million and for obligations of third parties where the individual amount exceeds euro 100 million and apart from investments and acquisitions and disposals of shareholdings involving control or affiliation or businesses or divisions where the value of the transaction exceeds euro 250 million. For the issue of guarantees where the amount exceeds the above thresholds, the Chairman must sign jointly with a Managing Director. The Chairman is authorized to act as a matter of urgency in the matters for which the Board of Directors is competent and is charged with overseeing the management of confidential information and ensuring the effectiveness and adequacy of the internal control system. Lastly, the Chairman is authorized to represent the Company with no limit to the amount involved in the performance of acts vis-à-vis any regulatory authority or governmental body, in judicial and extra-judicial settlements, and in arbitration proceedings and shareholders' and other meetings.
- Carlo Buora (Managing Director) is entrusted with the powers needed to carry out every transaction relating to the Company's activity, apart from investments and acquisitions and disposals of shareholdings involving control or affiliation or businesses or divisions and in general of goods and services where the value of the individual transaction exceeds euro 150 million. He may issue guarantees for obligations of Telecom Italia or its subsidiaries where the individual amount does not exceed euro 150 million and for obligations of third parties where the individual amount does not exceed euro 50 million. He must sign jointly with the other Managing Director (Riccardo Ruggiero) for the issue of guarantees for obligations of Telecom Italia or its subsidiaries where the individual amount is between euro 150 million and euro 250 million and for obligations of third parties where the individual amount is between euro 50 million and euro 100 million. Carlo Buora is also authorized to represent the Company with no limit to the amount involved in the performance of acts vis-à-vis any regulatory authority or governmental body, in judicial and extra-judicial settlements, and in arbitration proceedings and shareholders' and other meetings.
- Riccardo Ruggiero (Managing Director) is entrusted with the powers needed to carry out every transaction relating to the Company's activity, except for investments and acquisitions and disposals of shareholdings involving control or affiliation, businesses or divisions and in general of goods and services where the value of the individual transaction exceeds euro 75 million. He may issue guarantees for obligations of Telecom Italia or its subsidiaries where the individual amount does not exceed euro 75 million and for obligations of third parties where the individual amount does not exceed euro 25 million. Riccardo Ruggiero is also authorized to represent the Company with no limit to the amount involved in the performance of acts vis-à-vis any regulatory authority or governmental body, in judicial and extra-judicial settlements, and in arbitration proceedings and shareholders' and other meetings.

For the purposes of compliance with the above-mentioned thresholds, individual transaction is to be understood as meaning a set of transactions that are interconnected within the same strategic or executive structure.

Procedures adopted on a self-regulatory basis govern the information contained in the executive directors' reports to the Board of Directors and the Board of Auditors on the action they take using their delegated powers and the implementation of transactions approved by the Board of Directors. In particular, the Company has adopted a procedure formalizing the rules and methods for gathering and transmitting information on their activity, transactions with major implications

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for the profitability, financial position and/or assets and liabilities of the Company and the Group, transactions with related parties (including intra-group business) and atypical or unusual transactions.

■ Directors' remuneration

The shareholders' meeting established the total annual remuneration of the Board of Directors at euro 2.7 million (previously it had amounted to Lit. 3.6 billion), divided by the Board as follows:

- euro 114,000 to be paid to each director in office;
- an additional euro 63,000 to be paid to each of the four members of the Internal Control and Corporate Governance Committee (Guido Ferrarini, Francesco Denozza, Domenico De Sole and Marco Onado);
- an additional euro 52,000 to be paid to each of the three members of the Remuneration Committee (Luigi Fausti, Paolo Baratta and Pasquale Pistorio);
- an additional euro 20,000 to be paid to each of the three members of the Strategy Committee other than the Chairman of the Board and the Managing Director Carlo Buora (Domenico De Sole, Marco Onado and Pasquale Pistorio);
- an additional euro 20,000 to be paid to the director appointed to the Supervisory Panel set up under Legislative Decree 231/2001 (Guido Ferrarini).

The Board's Remuneration Committee, set up in 2000, is charged with fact-finding and advisory functions. In particular, it formulates proposals for the remuneration of the directors who hold particular offices and for the criteria for the remuneration of the Company's senior management. The Committee is composed exclusively of independent directors.

On 6 May 2004 the Board appointed the following directors to be members of the Remuneration Committee: Paolo Baratta, Pasquale Pistorio and Luigi Fausti, chairman. Subsequent to the renewal of the Board of Directors, the Committee met twice in 2004.

The current remuneration system for executive directors provides for them to receive a fixed component and an additional payment subject to the achievement of the objective for consolidated EBIT with positive Delta EVA, in other words when value is created for all investors.

There is no provision for stock options for either executive or non-executive directors. ⁽¹⁾

Further information on the compensation paid to the executive directors can be found in the relevant table in the Notes to the financial statements.

◀ (1) The Managing Director Riccardo Ruggiero is an exception in this respect since, prior to his being co-opted to the Board of Directors, as General Manager he was among the beneficiaries of a stock-option plan.

The remuneration system for management provides performance and loyalty incentives on top of a basic salary. The incentives include both cash payments and stock options. Details on the latter are contained in the Report on Operations in the section on "Human resources".

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■ THE INTERNAL CONTROL SYSTEM

■ The internal control system, internal auditing and the organizational model

The Company's internal control system has developed as a process intended to achieve substantial and procedural fairness, transparency and accountability by ensuring that transactions and, more generally, business-related activities are efficient and can be known and verified, that accounting and operational data are accurate, that applicable laws and regulations are complied with, and that the assets of the business are safeguarded, not least with a view to preventing the perpetration of fraud against the Company and financial markets.

The cardinal rules of the Company's internal control system are:

- (i) separation of roles in the performance of the principal activities involved in each operating process;
- (ii) traceability and constant visibility of decisions;
- (iii) decision-making on an objective basis.

The Board of Directors is responsible for the internal control system. It lays down the guidelines for the system and verifies that it is adequate and works effectively, making sure that the main corporate risks are appropriately identified and managed. To this end the Board uses the Internal Control and Corporate Governance Committee and a suitably independent person endowed with sufficient resources to perform the internal control function.

It is the Chairman of the Board who determines the mechanisms of the system and the manner in which it is to be implemented under the guidelines established by the Board; he is also responsible for ensuring the system's overall adequacy, its effectiveness and its adaptation to changes in operating conditions and the legislative and regulatory framework.

The basic functions of the person responsible for internal control are to verify the adequacy and effectiveness of the system and, where anomalies are found, to recommend the necessary remedies. The Board has appointed the Company's internal auditor (Telecom Italia Audit), in the person of the director assigned to the task, to be responsible for its internal control system. This company reports on its activity to the Board of Directors, the Internal Control and Corporate Governance Committee and the Board of Auditors.

Any maintenance work on the internal control system is performed by the competent sectors of the Company or Group companies. The efficient operation of the system is promoted by the appointment of managers of particular standing and authority within the organization as "persons responsible for implementation" (currently the head of the Group's Human Resources and the head of the Wireline Business Unit).

Internal auditing has been entrusted to the above-mentioned consortium company Telecom Italia Audit, in which Tim and TI Media also hold equity interests. The solution adopted maximizes the independence of the internal audit function with respect to Telecom Italia's corporate structures.

The Company's internal control system is completed by the so-called 231 Organizational Model, which goes beyond the mere application of the provisions of Legislative Decree 231/2001, since it provides a paradigm for the conduct of all those who act in the Company's name and on its behalf. More specifically, the model comprises "principles for dealings with governmental bodies" (elaborated as a set of rules for relations with representatives of such bodies) and "internal control checklists" listing the main stages of every process, the offences that may be committed in relation to individual processes, and the control activities to prevent the related risks from arising.

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The organizational model is reviewed periodically in the light of experience in its application and changes to the law subsequent to the initial framework created by Legislative Decree 231/2001. Monitoring of the functioning and compliance with the model is performed by a Supervisory Panel made up of a member of the Board of Auditors (Ferdinando Superti Furga, chairman), an independent director on the Internal Control and Corporate Governance Committee (Guido Ferrarini) and the person responsible for the internal control system. This ensures that the members of the Panel embody all the professional skills involved in the control of the Company's operations. The membership, term of office and powers of the present Panel were confirmed by the Board of Directors in their meeting on 6 May 2004.

The Supervisory Panel will encourage the Board of Directors to adapt the model as needed to changes in the legislative and regulatory framework, the nature of the Company's business activities and the ways they are conducted. It reports to the Board of Directors, the Internal Control and Corporate Governance Committee and the Board of Auditors on the checks performed and their results.

The shareholders' meeting of 6 May 2004 resolved that the member of the Board of Auditors serving on the Supervisory Panel should be paid a gross annual fee of euro 20,000, the same as that assigned by the Board of Directors to the member of the Internal Control and Corporate Governance Committee serving on the Panel.

Lastly, it should be noted that a special unit has been created within Telecom Italia Audit to provide operational support to the Supervisory Panels of Group companies by handling reports of violations of the organizational model and conducting compliance audits on the basis of the data received by way of the information flows that have been put in place.

■ The Internal Control and Corporate Governance Committee

Since 2000 Telecom Italia has had a Board of Directors Internal Control and Corporate Governance Committee, charged with advisory functions and the formulation of proposals. The Committee:

- (i) evaluates the adequacy of the internal control system;
- (ii) evaluates the work plan prepared by the person responsible for internal control, from whom it receives periodic reports;
- (iii) assesses, together with the heads of the Company's administrative departments and the external auditors, whether the accounting policies have been correctly applied and are homogeneous for the purpose of preparing the consolidated financial statements;
- (iv) evaluates the proposals made by the external auditors in order to be awarded the appointment, the audit plan and the results set out in the letter of suggestions;
- (v) reports to the Board of Directors at least once every half year on the activity performed and the adequacy of the internal control system;
- (vi) performs the additional tasks that may be assigned to it by the Board of Directors, particularly as regards relations with the external auditors; and
- (vii) monitors compliance with the rules of corporate governance and their periodic updating.

The Committee is composed exclusively of independent directors, in its meeting on 6 May 2004 the Board of Directors appointed Domenico De Sole, Francesco Denozza, Marco Onado and Guido Ferrarini (chairman).

In 2004 nine meetings were held, of which seven were after the renewal of the Board of Directors; attendance at the meetings was almost 100 per cent, with a member absent on just two occasions. Committee meetings are also attended by the Chairman of the Board of Auditors or by the auditor he designates. Where it is deemed desirable in the light of the issues on the agenda, the Committee and the Board of Auditors may hold joint meetings.

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In 2004 the Committee contributed significantly to the process of implementing the Company's corporate governance mechanisms, taking part in the related analyses, drafting and updating. In particular, the Committee agreed with amendments to the Group Code of Ethics designed to satisfy the requirements in connection with the obligations arising from the fact that Telecom Italia is registered in the United States pursuant to the Securities Exchange Act of 1934 and is therefore subject in some respects to US securities laws.

It also agreed with the Rules of Proceeding for the Shareholders' Meeting and the amendments made to the bylaws to adapt them to the changes in company law introduced by the "Vietti reform". The Committee examined and approved the setting up of the Strategy Committee and the introduction of the position of Lead Independent Director; it also took part in the revision of the Company's rules and regulations concerning transactions with related parties and in the updating of the 231 Organizational Model.

Last year the Committee drew up the proposal to be submitted by the Board of Directors for the appointment of Reconta Ernst & Young to audit the financial statements for the years 2004-2006; and examined issues concerning periodic financial reports (Company and consolidated financial statements, annual reports and half-yearly reports). It agreed with the launch of the so-called 404 Project aimed at identifying the steps to be taken to ensure compliance with Section 404 of the Sarbanes-Oxley Act. It followed the A/351 proceeding instituted by the Antitrust Authority in relation to alleged abuses of dominant position by Telecom Italia. In this connection it evaluated and agreed with the strategy adopted by management, first during the Authority's investigation and then in the appeal to the Lazio Administrative Tribunal. At the request of the Board it also monitored the steps taken by the Company to comply with the order issued by the Authority at the close of its investigation.

The Committee also played an active role in connection with the plan for the merger of Tim into Telecom Italia and verified the procedural correctness of the valuation methods and the fairness of the transaction as a whole. As mentioned earlier, it also chose Goldman Sachs as the advisor to act in a guarantee capacity alongside the financial advisors selected by the Company's management.

The Committee periodically checked the work of the internal auditor, Telecom Italia Audit, and in particular examined the report on the activities performed in carrying out the 2003 Audit Plan, the checks performed under the 2004 Audit Plan, and the progress made by the Group projects called Control Risk Self-Assessment and Check-Up of Administrative Systems. The Committee also examined and approved the audit plan for 2005 prepared by the person responsible for internal control and discussed the plan for the 2005 statutory audit with representatives of the external auditors, Reconta Ernst & Young.

■ STRATEGY COMMITTEE

In 2004 a Board of Directors Strategy Committee was established to increase the involvement of the Board in the Company's strategic decision-making, especially as regards guiding the evolutionary processes under way in the Group's business in the light of the rapid transformation of technologies and markets.

The Strategy Committee consists of the Chairman of the Board (who ensures the alignment and coordination of the activities of the Committee, the Board and management), the Managing Director charged with Group-wide corporate functions (and therefore not involved in the management of Business Units (Carlo Buora), and three non-executive directors (Domenico De Sole, Marco Onado and Pasquale Pistorio) specialized in the fields of technology, organizational strategies and corporate finance.

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The Committee is entrusted with the task of assisting the Board of Directors in making strategic choices in the light of competitive developments, with special reference to decisions concerning:

- the potential evolution of the structure of the telecommunications industry;
- the strategic positioning and business models of the Group;
- the evolution of the Group's organization in relation to its business models;
- the evolution of the Group's corporate and financial structure;
- the monitoring of the stage reached in the process of change.

In addition to calling on the heads of units within the Company, the Committee may employ consultants and external experts. It reports on its activity to the Board of Directors at least once a year, at the time the budget is presented.

■ BOARD OF AUDITORS

The Company's Board of Auditors took office in May 2003 and consists of five auditors: Ferdinando Superti Furga (chairman), Salvatore Spiniello and Gianfranco Zanda (elected from the slate presented by Olimpia) and Rosalba Casiraghi and Paolo Golia (elected from the slate presented by institutional investors).

The offices held by the auditors in other listed companies are shown below:

| | |
|--------------------------|--|
| Ferdinando Superti Furga | Director of Ipi S.p.A. and Risanamento S.p.A.; Auditor of Arnoldo Mondadori Editore S.p.A. and Edison S.p.A. |
| Rosalba Casiraghi | — |
| Paolo Golia | — |
| Salvatore Spiniello | Director of Fondiaria Sai S.p.A.; Chairman of the Board of Auditors of Immobiliare Lombarda S.p.A.; Auditor of Edison S.p.A., Telecom Italia Media S.p.A. and Unicredit Banca S.p.A. |
| Gianfranco Zanda | Auditor of Tim S.p.A. |

The Board of Auditors plays a key role in the Company's system of corporate governance.

In addition to the meetings of the Board of Auditors (14 in the year, some of which were held jointly with the Internal Control and Corporate Governance Committee), the auditors participated in the twelve meetings of the Board of Directors, so that contacts between the members of the two bodies were frequent.

The importance of the Board of Auditors is confirmed by the choices made with regard to US company law. In fact, as indicated in the annual report for 2003, the Board of Auditors is the Company's Audit Committee for purposes of the applicable US legislation.

In view of the requirement that the Audit Committee approve all the services the auditing firm (and associated persons) supply to the issuer and its directly and indirectly controlled subsidiaries, the Company has adopted a Group Procedure for the Appointment of Auditors.

In particular, this provides on a general basis for the centralized control of relations with auditing firms to prevent engagements for non-audit services being granted that fail to comply with the applicable Italian or US law and that ultimately could undermine auditor independence.

The procedure regulates the engagement of auditing firms and persons associated with them on a continuous basis, distinguishing between engagements that must be individually authorized in advance by the Audit Committee and those falling within categories subject to a generic authorization. The procedure significantly restricts the power of the Board of Directors (and the management) while enhancing the control function performed by the Company's Board of Auditors.

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The Company has also adopted the principle of employing the same auditing firm throughout the Group; in fact the appointment of other firms must be agreed in advance with the parent company following a reasoned request on which Telecom Italia's Board of Auditors gives its opinion on the basis of inquiries made by the person responsible for internal control.

In order to make available the broad range of information needed by the Board of Auditors to perform its control function effectively, a procedure has been put in place, as mentioned earlier, for the collection and transmission to the members of the Board of Auditors (and the directors) of information on: the activity carried out by the Company; the transactions of greatest significance for the Company's profitability, financial position and assets and liabilities; transactions with related parties (including intra-group transactions); and atypical and unusual transactions.

The procedures referred to above can be found on the Company's website under Investor Relations.

In addition to the tasks performed in its Audit Committee capacity, the Board of Auditors carried out supervisory functions provided for under Italian law: verifying that the transactions of greatest significance for the Company's profitability, financial position and assets and liabilities conformed with the law, the bylaws and the principles of correct management; checking that transactions with related parties complied with the self-regulatory principles and procedures adopted by the Company and that they were in its interest; and checking the adequacy of the organizational structure. The Board of Auditors also monitored the adequacy of the internal control system and that of the administrative and accounting system and the latter's reliability in correctly representing transactions. Lastly, the Board of Auditors investigated the reports it received under Article 2408 of the Civil Code and the complaints submitted to it during the year, as described in its report to the shareholders' meeting.

■ SHAREHOLDERS' MEETINGS

Ordinary and extraordinary shareholders' meetings were held on 6 May 2004. In addition to approving the annual report for 2003, appointing the new Board of Directors, engaging the external auditors for the three years 2004-06 and redetermining the fees to be paid to the Board of Auditors, the shareholders approved, in accordance with the bylaws, the Rules of Proceeding for the Shareholders' Meeting and some amendments to the bylaws. The latter served not only to bring the bylaws into line with the reform of company law but also (i) to broaden the powers of the Board of Directors under Article 2365 of the Civil Code; (ii) to exclude from the events giving the right of withdrawal the extension of the duration of the Company and the introduction/amendment of restrictions on the circulation of shares; (iii) to introduce the possibility of increasing the share capital for cash with the exclusion of the right of pre-emption within the limits laid down by law; (iv) to change the mechanism whereby shareholders are legitimized to attend shareholders' meetings; and (v) to authorize the Board of Directors to increase the share capital and to issue convertible bonds.

The Company has acted to increase the attendance of shareholders in meetings by providing the documents needed for informed participation to all those who request them and by allowing ordinary shareholders to vote by mail.

Furthermore, pursuant to the bylaws, the Company makes special areas available to associations of employee shareholders where they can provide information and collect proxy forms.

The special meeting of savings shareholders held on 26 October 2004 reappointed Professor Carlo Pasteris as the common representative for the three years 2004-06.

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■ CODE OF ETHICS

The Code of Ethics of the Telecom Italia Group can be considered as lying upstream from the whole system of corporate governance and as enshrining the set of fundamental values and principles that serve to ensure an ethically-oriented conduct of business. The Code, which has gradually been adopted by all the companies belonging to the Group, specifies the objectives to be aimed at and the values to be fostered in relation to all the main stakeholders Telecom Italia interacts with every day: shareholders, financial markets, customers, local communities and employees.

Like all the Company's other instruments of corporate governance, the Group Code of Ethics is continuously reviewed in the light of developments in the applicable law and operational and market practices, and with consideration also given to the results of the monitoring of units' compliance by the person responsible for internal control. The present version of the Code, last revised in March 2004, replaces that adopted following the completion of the merger of the "old" Telecom Italia into Olivetti on 4 August 2003. Compared with the earlier version, it takes account of the requirements deriving from the company's listing in the United States, primarily as regards the Code of Ethics referred to in the Sarbanes-Oxley Act and the Code of Conduct required by the listing standards of the New York Stock Exchange, which make it mandatory to have a code of conduct for certain categories of officers (executive, financial and accounting). In addition, the form and substance of the earlier text were improved by reorganizing and adding to the content.

The Group Code of Ethics is thus more closely coordinated with the Company's other instruments of corporate governance and increasingly at the centre of the internal control system.

The Code is available on the Company's website under Investor Relations.

■ RULES OF CONDUCT FOR TRANSACTIONS WITH RELATED PARTIES

As specified in the 2003 report on corporate governance, in 2002 the Company adopted guidelines (available on the Company's website under Corporate governance) for carrying out transactions with related parties. They are intended to ensure both procedural and substantial fairness and transparency by entrusting the related decisions to the Board of Directors.

In fact, under the guidelines, the Board of Directors is required to give advance approval to transactions with related parties, including intra-group transactions, apart from those of a customary nature to be concluded at standard conditions. To this end, provision is made for the Board to be adequately informed of all the relevant aspects: the nature of the relationship, the manner of carrying out the transaction, the economic and other conditions, the evaluation procedures used, the rationale for the transaction and the Company's interest in its implementation and the associated risks. Moreover, if the related party is a director or a party related via a director, he or she may only provide clarifications and must leave the meeting when the motion is examined and put to a vote.

Depending on the nature, value and other aspects of related-party transactions, the Board may be assisted by outside experts in order to prevent contracts being concluded at inappropriate conditions. Such experts must have suitable professional experience and qualifications in the field in question and their independence must be carefully assessed.

The changes made to the "Vietti reform" of company law by Legislative Decree 310/2004 were a factor in the revision of the guidelines, with the introduction of an explicit reference to a concept of "normality" applicable to intra-group transactions. Provision has also been made for a

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procedure (currently in preparation) to complete and overarch the system. More specifically, the aim of the procedure is to provide an objective basis for the treatment of concrete situations. Before any transaction is carried out, it will be necessary to consult an expert system (appropriately interfaced with a database containing the related parties of the Group companies that have adopted the guidelines) that will automatically provide – on the basis of information gathered using ad hoc checklists – indications concerning decision-making powers, internal information flows for reporting purposes, and the need for an external opinion in evaluating the congruousness of transactions. More detailed information on transactions with related parties can be found in this report in the section “Related party transactions”.

■ MANAGEMENT OF INFORMATION

Transparent relations with the market and the provision of accurate, clear and complete information are standards for the conduct of the members of the governing bodies, the management and all the employees of the Telecom Italia Group.

Confidential information is dealt with the Chairman of the Board of Directors on the basis of procedures for the internal processing and disclosure to third parties of documents and information concerning the Company, with special reference to price-sensitive information. As announced in the annual report for 2003, Telecom Italia has adopted a special procedure, partly amended in 2004, establishing the ways in which price-sensitive information is to be communicated to the market. It identifies the units of the Company’s organization involved and lays down guidelines for the action to be taken in the presence of rumours and in response to requests for information from the entities responsible for supervising and operating the markets (Consob and Borsa Italiana). The procedure also lays down guidelines for meetings with the financial community and the press, to ensure that information concerning the Company and the Group is not disclosed selectively.

The Company has also established a Disclosure Committee to provide assistance to the Board of Directors and top management in the processing and handling of data and news necessary for the correct provision of information. The main tasks of the Committee are:

- (i) to assist the Board in the preparation of corporate communications, the top management in the certification of the annual report in accordance with the Sarbanes-Oxley Act, and the Chairman of the Board of Directors in dealing with price-sensitive information;
- (ii) to ensure that corporate communications are prepared correctly with a view to their approval;
- (iii) to monitor the application of the procedures and controls for the collection, analysis and retention of data and information for publication and filing, verify their adequacy and effectiveness and propose corrective measures;
- (iv) to verify the correct application and need for updating of the “Procedure for communicating price-sensitive information” and suggest improvements where appropriate;
- (v) to supervise the structure and updating of the Company’s website as regards its institutional contents.

The Disclosure Committee Rules are posted on the Company’s website.

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■ CODE OF CONDUCT ON INSIDER DEALING

The Company's Code of Conduct on Insider Dealing, which underwent some purely formal changes in 2004, can be found on the Company's website. It lays down the rules of conduct and disclosure requirements applicable to transactions involving financial instruments issued by Group companies carried out by persons who, as a consequence of their positions, have access to material information (i.e. information capable of producing significant changes in the outlook for the profitability, financial position and/or assets and liabilities of the Company and the Group and likely, if made public, to have a significant effect on the price of the listed securities in question).

The criteria applied in drawing up the Code are consistent with the basic choices underpinning the Company's system of corporate governance: rigour (with provision made for the imposition of severe penalties) and transparency.

■ RULES OF PROCEEDING FOR SHAREHOLDERS' MEETINGS

On 6 May 2004 the shareholders' meeting approved the Rules of Proceeding for Shareholders' Meetings, as provided for in the bylaws.

The rules are substantially the same as those that were in force at the "old" Telecom Italia before it was merged into Olivetti, which had been found to provide effective support for conducting shareholders' meetings. The rules have therefore been updated and simplified, with the addition of a section on voting by mail, so as to ensure the document provides the fullest possible organizational and procedural guidance for an important moment in shareholders' participation in the life of the Company.

The rules of proceeding are posted on the Company's website under Investor Relations.

■ INVESTOR RELATIONS

A special unit, headed by a Managing Director (Carlo Buora), is responsible for handling relations with the financial community in Italy and abroad, while for retail investors there is a toll-free number to speak with the Company's Securities Service.

More detailed information can be found in the section "Financial communications".

Additional information can be obtained from the following addresses:

Institutional investors:

Telecom Italia S.p.A.

Investor Relations

Piazza degli Affari, 2

20123 Milano

Tel.: +39 02 8595 4131

E-mail: investor_relations@telecomitalia.it

Individual Investors:

Telecom Italia S.p.A.

Corporate Affairs - Gestione Azionariato

Piazza degli Affari, 2

20123 Milano

Toll-free number in Italy: 800 020220

Tel.: +39 011 4404900

E-mail: corporate.affairs@telecomitalia.it

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■ SHAREHOLDERS' AGREEMENTS

The largest shareholder of Telecom Italia is Olimpia S.p.A., with 21,8% of the ordinary share capital.

The shareholders of Olimpia S.p.A. have concluded a number of shareholders' agreements; notices containing extracts of the following have been published in the Italian press:

- agreement between Pirelli & C. S.p.A. (formerly Pirelli S.p.A.) and Edizione Holding S.p.A. - Edizione Finance International S.A., concluded on 7 August 2001 and subsequently amended;
- agreement between Pirelli & C. S.p.A. (formerly Pirelli S.p.A.), Unicredito Italiano S.p.A. and Banca Intesa S.p.A., concluded on 14 September 2001 and subsequently amended;
- agreement between Pirelli & C. S.p.A. (formerly Pirelli S.p.A.), Banca Intesa S.p.A., Unicredito Italiano S.p.A., Edizione Holding S.p.A. - Edizione Finance International S.A., Hopa S.p.A. and Olimpia S.p.A. concluded on 21 February 2003 and subsequently amended.

The shareholders of Olimpia S.p.A. are currently Pirelli & C. S.p.A. (57.66%), Edizione Finance International S.A. (16.8%), Unicredito Italiano S.p.A. (4.77%), Banca Intesa S.p.A. (4.77%) and Hopa S.p.A. (16%).

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■ EQUITY INVESTMENTS HELD BY DIRECTORS, STATUTORY AUDITORS AND GENERAL MANAGER

In accordance with article 79 of the regulation for the introduction of Legislative Decree No. 58 dated February 24, 1998, adopted by Consob under resolution No. 11971 dated May 14, 1999, and subsequent changes and supplements, in the following table are reported the investments held in Telecom Italia S.p.A. and in the Companies which it controls, by Directors and Statutory Auditors in office during 2004 or even for just a portion of the year in Telecom Italia S.p.A.

| Name | Company | Class of shares | Number of shares held at the end of 2003 (or at the date of appointment) | Number of shares purchased in 2004 | Number of shares sold in 2004 | Number of shares held at the end of 2004 (or at the date the person left office if it occurred before) |
|--------------------------------------|-----------------------|-----------------|--|------------------------------------|-------------------------------|--|
| Marco TRONCHETTI PROVERA | = | = | = | = | = | = |
| Gilberto BENETTON | Telecom Italia Mobile | Ordinary | = | 1,125,000 | = | 1,125,000 |
| Carlo Orazio BUORA | = | = | = | = | = | = |
| Riccardo RUGGIERO Direttore Generale | = | = | = | = | = | = |
| Paolo BARATTA | = | = | = | = | = | = |
| John Robert SOTHEBY BOAS | = | = | = | = | = | = |
| Umberto COLOMBO | = | = | = | = | = | = |
| Giovanni CONSORTE | Telecom Italia | Saving | 33,008 | = | 33,008 | = |
| | Telecom Italia Media | Ordinary | 40,183 | = | 40,183 | = |
| Francesco DENOZZA | = | = | = | = | = | = |
| Domenico DE SOLE | = | = | = | = | = | = |
| Luigi FAUSTI | Telecom Italia Mobile | Ordinary | 50,000 | = | = | 50,000 |
| Guido FERRARINI | = | = | = | = | = | = |
| Jean Paul FITOUSSI | = | = | = | = | = | = |
| Natale IRTI | = | = | = | = | = | = |
| Gianni MION | Telecom Italia | Saving | = | 15,000 ⁽¹⁾ | = | 15,000 |
| | Telecom Italia Mobile | Ordinary | = | 3,500 ⁽¹⁾ | = | 3,500 |
| | Telecom Italia Mobile | Saving | = | 5,000 ⁽¹⁾ | = | 5,000 |
| Pietro MODIANO | = | = | = | = | = | = |
| Massimo MORATTI | = | = | = | = | = | = |
| Marco ONADO | Telecom Italia Mobile | Saving | = | 4,700 | = | 4,700 |
| Renato PAGLIARO | = | = | = | = | = | = |
| Pasquale PISTORIO | Telecom Italia | Ordinary | 1,549,000 ⁽²⁾ | = | = | 1,549,000 |
| Carlo A. PURI NEGRI | = | = | = | = | = | = |
| Luigi ROTH | Telecom Italia | Ordinary | 11,553 ⁽¹⁾ | = | = | 11,553 |
| | Telecom Italia Mobile | Ordinary | 14,300 ⁽¹⁾ | = | = | 14,300 |
| | Telecom Italia Media | Ordinary | 726 ⁽¹⁾ | = | = | 726 |
| Pier Francesco SAVIOTTI | Telecom Italia Mobile | Ordinary | 10,000 | = | = | 10,000 |
| Giuseppe SALA Direttore Generale | = | = | = | = | = | = |
| Rosalba CASIRAGHI | = | = | = | = | = | = |
| Paolo GOLIA | Telecom Italia Mobile | Ordinary | = | 15,555 | 3,555 | 12,000 |
| Salvatore SPINIELLO | Telecom Italia | Ordinary | 82,922 | = | 82,922 | = |
| | Telecom Italia | Saving | 234,458 | = | 234,458 | = |
| | Telecom Italia Mobile | Ordinary | 10,000 | = | 10,000 | = |
| Ferdinando SUPERTI FURGA | Telecom Italia Mobile | Ordinary | 6,270 | = | 2,547 | 3,723 |
| Gianfranco ZANDA | = | = | = | = | = | = |

(1) Shares held directly.

(2) Of which 660,000 held indirectly.



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■ CONSOLIDATED BALANCE SHEETS

ASSETS

(in millions of euro)

| | 12/31/2004 | 12/31/2003 |
|--|---------------|---------------|
| RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS | | |
| - PORTION CALLED IN | 41 | — |
| - PORTION NOT CALLED IN | 4 | 4 |
| TOTAL RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS | 45 | 4 |
| INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS | | |
| - INTANGIBLE ASSETS | | |
| Start-up and expansion costs | 24 | 51 |
| Industrial patents and intellectual property rights | 2,548 | 1,850 |
| Concessions, licenses, trademarks and similar rights | 3,509 | 3,761 |
| Goodwill | 4 | 8 |
| Differences on consolidation | 25,637 | 27,137 |
| Work in progress and advances to suppliers | 751 | 742 |
| Other intangibles | 401 | 304 |
| TOTAL INTANGIBLE ASSETS | 32,874 | 33,853 |
| - FIXED ASSETS | | |
| Land and buildings | 1,759 | 1,814 |
| Plant and machinery | 14,206 | 14,302 |
| Manufacturing and distribution equipment | 62 | 46 |
| Other fixed assets | 718 | 597 |
| Construction in progress and advances to suppliers | 972 | 1,565 |
| TOTAL FIXED ASSETS | 17,717 | 18,324 |
| - LONG-TERM INVESTMENTS | | |
| Equity investments in: | | |
| unconsolidated subsidiaries | 11 | 5 |
| affiliated companies | 625 | 955 |
| other companies | 419 | 501 |
| Total equity investments | 1,055 | 1,461 |
| Advances on future capital contributions | 9 | 9 |
| Accounts receivable: (*) | | |
| unconsolidated subsidiaries | — | 3 |
| affiliated companies | 32 | 54 |
| other receivables | 43 | 281 |
| Total accounts receivable | 75 | 338 |
| Other securities | 7 | 12 |
| Treasury stock (total par value of euro 56 million at 12/31/2004) | 393 | 393 |
| TOTAL LONG-TERM INVESTMENTS | 1,866 | 2,396 |
| TOTAL INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS | 52,457 | 54,573 |
| CURRENT ASSETS | | |
| - INVENTORIES | | |
| Raw materials and supplies | 12 | 24 |
| Work in progress and semifinished goods | 17 | 22 |
| Contract work in process | 96 | 105 |
| Finished goods and merchandise: | | |
| finished goods | 1 | 7 |
| merchandise | 309 | 267 |
| Advances to suppliers | — | 1 |
| TOTAL INVENTORIES | 435 | 426 |
| - ACCOUNTS RECEIVABLE (**) | | |
| Trade accounts receivable | 1 | 1 |
| Accounts receivable from unconsolidated subsidiaries | — | — |
| Accounts receivable from affiliated companies | — | — |
| Taxes receivable | 8 | 69 |
| Deferred tax assets | 1,785 | 3,172 |
| Other receivables | 18 | 64 |
| TOTAL ACCOUNTS RECEIVABLE | 1,812 | 3,306 |
| - SHORT-TERM FINANCIAL ASSETS | | |
| Equity investments in unconsolidated subsidiaries | — | 170 |
| Equity investments in affiliated companies | — | 708 |
| Other securities | 932 | 2,719 |
| Receivables for sales of securities | 2 | 60 |
| TOTAL SHORT-TERM FINANCIAL ASSETS | 934 | 3,657 |
| - LIQUID ASSETS | | |
| Bank and postal accounts | 8,558 | 4,870 |
| Cash and valuables on hand | 4 | 7 |
| TOTAL LIQUID ASSETS | 8,562 | 4,877 |
| TOTAL CURRENT ASSETS | 22,930 | 24,599 |
| ACCRUED INCOME AND PREPAID EXPENSES | | |
| Issue discounts and similar charges | 241 | 240 |
| Accrued income and other prepaid expenses | 936 | 1,085 |
| TOTAL ACCRUED INCOME AND PREPAID EXPENSES | 1,177 | 1,325 |
| TOTAL ASSETS | 76,609 | 80,501 |

(*) Amounts due within one year

(**) Amounts due beyond one year

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LIABILITIES AND SHAREHOLDERS' EQUITY

(in millions of euro)

| | 12/31/2004 | 12/31/2003 |
|---|---------------|---------------|
| SHAREHOLDERS' EQUITY | | |
| PARENT COMPANY INTEREST IN: | | |
| - SHARE CAPITAL | 8,865 | 8,854 |
| - RESERVE FOR TREASURY STOCK IN PORTFOLIO OF THE PARENT COMPANY AND UNCONSOLIDATED SUBSIDIARIES | 393 | 393 |
| - RESERVES AND RETAINED EARNINGS | 5,133 | 5,653 |
| - NET INCOME | 781 | 1,192 |
| TOTAL PARENT COMPANY INTEREST | 15,172 | 16,092 |
| MINORITY INTEREST IN: | | |
| - SHARE CAPITAL, RESERVES AND RETAINED EARNINGS | 3,568 | 3,261 |
| - NET INCOME | 1,121 | 1,236 |
| TOTAL MINORITY INTEREST | 4,689 | 4,497 |
| TOTAL SHAREHOLDERS' EQUITY | 19,861 | 20,589 |
| RESERVES FOR RISKS AND CHARGES | | |
| Reserve for pensions and similar obligations | 40 | 42 |
| Reserve for taxes and reserve for deferred taxes | 460 | 404 |
| Consolidation reserve for future risks and charges | - | 1 |
| Other reserves | 1,998 | 2,476 |
| TOTAL RESERVES FOR RISKS AND CHARGES | 2,498 | 2,923 |
| RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES | 1,324 | 1,296 |
| LIABILITIES | (**) | (**) |
| Debentures | 29,637 | 29,640 |
| Convertible debentures | 4,789 | 5,592 |
| Due to banks | 1,030 | 1,830 |
| Due to other lenders | 1,305 | 1,623 |
| Advances | - | 50 |
| Trade accounts payable | 1 | 6,789 |
| Accounts payable to unconsolidated subsidiaries | - | 12 |
| Accounts payable to affiliated companies | 15 | 293 |
| Taxes payable | 10 | 542 |
| Contributions to pension and social security institutions | 1,040 | 1,356 |
| Other liabilities | 43 | 2,860 |
| TOTAL LIABILITIES | 37,870 | 50,587 |
| ACCRUED EXPENSES AND DEFERRED INCOME | | |
| Issue premiums | 32 | 39 |
| Accrued expenses and deferred income | 2,307 | 2,347 |
| TOTAL ACCRUED EXPENSES AND DEFERRED INCOME | 2,339 | 2,386 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | 76,609 | 80,501 |

(**) Amounts due beyond one year

MEMORANDUM ACCOUNTS

(in millions of euro)

| | 12/31/2004 | 12/31/2003 |
|--|--------------|--------------|
| GUARANTEES PROVIDED | | |
| Sureties: | | |
| on behalf of unconsolidated subsidiaries | 3 | 4 |
| on behalf of affiliated companies | 658 | 864 |
| on behalf of others | 178 | 195 |
| Total sureties | 839 | 1,063 |
| Endorsements | - | - |
| Other guarantees: | | |
| on behalf of unconsolidated subsidiaries | 1 | 1 |
| on behalf of others | 111 | 91 |
| Total other guarantees | 112 | 92 |
| TOTAL GUARANTEES PROVIDED | 951 | 1,155 |
| COLLATERAL PROVIDED | | |
| For obligations of others, of affiliated companies | - | 107 |
| For own obligations, not including liabilities | 7 | 7 |
| TOTAL COLLATERAL PROVIDED | 7 | 114 |
| PURCHASES AND SALES COMMITMENTS | 4,387 | 208 |
| OTHER MEMORANDUM ACCOUNTS | 108 | 105 |
| TOTAL MEMORANDUM ACCOUNTS | 5,453 | 1,582 |

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■ CONSOLIDATED STATEMENTS OF INCOME

(in millions of euro)

| | 2004 | 2003 |
|--|----------------|----------------|
| PRODUCTION VALUE | | |
| Sales and service revenues | 31,237 | 30,850 |
| Changes in inventories of work in progress, semifinished and finished goods | (6) | 13 |
| Changes in inventory of contract work in process | (6) | (87) |
| Increases in capitalized internal construction costs | 742 | 805 |
| Other revenue and income: | | |
| operating grants | 12 | 14 |
| other | 303 | 331 |
| Total other revenue and income | 315 | 345 |
| TOTAL PRODUCTION VALUE | 32,282 | 31,926 |
| PRODUCTION COSTS | | |
| Raw materials, supplies and merchandise | 2,336 | 1,973 |
| Semifinished and finished goods | 78 | 108 |
| Services | 9,857 | 9,684 |
| Use of property not owned | 1,087 | 1,156 |
| Personnel costs: | | |
| wages and salaries | 2,883 | 3,078 |
| social security contributions | 872 | 921 |
| termination indemnities | 189 | 200 |
| other costs | 101 | 104 |
| Total personnel costs | 4,045 | 4,303 |
| Amortization, depreciation and writedowns | | |
| amortization of intangible assets | 3,116 | 3,109 |
| depreciation of fixed assets | 3,530 | 3,670 |
| other writedowns of intangibles and fixed assets | 5 | 6 |
| writedowns of receivables included in current assets and liquid assets | 275 | 471 |
| Total amortization, depreciation and writedowns | 6,926 | 7,256 |
| Changes in inventory of raw materials, supplies and merchandise | (37) | 40 |
| Provisions for risks | 74 | 70 |
| Other provisions | 7 | 24 |
| Miscellaneous operating costs | 709 | 523 |
| TOTAL PRODUCTION COSTS | 25,082 | 25,137 |
| OPERATING INCOME | 7,200 | 6,789 |
| FINANCIAL INCOME AND EXPENSE | | |
| Income from equity investments: | | |
| dividends from unconsolidated subsidiaries | 10 | 3 |
| dividends from other companies | 9 | 6 |
| other income from equity investments | 97 | 8 |
| Total income from equity investments | 116 | 17 |
| Other financial income from: | | |
| accounts receivable included in long-term investments | | |
| affiliated companies | 4 | 21 |
| other | 10 | 8 |
| Total from accounts receivable included in long-term investments | 14 | 29 |
| securities, other than equity investments, included in long-term investments | 1 | — |
| securities, other than equity investments, included in current assets | 52 | 174 |
| other income | | |
| interest and fees from unconsolidated subsidiaries | — | 1 |
| interest and fees from affiliated companies | — | 2 |
| interest and fees from others and miscellaneous income | 754 | 610 |
| Total other income | 754 | 613 |
| Total other financial income | 821 | 816 |
| Interest and other financial expense: | | |
| interest and fees paid to affiliated companies | (2) | (11) |
| interest and fees paid to others and miscellaneous expense | (2,726) | (2,949) |
| Total interest and other financial expense | (2,728) | (2,960) |
| Foreign exchange gains and losses | (44) | (27) |
| TOTAL FINANCIAL INCOME AND EXPENSE | (1,835) | (2,154) |

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(in millions of euro)

| | 2004 | 2003 |
|---|--------------|----------------|
| VALUE ADJUSTMENTS TO FINANCIAL ASSETS | | |
| Upward adjustments of | | |
| equity investments | 81 | 65 |
| securities, other than equity investments, included in current assets | 11 | 3 |
| Total upward adjustments | 92 | 68 |
| Writedowns of | | |
| equity investments | (80) | (154) |
| long-term investments, other than equity investments | (11) | (5) |
| securities, other than equity investments, included in current assets | – | (19) |
| Total writedowns | (91) | (178) |
| TOTAL VALUE ADJUSTMENTS TO FINANCIAL ASSETS | 1 | (110) |
| EXTRAORDINARY INCOME AND EXPENSE | | |
| Income | | |
| gains on disposals | 190 | 105 |
| miscellaneous | 987 | 1,746 |
| Total income | 1,177 | 1,851 |
| Expense | | |
| losses on disposals | (16) | (237) |
| prior years' taxes | (31) | (48) |
| provisions and writedowns of equity investments | (581) | (879) |
| miscellaneous | (959) | (1,770) |
| Total expense | (1,587) | (2,934) |
| TOTAL EXTRAORDINARY ITEMS | (410) | (1,083) |
| INCOME BEFORE TAXES | 4,956 | 3,442 |
| Income taxes, current and deferred | (3,054) | (1,014) |
| NET INCOME BEFORE MINORITY INTEREST | 1,902 | 2,428 |
| Minority interest | (1,121) | (1,236) |
| NET INCOME | 781 | 1,192 |

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■ NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

INTRODUCTION

The consolidated financial statements for the year ended December 31, 2004 of the Telecom Italia Group have been prepared in accordance with Legislative Decree No. 127/1991 which introduced the EEC VII Directive into Italian law with regard to consolidated financial statements, in addition to the provisions of the Italian Civil Code with regard to statutory financial statements, as amended by Legislative Decree No. 6 dated January 17, 2003 and successive amendments, concerning the "Fundamental Reform of Corporate Law" where applicable by analogy or by explicit reference to consolidated financial statements.

The consolidated statement of cash flows, although presented in the Report on Operations, constitutes an integral part of these financial statements consisting of the consolidated balance sheet, the consolidated statement of income and the statement of changes in consolidated shareholders' equity and the notes to the consolidated financial statements.

The scope and principles of consolidation, the summary of significant accounting policies, along with the composition and changes in the individual components of the consolidated financial statements are set out below.

All amounts are stated in millions of euro, unless otherwise indicated.

■ SCOPE OF CONSOLIDATION

The scope of consolidation at December 31, 2004 includes the Italian and foreign companies listed in Annex 6, in which Telecom Italia holds a majority of voting rights, and all other companies in which it exercises a dominant influence.

Companies in which Telecom Italia holds between a 10% (if listed), 20% (if unlisted) and a 50% interest in share capital, with voting rights, including jointly controlled companies and companies in which the Parent Company exercises a significant influence, have been accounted for using the equity method.

The following changes have taken place in the scope of consolidation:

Since December 31, 2003:

a) added to the scope of consolidation:

- for *Wireline*:
Telefonia Mobile Sammarinese S.p.A. (formerly accounted for using the equity method);
TI Sparkle Singapore;
Latin American Nautilus Brasil Participacoes Ltda;
- for *Mobile*:
TIM Italia S.p.A.;
- per *Internet & Media*:
TI Media Broadcasting S.r.l.;
- for *IT Market*:
IAK S.r.l.;
- for *IT Group*:
I.T. Telecom S.r.l.;
- for *Olivetti Tecnost*:
Yminds S.A. (formerly accounted for using the equity method);
- for *Other activities*:
Edotel S.p.A. (formerly accounted for using the equity method);

b) eliminated from the scope of consolidation:

- for *Wireline*:
TMI Telemedia International Luxembourg S.A. (put into liquidation), Atesia (80% interest sold in December 2004);
- for *Internet and Media*:
CIPi S.p.A. (sold in January 2004), GPP S.p.A., Editoriale Quasar S.r.l., Editoriale JCE S.p.A. Group, Editoriale Faenza Editrice S.p.A. Group, Quasar e Associati S.r.l., Faenza Editrice Iberica S.L., Faenza Editrice do Brasil Ltda, Promo Advertising S.r.l. (sold in June 2004);

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- for *IT Market*:
Webegg S.p.A., W.P. Winner Project B.V., Software Factory S.p.A, Telemedia Applicazioni S.p.A (interest sold in July 2004);
- for *IT Group*:
Teco Soft Argentina SA (put into liquidation), Telesoft Russia Zao (sold in April 2004);
- for *Olivetti Tecnost*:
Olivetti de Venezuela C.A. (liquidation closed in April 2004), Olivetti Colombiana S.A., Diaspron do Brasil S.A., Olivetti Servicios y Soluciones Integrales S.A. de C.V., Olivetti Peruana S.A., Alladium S.p.A., Multidata S.A. Eletronica Industria e Comercio, Olivetti Lexikon Nordik AB, Olivetti Argentina S.A.C.e.I., Olivetti Latin America Trading Associates S.A., Olivetti Tecnost (H.K.), Olivetti Lexikon Benelux S.A., Royal Consumer Information Products Inc., Dedita S.p.A. (put into liquidation);
- for *Other activities*:
Olivetti International (Service) S.A., Olivetti International N.V., Olivetti International Finance N.V.S.A., TILab General Partner S.A, Olivetti Rap S.A., Olivetti Telemedia Investments B.V., Netesi S.p.A. (put into liquidation);

c) companies involved in mergers:

- for *Mobile*:
Telepisa Celular S.A., Telecearà Celular S.A. , Telern Celular S.A., Telpa Celular S.A. and Telasa Celular in TIM Nordeste Telecomunicacoes S.A. (ex-Telpe);
Tele Nordeste Participações S.A in Tele Celular Sul Participações;
- for *South America*:
Americatel Perú S.A. in Diveo Telecomunicaciones del Perú (which took the name of Americatel Perú S.A.);
- for *Internet and Media*:
PBS Professional Business Software S.p.A. in Gruppo Buffetti S.p.A.;
- for *It Group*:
It Telecom S.p.A. in Telecom Italia S.p.A.;
EPIClink S.p.A. in Telecom Italia S.p.A.;
- for *Olivetti Tecnost*:
Olivetti da Amazonia Industria e Comercio Ltda in Olivetti do Brasil S.A.;
- for *Other activities*:
Olivetti International S.A. in Telecom Italia Finance S.A.;
Olivetti Finance N.V. in Telecom Italia Finance S.A.
Vertico S.p.A in ISM S.r.l.

At December 31, 2004, Telecom Italia's subsidiaries and affiliates listed in Annexes 6 to 9, are categorized as follows:

| | Subsidiaries | | | Affiliates | | | Total |
|-------------------------------|--------------|------------|------------|------------|-----------|-----------|------------|
| | Italy | Abroad | Total | Italy | Abroad | Total | |
| Companies: | | | | | | | |
| • consolidated line-by-line | 60 | 113 | 173 | | | | 173 |
| • valued by the equity method | - | 2 | 2 | 27 | 27 | 54 | 56 |
| • valued at cost | 20 | 12 | 32 | 25 | 5 | 30 | 62 |
| Total companies | 80 | 127 | 207 | 52 | 32 | 84 | 291 |

■ SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements used in consolidation are those of each single consolidated company at December 31, 2004, approved by the respective boards, and adjusted where necessary to conform to the accounting policies adopted by the Parent Company, Telecom Italia.

The financial statements expressed in foreign currency have been translated into euro by applying the average annual exchange rate to the individual items of the statement of income, with the exception of subsidiaries and affiliates operating in hyperinflationary economies using inflation accounting which have translated their statements of income at the year-end exchange rates instead of at the average rates. The balance sheet is translated at the year-end exchange rate.

The difference arising from the translation of beginning shareholders' equity and the net result for the year at the year-end exchange rate is recorded in reserves under consolidated shareholders' equity.

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The exchange rates used are those presented in "Other information".

All subsidiaries included in the scope of consolidation have been consolidated using the line-by-line method, which can be summarized as follows:

- assumption of the total amount of assets, liabilities, revenues and expenses, regardless of the interest held, separately showing the minority interest in shareholders' equity and net income
- the difference arising from the elimination of the carrying value of an investment in a company included in the scope of consolidation against the underlying share of the shareholders' equity at the date of acquisition is allocated, where possible, to the assets and liabilities of the company. Any residual amount is treated as follows:
 - if positive, it is recorded in "differences on consolidation" under "intangible assets" and is amortized on the straight-line method over the estimated time required to recover the amount and, in any case, not more than 20 years;
 - if negative, it is recorded in shareholders' equity as "consolidation reserve", or, when the amount is due to expectations of unfavorable financial results, to "consolidation reserve for future risks and charges";
- elimination of receivables and payables, as well as expenses and revenues among consolidated companies;
- elimination of profit included in fixed assets and intangible assets which stem from intragroup purchases of goods and services produced internally by the Group at market prices. The portion of intragroup revenues referring to the above goods and services has been reclassified, net of intragroup profit, to the item "increase in capitalized internal construction costs".

■ ACCOUNTING POLICIES

The accounting policies adopted in preparing the consolidated financial statements conform to the law and have been applied on a basis consistent with the prior year.

The accounting policies are set out below:

■ Intangible assets

Intangible assets are recorded at acquisition or production cost and are amortized on the straight-line method over their estimated period of benefit, as follows:

| | |
|---|---|
| Licenses, trademarks and similar rights | Contract term |
| Goodwill | Years expected to be benefited (in any case, not more than 20 years) |
| Software | Generally 3 years |
| Leasehold improvements | Lesser of the period of future economic benefit of the expenses incurred or the residual lease period |

Capitalized software costs (including those for internal use) represent costs for the development of new software or the implementation of existing software for the introduction of new features. The Group applies the same principle to website development costs. All costs for ordinary software maintenance (upgrades), that is, costs which do not involve the introduction of additional features and costs for the preliminary stages of software development are expensed in the statement of income in the year incurred.

■ Fixed assets

Fixed assets are recorded at acquisition or production cost (including incidental purchase costs and expenses directly attributable to construction). They are depreciated on the straight-line method over their estimated useful lives or possibility of utilization. They include inflation adjustments required or allowed by specific laws in the countries in which the fixed assets are located.

Construction in progress is stated at the amount of direct costs incurred. Ordinary maintenance is expensed in the statement of income in the year incurred. The elimination, disposal or sale of fixed assets is recorded in the financial statements by eliminating the cost and accumulated depreciation from the balance sheet and booking the related gain or loss in the statement of income.

■ Equity investments

Equity investments considered long-term in nature are recorded in long-term investments or, if acquired for subsequent sale, recorded in short-term financial assets.

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Long-term equity investments in unconsolidated subsidiaries and affiliates are generally valued by the equity method; positive differences arising upon acquisition, between the carrying value of the investments in said companies and the underlying share of net equity at current values, are included in the value of the investments and amortized on the straight-line method over their expected period of recoverability. Such amortization is charged to the statement of income in "value adjustments to financial assets" under writedowns of equity investments.

Other long-term investments in unconsolidated companies are recorded at acquisition or subscription cost, including incidental costs, adjusted for any reasonable expectations of a decline in profitability or recoverability in future years.

In the case of a permanent impairment, the value of such investments is written down and the impairment in value in excess of the corresponding carrying value is recorded in "reserves for risks and charges".

Contracts for securities lending are represented in the financial statements as two functionally related transactions: a loan and a "repurchase transaction" on the securities with the obligation of the borrower to resell them at maturity. Accordingly, "Other receivables" and "Other liabilities" include, respectively, a receivable and a payable of the same amount at the fixed amount of the contract (market price of stock and bonds at the date of delivery of the securities).

Equity investments included under current assets, consisting mainly of shares of consolidated listed companies purchased for trading purposes, are stated at the lower of cost and estimated realizable value, based on the year-end stock market prices.

For equity investments in long-term investments and short-term financial assets, the cost flows are determined by reference to the "weighted average cost method for each movement".

■ Writedown of long-term assets

Long-term assets (intangibles, including goodwill and differences on consolidation, fixed assets and equity investments) are written down when there is a permanent impairment to below their net book value. Except for goodwill and differences on consolidation, the lower value is not maintained in subsequent financial statements, if the underlying assumptions are no longer correct. The Group periodically evaluates its long-term assets for any permanent impairments in value. The writedown is recognized when the recoverable value of the asset is below the net book value and, in this case, the amount of the writedown is given by the difference between the two amounts, as stated in Article 2426, paragraph 1, item 3 of the Italian Civil Code.

■ Other securities (other than equity investments)

Securities that the company intends to hold to maturity are included among long-term investments; those bought for trading purposes are listed under short-term financial assets.

Securities held as long-term investments are valued at cost, adjusted by any permanent impairment in value.

Securities included in current assets are valued at the lower of cost of acquisition and realizable value based on market prices.

Writedowns of securities will be reversed in subsequent years, if the underlying assumptions are no longer correct.

Securities acquired under "repurchase agreements", for which the obligation exists to resell them at maturity, are included at purchase cost in receivables under short-term financial assets. The difference between the sales price and the purchase price is allocated to income on the accrual principle with a contra-entry to accrued income/expense in the balance sheet.

■ Inventories

Inventories are valued at the lower of purchase or production cost and market.

The methods used in computing cost are the following:

- raw materials and finished goods: LIFO with annual adjustments;
- merchandise: weighted average cost for each movement;
- work in progress and semifinished goods: production cost;
- contract work in process:
 - contracts covering less than 12 months: industrial cost;
 - contracts covering more than one year: at estimated revenues using the percentage of completion method.

In determining the value of contract work in process, anticipated losses upon completion and any other risks are also taken into account. Inventories of raw materials, finished goods and merchandise which exceed foreseeable manufacturing requirements, are slow moving or have become obsolete are written down on the basis of their estimated future utilization or their estimated realizable value.

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■ Accounts receivable and liabilities

Accounts receivable are stated at estimated realizable value and classified under long-term investments or current assets. Estimated realizable value is based upon an analysis of receivables at year-end. Uncollectible receivables are accounted for in the year they are identified. Liabilities are shown at their nominal value.

■ Transactions in foreign currency

Monetary assets and liabilities are accounted for at the exchange rate as of the transaction date and adjusted to the exchange rates prevailing at year-end, taking into account hedging contracts. Unrealized positive and negative differences arising the adjustment of such items to the year-end exchange rate are recorded in the statement of income.

■ Receivables transactions

Securitization

Accounts receivable sold under securitization transactions are reversed from the balance sheet with a contra-entry for the consideration received on the sale; the amount paid is represented by the non-repeatable amount received immediately (without recourse) whereas the deferred portion is recorded in Other receivables (financial) in current assets. This balance sheet caption is presented net of the relative allowance account calculated on the basis of estimated realizable value; the changes in the allowance account are booked to Financial expense in the statement of income. The difference between the carrying value of the receivables sold and the agreed consideration (including the portion of the payment which is deferred) is recognized in the statement of income on the accrual basis in "miscellaneous operating costs", for the trading portion and in "interest and other financial expense" for the financial portion. All expenses incurred for the securitization program are recorded in "costs for services".

■ Accruals and deferrals

These items are recorded on the accrual basis.

■ Reserves for risks and charges

"For taxes, for deferred taxes"

This reserve includes prudent provisions for estimated tax charges, including any surtaxes and late payment interest, on positions not yet agreed or in dispute, and deferred taxes calculated as described in the note on income taxes.

"Other reserves"

These reserves relate primarily to provisions to cover risks and charges for losses or liabilities of certain or likely existence whose amount or date of occurrence could, however, not be determined at the end of the year. The provisions reflect the best possible estimate, based on the commitments made and on the data available.

■ Reserve for employee termination indemnities

The amount of this reserve is determined in accordance with current laws and collective bargaining agreements and includes the liability matured at the end of the year in favor of all personnel employed by the Italian consolidated companies, net of advances paid.

■ Due to shareholders for loans

For purposes of the presentation of such liabilities in the financial statements, "Shareholders" are considered parties which hold directly at least 2% of the share capital of the Parent Company at the end of the year. At December 31, 2004, shareholders holding at least 2% of the share capital of Telecom Italia had made no loans to the company.

■ Employee benefit obligations under Law No. 58/1992

Telecom Italia, under Law No. 58/1992, is obliged to guarantee a uniform insurance status to all employees in service in the companies, Stet, Sip, Italcable and Telespazio, as of February 20, 1992, as well as those who moved from the Public Administration to Iritel, under the Telephone Workers' Social Security Fund – FPT, which became part of the general "Employees Pension Fund" beginning January 1, 2000.

At the present time, the amount of the liability can be estimated only roughly due to disagreements with the National Social Security Institute (Istituto Nazionale della Previdenza Sociale – INPS) relating to the manner in which to calculate the amount due and the fact that at December 31, 2004 INPS had not yet notified the Company of all the positions to be unified.

In the 1999 consolidated financial statements of the Olivetti group, when determining the difference on consolidation arising at the time of acquisition – on the part of Olivetti S.p.A. – of the controlling interest in Telecom Italia, an amount corresponding to the minimum liability then estimated was recorded in payables for "contributions to pension and social security institutions".

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The dispute with INPS concerns the application of the criteria established by the preceding Law No. 29/1979 for the employees who had already filed an application to join – still not processed by INPS – pursuant to the same law; the parties have agreed that the differences in interpretation shall be settled through test appeals before the ordinary magistrate. While awaiting these decisions, Telecom Italia has agreed to pay, with reservation, the amounts requested by INPS, subject to subsequent equalization adjustments, if the Courts ultimately accept the Company's interpretation. The payments requested by INPS are made in fifteen equal annual deferred installments (including annual interest of 5%), based on notification of the expenses by INPS.

Moreover, these consolidated financial statements at December 31, 2004 include euro 472 million of residual payables to INPS, relating to the estimate referring to the employees of the former State Company for Telephone Services (ASST) which the special Ministerial Commission established under Law No. 58/1992 had made upon the transfer of the assets of the Post and Telecommunications Administration to Iritel, and recorded by the latter company in its financial statements at December 31, 1993.

■ Grants

Both operating grants (directly credited to the statement of income) and capital grants or grants for installations are recorded in the accounting period in which the paperwork documenting the grants is received, or in the period in which the respective costs are incurred, provided that the certainty of payment is confirmed by established procedures. Such grants are not subject to restrictions regarding their use and are not subject to reimbursement.

Specifically, capital grants are recorded in deferred income and recognized in future years in the statement of income in relation to the amount of depreciation taken on the underlying assets to which the grants refer.

■ Revenues and expenses

Revenues and expenses are recorded on an accrual basis.

In particular, revenues are recognized in the consolidated statement of income as follows:

- telecommunications services (wireline and mobile): in the year in which the services are rendered; in particular, traffic revenues are shown gross of the amounts due to other carriers which are recorded, for the same amount, in production costs. Certain services deriving from wireline and mobile telephony are invoiced in advance and recognized as revenues when they are used. The revenues deriving from other telecommunications services, principally those related to network access, long-distance calls and the use of local and wireless networks, are recognized in the statement of income on the basis of the minutes of traffic used or on the basis of fixed rates by contract. The revenues deriving from installations or activations are recognized in the statement of income at the date of installation or activation. The revenues and costs relating to sales of wireless equipment and related accessories are recognized in the statement of income at the time of delivery and acceptance on the part of the customers in that these revenues are considered separate from the revenues deriving from the use of wireless services;
- information technology and innovative network services, other activities: to the extent to which the related services were carried out during the fiscal year;
- internet and media: I) revenues are recognized in proportion to the extent of the service rendered, taking into account the contractual regulations; II) revenues from the sale of advertising of on-line services are recognized as revenues when the advertising appears on the website; III) revenues for Internet access and related services, mainly subscriptions, are recognized in the period in which the subscription is in effect, using the straight-line method.

Costs related to the production or purchase of programs that are not of recurring benefit (such as variety shows, talk shows, game shows, journalistic and cultural inquiry shows, investigative reporting programs, news, info-entertainment shows and reality shows), including sports and journalistic rights and programs, are charged to the statement of income when the program is broadcast. In the case of a purchase of rights for an entire sports season, the total cost is allocated prorata over the events that make up the season and charged to the statement of income at the time of each event.

Costs related to rights on movies, made-for-TV movies, serials, cartoons, film shorts and similar programs purchased for a period of less than 12 months are always expensed on the basis of broadcasting.

■ Assets purchased under finance lease contracts

In accordance with the Italian National Accounting Principle No. 17 (Consolidated Financial Statements), assets under finance lease contracts which have a purchase option at the end of the lease term are recorded as fixed assets and depreciated, from the date of the contract, using rates consistent with those used on similar owned assets. Contemporaneously, a financial liability of an equal amount is recorded, against which

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the portions of principal paid are deducted. The finance charges and depreciation expense on the assets purchased by lease, for the period, are recorded in the statement of income.

However, it should be noted that the conditions provided by the Italian Civil Code (as amended by Legislative Decree No. 6 dated January 17, 2003 and subsequent amendments and integrations) for the classification of a transaction as a finance lease are broader than those provided by the Italian National Accounting Principle No. 17.

This difference, therefore, requires disclosure in the notes to the 2004 consolidated financial statements of the assets under finance leases (including leasebacks resulting in a finance lease or sale and leasebacks) that had previously been considered operating leases because their contracts did not provide for the option to purchase those assets.

Had these contracts been accounted for using the finance method, in accordance with the new provisions of the Italian Civil Code, entries would have been made in the statement of income for the interest on the financed principal and for the depreciation charge of the value of the assets purchased by lease; additionally, entries would have been made in the balance sheet to record the fixed assets under assets and the residual debt under liabilities. Furthermore, use of this method would also have resulted in the deferral of any gains on sale and leaseback transactions over the finance lease term.

■ Income taxes

Current income taxes are computed on the basis of a realistic estimate of the income tax charge according to the tax laws in force in each country; the related income tax payable is shown net of payments on account, withholding taxes and tax credits in "taxes payable". Any net receivable position is shown in "other receivables".

Deferred income taxes are calculated in the financial statements of the individual consolidated companies on the basis of the temporary differences between the value attributed to the assets and liabilities for statutory purposes and the value attributed to the same assets and liabilities for tax purposes, as well as on the consolidation adjustments in the consolidated financial statements. Deferred tax assets, including benefits from tax loss carryforwards, are booked in "other receivables" in current assets. The tax benefit relating to tax loss carryforwards is recorded only when there is reasonable certainty of recovery.

Deferred tax assets and liabilities are offset, whenever the assumptions for doing so exist. Deferred taxes on tax-deferred reserves and funds carried by the consolidated companies or the companies accounted for using the equity method are booked if such reserves are expected to be distributed or, in any case, utilized and their distribution or utilization will give rise to a tax charge.

During 2004, the consolidated national tax return procedure became applicable for the first time; Telecom Italia will adhere to it jointly with certain subsidiaries.

The relative regulation, provided by articles 117 to 129 of the new Italian Income Tax Code (T.U.I.R.), involves the computation, for Corporate Income Tax (IRES) purposes, of a single aggregate taxable income amounting to the algebraic sum of the incomes and/or losses of the Parent Company and the subsidiaries adhering to the procedure and, thus, the settlement of a single income tax to be paid or a single overpayment to be refunded or carried forward under the control of the Parent Company. The carryforward of any consolidated losses also rests with the Parent Company.

The consolidated national tax return procedure makes it possible, from 2004, to recognize the losses in the same year as the adhering companies if, and to the extent that, they offset the incomes of the other adhering companies, and to financially compensate the individual receivable and payable positions.

■ Capitalization of interest

Interest on construction projects is capitalized only when loans have been taken out that can be specifically attributed to the project.

■ Minority interest recorded as a charge to the Group

When the total losses attributable to minority shareholders exceed their interest in the investee's share capital, such excess will be recorded as a charge to the majority shareholders and, in that case, the minority interest in future earnings will be attributed to the majority interest in earnings, up to the amount necessary to recover the losses previously absorbed by the latter. However, if the minority shareholders have expressly indicated their intention to cover the losses, the excess will be recorded as an asset in the consolidated financial statements.

■ Memorandum accounts

"*Collateral and guarantees provided*" are recorded for an amount equal to the remaining liability or other guarantee provided; those in foreign currencies are translated at year-end exchange rates.

"*Purchases and sales commitments*" are determined on the basis of the unperformed portion of contracts outstanding at the end of the fiscal year which do not fall under the normal "operating cycle".

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■ Derivative financial instruments

Derivative financial instruments are used by the Telecom Italia Group to hedge exposure to interest rate and exchange rate risks.

For financial instruments used to hedge interest rate risks, the interest differentials are recorded in the statement of income in "financial income and expense" based on the accrual principle.

For financial instruments used to hedge exchange rate risks, the cost (or "financial component" calculated as the difference between the spot rate at the date of stipulating the contract and the forward rate) is recorded in the statement of income in "financial income and expense" based on the accrual principle.

Premiums relating to option-type financial instruments are recorded in "other liabilities" or "other receivables" and, if exercised, are considered as an incidental charge to the purchase or sale value of the underlying instruments; if the option is not exercised the premium is recorded in the statement of income under financial income (financial expense).

In this manner, the derivative financial instruments are valued consistently with the underlying asset and liability, for each transaction, and any net expense is recognized in the statement of income.

Option-type derivative financial instruments existing at the end of the year are valued at the lower of cost and market value at the balance sheet date.

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■ CONSOLIDATED BALANCE SHEETS - ASSETS

RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS

■ PORTION CALLED IN

euro 41 million

(euro 0 million at 12/31/2003)

The portion called in of receivables from shareholders for capital contributions increased by euro 41 million compared to the prior year and refers to TIM for euro 38 million and to the Parent Company for 3 million for shares subscribed to by management under stock option plans and not yet issued at December 31, 2004.

■ PORTION NOT CALLED IN

euro 4 million

(euro 4 million at 12/31/2003)

The portion not called in of receivables from shareholders for capital contributions has remained unchanged compared to the prior and refers to Agrisian.

INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS

■ INTANGIBLE ASSETS

euro 32,874 million

(euro 33,853 million at December 31, 2003)

Intangible assets decreased by euro 979 million compared to December 31, 2003. A breakdown of the composition and the changes in this account are provided below:

| (in millions of euro) | 12/31/2003 | Additions | Amor- tization | Other changes | 12/31/2004 |
|--|---------------|--------------|-------------------|------------------|---------------|
| Start-up and expansion costs | 51 | - | (24) | (3) | 24 |
| Industrial patents and intellectual property rights | 1,850 | 571 | (1,193) | 1,320 | 2,548 |
| Concessions, licenses, trademarks and similar rights | 3,761 | 20 | (255) | (17) | 3,509 |
| Goodwill | 8 | - | (4) | - | 4 |
| Differences on consolidation | 27,137 | 430 | (1,554) | (376) | 25,637 |
| Work in progress and advances to suppliers | 742 | 1,345 | - | (1,336) | 751 |
| Other intangibles | 304 | 79 | (86) | 104 | 401 |
| Total | 33,853 | 2,445 | (3,116) | (308) | 32,874 |

■ Start-up and expansion costs

euro 24 million

Start-up and expansion costs refer primarily to underwriting commissions paid in connection with capital increases by the Parent Company

■ Industrial patents and intellectual property rights

euro 2,548 million

Industrial patents and intellectual property rights consist almost entirely of applications software purchased outright and user licenses for an indefinite time period.

■ Concessions, licenses, trademarks and similar rights

euro 3,509 million

Concessions, licenses, trademarks and similar rights decreased by euro 252 million and refer to the Mobile Business Unit for euro 3,201 million, principally for the residual cost on the UMTS and PCS licenses (of which euro 2,283 million relates to TIM), and to other Group companies for euro 308 million, mainly for Indefeasible Rights of Use (IRU).

■ Differences on consolidation

euro 25,637 million

Differences on consolidation decreased by euro 1,500 million compared to December 31, 2003 (net of amortization and writedowns). The change is due to:

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- increases, mainly for the differences on consolidation booked following the purchase of 40% of the company Finanziaria Web from the De Agostini group by TI Media (euro 324 million), written down by euro 282 million, the difference on consolidation booked following the purchase of the remaining stake in the Venezuelan subsidiary Digitel (euro 95 million), the reclassification to long-term investments, and consequent booking of the relative difference on consolidation of euro 178 million, of TIM shares held by the Parent Company and booked in current assets up to December 2004, the date of the announcement of the cash tender offer for TIM shares and the plan for the merger of TIM in Telecom Italia;
- decreases, mainly for amortization (euro 1,554 million) and writedowns during the year (euro 460 million, relating to Webfin for euro 282 million, to the subsidiary Entel Chile for euro 162 million, to Med 1 euro for 9 million and the to South American company Blah! for euro 7 million).

The balance of euro 25,637 at December 31, 2004 not only refers to the difference on consolidation of euro 23,537 million which originated following the acquisition of the control of Telecom Italia by Olivetti and subsequent purchases of Telecom Italia shares, before the merger, but also to:

| (in millions of euro) | 12/31/2004 |
|-------------------------------|--------------|
| TIM | 806 |
| TI Media | 456 |
| Entel Chile | 282 |
| Corporacion Digitel | 141 |
| Holding Media e Comunicazione | 121 |
| Other companies | 294 |
| Total | 2,100 |

The remaining amount of differences on consolidation reflects the existence of favorable future prospects and higher values intrinsic in the investment holdings.

- **Work in progress and advances to suppliers** **euro 751 million**
Work in progress and advances to suppliers increased by euro 9 million, compared to December 31, 2003, and represent the difference between the capitalization of costs incurred mainly by Telecom Italia for software projects in progress and the projects which came into use during the year.

- **Other intangibles** **euro 401 million**
Other intangibles, totaling euro 401 million (euro 304 million at December 31, 2003), mainly refer to leasehold improvements.

■ **FIXED ASSETS** **euro 17,717 million**

(euro 18,324 million at December 31, 2003)

Fixed assets decreased by euro 607 million, compared to the end of 2003, mainly as a result of the difference between additions and depreciation during the year, as well as the foreign exchange effect. Fixed assets are shown net of the relative accumulated depreciation and writedowns. An analysis of fixed assets is provided in the following table:

| (in millions of euro) | Owned assets | | | Assets under finance leases | | | 12/31/2004 | 12/31/2003 |
|--|---------------|--------------------------|---------------|-----------------------------|--------------------------|------------|----------------|----------------|
| | Gross value | Accumulated depreciation | Net value | Gross value | Accumulated depreciation | Net value | Net book value | Net book value |
| Land and buildings | 3,145 | 1,519 | 1,626 | 161 | 28 | 133 | 1,759 | 1,814 |
| Plant and machinery | 59,574 | 45,369 | 14,205 | 17 | 16 | 1 | 14,206 | 14,302 |
| Manufacturing and distribution equipment | 733 | 671 | 62 | - | - | - | 62 | 46 |
| Other fixed assets | 3,210 | 2,515 | 695 | 48 | 25 | 23 | 718 | 597 |
| Construction in progress and advances to suppliers | 972 | - | 972 | - | - | - | 972 | 1,565 |
| Total | 67,634 | 50,074 | 17,560 | 226 | 69 | 157 | 17,717 | 18,324 |

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A summary of the changes in fixed assets during the year is shown in the following table:

| (in millions of euro) | 2004 | 2003 |
|--|---------------|---------------|
| Opening balance | 18,324 | 19,449 |
| – Additions | 3,320 | 3,111 |
| – Disposals and contributions | (64) | (404) |
| – Depreciation | (3,530) | (3,670) |
| – Change in the scope of consolidation | (39) | (197) |
| – Writedowns | (93) | (29) |
| – Translation adjustment and other | (201) | 64 |
| Closing balance | 17,717 | 18,324 |

Other changes refer mainly to the Mobile Business Unit for the reclassifications of fixed assets to intangibles made by the Brazilian companies and the depreciation charge for the year booked by TIM and covered by the Reserve for technological revisions.

Additions for the year amount to euro 3,320 million (euro 3,111 million in 2003) and include the purchase of buildings from Fintecna; a breakdown of additions by Business Unit/Operating Function is as follows:

| (in millions of euro) | 2004 | 2003 |
|--|--------------|--------------|
| Wireline | 1,299 | 1,497 |
| Mobile | 1,621 | 1,244 |
| South America | 145 | 116 |
| Internet and Media | 27 | 32 |
| Olivetti-Tecnost | 14 | 14 |
| IT Market | 18 | 13 |
| IT Group | 73 | 106 |
| Other activities and intragroup eliminations | 123 | 89 |
| Total | 3,320 | 3,111 |

Additions by geographical area based upon the location of the company are detailed as follows:

GEOGRAPHICAL AREA

| (in millions of euro) | 2004 | 2003 |
|----------------------------|--------------|--------------|
| Italy | 2,165 | 2,288 |
| Rest of Europe | 270 | 176 |
| North America | 5 | 3 |
| Central and South America | 879 | 643 |
| Australia, Africa and Asia | 1 | 1 |
| Total | 3,320 | 3,111 |

■ Assets purchased under finance lease contracts

Until now finance leases have been recorded in the consolidated financial statements of the Telecom Italia Group in accordance with the finance method, as recommended by Italian National Accounting Principle No. 17.

However, it should be noted that the conditions provided by the Italian Civil Code (as amended by Legislative Decree No. 6 dated January 17, 2003 and subsequent amendments and integrations) for the classification of a transaction as a finance lease are broader than those set forth in national practice which considers the existence of an option to purchase at the end of the contract to be a determining element.

This difference, therefore, requires disclosure in the notes to the 2004 consolidated financial statements of the assets under finance leases (including leasebacks resulting in a finance lease or sale and leasebacks) that had previously been considered operating leases because their contracts did not provide for the option to purchase those assets.

Had these contracts been accounted for using the finance method, in accordance with the new provisions of the Italian Civil Code, entries would have been made in the statement of income for the interest on the financed principal and for the depreciation charge of the value of the assets purchased by lease; additionally, entries would have been made in the balance sheet to record the fixed assets under assets and the residual debt under liabilities. Furthermore, use of this method would also have resulted in the deferral of any gains on sale and leaseback transactions over the finance lease term.

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The effects of this accounting treatment are described in the following table:

| BALANCE SHEET | | (in millions of euro) |
|---|--|-----------------------|
| Assets: | | |
| a) Outstanding contracts: | | |
| • assets under finance lease contracts at December 31, 2003, net of writedowns of euro 26 million and accumulated depreciation of euro 199 million) | | 1,421 |
| • assets under new finance lease contracts in 2004 (+) | | 36 |
| • assets purchased under finance lease contracts in 2004 (-) | | - |
| • depreciation charge in 2004 (-) | | (114) |
| • writedowns/writebacks on assets under finance lease contracts in 2004 (+/-) | | - |
| • assets under finance lease contracts at December 31, 2003, net of writedowns of euro 26 million and accumulated depreciation of euro 313 million)i | | 1,343 |
| b) Assets purchased in 2004: | | |
| • total higher value of assets purchased, compared to their accounting net book value | | - |
| c) Liabilities: | | |
| • Implicit liabilities for finance lease transactions at December 31, 2003 (of which euro 69 million due within one year, euro 264 million due between two and five years and euro 1,377 million due beyond five years) | | 1,710 |
| • mplicit liabilities arising in 2004 (+) | | 38 |
| • repayment of principal and assets purchased in 2004 (-) | | (76) |
| • implicit liabilities for finance lease transactions at December 31, 2004 (of which euro 84 million due within one year, euro 276 million due between two and five years and euro 1,312 million due beyond five years) | | 1,672 |
| d) Total gross effect at December 31, 2004 (a + b - c) | | (329) |
| e) Tax effect | | 84 |
| f) Balance sheet effect at December 31, 2004 of leasing transactions recognized using the finance method compared to the operating method (d - e) | | (245) |

| STATEMENT OF INCOME EFFECT | | (in millions of euro) |
|--|--|-----------------------|
| Reversal of installments on finance lease transactions (+) | | 219 |
| Recognition of financial expenses on finance lease transactions (-) | | (143) |
| Recognition of: | | |
| • depreciation charge: | | |
| • on outstanding contracts (-) | | (115) |
| • on assets purchased (-) | | - |
| • writedowns/writebacks on assets under finance lease contracts (+/-) | | - |
| Effect on income before taxes | | (39) |
| Recognition of tax effect | | 14 |
| Statement of income effect of leasing transactions recognized using the finance method compared to the operating method | | (25) |

■ Assets sold under finance lease contracts

The Telecom Italia Group has contracts in existence which provide for the sale by lease of leased assets to customers that include the performance of accessory services ("full rent formula"), which the Group has available under leasebacks contracts resulting in financing leases.

In accordance with standard Italian practice, both contracts have been considered operating leases in that they do not provide for the option to purchase those assets, whereas they present the conditions provided by IAS 17 and the Italian Civil Code (as amended by Legislative Decree No. 6 dated January 17, 2003 and subsequent amendments and integrations) for the classification of those transactions as finance leases.

The adoption of the finance method for the recording of these contracts would have resulted in the recording of financial receivables from the customers (lessees) and the recording of financial payables with the parties arranging the leaseback under a finance lease (lessors). Furthermore, this method would have resulted in the deferral, over the term of the leaseback contract, of any gains deriving from sale and leaseback transactions where the lease is a finance lease, through the deferral accounts.

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The entries in the statement of income for these transactions would relate to the reversal of the income from the lessee lease receivable obligation and of the expenses for the lease payable obligation to the lessors, as well as the recording of interest income on the principal, related to the assets sold under finance leases, and interest expense for the leaseback arrangement under finance leases.

In consideration of the type of contracts signed and of the alignment of the values of the related assets and liabilities to which they refer, the adoption of the finance method would have essentially resulted in a matching of the positive and negative effects recorded in the statement of income with respect to these contracts with, consequently, a neutral impact on the value of shareholders' equity at year end.

The effects of this accounting method are set out in the table below:

| BALANCE SHEET (in millions of euro) | |
|---|-----|
| a) Liabilities: | |
| • Implicit liabilities for finance lease transactions at December 31, 2003 (of which euro 7 million due within one year, euro 12 million due between two and five years and euro 0 million due beyond five years) | 20 |
| • implicit liabilities arising in 2004 (+) | 13 |
| • repayment of principal and assets purchased in 2004 (-) | (8) |
| • Implicit liabilities for finance lease transactions at December 31, 2004 (of which euro 9 million due within one year, euro 16 million due between two and five years and euro 0 million due beyond five years) | 25 |
| b) Deferred income and reserves for risk and charges | 1 |
| Assets: | |
| c) Recognition of implicit receivables, represented by: | |
| • implicit receivables for finance lease transactions at December 31, 2003 | 18 |
| • implicit receivables arising in 2004 (+) | 14 |
| • receipt of principal (-) | (8) |
| • writedowns/writebacks for uncollectibility (+/-) | - |
| Receivables implicit for finance lease transactions at December 31, 2004 | 24 |
| d) Total gross effect at December 31, 2004 (c-a + b) | - |
| e) Tax effect | - |
| f) Balance sheet effect at December 31, 2004 of leasing transactions recognized using the finance method compared to the operating method (d-e) | - |

| STATEMENT OF INCOME (in millions of euro) | |
|--|-----|
| Reversal of: | |
| • depreciation charge for the year of assets leased under finance contracts (+) | - |
| • income on finance lease payments recognized during the year (-) | (9) |
| • expense for lease payments on finance lease contracts (+) | 9 |
| Recognition of financial income, for implicit interest (+) | 1 |
| Recognition of financial expenses on finance lease transactions (-) | (1) |
| Writebacks/writedowns on assets leased under finance lease contracts (+/-) | |
| Effect on income before taxes | - |
| Recognition of tax effect | - |
| Statement of income effect of leasing transactions recognized using the finance method compared to the operating method | - |

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■ LONG-TERM INVESTMENTS

euro 1,866 million

(euro 2,396 million at December 31, 2003)

Long-term investments, which decreased by euro 530 million from December 31, 2003, comprise the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|--|--------------|--------------|--------------|
| Equity investments in | | | |
| • unconsolidated subsidiaries | 11 | 5 | 6 |
| • affiliated companies | 625 | 955 | (330) |
| • other companies | 419 | 501 | (82) |
| | 1,055 | 1,461 | (406) |
| Advances on future capital contributions | 9 | 9 | - |
| | 1,064 | 1,470 | (406) |
| Accounts receivable: | | | |
| • unconsolidated subsidiaries | 4 | 5 | (1) |
| • affiliated companies | 60 | 117 | (57) |
| • other receivables | 338 | 399 | (61) |
| | 402 | 521 | (119) |
| Other securities | 7 | 12 | (5) |
| Treasury stock | 393 | 393 | - |
| Total | 1,866 | 2,396 | (530) |

■ Equity investments in unconsolidated subsidiaries

euro 11 million

Equity investments in unconsolidated subsidiaries, amounting to euro 11 million, increased by euro 6 million compared to December 31, 2003.

■ Equity investments in affiliated companies

euro 625 million

Equity investments in affiliated companies, amounting to euro 625 million, decreased by euro 330 million compared to December 31, 2003.

Equity investments in affiliated companies refer to the following:

| (in millions of euro) | 12/31/2003 | Additions | Disposals/ reimbursements of capital | Valuation using equity method (*) | 12/31/2004 |
|------------------------------|------------|-----------|--|---|------------|
| Etec S.A. | 392 | 26 | | (128) | 290 |
| Italtel Holding | 35 | | | (8) | 27 |
| LI.SIT | 49 | | | (10) | 39 |
| Mirror International Holding | 48 | | (48) | | - |
| Netco Redes | 24 | | (24) | | - |
| Sky Italia | 44 | 55 | (99) | | - |
| Tiglio I | 234 | | (76) | (5) | 153 |
| Tiglio II | 78 | | (25) | 7 | 60 |
| Other | 51 | 2 | (5) | 8 | 56 |
| Total | 955 | 83 | (277) | (136) | 625 |

(*) Includes the share of the equity in the earnings and losses for the year, amortization of goodwill, writedowns and adjustments on the translation of foreign currency financial statements.

Investments valued using the equity method include the unamortized portion of the excess of book values over the corresponding share of the underlying net equity at current values at the time of purchase. The excess amounts in total to euro 89 million (euro 101 million at December 31, 2003), of which euro 88 million refers to Etec S.A. Cuba.

As described in detail in the Report on Operations, in 2004, the equity investments held in Sky Italia, Mirror International Holding and Netco Redes and the reserves were distributed by Tiglio I and Tiglio II.

On February 19, 2004, the merger of Is TIM and Aycell was finalized by conferring the assets and liabilities of Is TIM and Aycell to Avea I.H.A.S. (owned 40% by TIM International, 40% by Turk Telekom and 20% by the Is Bank group).

At December 31, 2004, the carrying value of the affiliated company Avea I.H.A.S. has been maintained at a nil in view of the indications

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contained in International Accounting Standards (IAS 31 and its interpretation) which require that, in the event of the contribution of non-monetary assets to a joint venture, the transaction should be accounted for at the pre-existing carrying values.

A list of the companies valued using the equity method is provided in Annex 7; equity investments in unconsolidated subsidiaries and affiliates are listed in Annex 8.

■ Equity investments in other companies

euro 419 million

Equity investments in other companies, amounting to euro 419 million, decreased by euro 82 million from December 31, 2003 mainly on account of the sale of Cirsà, 3.1% of Euskaltel, Pirelli & C. Real Estate shares and the reimbursement from Solpart following the reduction of its share capital.

Equity investments in other companies refer to the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 |
|-------------------------|------------|------------|
| Mediobanca | 113 | 113 |
| Solpart Participações | 95 | 111 |
| Neuf Telecom (ex Ldcom) | 51 | 51 |
| Cirsà | - | 41 |
| Medio Credito Centrale | 36 | 36 |
| Consortium | 20 | 20 |
| Fin. Priv. | 15 | 15 |
| Brasil Telecom | 14 | - |
| Euskaltel | 13 | 27 |
| Intelsat | 13 | 12 |
| Forthnet | 10 | 14 |
| Sia | 11 | 11 |
| Pirelli Real Estate | - | 15 |
| Other | 28 | 35 |
| Total | 419 | 501 |

The Extraordinary Shareholders' Meeting of Solpart voted to reduce share capital partly through a cash reimbursement and partly by the distribution of ordinary shares and preferred shares of the subsidiary Brasil Telecom Participações S.A.. As a result of this resolution, the Telecom Italia group received 1,319,945,886 ordinary shares and 1,326,370,406 preferred shares of Brasil Telecom.

The reduction in Solpart's share capital did not involve a change in the number of ordinary and preferred shares owned by each shareholder, whereas the per share value was reduced.

■ Advances on future capital contributions

euro 9 million

Advances on future capital contributions at December 31, 2004 mainly refer to advances made by the Parent Company to Telegono (euro 9 million).

■ Accounts receivable from unconsolidated subsidiaries

euro 4 million

Accounts receivable from unconsolidated subsidiaries, amounting to euro 4 million, are represented by non-interest-earning loans made by Matrix S.p.A. to Emax-Trade S.p.A. in liquidation and by H.M.C. to H.M.C. Pubblicità in liquidation.

■ Accounts receivable from affiliated companies

euro 60 million

Accounts receivable from affiliated companies, amounting to euro 60 million, decreased by euro 57 million compared to December 31, 2003. Such receivables mostly refer to loans made to Avea I.H.A.S. (euro 29 million), Aree Urbane (euro 20 million), Golden Lines Int. Communic. Services (euro 5 million), Telegono (euro 3 million) and Tiglio II (euro 3 million).

■ Other receivables

euro 338 million

Other receivables decreased from euro 399 million at December 31, 2003 to euro 338 million. They mainly refer to the receivable from PTT Srbija for the remaining amount due on the sale of Telekom Srbija (euro 75 million) and the booking of the cost of the two call options on the share capital of Sofora Argentina (euro 49 million). Moreover, this caption comprises the receivable from the prepayment of taxes on the reserve for employee termination indemnities (euro 55 million), loans made to employees (euro 90 million), security deposits and other long-term receivables (euro 69 million).

■ Other securities

euro 7 million

Other securities, amounting to euro 7 million, decreased by euro 5 million compared to December 31, 2003.

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■ Treasury stock

euro 393 million

Treasury stock remains unchanged compared to December 31, 2003 and includes 101,208,867 Telecom Italia ordinary shares, of which 1,272,014 are held by the Parent Company and 99,936,853 shares held by Telecom Italia Finance.

* * *

Disclosure according to art. 2427, paragraph 6 of the Italian Civil Code in respect of the breakdown of accounts receivable by geographical area is presented in the attached Annex 3.

CURRENT ASSETS

■ INVENTORIES

euro 435 million

(euro 426 million at December 31, 2003)

Inventories consist of the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|---|------------|------------|-------------|
| Raw materials and supplies | 12 | 24 | (12) |
| Merchandise | 309 | 267 | 42 |
| | 321 | 291 | 30 |
| Work in progress and semifinished goods | 17 | 22 | (5) |
| Finished goods | 1 | 7 | (6) |
| | 18 | 29 | (11) |
| Contract work in process | 96 | 105 | (9) |
| Advances to suppliers | - | 1 | (1) |
| | 96 | 106 | (10) |
| Total | 435 | 426 | 9 |

Inventories are held by companies providing telecommunications services for euro 256 million (euro 203 million at December 31, 2003), companies in the information technology sector for euro 50 million (euro 83 million at December 31, 2003), the Olivetti Tecnost group for euro 81 million (euro 91 million at December 31, 2003) and other minor companies for euro 48 million (euro 49 million at December 31, 2003).

The increase in "merchandise" refers to the Parent Company for euro 48 million in conjunction with higher inventories connected with the marketing of Aladino cordless phones and videophones and other Group companies for -euro 6 million.

"Raw materials and supplies" and "work in progress and semifinished goods" approximate current costs.

■ ACCOUNTS RECEIVABLE

euro 12,999 million

(euro 15,639 million at December 31, 2003)

A breakdown of accounts receivable, which decreased by euro 2,640 million, is provided below:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|--|---------------|---------------|----------------|
| Trade accounts receivable | 7,203 | 7,640 | (437) |
| • allowance for doubtful accounts | (789) | (790) | 1 |
| Total trade accounts receivable | 6,414 | 6,850 | (436) |
| Accounts receivable from unconsolidated subsidiaries | 14 | 30 | (16) |
| Accounts receivable from affiliated companies | 188 | 149 | 39 |
| Taxes receivable | 778 | 1,653 | (875) |
| Deferred tax assets | 3,706 | 5,013 | (1,307) |
| Other receivables | 1,899 | 1,944 | (45) |
| Total | 12,999 | 15,639 | (2,640) |

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■ Trade accounts receivable

euro 6,414 million

Gross trade accounts receivable total euro 7,203 million and consist, for the most part, of receivables for telecommunications services. Trade accounts receivable refer, in particular, to Telecom Italia (per euro 3,468 million) and TIM (per euro 1,236 million). This caption also includes euro 1,151 million of receivables due from other telecommunications operators.

Receivables have been adjusted to estimated realizable value by the allowance for doubtful accounts.

Furthermore, the following accounts receivable securitization and factoring transactions were carried out:

Securitization

The program for the securitization of trade accounts receivable generated by services rendered to Telecom Italia Wireline clientele began during 2001 and has continued in 2004.

During 2004, the total amount of trade accounts receivable sold under the securitization program was equal to euro 8.8 billion and refers to Telecom Italia's receivables from consumer and microbusiness customers. At December 31, 2004, receivables sold amount to euro 809 million (of which euro 773 million is not yet due).

The securitization transaction led to a reduction in net financial indebtedness of euro 786 million at December 31, 2004 (euro 851 million at the end of 2003).

Furthermore, at December 31, 2004, Telecom Italia recorded short-term financial payables of euro 212 million for a loan made by TI Securitisation Vehicle S.r.l. out of the excess liquidity generated by the securitization transaction.

Under the securitization program, in July 2004, TI Securitisation Vehicle S.r.l. (TISV) reimbursed the second and fourth tranches of the securities, respectively, called Series 2001-1, Class A2, issued in June 2001, for an amount equal to euro 150 million, and Series 2003-1, Class A1, for an amount equal to euro 100 million. Prior to this reimbursement, in June 2004, TISV issued a new tranche of securities for an amount of euro 250 million, called Series 2004-1, Class A1, at a floating rate with a spread of 12 basis points on the 3-month Euribor maturing July 25, 2006, to be added to the existing Series 2003-1 Class A3 securities for an amount of euro 450 million with a similar maturity date. Therefore, the total securities of the securitization currently outstanding continues to be equal to euro 700 million. As in the case of the securities previously issued, the Fitch, Moody's and Standard & Poor's rating agencies assigned the maximum rating of AAA/Aaa/AAA.

Factoring

In 2004 Telecom Italia, TIM, Olivetti-Tecnost and Path.net sold trade accounts receivable without recourse for a total of euro 4,346 million, of which euro 1,175 million is not yet due.

These factoring transactions led to a reduction in net financial indebtedness at December 31, 2004 of euro 1,038 million, of which euro 966 million refers to transactions executed in 2004 and euro 71 million to transactions concluded in December 2003.

■ Accounts receivable from unconsolidated subsidiaries

euro 14 million

Accounts receivable from unconsolidated subsidiaries include loans of euro 6 million and trade accounts receivables and other receivables from unconsolidated subsidiaries of euro 8 million.

■ Accounts receivable from affiliated companies

euro 188 million

Accounts receivable from affiliated companies of euro 188 million increased by euro 39 million and refer to trade, financial and other receivables. The most significant amounts relate to LI.SIT. (euro 77 million), Teleleasing (euro 67 million), Tiglio I (euro 9 million) and Shared Service Center (euro 7 million).

■ Taxes receivable

euro 778 million

Taxes receivable amount to euro 778 million (euro 1,653 million at December 31, 2003). The decrease of euro 875 million mainly refers to Telecom Italia (euro 868 million) for the sale of IRPEG receivables to TIM to be used to pay the 2004 on-account payment for the IRES corporate income tax.

■ Deferred tax assets

euro 3,706 million

Deferred tax assets amount to euro 3,706 million (euro 5,013 million at December 31, 2003). The reduction from December 31, 2003 can be ascribed to the Parent Company and TIM and is essentially due to deferred tax assets which reversed during the year in respect of investment writedowns, tax loss carryforwards and reserves for risks and charges.

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The net balance of deferred tax assets and liabilities is made up as follows:

| (in millions of euro) | 12/31/2004 | 12/31/2003 |
|----------------------------|--------------|--------------|
| Deferred tax assets | 3,706 | 5,013 |
| Reserve for deferred taxes | (225) | (252) |
| Total | 3,481 | 4,761 |

The main components forming the net receivable balance, divided by nature, are the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 |
|---|--------------|--------------|
| Writedowns | 2,310 | 3,260 |
| Tax losses carried forward | 532 | 663 |
| Reserves for risks and charges | 249 | 428 |
| Reserve for employee benefits Law 58/92 | 237 | 265 |
| Allowance for doubtful accounts | 153 | 179 |
| Unrealized intragroup profits | 61 | 78 |
| Other deferred items | 164 | 140 |
| Withholding tax on interest | (61) | (132) |
| Accelerated depreciation | (164) | (72) |
| Other | - | (48) |
| Net receivable balance | 3,481 | 4,761 |

At December 31, 2004, the Group has tax loss carryforwards amounting to euro 5,957 million, with the following expiry dates.

| Year of expiration | (in millions of euro) |
|-------------------------------------|-----------------------|
| 2005 | 160 |
| 2006 | 276 |
| 2007 | 583 |
| 2008 | 1,604 |
| 2009 | 29 |
| Expiring after 2009 | 1 |
| Without expiration | 3,304 |
| Total tax loss carryforwards | 5,957 |

No deferred tax assets have been set aside when there is uncertainty over their recoverability against future taxable profits. Specifically, tax loss carryforwards, which have not been considered in the determination of deferred tax assets amount to some euro 4,300 million at December 31, 2004. Moreover, at December 31, 2004, some euro 267 million of deferred tax assets have not been booked since their recovery is not reasonably assured.

At December 31, 2004, no taxes have been set aside on tax-deferred reserves subject to taxation in the event of distribution and/or utilization since no transactions are expected to be entered into that would warrant their distribution or utilization.

During the course of the year, the Parent Company decided to subscribe to the new consolidated national tax return procedure for group taxation jointly with some subsidiaries.

■ Other receivables

euro 1,899 million

Other receivables total euro 1,899 million (euro 1,944 million at December 31, 2003). Details are as follows:

- financial receivables, totaling euro 375 million (euro 796 million at December 31, 2003), decreased by euro 421 million mainly on account of the close of the securities lending agreement on bonds of Olivetti Finance (now Telecom Italia Finance) (euro 300 million). Financial receivables for the most part refer to the deferred portion of the trade accounts receivable securitization transactions by Telecom Italia (euro 338 million);

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- other receivables, totaling euro 1,524 million (euro 1,148 million at December 31, 2003), refer to the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 |
|------------------------------|--------------|--------------|
| Customer receipts in transit | 81 | 91 |
| Employees | 62 | 68 |
| Sundry receivables | 1,381 | 989 |
| Total | 1,524 | 1,148 |

Sundry receivables include accounts receivable sold through factoring transactions deriving from sales of accounts receivable without recourse from trading partners with a maturity clause (euro 320 million at December 31, 2004, euro 412 million at December 31, 2003). The increase from December 31, 2003 is due to the booking of the receivable from the Financial Administration (euro 621 million) for the accrual of prior period income relating to the TLC license fee and the relative interest paid by Telecom Italia and TIM for the year 1999 as a result of the decision handed down by the TAR of Lazio No. 47/2005 of January 4, 2005, which upheld the appeal filed by Telecom Italia and cancelled the Ministerial Decree dated March 21, 2000 regarding the TLC fee instituted by Law 448/1998 declaring it to be illegal.

In 2004, the Group also sold receivables of euro 35 million for interest accrued on IRPEG receivables from the Ministry of Finance.

* * *

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of accounts receivables by geographical area is presented in Annex 3.

■ SHORT-TERM FINANCIAL ASSETS

euro 934 million

(euro 3,657 million at December 31, 2003)

Short-term financial assets decreased by 2,723 million compared to December 31, 2003; they include the following:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|---|------------|--------------|----------------|
| Equity investments in unconsolidated subsidiaries | - | 170 | (170) |
| Equity investments in affiliated companies | - | 708 | (708) |
| Other securities | 932 | 2,719 | (1,787) |
| Receivables for sales of securities | 2 | 60 | (58) |
| Total | 934 | 3,657 | (2,723) |

Equity investments in unconsolidated subsidiaries at December 31, 2003 had included the value of TIM shares purchased for later trading. These shares, starting from the month of December 2004, have been consolidated following the announcement of the cash tender offer for TIM shares and the merger of TIM in the Parent Company Telecom Italia.

Equity investments in affiliated companies show a nil balance following the sale of Telekom Austria in January 2004 (euro 708 million).

Other securities consist of own bonds (euro 163 million), other bonds (euro 431 million) and commercial paper (euro 328 million) held by Telecom Italia Finance and other bonds held by other companies (euro 10 million).

The decrease of euro 1,787 million from December 31, 2003 refers to the cancellation, on March 26, 2004, of Euro 850 million of securities, repurchased in prior years, originally issued by Olivetti Finance N.V. S.A. (merged by Telecom Italia Finance effective June 1, 2004). Such securities included euro 650 million of bonds maturing July 2004 out of a total of euro 4,200 million (the amount still outstanding is euro 3,550 million) and euro 200 million of bonds maturing February 2005, which, after this transaction, have been completely cancelled.

The further reduction is mainly due to the sale of securities.

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The carrying values of equity investments at the end of the year have been aligned to market values; other securities have been recorded at the lower of purchase cost and estimated realizable value represented by market prices at the end of the year.

■ LIQUID ASSETS

euro 8,562 million

(euro 4,877 million at December 31, 2003)

Liquid assets consist mainly of funds on deposit in Italian and foreign banks in current accounts. The increase of euro 3,685 million is partly due to the issue of bonds during the year. The choice of the type of investment of the liquidity was essentially due to the need to have liquid resources available for the partial payment of the price, equal to euro 2,504 million, on the shares tendered under the cash tender offer for TIM shares.

■ ACCRUED INCOME AND PREPAID EXPENSES

euro 1,177 million

(euro 1,325 million at December 31, 2003)

This item, which decreased by euro 148 million, can be analyzed as follows:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|--|--------------|--------------|--------------|
| Issue discounts and similar charges | 241 | 240 | 1 |
| Accrued income: | | | |
| • production value | 10 | 20 | (10) |
| • financial income | 421 | 475 | (54) |
| • other | - | - | - |
| | 431 | 495 | (64) |
| Other prepaid expenses: | | | |
| • production costs | 179 | 164 | 15 |
| • financial expense | 294 | 387 | (93) |
| • other | 32 | 39 | (7) |
| | 505 | 590 | (85) |
| Accrued income and other prepaid expenses | 936 | 1,085 | (149) |
| Total | 1,177 | 1,325 | (148) |

* * *

An analysis of accounts receivable and accrued income by maturity and type is provided in Annex 1.

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of receivables by geographical area is presented in Annex 3.

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■ LIABILITIES AND SHAREHOLDERS' EQUITY

SHAREHOLDERS' EQUITY

euro 19,861 million

(euro 20,589 million at December 31, 2003)

A breakdown of shareholders' equity is presented below:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|-------------------------|---------------|---------------|--------------|
| Parent Company interest | 15,172 | 16,092 | (920) |
| Minority interest | 4,689 | 4,497 | (192) |
| Total | 19,861 | 20,589 | (728) |

Telecom Italia's interest in shareholders' equity decreased by euro 920 million compared to December 31, 2003. The decrease is mainly due to the difference between dividends paid (euro 1,730 million, net of dividends on shares held by Telecom Italia Finance) and the result for the year (euro 781 million, euro 1,192 million in 2003).

■ SHARE CAPITAL

euro 8,865 million

Share capital of Telecom Italia amounts to euro 8,865 million (euro 8,854 million at December 31, 2003) and consists of 10,322,001,069 ordinary shares and 5,795,921,069 savings shares, all with a par value of euro 0.55 each.

The increase compared to the previous year (euro 11 million) is due to the conversion of convertible bonds and the exercise of stock options by employees.

■ RESERVE FOR TREASURY STOCK IN THE PORTFOLIO OF THE PARENT COMPANY AND UNCONSOLIDATED SUBSIDIARIES

euro 393 million

The Reserve for treasury stock in the portfolio of the Parent Company and unconsolidated subsidiaries amounts to euro 393 million, which is unchanged from December 31, 2003. This item refers to 101,208,867 Telecom Italia ordinary shares of which 1,272,014 shares are held by the Parent Company, having been purchased in previous years, and 99,936,853 shares held by Telecom Italia Finance (originally held by Olivetti International S.A.), having been received in exchange for the shares of Tecnost S.p.A. following the merger of Tecnost in Olivetti in 2000.

■ PARENT COMPANY INTEREST IN RESERVES AND RETAINED EARNINGS

euro 5,133 milioni

The Parent Company interest in reserves and retained earnings of euro 5,133 million decreased by euro 520 million principally due to the payment of dividends (euro 538 million).

This item includes the Parent Company's own retained earnings and reserves, as well as the consolidated companies' retained earnings, inflation adjustment reserves and tax-deferred reserves. No deferred taxes have been provided on the latter reserves since, based on current plans, no transactions are expected to be entered into that would warrant their taxation.

The reconciliation of Telecom Italia's financial statements with the consolidated financial statements as regards shareholders' equity and net result for the year, and the changes in the components of consolidated shareholders' equity, are provided in Annexes 4 and 5.

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RESERVES FOR RISKS AND CHARGES

euro 2,498 million

(euro 2,923 million at December 31, 2003)

These reserves decreased by euro 425 million from December 31, 2003 and refer to the following:

- Reserve for pensions and similar obligations euro 40 million

The reserve for pensions and similar obligations, amounting to euro 40 million (euro 42 million at December 31, 2003), includes the reserve for agents' leaving indemnities and the liabilities relating to pension funds set up for the employees of certain foreign subsidiaries.
- Reserve for taxes and reserve for deferred taxes euro 460 million

The reserve for taxes, amounting to euro 460 million (euro 404 million at December 31, 2003), consists of the taxes set aside during the year and estimated tax liabilities on positions still to be agreed or in dispute. The increase is for the most part in reference to the Parent Company (euro 49 million).

The reserve for deferred taxes, amounting to euro 225 million (euro 252 million at December 31, 2003), includes deferred taxes provided by the individual consolidated companies on the income components subject to deferred taxation, mainly accelerated depreciation.
- Consolidation reserve for future risks and charges euro 0 million

The consolidation reserve for future risks and charges shows a nil balance compared to December 31, 2003.
- Other reserves euro 1,998 million

Other reserves, amounting to euro 1,998 million, decreased by euro 478 million compared to December 31, 2003.

Other reserves include:

- the TIM group's reserves totaling euro 548 million (euro 572 million at December 31, 2003) to cover the TIM group's exposure with the affiliated company Avea. Such reserves, set aside in 2002 following counter-guarantees provided to lending banks of Is TIM (now Avea I.H.A.S.), are still in force since the guarantees still exist in respect of the liabilities of the company resulting from the merger of Is TIM and TurkCell (Avea I.H.A.S.);
- reserves, equal to 85 million, for the investments held in Med 1 and Med Nautilus, after reaching a preliminary agreement in December 2004 with the minority shareholders of Med SA, Med Ltd and Med 1 to resolve certain conflicting situations referring to MED SA's and Telecom Italia's put, respectively, on 49% of Med Ltd and Med 1 shares, also to resolve the arbitration proceedings set into motion in Luxembourg by the Fishman group (FTT) aimed at the restitution of the sums paid to the Telecom Italia Group in 2000 for the purchase of 30% of MED SA. The transactions negotiated, which call for the buyback of all the minority shares in Med Ltd and in Med 1, allow Telecom Italia to strengthen its presence in the IP services and "wholesale" data sector in the eastern Mediterranean area;
- the reserves for contractual risks and other risks for a total of euro 561 million, mainly in respect of operating activities and including euro 152 million relating to the sanction levied on the Parent Company by the Antitrust Authority for the alleged use of a dominant position;
- the reserves for corporate restructuring totaling euro 75 million, mainly relating to employee cutbacks and layoffs, of which euro 48 million regards Telecom Italia;
- the reserves set aside by TIM for risks and charges inherent to the regulatory framework (euro 100 million) and for technological revisions (euro 5 million);
- the reserve of euro 264 million relating to financial expenses for the premium on the redemption of notes issued by Telecom Italia Finance and euro 26 million for risks on derivative contracts;
- the reserve for the losses of subsidiaries and affiliates of euro 109 million and for extraordinary corporate-related transactions of euro 225 million.

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RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES

euro 1,324 million

(euro 1,296 million at December 31, 2003)

The reserve for employee termination indemnities increased by euro 28 million compared to December 31, 2003 and relates only to Italian Group companies.

| | |
|---|--------------|
| (in millions of euro) | |
| January 1 | 1,296 |
| Change during the year: | |
| Provisions charged to income | 189 |
| Utilizations for: | |
| • indemnities paid to employees who terminated employment | (91) |
| • advances | (20) |
| • pension funds | (29) |
| Equalization tax on revaluation of employee termination indemnities and other changes | (21) |
| December 31 | 1,324 |

"Other changes" mainly refer to the change in the scope of consolidation.

LIABILITIES

euro 50,587 million

(euro 53,307 million at December 31, 2003)

A breakdown of liabilities, which decreased by euro 2,720 million from December 31, 2003, is presented below:

| (in millions of euro) | 12/31/2004 | | | 12/31/2003 | | |
|--|--------------------|---|---------------|--------------------|---|---------------|
| | Financial payables | Trade accounts payable and other payables | Total | Financial payables | Trade accounts payable and other payables | Total |
| Debentures | 29,640 | | 29,640 | 30,053 | | 30,053 |
| Convertible debentures | 5,592 | | 5,592 | 7,312 | | 7,312 |
| Total debentures | 35,232 | | 35,232 | 37,365 | | 37,365 |
| Due to banks | 1,830 | | 1,830 | 2,460 | | 2,460 |
| Due to other lenders | 1,623 | | 1,623 | 1,012 | | 1,012 |
| Advances | - | 50 | 50 | - | 141 | 141 |
| Trade accounts payable | 4 | 6,785 | 6,789 | 9 | 5,848 | 5,857 |
| Accounts payable to unconsolidated subsidiaries | 3 | 9 | 12 | 9 | 9 | 18 |
| Accounts payable to affiliated companies | 21 | 272 | 293 | 33 | 137 | 170 |
| Taxes payable | - | 542 | 542 | 58 | 1,418 | 1,476 |
| Contributions to pensions and social security institutions | - | 1,356 | 1,356 | - | 1,514 | 1,514 |
| Other liabilities | 131 | 2,729 | 2,860 | 519 | 2,775 | 3,294 |
| Total | 38,844 | 11,743 | 50,587 | 41,465 | 11,842 | 53,307 |

■ Debentures

euro 29,640 million

Debentures total euro 29,640 million and decreased by euro 413 million compared to December 31, 2003 (euro 30,053 million). The regulations and/or Offering Circular relating to the notes described below are available on the corporate website <http://www.telecomitalia.it>.

Details are as follows:

Notes issued by Telecom Italia S.p.A. (for a total of euro 7,151 million):

- notes for euro 2,500 million, issued on February 1, 2002, divided into two tranches of euro 1,250 million each, at annual fixed rates, respectively, with a coupon of 5.625% maturing on February 1, 2007 and a coupon of 6.25% maturing on February 1, 2012. The issue is part of the "Global Medium Term Note Program";

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- notes 2002 – 2022 reserved for subscription by employees, in service and retired, of companies directly and indirectly controlled by Telecom Italia, with headquarters in Italy, for euro 216 million;
- notes for euro 3,000 million, issued on January 29, 2004, divided into three tranches: the first, for euro 1,000 million, with an annual coupon indexed to the 3-month Euribor + 0.33 basis points, maturing October 29, 2007; the second, for euro 750 million, with an annual fixed-rate coupon of 4.50%, maturing on January 28, 2011; the third, for euro 1,250 million, with an annual fixed-rate coupon of 5.375%, maturing on January 29, 2019. On November 24, 2004, Telecom Italia received authorization from CONSOB to publish the prospectus relating to the admission of the notes for listing on Borsa Italia S.p.A.'s EuroMOT screen-based trading market;
- notes for euro 110 million issued on April 8, 2004 with a quarterly coupon equal to the 3-month Euribor + 0.60%, maturing March 30, 2009;
- notes of GBP 850 million (equivalent to euro 1,205 million) issued on June 24, 2004, with an annual fixed-rate coupon of 6.375%, maturing June 24, 2019;
- notes for euro 120 million issued on November 23, 2004 with a quarterly coupon equal to the 3-month Euribor + 0.66%, maturing November 23, 2015.

The notes issued in 2004 fall under Telecom Italia's Euro Medium Term Note Program (EMTN) for a total of euro 10 billion approved by the Board of Directors on October 10, 2003.

Notes issued by Telecom Italia Finance S.A. and guaranteed by Telecom Italia S.p.A. (for a total of euro 16,803 million):

- notes issued April 20, 2001 by the subsidiary Sogerim (merged in Telecom Italia Finance S.A. in 2002) on international markets for a total of euro 6,000 million. The issue is divided into three tranches: the first, for euro 1,000 million at quarterly floating interest rates, maturing April 20, 2004, and therefore already redeemed; the second, for euro 2,745 million (net of the notes repurchased by Telecom Italia Finance starting July 2004 for a total of euro 255 million) with an annual fixed-rate coupon of 6.375%, maturing April 20, 2006; the third for euro 2,000 million with an annual fixed-rate coupon of 7.25%, maturing April 20, 2011;
- notes 1999 – 2009 (originally Olivetti International N.V.) for euro 1,500 million with an annual fixed-rate coupon of 5.15%, maturing in February 9, 2009;
- notes 1986-2046 (originally Olivetti International N.V.) for CHF 100 million (equivalent to euro 65 million) with an annual fixed-rate coupon of 5.625%, maturing in June 12, 2046.

All of the notes listed below were originally issued by Olivetti Finance N.V. (merged in Telecom Italia Finance effective June 1, 2004) and are guaranteed by Telecom Italia S.p.A. under the Euro Medium Term Note Program (EMTN):

- notes 2002-2005 for euro 500 million with a quarterly coupon indexed to the 3-month Euribor + 130 basis points. The noteholder has the option of extending maturity for successive periods of 21 months, up to a total maximum of 10 years (the final maturity date is set for March 14, 2012). In accordance with the terms and conditions of the notes, noteholders in possession of notes totaling euro 283,000 chose not to extend the notes (March 14, 2005). For those, instead, that decided to extend the maturity date, for notes totaling euro 499,717,000, Telecom Italia Finance S.A. issued new notes on December 14, 2004 denominated "Telecom Italia Finance S.A. euro 499,717,000 Guaranteed Floating Rate Extendable Notes Due 2006" with a new maturity date of December 14, 2006;
- notes 2002-2006 for euro 1,100 million with a quarterly coupon indexed to the 3-month Euribor plus a spread of 1.25%, maturing in January 3, 2006;
- notes 2002-2007 for euro 1,750 million with an annual fixed-rate coupon of 6.5%, maturing on April 24, 2007;
- notes 2003-2008 for euro 1,750 million with an annual fixed-rate coupon of 5.875%, maturing on January 24, 2008;
- notes 1999-2009 (originally Olivetti International Finance N.V.) for euro 2,350 million with an annual fixed-rate coupon of 6 1/8% + a 0.45% step-up, maturing on July 30, 2009;
- notes 2002-2012 for euro 1,000 million with an annual fixed-rate coupon of 7.25%, maturing on April 24, 2012;
- notes 2003-2013 for euro 850 million with an annual fixed-rate coupon of 6.875%, maturing on January 24, 2013;
- notes 2002-2032 for JPY 20 billion (equivalent to euro 143 million) with a six-month fixed-rate coupon of 3.55%, maturing on May 14, 2032 (callable by the issuer annually beginning from May 14, 2012);
- notes 2002-2032 for euro 250 million with an annual fixed-rate coupon of 7.77%, maturing on August 9, 2032;
- notes 2003-2033 for euro 800 million with an annual fixed-rate coupon of 7.75%, maturing on January 24, 2033.

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Notes issued by Telecom Italia Capital S.A. and guaranteed by Telecom Italia S.p.A. (for a total of euro 5,506 million):

- issue of multi-tranche fixed-rate notes on October 29, 2003, for USD 4,000 million. The issue is divided into three tranches as follows:
 - Serie A, for USD 1,000 million (equivalent to euro 734 million), with an annual fixed-rate coupon of 4%, maturing on November 15, 2008;
 - Serie B, for USD 2,000 million (equivalent to euro 1,468 million), with an annual fixed-rate coupon of 5.25%, maturing on November 15, 2013;
 - Serie C, for USD 1,000 million (equivalent to euro 734 million), with an annual fixed-rate coupon of 6.375%, maturing on November 15, 2033;
- issue of multi-tranche fixed-rate notes on October 6, 2004, for USD 3,500 million. The issue is divided into three tranches as follows:
 - Serie A, for USD 1,250 million (equivalent to euro 918 million) with an annual fixed-rate coupon of 4%, maturing on January 15, 2010;
 - Serie B, for USD 1,250 million (equivalent to euro 918 million) with an annual fixed-rate coupon of 4.95%, maturing on September 30, 2014;
 - Serie C, for USD 1,000 million (equivalent to euro 734 million) with an annual fixed-rate coupon of 6%, maturing on September 30, 2034.

Notes issued by Entel Chile (for a total of euro 180 million):

- notes maturing between 2005 and 2023 issued by Entel Chile.

The following table shows the notes issued to third parties by companies in the Telecom Italia Group, divided by issuing company:

| Currency | Amount (in millions) | Equivalent amount in millions of euro | Coupon | Issue date | Maturity date | Issue price (%) |
|--|-------------------------|---|----------------------------|------------|---------------|--------------------|
| Notes issued by Telecom Italia S.p.A. | | | | | | |
| Euro | 1,250 | 1,250 | 5.625% | 2/1/02 | 2/1/07 | 99.841 |
| Euro | 1,000 | 1,000 | 3-month Euribor + 0.33% | 1/29/04 | 10/29/07 | 99.927 |
| Euro | 110 | 110 | 3-month Euribor + 0.60% | 4/8/04 | 3/30/09 | 100 |
| Euro | 750 | 750 | 4.500% | 1/29/04 | 1/28/11 | 99.56 |
| Euro | 1,250 | 1,250 | 6.250% | 2/1/02 | 2/1/12 | 98.952 |
| Euro | 120 | 120 | 3-month Euribor + 0.66% | 11/23/04 | 11/23/15 | 100 |
| Euro | 1,250 | 1,250 | 5.375% | 1/29/04 | 1/29/19 | 99.07 |
| GBP | 850 | 1,205 | 6.375% | 6/24/04 | 6/24/19 | 98.85 |
| Euro | 216 | 216 | 6-month Euribor | 1/1/02 | 1/1/22 | 100 |
| Subtotal | | 7,151 | | | | |
| Notes issued by Telecom Italia Finance S.A. and guaranteed by Telecom Italia S.p.A. | | | | | | |
| Euro | 0,3 | 0,3 | 3-month Euribor + 1.3% (d) | 3/14/02 | 3/14/05 | 100 |
| Euro | 499,7 | 499,7 | 3-month Euribor + 1.3% (d) | 12/14/04 | 12/14/06 | 100 |
| Euro | 1,100 | 1,100 | 3-month Euribor + 1.25% | 5/29/02 | 1/3/06 | 99.456 (*) |
| Euro | 2,745 | 2,745 | 6.375% (a) | 4/20/01 | 4/20/06 | 99.937 |
| Euro | 1,750 | 1,750 | 6.500% | 4/24/02 | 4/24/07 | 100.911 (*) |
| Euro | 1,750 | 1,750 | 5.875% | 1/24/03 | 1/24/08 | 99.937 |
| Euro | 1,500 | 1,500 | 5.15% (b) | 2/9/99 | 2/9/09 | 99.633 |
| Euro | 2,350 | 2,350 | 6.575% (c) | 7/30/99 | 7/30/09 | 98.649 (*) |
| Euro | 2,000 | 2,000 | 7.25% (a) | 4/20/01 | 4/20/11 | 99.214 |
| Euro | 1,000 | 1,000 | 7.25% | 4/24/02 | 4/24/12 | 101.651 (*) |
| Euro | 850 | 850 | 6.875% | 1/24/03 | 1/24/13 | 99.332 |
| JPY | 20,000 | 143 | 3.550% | 4/22/02 | 5/14/32 | 99.25 |
| Euro | 250 | 250 | 7.770% | 8/9/02 | 8/9/32 | 100.2 |
| Euro | 800 | 800 | 7.750% | 1/24/03 | 1/24/33 | 100.191 (*) |
| CHF | 100 | 65 | 5.625% | 6/12/86 | 6/12/46 | 99.000 |
| Subtotal | | 16,803 | | | | |

(*) Weighted average issue price for notes issued with more than one tranche.

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| Currency | Amount (in millions) | Equivalent amount in millions of euro | Coupon | Issue date | Maturity date | Issue price (%) |
|--|-------------------------|---|----------------------------|--------------------------|--------------------------|--------------------|
| Notes issued by Telecom Italia Capital S.A. and guaranteed by Telecom Italia S.p.A. | | | | | | |
| USD | 1,000 | 734 | 4.000% | 29/10/03 | 11/15/08 | 99.953 |
| USD | 1,250 | 918 | 4.000% | 10/6/04 | 1/15/10 | 99.732 |
| USD | 2,000 | 1,468 | 5.250% | 10/29/03 | 11/15/13 | 99.742 |
| USD | 1,250 | 918 | 4.950% | 10/6/04 | 9/30/14 | 99.651 |
| USD | 1,000 | 734 | 6.375% | 10/29/03 | 11/15/33 | 99.558 |
| USD | 1,000 | 734 | 6.000% | 10/6/04 | 9/30/34 | 99.081 |
| Subtotal | | 5,506 | | | | |
| Notes issued by Entel Chile | | | | | | |
| CLP-UF(**) | 136,097 | 180 | Between 5.96% and 8.06% | Between 2000 and 2002 | Between 2005 and 2023 | |
| Subtotal | | 180 | | | | |
| Total | | 29,640 | | | | |

(**) UF = Unit of account indexed to a basket of currencies.

Mechanism of how coupons change on step-up/step-down notes in relation to the rating

(a) Telecom Italia Finance S.A. notes

"Euro Notes": euro 2,745 million, 6.375%, maturing April 2006
euro 2,000 million 7.25%, maturing April 2011

These securities carry protection for investors which would be triggered by a change in the rating assigned to Telecom Italia to below the Baa1/BBB+ ratings (by Moody's and S&P's, respectively): each downgrade in the rating by one notch by each of the two rating agencies to below the stated thresholds would cause an increase in the coupon interest (or in the spread above the Euribor for floating-rate securities) by 0.25%, starting from the coupon subsequent to the downgrade in the rating.

The downgrade in the rating from the thresholds is evaluated at the end of each coupon period and, on the basis of this evaluation, the interest for the next coupon is fixed; therefore, changes in the ratings during the coupon interest period would have no impact on the coupon in progress at that particular time.

Nevertheless, the relative step-up/step-down will only be applied when the rating at the end of the coupon period is different from the rating at the end of the preceding coupon period.

By virtue of this mechanism, the original coupons for these securities, respectively 6.125% and 7%, were increased by 0.25% due to the rating of Baa2 assigned by Moody's in August 2003. In the case of the two securities, the increase was applied beginning from the coupon period which started in April 2004; accordingly, the coupon is equal to 6.375% for securities maturing in April 2006 and 7.25% for securities maturing in April 2011.

The ratings assigned to Telecom Italia on December 7, 2004 by the various agencies are the following:

Standard & Poor's: BBB+, stable outlook
Moody's: Baa2, stable outlook
Fitch IBCA: A-, negative outlook

(b) Telecom Italia Finance S.A. notes, Euro 1,500 million, 5.15%, maturing February 2009

These notes carry protection for investors which would be triggered by a downgrade in the minimum rating (among the ratings assigned by the various agencies, in this specific case, Baa2 by Moody's).

At the beginning of every coupon period, this minimum rating will be checked, and depending upon the rating, the coupon interest will fixed; once fixed, changes in the minimum rating during the coupon period will have no effect on the coupon to be paid, and will only have an impact when the next coupon interest rate is fixed (if the changes are still in effect).

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Starting from the initial level of the coupon at issue (5%), a 0.15% increase in interest was granted to investors definitively up to the maturity date, bringing the current coupon interest rate to 5.15%.

This current coupon can be further increased in relation to the level of the minimum rating:

- if at the time the coupon interest is fixed the minimum rating is Ba1/BB+ or below, the current coupon will be increased by 1.5%;
- if at the time the coupon interest is fixed the minimum rating is Baa3/BBB-, the current coupon will be increased by 0.5%;
- ratings higher than the minimum rating do not lead to increases in the current coupon.

Therefore, only future downgrades in the minimum rating could cause an increase in the current coupon; this coupon, instead, cannot be reduced because of upgrades in the rating.

(c) Telecom Italia Finance S.A. notes, euro 2,350 million, 6.575%, maturing July 2009

These securities carry protection for investors which would be triggered by a change in the minimum rating (among those assigned by the various agencies, in this specific case, Baa2 by Moody's).

At the beginning of every coupon period, this minimum rating will be checked and depending upon the rating, the coupon interest will be fixed; once fixed, changes in the minimum rating during the coupon period will have no effect on the coupon to be paid, and will only have an impact when the next coupon interest rate is fixed (if the changes are still in effect).

Starting from the initial level of coupon interest at issue (6.125%), the coupon that will effectively be paid will be increased in relation to the level of the minimum rating:

- if, at the time the coupon is fixed, the minimum rating is Ba1/BB+ or below, the original coupon will be increased by 1.95%;
- if, at the time the coupon interest is fixed, the minimum rating is Baa3/BBB-, the original coupon will be increased by 0.95%;
- if, at the time the coupon interest is fixed, the minimum rating is Baa2/BBB, the original coupon will be increased by 0.45%;
- if, at the time the coupon interest is fixed, the minimum rating is Baa1/BBB+, the original coupon will be increased by 0.15%;
- ratings higher than the minimum rating do not lead to increases in the original coupon.

Under this mechanism, since October 2000 (the date the mechanism was first introduced), the original coupon has been increased by 0.45% (reaching the current 6.575%).

Future upgrades/downgrades in the minimum rating could cause a reduction/increase in the coupon according to the mechanism described above.

(d) Telecom Italia Finance S.A. notes, euro 500 million Floating Rate Notes (3 month-Euribor + 1.3%) maturing March 2005

These notes can be extended at the discretion of the investor for successive periods of 21 months with the final maturity date not to extend beyond March 14, 2012.

In accordance with the terms and conditions of the notes, noteholders in possession of notes totaling euro 283,000 chose not to extend the notes (maturity on March 14, 2005).

For those, instead, that decided to extend the maturity date, for notes totaling euro 499,717,000, Telecom Italia Finance S.A. issued new notes on December 14, 2004 denominated "Telecom Italia Finance S.A. euro 499,717,000 Guaranteed Floating Rate Extendable Notes Due 2006" with a new maturity date of December 14, 2006.

These new notes carry the same characteristics as the previous notes but have a new ISIN Code and Common Code.

■ Convertible debentures

euro 5,592 million

Convertible debentures total euro 5,592 million and decreased by euro 1,720 million compared to December 31, 2003 (euro 7,312 million).

Details are as follows:

- bonds 2001-2010 issued by Telecom Italia S.p.A. (former Olivetti S.p.A.) for euro 2,386 million, net of 1,292,835 bonds for which the conversion into shares had already been requested at the date of December 31, 2004 with the consequent reduction in the quantity of bonds still convertible, with an contra-entry to a payable to future shareholders – the corresponding 609,625 ordinary shares were issued on January 14, 2005 – convertible into Telecom Italia S.p.A. shares, with an annual fixed-rate coupon of 1.5% with a premium on redemption equal to 118.37825% of the issue price, maturing in January 2010. These bonds thus result in a total debt of euro 2,825 million. The annual yield upon maturity is 3.5% and the conversion will be at a ratio of 0.471553 new Telecom Italia shares for each euro 1,000 bond held;

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- bonds 2000-2005 issued by Telecom Italia Finance S.A. (originally Olivetti Finance N.V.) for euro 708 million, redeemable in new Telecom Italia ordinary shares, with the right of the issuer to pay off the amount due in cash, with an annual fixed-rate coupon of 1% and a premium on redemption of 113.40616% of the issue price, maturing in November 2005. Those bonds, which, accordingly, result in a total debt of euro 803 million, are convertible into 169,928,259 shares (exercise price of approximately euro 4.1684). The annual yield upon maturity is 3.5% and the conversion will be at a ratio of 239.8991704 new Telecom Italia shares for each euro 1,000 bond held;
- bonds issued in March 2001 by Sogerim (merged in 2002 in Telecom Italia Finance S.A.) for euro 2,500 million, convertible into TIM or Seat Pagine Gialle shares, with the right of the issuer to pay off the amount due in cash, with an annual fixed-rate coupon of 1% and a premium on redemption of 117.69% of the issue price, maturing in March 2006. The spin-off transaction and the consequent disposal of the equity investment in the beneficiary company Nuova Seat Pagine Gialle, did not result in any changes in the terms of the bonds since their conditions allowed ample flexibility in the method of settlement. These are five-year bonds and the right to redemption before maturity at the end of the third year (March 2004) was exercised by the bondholders for euro 466,000. The bonds decreased by euro 536 million in September 2002 due to the purchase of own bonds by Telecom Italia Finance S.A. which were subsequently cancelled; the bonds are currently equal to euro 1,964 million. Such bonds are convertible into 180,453,860 TIM shares at an exercise price of about euro 10.88 or into 707,460,852 Seat Pagine Gialle shares at an exercise price of about euro 2.01 and into 125,606,848 TI Media shares at an exercise price of about euro 4.3. The annual yield upon maturity is 4.25% and the conversion will be in at a ratio of 91.879193537 TIM shares or 360.2080473 Seat Pagine Gialle shares and 63.953500 TI Media shares for each euro 1,000 bond held.

A summary of convertible bonds held by third parties issued by companies of the Telecom Italia Group, by issuer company, is presented below:

| Currency | Amount (in millions) | Coupon | Underlying shares | Issue date | Maturity date | Issue price (%) |
|--|-------------------------|--------|-------------------------------------|------------|---------------|--------------------|
| Convertible bonds issued by Telecom Italia S.p.A. | | | | | | |
| Euro | 2,825 | 1.50% | TI S.p.A. | 11/23/01 | 1/1/10 | 100 |
| Convertible bonds issued by Telecom Italia Finance S.A. and guaranteed by TI S.p.A. | | | | | | |
| Euro | 803 | 1.00% | TI S.p.A. | 11/3/00 | 11/3/05 | 100 |
| Euro | 1,964 | 1.00% | TIM/TI Media/ Seat Pagine Gialle | 3/15/01 | 3/15/06 | 100 |
| Total | 5,592 | | | | | |

Financial covenants / other covenant / other features

Securities summarized here do not contain either financial covenants or clauses that would force the early redemption of the notes in relation to events other than the solvency of Telecom Italia Group.

For example, there are no clauses that would cause the redemption of the notes if the ratings are downgraded to below the stated thresholds. The guarantees provided by Telecom Italia S.p.A. on notes issued by its foreign subsidiaries are all full and unconditional.

None of the transactions summarized here carry any other interest rate structures or structural complexities.

Since these notes have been placed principally with institutional investors on major world capital markets (Euromarket and the U.S.A.), the terms which regulate the notes are in line with the market practice for similar transactions effected on these same markets.

In particular, the notes issued by Telecom Italia Capital S.A. in October 2003, guaranteed by Telecom Italia, for an amount of USD 4,000 million, were covered by a covenant that required Telecom Italia Capital S.A. and Telecom Italia to effect a SEC-registered exchange offer in order to allow investors to exchange the originally purchased notes with listed and freely traded notes without restrictions. The offer was executed on October 14, 2004, in fulfillment of the covenant.

Moreover, the new notes issued by Telecom Italia Capital S.A. in October 2004, guaranteed by Telecom Italia, for an amount of USD 3,500 million, carry a similar covenant which requires Telecom Italia Capital S.A. and Telecom Italia to effect a SEC-registered exchange offer. In the event Telecom Italia Capital S.A. does not complete the registered exchange offer by October 31, 2005, this would call for an increase in the coupon by 0.50% until such time as the exchange offer is completed.

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- **Due to banks** **euro 1,830 million**
Due to banks, totaling euro 1,830 million (euro 2,460 million at December 31, 2003), are secured by collateral of euro 99 million, mainly referring to Maxitel.
Moreover, 2,883,959 Digitel shares held by TIM International are pledged to guarantee a credit facility granted to the company in 2002, whereas 1,337,542,451 TIM Perù shares held by TIM International are pledged to guarantee a loan granted to the company International Finance Corporation (IFC).
- **Due to other lenders** **euro 1,623 million**
Due to other lenders, totaling euro 1,623 million, increased by euro 611 million compared to December 31, 2003. This caption refers mainly to payables by:
– Telecom Italia, for euro 1,085 million, principally for derivative financial transactions with various banking institutions to hedge bonds and loans made by subsidiaries (euro 632 million), for short-term loans made by TI Securitization Vehicle S.r.l. from excess liquid resources generated by securitization transactions (euro 212 million), for loans made by Cassa Depositi e Prestiti (euro 140 million) and for loans made by the Fondo per l'innovazione tecnologica (euro 52 million);
– Telecom Italia Finance S.A. (originally Olivetti International Finance N.V.), for euro 143 million, for the loan due October 29, 2029 made by a Japanese investor and originally set up in the form of bonds. Telecom Italia put into place a CCIRS on this loan to cancel the Japanese yen/euro exchange and interest rate risk, after which the debt is equal to euro 174 million.
– Telecom Italia Capital S.A., for euro 262 million, for derivative financial transaction with various institutions to hedge bonds.
- **Advances** **euro 50 million**
Advances, totaling euro 50 million, decreased by euro 91 million compared to December 31, 2003.
- **Trade accounts payable** **euro 6,789 million**
Trade accounts payable, totaling euro 6,789 million, increased by euro 932 million compared to December 31, 2003. The increase is due to higher payables by the Mobile Business Unit which is partly offset by the reduction in the payables of the Parent Company and the IT Market Business Unit.
This item also includes euro 649 million of amounts due to other telecommunications operators.
It should be mentioned that the TIM group pledged Maxitel shares to guarantee the supply contract between Maxitel and Ericsson.
- **Accounts payable to unconsolidated subsidiaries** **euro 12 million**
Accounts payable to unconsolidated subsidiaries, totaling euro 12 million, decreased by euro 6 million compared to December 31, 2003. The balance includes financial payables of euro 3 million and trade accounts payable and other payables of euro 9 million.
- **Accounts payable to affiliated companies** **euro 293 million**
Accounts payable to affiliated companies, totaling euro 293 million, increased by euro 123 million compared to December 31, 2003. They include financial payables of euro 21 million (euro 15 million due to Teleleasing and euro 6 million due to Shared Service Center) and trade accounts payable and other payables of euro 272 million, mainly due to the Italtel group (euro 150 million), Siemens Informatica (euro 61 million) and Shared Service Center (euro 34 million).
- **Taxes payable** **euro 542 million**
Taxes payable, totaling 542 million, decreased by euro 934 million compared to December 31, 2003. Taxes payable include euro 59 million of income taxes payable, euro 483 million of payables for VAT, other indirect taxes and taxes withheld by the company as a substitute taxpayer.
- **Contributions to pensions and social security institutions** **euro 1,356 million**
Contributions to pensions and social security institutions, totaling euro 1,356 million, decreased by euro 158 million compared to December 31, 2003; they refer to amounts owed to social security and health institutions. This item includes euro 1,190 million payable to INPS for the remaining balance of employee benefit obligations estimated pursuant to Law No. 58/1992, of which euro 472 million was assessed for employees of the former IRI TEL and euro 718 million for the other employees of the Telecom Italia Group.
- **Other liabilities** **euro 2,860 million**
Other liabilities, totaling euro 2,860 million, decreased by euro 434 million compared to December 31, 2003. A breakdown is provided below:
- financial payables total euro 131 million (euro 519 million at December 31, 2003), of which euro 388 million relates to the close of the securities lending agreement carried out by Olivetti Finance, now Telecom Italia Finance (euro 300 million). They include euro 50 million for the residual liabilities of the Mobile Business Unit on the UMTS licenses in Greece and the GSM license in Brazil;

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- sundry liabilities total euro 2,729 million (euro 2,775 million at December 31, 2003). Details are as follows:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|---|--------------|--------------|-------------|
| Customer-related items | 1,577 | 1,672 | (95) |
| Employee-related items | 783 | 826 | (43) |
| Telecommunications license fee | 29 | 24 | 5 |
| Other recurring and miscellaneous items | 340 | 253 | 87 |
| Total | 2,729 | 2,775 | (46) |

In particular, customer-related items consist of deposits paid by customers, pre-billed basic subscriber charges, as well as prepaid traffic.

ACCRUED EXPENSES AND DEFERRED INCOME

euro 2,339 million

(euro 2,386 million at December 31, 2003)

A breakdown of accrued expenses and deferred income, which decreased by euro 47 million, is provided below:

| (in millions of euro) | 12/31/2004 | 12/31/2003 | Change |
|---|--------------|--------------|-------------|
| Issue premiums | 32 | 39 | (7) |
| Accrued expenses: | | | |
| • production costs | 20 | 15 | 5 |
| • financial | 1,338 | 1,279 | 59 |
| • other charges | 20 | 33 | (13) |
| | 1,378 | 1,327 | 51 |
| Deferred income | | | |
| • capital grants (unavailable amount) | 209 | 263 | (54) |
| • other costs relating to production value | 625 | 510 | 115 |
| • financial | 10 | 12 | (2) |
| • other | 85 | 235 | (150) |
| | 929 | 1,020 | (91) |
| Accrued expenses and deferred income | 2,307 | 2,347 | (40) |
| Total | 2,339 | 2,386 | (47) |

* * *

An analysis of liabilities and accrued expenses by maturity and type is provided in Annex 2.

Disclosure according to art. 2427, paragraph 6 of the Italian Civil Code in respect of the breakdown of liabilities by geographical area is presented in the attached Annex 3.

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■ MEMORANDUM ACCOUNTS

Memorandum accounts at December 31, 2004 total euro 5,453 million and increased, compared to December 31, 2003, by euro 3,871 million.

Memorandum accounts are detailed as follows:

| (in millions of euro) | 12/31/2004 | 12/31/2003 |
|---------------------------------|--------------|--------------|
| Guarantees provided | 951 | 1,155 |
| Collateral provided | 7 | 114 |
| Purchases and sales commitments | 4,387 | 208 |
| Other memorandum accounts | 108 | 105 |
| Total | 5,453 | 1,582 |

■ GUARANTEES PROVIDED

euro 951 million

Guarantees provided, net of counter-guarantees received of euro 435 million, total euro 951 million and mainly consist of sureties provided by Telecom Italia and TIM on behalf of affiliated companies (of which euro 454 million is in the interests of Avea I.H.A.S.) and on behalf of others for medium/long-term loan transactions and guarantees on telephone licenses issued abroad.

■ COLLATERAL PROVIDED

euro 7 million

Collateral provided amounts to euro 7 million (a reduction of euro 107 million compared to December 31, 2003. The reduction is mainly due to the removal of obligations deriving from the supply contracts signed between Is TIM and Ericsson and Siemens following the execution of the merger of Is TIM in Avea I.H.A.S.).

■ PURCHASES AND SALES COMMITMENTS

euro 4,387 million

Purchases and sales commitments at the end of the year, respectively, of euro 4,366 million and euro 21 million, refer to commitments, not yet fulfilled, which do not fall within the normal "operating cycle" of the Group. Commitments increased compared to 2003 due to the addition of 9- to 21-year building lease obligations under purchase commitments which had previously been included under other information..

In particular, purchases commitments refer mainly to:

- 9- to 21-year future lease obligations on buildings equal to euro 4,080 million;
- other future lease obligations, increased by the purchase option (euro 101 million);
- orders to Telenergia's suppliers (euro 134 million) relating to the agreement to supply electrical energy reached with the company Endesa Italia for the three-year period 2004-2006;
- options rights (euro 19 million) granted to Finsiel for the sale of the stock (30.20%) held in Value Team (former Webegg S.p.A.), which can be exercised between June 30, 2008 and March 31, 2009.

In December 2004, Telecom Italia reached a preliminary agreement with the minority shareholders of Med SA, Med Ltd and Med 1 to resolve certain conflicting situations referring to MED SA's and Telecom Italia's put, respectively, on 49% of Med Ltd and Med 1 shares, also to resolve the arbitration proceedings set into motion in Luxembourg by the Fishman group (FTT) aimed at the restitution of the sums paid to TII N.V. in 2000 for the purchase of 30% of MED SA;

The transactions negotiated, which call for the buyback of all the minority shares in Med Ltd and in Med 1, allow Telecom Italia to strengthen its presence in the IP services and "wholesale" data sector in the eastern Mediterranean area. At the same time, the non-strategic assets of certain local Israeli activities managed by the same Med 1 and Med Ltd will be sold to the counterpart. The transaction will be executed in 2005 after approval is received from the competent regulatory authorities and other conditions precedent have been met.

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■ OTHER MEMORANDUM ACCOUNTS

euro 108 million

Other memorandum accounts of euro 108 million refer mainly to third-party assets held by the individual consolidated companies, principally those in the information technology sector and the Olivetti Tecnost Group.

Furthermore:

- with regard to the merger of Is TIM and Aycell, the TIM Group is committed, up to December 31, 2006, to pay a maximum of USD 150 million for capital increases and to provide sureties up to a maximum of USD 150 million;
- the consolidated companies of the Group issued weak letters of patronage totaling euro 165 million chiefly on behalf of affiliated companies to guarantee insurance policies, lines of credit and overdraft arrangements;
- assets held by third parties on loan, on deposit for safekeeping or for similar purposes amount to euro 254 million and consist mainly of equipment leased to customers;
- collateral received amounts to euro 4 million, mainly for guarantees received by TIM (euro 2 million) and referring to supply contracts;
- guarantees received amount to euro 248 million, mainly for guarantees received by TIM (euro 199 million) and referring to supply contracts;
- guarantees provided by others for obligations of Group companies, which consist primarily of sureties to guarantee the proper performance of non-financial contractual obligations, total euro 1,162 million, of which euro 839 million refers to the Parent Company. They also comprise euro 207 million related to the surety policy issued by Fondiaria Assicurazioni S.p.A. in the interests of Agrisian on behalf of MIPAF – Ministry of Agriculture and Forest Policies;
- the value of the shares of employees and shareholders deposited at December 31, 2004 at the companies of the Group amount to approximately euro 233 million;

■ DERIVATIVE FINANCIAL INSTRUMENTS

Derivative financial instruments are used by the Telecom Italia Group to manage its exposure to foreign exchange rate and interest rate risks and to diversify the parameters of debt so that costs and volatility can be reduced to within prefixed operational limits.

Derivative financial instruments at December 31, 2004 are principally used by the Group for the management of its debt positions. They include interest rate swaps (IRS) and interest rate options (IRO) to reduce interest rate exposure on fixed-rate and floating-rate bank loans and bonds and cross currency and interest rate swaps (CCIRS) and currency forwards to convert loans secured in different foreign currencies to the functional currencies of the various companies of the Group.

IRSs and IROs, involve or can involve, at specified maturity dates, the exchange of flows of interest calculated on the notional amount at the agreed fixed or floating rates, with the counterparts.

The same also applies to CCIRSs which, in addition to the settlement of periodic interest flows, can involve the exchange of principal, in the respective currencies of denomination, at maturity and eventually at another date.

■ Foreign exchange risk

At December 31, 2004, the Telecom Italia Group companies had forward foreign exchange contracts and options outstanding for the purchase and sale of foreign currency at specified exchange rates for an equivalent amount of euro 872 million, of which:

| EUROPEAN COMPANIES | |
|--|-------------------------------------|
| Description | Notional amount in millions of euro |
| Transactions put into place by Telecom Italia Finance S.A. | 302 |
| Transactions put into place by Telecom Italia S.p.A. | 79 |
| Transactions put into place by TIM S.p.A. | 173 |
| Transactions put into place by Telecom Italia Media S.p.A. | 1 |
| Transactions put into place by Telecom Italia Sparkle S.p.A. | 6 |
| Transactions put into place by Olivetti Tecnost S.p.A. | 23 |
| Total european companies | 584 |

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LATIN AMERICAN COMPANIES

| Description | Equivalent notional amount in millions of euro |
|--|--|
| Currency forward transactions put into place by Entel Chile S.A. | 232 |
| Currency Forward transactions put into place by TIM Perù S.A.C. | 56 |
| Total latin american companies | 288 |

Given the limited core of the currency market on Latin American currencies, the contracts are often carried out for short terms and then renewed each time for successive maturity dates.

■ Interest rate risk

At December 31, 2004, the Telecom Italia Group companies had contracts relating to financial liabilities recorded in the financial statements, for total principal equal to an equivalent amount of euro 16,589 million. Details by European companies and Latin American companies are the following:

EUROPEAN COMPANIES

| Description | Notional amount in millions of euro |
|---|-------------------------------------|
| Floating to fixed IRS transactions put into place by Telecom Italia S.p.A. | 6 |
| Floating to floating IRS transactions put into place by Telecom Italia S.p.A. | 148 |
| CCIRS transactions put into place by Telecom Italia S.p.A. | 5,193 (*) |
| CCIRS transactions put into place by Telecom Italia Capital S.A. | 2,831 |
| IRS transactions put into place by Telecom Italia Finance S.A. maturing March 2005 on bonds of euro 500 million carried by Telecom Italia Finance S.A., originally issued by Olivetti Finance N.V. (2002-2005) and extended for euro 499.7 million to December 2006 | 500 |
| IRS transactions effected by Telecom Italia Finance S.A. maturing January 2006 on bonds of euro 1,100 million carried by Telecom Italia Finance S.A., originally issued by Olivetti Finance N.V. (2002-2006) | 1,100 |
| IRS transactions put into place by Telecom Italia Finance S.A. maturing April 2007 on bonds of euro 1,750 million carried by Telecom Italia Finance S.A., originally issued by Olivetti Finance N.V. (2002-2007) | 1,300 |
| IRS transactions put into place by Telecom Italia Finance S.A. maturing January 2008 on bonds of euro 1,750 million carried by Telecom Italia Finance S.A., originally issued by Olivetti Finance N.V. (2003-2008) | 1,300 |
| IRS transactions maturing February 2009 put into place by Telecom Italia Finance S.A. on bonds of euro 1,500 million carried by Telecom Italia Finance S.A., originally issued by Olivetti International Finance N.V. (1999-2009) | 500 |
| IRS transactions effected by Telecom Italia Finance S.A. maturing July 2009 on bonds of euro 2,350 million carried by Telecom Italia Finance S.A. originally issued by Olivetti International Finance N.V. (1999-2009) | 2,050 |
| IRS transactions effected by Telecom Italia Finance S.A. maturing April 2011 on bonds of euro 2,000 million carried by Telecom Italia Finance S.A., originally issued by Sogirim S.A. (2001-2011) | 400 |
| IRS transactions put into place by Telecom Italia Finance S.A. maturing April 2012 on bonds of euro 1,000 million carried by Telecom Italia Finance S.A., originally issued by Olivetti Finance N.V. (2002-2012) | 950 |
| IRS transactions put into place by Telecom Italia Finance S.A. maturing June 2046, on bonds of CHF 100 million (1986-2046) carried by Telecom Italia Finance S.A., originally issued by Olivetti International N.V. | 65 |
| Total | 16,343 |

(*) The protection structure is forfeit for euro 345 million in the event of the insolvency of Telecom Italia S.p.A.

The above-described transactions are analyzed below in addition to transactions that are largely terminated (because of certainty of all remaining financial flows), but not yet matured:

- The floating to fixed IRS transactions (4.71%) put into place by Telecom Italia S.p.A. for a notional amount of euro 6 million refer to EIB loans at floating rates.
- The floating to floating IRS transactions put into place by Telecom Italia S.p.A. for a notional amount of euro 148 million refer to indexed loans at domestic parameters (Rendint, Rolint, Robot) with conversion to the 6-month Euribor.
- CCIRS transactions put into place by Telecom Italia S.p.A. and amounting to euro 5,193 million refer to:
 - for *euro 3,409 million* with reference to the floating rate intragroup loan in USD, received from the subsidiary Telecom Italia Capital S.A. following the bonds issued in October 2003 for a total amount of USD 4,000 million, equivalent to euro 2,937 million at December 31, 2004, with conversion of the loan to:
 - quarterly floating rate in euro maturing November 2008 for euro 851 million;

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- semiannual average 5.04% fixed rate in euro maturing November 2013 for euro 1,707 million, of which euro 470 million through two distinct and linked transactions;
- semiannual 5.99% fixed rate in euro maturing November 2033 for euro 851 million.

Moreover, with regard to the fixed-rate bond issue of USD 4,000 million (euro 2,937 million at the euro/USD exchange rate at December 31, 2004), Telecom Italia Capital S.A. put IRS contracts into place to convert the semiannual fixed-rate coupon of 4% on USD 1,000 million maturing November 2008, of 5.25% on USD 2,000 million maturing November 2013, of 6.38% on USD 1,000 million maturing November 2033 to quarterly floating interest rates in USD.

- for *euro 174 million*, with reference to the "Dual Currency" loan with a notional principal of JPY 20 billion and a 5% fixed interest rate with a step-up of +0.45% in USD maturing October 2029, originally received by Olivetti International Finance N.V., equivalent to euro 143 million at December 31, 2004, now carried by Telecom Italia Finance S.A., the following was put into place:
 - by Telecom Italia Finance S.A., an IRS in which Telecom Italia Finance S.A. converts the 5.00% fixed rate in USD to the 6-month Libor in JPY;
 - by Telecom Italia S.p.A., a CCIRS in which Telecom Italia S.p.A., with regard to the infragroup loan in JPY, receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is forfeit in the event of the insolvency of Telecom Italia S.p.A.;
 - by Telecom Italia S.p.A., an IRS with the conversion of the semiannual floating rate in euro to a 6.94% fixed rate up to maturity.
- for *euro 171 million*, with reference to the bonds 2002/2032 in JPY 20 billion, with a 3.55% fixed rate coupon maturing May 2032 originally issued by Olivetti Finance N.V., equivalent to euro 143 million at December 31, 2004, the following was put into place:
 - by Telecom Italia Finance S.A. an IRS contract in which Telecom Italia Finance S.A. receives the semiannual coupon of 3.55% in JPY and pays a semiannual floating rate in JPY;
 - by Telecom Italia S.p.A., a CCIRS contract on a floating rate infragroup loan in JPY in which Telecom Italia S.p.A. receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is forfeit in the event of the insolvency of Telecom Italia S.p.A..
- for *euro 150 million*, CCIRSs linked to an EIB loan in USD, equivalent to euro 132 million at December 31, 2004, were put into place with conversion to a floating rate in euro.
- for *euro 1,289 million*, with regard to bonds 2004/2019 with an annual 6.375% fixed rate in GBP maturing June 2019, equivalent to euro 1,206 million at December 31, 2004, CCIRSs were put into place with three-year maturities with conversion to the 6-month Euribor rate.
- CCIRS transactions put into place by Telecom Italia Capital S.A. and amounting to euro 2,831 million refer to bonds issued in October 2004 for USD 3,500 million, equivalent to euro 2,570 million at December 31, 2004, with conversion to:
 - semiannual floating rate in euro for euro 1,014 million maturing January 2010;
 - semiannual floating rate in euro for euro 1,011 million maturing September 2014;
 - semiannual floating rate in euro for euro 806 million maturing September 2034;
- On the bonds 2002/2005 of euro 500 million at a quarterly floating rate maturing March 2005 issued by Telecom Italia Finance S.A. and extended for euro 499.7 million up to December 2006, the company Telecom Italia Finance S.A. put into place IRS contracts for a total of euro 500 million, in which Telecom Italia Finance S.A. receives a quarterly floating rate in euro and pays a quarterly 4.36% fixed rate.
- On the bonds 2002/2006 of euro 1,100 million at a quarterly floating rate maturing January 2006 issued by Telecom Italia Finance S.A., the company Telecom Italia Finance S.A. put into place:
 - an IRS contract for euro 900 million, in which Telecom Italia Finance S.A. receives a quarterly floating rate and pays a 2.68% fixed rate;
 - an IRS contract for euro 200 million, in which Telecom Italia Finance S.A. receives a quarterly floating rate of +1.25% and pays a 3.83% fixed rate.
- On the bonds 2002/2007 of euro 1,750 million with a 6.50% fixed-rate coupon, maturing April 2007, issued by Telecom Italia Finance S.A., the company Telecom Italia Finance S.A. put into place for euro 1,300 million:
 - an IRS contract for *euro 500 million*, in which the fixed rate is converted to a semiannual rate in SEK calculated on that notional amount in euro set in arrears with the further purchase of a cap at 3.75% and a knock-out at 5.30%;
 - an IRS contract for *euro 350 million*, in which the fixed rate is converted to a 6-month Libor in USD, calculated on that notional amount in euro, set in arrears and with the following additional transactions:
 - a) purchase of a cap with an increasing rate from 2.75% to 3.75% starting April 2005;
 - b) sale of a cap with an increasing rate from 3.75% to 4.75% starting April 2005;
 - c) sale of a cap with an increasing rate from 4.40% to 5.40% starting April 2005;
 - d) sale of a floor with an increasing rate from 2.50% to 3.50% and a knock-in at increasing rates from 2.25% to 3.25% starting April 2005.
 - an IRS contract for euro 450 million, in which the annual 6.50% fixed rate is converted to a 3-month Euribor.

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- On the bonds 2003/2008 of euro 1,750 million with a 5.875% fixed rate coupon maturing January 2008 issued by Telecom Italia Finance S.A., the company Telecom Italia Finance S.A. put into place, for euro 1,300 million:
 - an IRS contract for *euro 250 million*, in which the annual 5.875% fixed rate is converted to a semiannual floating rate in euro set in arrears semiannually with the following additional transactions:
 - a) purchase of a cap at 3.88% with a knock-out at increasing rates from 4.50% to 5.70% starting January 2005;
 - b) sale of a floor with an increasing rate from 2.62% to 3.52% starting January 2005.
 In the last two years, receipt of the annual fixed rate of 5.875% is applicable as long as the 10-year swap rates in GBP remain above 3.80%.
 - an IRS contract for *euro 500 million*, in which the annual 5.875% fixed rate is converted to an annual 4.24% fixed rate up to January 2005 and a 3-month Libor rate in USD from January 2005 up to maturity. In the last three years, receipt of the annual 5.875% fixed rate is applicable as long as the 10-year swap rates in USD remain below 6.50% and the 5-year rates in USD remain above 2.82%;
 - an IRS contract for *euro 350 million*, in which the annual 5.875% fixed rate is converted to an annual 4.24% fixed rate up to January 2005 and 5.23% from January 2005 up to maturity. In the last three years, the receipt of the annual 5.875% fixed rate is applicable as long as the difference between the 10-year swap rates in USD remains above 3.55% and the 5-year rates in USD remain between 2.95% and 5.66%;
 - an IRS contract for *euro 200 million*, in which the annual 5.875% fixed rate is converted to an annual 5.59% fixed rate up to January 2005 and a quarterly floating rate in USD, calculated on that notional amount in euro, from January 2005 up to maturity.
- On the bonds 1999/2009 of euro 1,500 million at a 5% fixed rate with a step-up of +0.15% maturing February 2009 carried by Telecom Italia Finance S.A., originally issued by Olivetti International N.V., Telecom Italia Finance S.A. put into place an IRS for euro 500 million, in which the annual fixed rate of 5% is converted to a quarterly fixed rate of 3.52% up to February 2005 and a quarterly fixed rate of 3.54% from February 2005 to February 2006. Starting February 2006, the fixed rate of 3.54% can be replaced by a quarterly floating rate in euro set in arrears if such rate is higher than 5.75%. Moreover, the flow to be received by Telecom Italia Finance S.A. in the last two years is applicable as long as the 5-year swap rates in euro remain above the 1-year swap rates in euro.
- On the bonds 1999/2009 (maturing July 2009) of euro 2,350 million at an annual 6.125% fixed rate with a step-up of +0.45% carried by Telecom Italia Finance S.A. (originally issued by Olivetti International Finance N.V.), the company Telecom Italia Finance S.A. put into place the following transactions, at the same maturity dates, for euro 2,050 million:
 - an IRS contract for *euro 900 million*, in which the annual 6.125% fixed rate is converted to a semiannual floating rate in euro;
 - an IRS contract for *euro 500 million*, in which the annual 6.125% fixed rate is converted to a semiannual floating rate in euro set in arrears with the further sale of a floor at 3.25% up to January 2005. From January 2005 up to maturity, the annual 6.125% fixed rate is converted to a floating rate in SEK, calculated on that notional amount in euro, set in arrears with the further purchase of a cap at 4.75% and a knock-out at 6.00%. Moreover, the flow to be received by Telecom Italia Finance S.A. in the last three years is applicable as long as the 5-year swap rates in euro remain above the 1-year swap rates in euro;
 - an IRS contract for *euro 650 million*, in which the annual 6.125% fixed rate is converted to an annual 5.73% fixed rate through the following additional transactions:
 - a) sale of a cap at 7.25% on the semiannual floating rate in USD set in arrears starting July 2007, calculated on the above-mentioned notional amount in euro;
 - b) sale of a floor on the semiannual floating rate in USD set in arrears starting January 2006, calculated on the above-mentioned notional amount in euro, and with an increasing rate from 2.40% to 3.25%. Up to January 2006, furthermore, the floor is subject to a knock-in with increasing rates from 2.00% to 2.60%.
- On the bonds 2001/2011 of euro 2,000 million with a 7% fixed rate maturing April 2011 issued by Telecom Italia Finance S.A., the company Telecom Italia Finance S.A. put into place the following transactions for euro 400 million:
 - an IRS contract for *euro 300 million*, in which the annual 7% fixed rate is converted to a quarterly floating rate in euro and with the following additional transactions:
 - a) purchase of a cap at 4.62%;
 - b) sale of a cap at 5.75%;
 - c) sale of a floor with an increasing strikes from 2.45% to 3.75% and a knock-in at increasing rates from 1.95% to 3.35% starting July 2005;
 - an IRS contract for *euro 100 million* in which the annual 7% fixed rate is converted to a semiannual floating rate.
- On the bonds 2002/2012 of euro 1,000 million with a 7.25% fixed rate maturing April 2012 issued by Telecom Italia Finance S.A., the company Telecom Italia Finance S.A. put into place the following transactions for euro 950 million:
 - an IRS contract for *euro 300 million* in which Telecom Italia Finance S.A. receives an annual 7.25% fixed rate (from April 2008, the receipt of the annual fixed rate is applicable as long as the 10-year swap rate remains above the 2-year swap rate) and pays a quarterly 6.06% fixed

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rate up to April 2005 and a 5.94% fixed rate from April 2005 to April 2008. Starting from April 2005, the 5.94% fixed rate can be replaced by a quarterly floating rate in euro if such rate is higher than 6.25%;

- an IRS contract for *euro 150 million* in which Telecom Italia Finance S.A. receives an annual 7.25% fixed rate and pays a quarterly fixed rate up to October 2005 and, successively, a semiannual variable rate in JPY calculated on the notional amount in euro, set in arrears with the further purchase of a cap at 2% and a knock-out at 3.50%;
 - an IRS contract for *euro 200 million*, in which Telecom Italia Finance S.A. receives an annual 7.25% fixed rate and pays a semiannual 7.49% fixed rate less the change, measured at the beginning and end of each semiannual period of reference, in the 5-year swap rate in forward euro at October 24, 2012;
 - an IRS contract for *euro 200 million*, in which Telecom Italia Finance S.A. receives an annual 7.25% fixed rate and pays a semiannual 7.48% fixed rate less the change, measured at the beginning and end of each semiannual period of reference, in the 10-year swap rate in forward euro at October 24, 2012;
 - an IRS contract for *euro 100 million*, in which Telecom Italia Finance S.A. receives an annual 7.25% fixed rate and pays a semiannual 7.43% fixed rate less the change, measured at the beginning and end of each semiannual period of reference, in the 30-year swap rate in forward euro at October 24, 2012.
- On the bonds 1986/2046 of CHF 100 million (equivalent to euro 65 million at December 31, 2004) at a 5.625% fixed rate maturing June 2046 carried by Telecom Italia Finance S.A., originally issued by Olivetti International N.V., the company Telecom Italia Finance S.A. put an IRS contract into place with the same amount and maturity date by which the annual fixed rate is converted to a semiannual floating rate in CHF.

LATIN AMERICAN COUNTRIES

| Description | Equivalent notional amount in millions of euro |
|---|--|
| CCIRS transactions put into place by TIM Participacoes S.A. | 11 |
| CCIRS transactions put into place by TIM Celular S.A. | 163 |
| CCIRS transactions put into place by Maxitel S.A. | 21 |
| IRS transactions put into place by Entel Chile S.A. | 33 |
| IRO transactions put into place by Entel Chile S.A. | 18 |
| Total Latin American Companies | 246 |

In addition to the derivative financial instruments covering debt, at December 31, 2004, the Luxembourg subsidiary Telecom Italia Finance S.A. put into place IRSs and Currency Forwards on financial assets for approx. euro 125 million.

Consistently with the accounting principles disclosed previously, the negative difference, if any, on the valuation of the above detailed derivative financial instruments at fair value, is recognized in the statement of income under financial expenses.

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■ CONSOLIDATED STATEMENTS OF INCOME

■ PRODUCTION VALUE

euro 32,282 million

(euro 31,926 million in 2003)

Production value increased by euro 356 million (+1.11% compared to 2003) and includes the captions below.

■ Sales and service revenues

euro 31,237 million

Sales and service revenues amount to euro 31,237 million and increased by euro 387 million compared to 2003 (+1.3 % compared to 2003). This increase is essentially due to the positive trend of mobile and wireline telephone services (euro 1,469 million), countered by the change in the scope of consolidation (euro 895 million) mainly as a result of the spin-off and sale of Nuova Seat Pagine Gialle, effective August 1, 2003 (euro 703 million). Revenues were also impacted by the reduction in the revenues of the IT Market Business Unit (-122 million, mainly as a result of the termination of the Telcal project), the Olivetti Tecnost Business Unit (-euro 93 million) and the wireline and integrated companies in Latin America (-euro 34 million).

A breakdown by Business Unit is presented below:

| (in millions of euro) | Wireline | Mobile | South America | Internet and Media | Olivetti-Tecnost | IT Market | IT Gruppo | Sub-total | Other activities and eliminations | Consolidated Group revenues |
|-----------------------|---------------|---------------|---------------|--------------------|------------------|------------|--------------|---------------|-----------------------------------|-----------------------------|
| Third parties | 15,761 | 12,634 | 1,068 | 404 | 544 | 682 | 22 | 31,115 | 122 | 31,237 |
| Intragroup | 1,810 | 266 | 8 | 193 | 57 | 47 | 943 | 3,324 | (3,324) | - |
| 2004 | 17,571 | 12,900 | 1,076 | 597 | 601 | 729 | 965 | 34,439 | (3,202) | 31,237 |
| Third parties | 15,364 | 11,562 | 1,102 | 1,122 | 637 | 804 | 41 | 30,632 | 218 | 30,850 |
| Intragroup | 1,852 | 220 | 9 | 175 | 18 | 87 | 1,059 | 3,420 | (3,420) | - |
| 2003 | 17,216 | 11,782 | 1,111 | 1,297 | 655 | 891 | 1,100 | 34,052 | (3,202) | 30,850 |

Revenues from telecommunications services are shown gross of the amount due to other operators of euro 4,623 million (euro 4,534 million in 2003).

A breakdown of revenues by customers' geographical locations is as follows:

| Geographical area (in millions of euro) | 2004 | | 2003 | |
|--|---------------|---------------|---------------|---------------|
| Italy | 24,608 | 78.8% | 24,811 | 80.5% |
| Rest of Europe | 2,588 | 8.3% | 2,478 | 8.0% |
| North America | 537 | 1.7% | 589 | 1.9% |
| Central and South America | 3,118 | 10.0% | 2,566 | 8.3% |
| Australia, Africa and Asia | 386 | 1.2% | 406 | 1.3% |
| Total | 31,237 | 100.0% | 30,850 | 100.0% |

■ Other revenue and income

euro 315 million

Other revenue and income amount to euro 315 million (euro 345 million in 2003) and include the following:

| (in millions of euro) | 2004 | 2003 | Change |
|---|------------|------------|-------------|
| - operating grants | 12 | 14 | (2) |
| - gains on disposal of intangibles and fixed assets | 8 | 11 | (3) |
| - portion of capital grants/grants for installations recorded in income | 53 | 64 | (11) |
| - other income | 242 | 256 | (14) |
| Total | 315 | 345 | (30) |

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In particular:

- operating grants, for the most part, refer to the amounts bestowed by public institutions to defray the costs incurred for research, development and technological innovation;
- the portion of capital grants/grants for installations recorded in income recorded in income represents the portion that became available during the year;
- other income from ordinary operations mainly includes charges to customers by the telecommunications services companies for the late payment of telephone bills (euro 85 million compared to euro 91 million in 2003).

PRODUCTION COSTS

(euro 25,137 million in 2003)

euro 25,082 million

Production costs decreased by euro 55 million compared to 2003 (-0.2% compared to 2003) and includes the following captions.

■ Raw materials, supplies and merchandise/Semifinished and finished goods **euro 2,414 million**

Raw materials, supplies and merchandise amount to euro 2,336 million (euro 1,973 million in 2003) and semifinished and finished goods total euro 78 million (euro 108 million in 2003). These costs, which principally represent purchases of raw materials and other goods to be used in operations, increased in total by euro 333 million, mainly on account of the mobile and wireline promotional campaign during the Christmas season. Specifically, euro 240 million of the increase refers to purchases of telephone equipment, mainly the Aladino cordless phone and videotelephones, primarily by Telecom Italia.

■ Services/Use of property not owned **euro 10,944 million**

Service costs total euro 9,857 million (euro 9,684 in 2003) and the cost for the use of property not owned amounts to euro 1,087 million (euro 1,156 million in 2003). Overall, these two items increased by 104 million, principally due to the increase in the costs for the operation and development of mobile telecommunications services (euro 98 million), wireline telecommunications (euro 145 million) and higher costs of the other Group companies (euro 133 million). These were partly compensated by the absence of costs for the purchase of satellite capacity by Telecom Italia (euro 54 million) and the change in the scope of consolidation due to the sale of Nuova Seat Pagine Gialle (euro 218 million).

■ Personnel costs **euro 4,045 million**

Personnel costs amount to euro 4,045 million (euro 4,303 million in 2003), including euro 3,011 million to companies which provide telecommunications services.

The decrease is due to the change in the scope of consolidation and the reduction in the average number of employees of the Parent Company. At December 31, 2004, employees of the Group number 91,365 (93,187 at December 31, 2003). This is a reduction of 1,822 persons, owing to an increase of 290 persons due to turnover and a decrease of 2,112 caused by the change in the scope of consolidation.

A breakdown of employees by business segment is presented as follows:

| | 12/31/2004 | 12/31/2003 | Change |
|--------------------|---------------|---------------|----------------|
| Wireline | 50,383 | 50,766 | (383) |
| Mobile | 20,361 | 18,888 | 1,473 |
| South America | 5,080 | 4,953 | 127 |
| Internet and Media | 1,805 | 2,029 | (224) |
| Olivetti-Tecnost | 2,108 | 2,395 | (287) |
| IT Market | 4,131 | 4,827 | (696) |
| IT Group | 3,160 | 4,107 | (947) |
| Other activities | 4,337 | 5,222 | (885) |
| Total | 91,365 | 93,187 | (1,822) |

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The breakdown of employees by geographical area is as follows:

| | Executives | Middle management | Clerical staff | Technicians | 12/31/2004 | 12/31/2003 |
|----------------------------|--------------|-------------------|----------------|-------------|---------------|---------------|
| Italy | 1,616 | 4,805 | 67,762 | 851 | 75,034 | 78,069 |
| Rest of Europe | 49 | 361 | 2,216 | 1 | 2,627 | 2,294 |
| North America | 11 | 37 | 95 | 2 | 145 | 261 |
| Central and South America | 123 | 771 | 12,589 | 27 | 13,510 | 12,512 |
| Australia, Africa and Asia | 4 | 25 | 20 | - | 49 | 51 |
| Total | 1,803 | 5,999 | 82,682 | 881 | 91,365 | 93,187 |

The equivalent average number of salaried employees in 2004 was 88,892 (95,804 in 2003).

A breakdown by category follows:

| | 2004 | 2003 |
|-------------------|---------------|---------------|
| Executives | 1,906 | 2,156 |
| Middle management | 6,055 | 6,210 |
| Clerical staff | 79,987 | 83,035 |
| Technicians | 944 | 4,403 |
| Total | 88,892 | 95,804 |

■ Amortization, depreciation and writedowns

euro 6,926 million

Amortization, depreciation and writedowns amount to euro 6,926 million (euro 7,256 million in 2003) and decreased by euro 330 million. Details are as follows:

- the amortization of intangible assets amounts to euro 3,116 million (euro 3,109 in 2003), with an increase of euro 7 million. The reduction in the amortization charge of differences on consolidation of euro 276 million, essentially in connection with the sale of Nuova Seat Pagine Gialle and the writedowns made in 2003, compensate the higher amortization charge for other intangible assets, principally in respect of the amortization of TIM's UMTS license (euro 134 million);
- the depreciation of fixed assets amounts to euro 3,530 million, compared to euro 3,670 million in 2003, with a decrease of euro 140 million. A breakdown of depreciation expense by asset category is provided below:

| (in millions of euro) | 2004 | 2003 | Change |
|--|--------------|--------------|--------------|
| Non-industrial and industrial buildings | 109 | 121 | (12) |
| Plant and machinery | 3,142 | 3,255 | (113) |
| Manufacturing and distribution equipment | 28 | 31 | (3) |
| Other fixed assets | 251 | 263 | (12) |
| Total | 3,530 | 3,670 | (140) |

- other writedowns of intangibles and fixed assets total euro 5 million (euro 6 million in 2003);
- writedowns of receivables included in current assets and liquid assets amount to euro 275 million (euro 471 million in 2003) and decreased by euro 196 million. The writedowns refer to the adjustment made to bring receivables in line with estimated realizable value, especially with reference to Telecom Italia (euro 101 million), the Entel Chile group (euro 56 million), TIM (euro 42 million), the foreign mobile telephone companies (euro 26 million) and Telecom Italia Sparkle (euro 27 million).

■ Provisions for risks and other provisions

euro 81 million

Provisions for risks and other provisions total euro 81 million (euro 94 million in 2003) and consist of provisions made during the year to the reserves for contractual risks and other risks and the reserve for pending litigation.

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■ Miscellaneous operating costs

euro 709 million

Miscellaneous operating costs amount to euro 709 million compared to euro 523 million in 2003. They refer to the following:

| (in millions of euro) | 2004 | 2003 | Change |
|---|------------|------------|------------|
| TLC operating fees | 126 | 84 | 42 |
| Losses on disposal of intangibles and fixed assets | 23 | 18 | 5 |
| Expenses connected with receivables management | 141 | 91 | 50 |
| Indirect duties and annual taxes, including the local property tax (I.C.I.) | 145 | 128 | 17 |
| Association due and membership fees and other costs | 274 | 202 | 72 |
| Total | 709 | 523 | 186 |

The increase in "expenses connected with receivables management" of euro 50 million is basically due to Telecom Italia for expenses connected with the management of relations with the other telephone operators (euro 33 million).

FINANCIAL INCOME AND EXPENSE

– euro 1,835 million

(– euro 2,154 million in 2003)

Financial income and expense refers to the following items:

| (in millions of euro) | 2004 | 2003 | Change |
|--------------------------------------|----------------|----------------|------------|
| Income from equity investments | 116 | 17 | 99 |
| Other financial income | 821 | 816 | 5 |
| Interest and other financial expense | (2,728) | (2,960) | 232 |
| Foreign exchange gains and losses | (44) | (27) | (17) |
| Total | (1,835) | (2,154) | 319 |

■ Income from equity investments

euro 116 million

Income from equity investments totals euro 116 million (euro 17 million in 2003). In particular, this caption includes euro 62 million of gains on the sale of the residual stake held in Telekom Austria in January 2004 and euro 24 million for the release of the residual portion of the gain on the sale of Mobikom Austria to the same Telekom Austria in 2002. Dividends on TIM shares posted in current assets (euro 10 million) are also included here.

■ Other financial income

euro 821 million

Other financial income of euro 821 million (euro 816 million in 2003), includes the following:

| (in millions of euro) | 2004 | 2003 | Change |
|--|------------|------------|----------|
| Interest and capital gains on securities | 53 | 174 | (121) |
| Interest and fees from: | | | |
| - unconsolidated subsidiaries | - | 1 | |
| - affiliated companies | 4 | 23 | |
| - banks | 149 | 192 | (63) |
| Income on derivative financial instruments | 518 | 278 | 240 |
| Other | 97 | 148 | (51) |
| Total | 821 | 816 | 5 |

Other financial income includes euro 32 million (euro 64 million in 2003) of income from the application of inflation accounting principles.

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■ Interest and other financial expense

euro 2,728 million

Interest and other financial expense amounts to euro 2,728 million (euro 2,960 million in 2003) and includes the following:

| (in millions of euro) | 2004 | 2003 | Change |
|--|--------------|--------------|--------------|
| Interest and fees paid to: | | | |
| - affiliated companies | 2 | 11 | |
| - banks | 86 | 254 | |
| - suppliers and other lenders | 31 | 56 | 321 |
| Interest and other charges on note issues | 1,939 | 1,852 | (202) |
| Expenses on derivative financial instruments | 413 | 216 | 197 |
| Other financial expenses | 257 | 571 | (314) |
| Total | 2,728 | 2,960 | (232) |

Other financial expense comprises euro 1 million (euro 11 million in 2003) of expenses from the application of inflation accounting principles.

The decrease in financial expense can mainly be ascribed to the absence of expenses in connection with the put/call options with JP Morgan for Seat Pagine Gialle shares (euro 236 million) and the fees incurred for the credit lines allocated to the Olivetti and Telecom Italia merger (euro 98 million).

The improvement is partly offset by the increase in other expenses not directly correlated to debt exposure.

■ Foreign exchange gains and losses

– euro 44 million

Foreign exchange gains and losses show a net loss of 44 million (a net loss of euro 27 million in 2003). Details are as follows:

| (in millions of euro) | 2004 |
|--------------------------------|--------------|
| Foreign exchange gains | |
| - from amounts realized | 304 |
| - from adjustments | 140 |
| Total | (A) 444 |
| Foreign exchange losses | |
| - from amounts realized | 400 |
| - from adjustments | 88 |
| Total | (B) 488 |
| Total | (A - B) (44) |

VALUE ADJUSTMENTS TO FINANCIAL ASSETS

euro 1 million

(– euro 110 million in 2003)

These include:

| (in millions of euro) | 2004 | 2003 | Change |
|---|-------------|--------------|------------|
| Upward adjustments of: | | | |
| - equity investments | 81 | 65 | 16 |
| - securities, other than equity investments, included in current assets | 11 | 3 | 8 |
| | 92 | 68 | 24 |
| Writedowns of: | | | |
| - equity investments | (80) | (154) | 74 |
| - long-term investments, other than equity investments | (11) | (5) | (6) |
| - securities included in current assets other than equity investments | - | (19) | 19 |
| | (91) | (178) | 87 |
| Total | 1 | (110) | 111 |

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Value adjustments to financial assets amount to a net income balance of euro 1 million. They refer to:

- amortization of goodwill arising at the time of the purchase of the equity investments in companies accounted for using the equity method, equal to euro 12 million (euro 13 million in 2003);
- upward adjustments of securities and equity investments included in current assets of euro 42 million (euro 4 million in 2003) and writedowns of long-term securities of euro 11 million (euro 5 million in 2003), with an improvement due to the writeback of euro 32 million (euro 2 million in 2003) to mark-to-market TIM shares in current assets at the beginning of December 2004;
- the Group's share of the equity in the earnings and losses of the unconsolidated companies accounted for using the equity method amounts to a loss of euro 18 million (euro 78 million in 2003). The decrease of euro 60 million refers mostly to Sky Italia (loss of euro 96 million in 2003) and Etec. S.a. Cuba (earnings of euro 33 million in 2003).

EXTRAORDINARY INCOME AND EXPENSE

– euro 410 million

(– euro 1,083 million in 2003)

Extraordinary income and expense shows a net expense balance of euro 410 million (a net expense balance of euro 1,083 million in 2003) which includes euro 1,177 million of income and euro 1,587 million of expense.

■ Extraordinary income of euro 1,177 million comprises:

- euro 190 million relating to gains on the disposals of equity investments, fixed assets and business segments (euro 105 million in 2003) which include euro 24 million from the sale of the entire stake held in Mirror International Holding Sarl as well as euro 61 million relating to the release of the remaining part of the gain on the sale, in 2001, of 70% of Mirror International Holding, the company to which the investments in satellite consortia had previously been sold;
- euro 621 million of prior period income relating to the TLC license fee (euro 1,465 million in 2003 relating to the non-existence of liabilities and reserves for the TLC license fee);
- euro 366 million of prior period income and other extraordinary income, of which euro 177 million is for the release of the reserves for risks, of which euro 109 million was set aside for the Brazilian subsidiary TIM Celular and euro 189 million for prior period income and other extraordinary income (euro 281 million in 2003, of which euro 131 million had been for prior period income arising from the recovery of accrued pre-amortization interest on expenses subject to Law 58/1992).

■ Extraordinary expense of euro 1,587 million comprises:

- euro 282 million relating to the settlement with De Agostini, which ended with the purchase of 40% of Webfin for euro 325 million (of which euro 287 million refers to the price and euro 38 million to the reimbursement of expenses incurred by De Agostini Invest to cover the losses and recapitalize Webfin starting from July 2001) compared to a value established by independent valuers of euro 43 million;
- euro 182 million (euro 273 million in 2003) of expenses and provisions for employee cutbacks and layoffs (of which euro 146 million is borne by the Parent Company, euro 196 million in 2003);
- euro 169 million (euro 406 million in 2003) to write down the differences on consolidation relating to consolidated companies: euro 162 million for Entel Chile following the decision to dispose of the subsidiary and euro 7 million for the South American mobile telephone company Blah! to downsize operations. In 2003, the writedowns of the differences on consolidation had included euro 195 million for Entel Chile, euro 132 million for Digitel Corporation, euro 42 million for EPIClink and euro 37 million for other minor companies;
- euro 158 million for the reorganization of the investments held by the Telecom Italia Group in the Mediterranean Nautilus group and in the Med 1 group, after reaching a preliminary agreement in December 2004 with the minority shareholders of Med SA, Med Ltd and Med 1 to resolve certain conflicting situations referring to MED SA's and Telecom Italia's put, respectively, on 49% of Med Ltd and Med 1 shares, also to resolve the arbitration proceedings set into motion in Luxembourg by the Fishman group (FTT) aimed at the restitution of the sums paid to the Telecom Italia Group in 2000 for the purchase of 30% of MED SA..

The transactions negotiated, which call for the buyback of all the minority shares in Med Ltd and in Med 1, allow Telecom Italia to strengthen its presence in the IP services and "wholesale" data sector in the eastern Mediterranean area;

- euro 152 million relating to provisions to reserves for extraordinary risks for the sanction levied on the Parent Company by the Antitrust Authority for the alleged abuse of a dominant position;
- euro 100 million (euro 295 million in 2003) for provisions and writedowns of fixed assets and intangibles, made by the Latin American Nautilus group (euro 56 million) under reorganization programs, by the Entel Chile group (euro 11 million) and by other minor companies (euro 33 million). In 2003, the provisions and writedowns of fixed assets and intangibles had been booked by the Latin American Nautilus group (euro 235 million), by Telecom Italia Learning Service (euro 27 million), by EPIClink (euro 15 million) and by other minor companies (euro 18 million);

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- euro 66 million for expenses under ex Law 58/1992 to cover employees under the former "Telephone Employees Pension Fund" (FPT) (euro 387 million in 2003, inclusive of euro 315 million for the recalculation of the debt in view of the progress on the dispute with INPS);
- euro 27 million for the provision to adjust the investment in Finsiel to its estimated sales value;
- euro 451 million for other extraordinary expenses and prior period expenses. Details are as follows:
 - euro 121 million to writeoff prior years' receivables balances carried out by the Parent Company and other Group companies;
 - euro 42 million of expenses connected with the cash tender offer for TIM shares and the announced merger of TIM and the Parent Company Telecom Italia;
 - euro 37 million of expenses booked by the Parent Company for damages caused to the company's assets as a result of natural events or brought about by third parties (euro 33 million in 2003);
 - euro 31 million of prior years' indirect duties and taxes (euro 48 million in 2003, inclusive of the portion of the cost of the tax amnesty not covered by the reserve for income taxes);
 - euro 27 million for the Parent Company's booking of liabilities relating to prior years, principally in respect of matters concerning interconnection (euro 35 million in 2003);
 - euro 19 million relating to provisions for corporate-related transactions;
 - euro 16 million for losses on the sale of intangibles, fixed assets and long-term investments (euro 42 million in 2003);
 - euro 2 million (euro 139 million in 2003) for provisions for risks and charges on equity investments. In 2003, the provisions for risks and charges on equity investments had included euro 59 million relating to the Digitel dispute and euro 30 million to expenses to be paid to Mirror in reference to the lower price on the sale of Inmarsat compared to the reference value used in 2001 when Inmarsat was transferred by Telecom Italia to Mirror;
 - euro 156 million of prior period expenses and other extraordinary expenses (euro 238 million in 2003).

Extraordinary expenses in 2003 had included, in addition to the above:

- losses and expenses relating to the spin-off and sale of Nuova Seat Pagine Gialle (euro 269 million) and the writedown of the differences on consolidation of TI Media (euro 348 million);
- expenses referring to the Telecom Italia and Olivetti merger (euro 118 million) and the settlement with Pagine Italia (euro 55 million).

■ INCOME TAXES, CURRENT AND DEFERRED

euro 3,054 million

(euro 1,014 million in 2003)

Income taxes of euro 3,054 million include current taxes for euro 1,579 million and the credit balance of deferred tax benefits of euro 1,475 million.

The higher taxes of euro 2,040 million are principally due to a better result, of which euro 230 million of taxes relates to the prior period income recorded as a result of the cancellation of the TLC license fee (euro 621 million) and the fact that non-recurring deferred tax assets had been booked in 2003 (euro 1,266 million).

The reconciliation between the nominal tax rate of the Group, equal to 33% for income taxes for year, and the effective tax rate is presented in the following table:

| (in millions of euro) | | % |
|---|--------------|------------|
| Income before taxes | 4,956 | |
| Theoretical taxes at 33% | 1,635 | 33% |
| • Tax losses for the year not considered recoverable | 168 | 4% |
| • Tax losses not considered recoverable in previous years and recovered during the year | (15) | (1%) |
| • Deferred tax benefits not set aside in prior years and considered recoverable during the year | (170) | (3%) |
| • Amortization of goodwill | 472 | 9% |
| • Permanent differences: | | |
| - Non-deductible costs | 290 | 6% |
| - Non-taxable earnings and losses of foreign companies not carried forward | 39 | 1% |
| - Other net differences | (105) | (2%) |
| | 2,314 | 47% |
| • IRAP and other taxes calculated on a basis other than taxable income | 740 | 15% |
| Effective taxes booked to statement of income | 3,054 | 62% |

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■ Remuneration to Directors and Statutory Auditors

Total remuneration to which the Directors, Statutory Auditors and General Managers of "Telecom Italia pre-merger", and Olivetti and Telecom Italia post-merger, were entitled for fiscal 2004, for the posts held during the course of the year, even for a part of the year, and for the posts of Directors, Statutory Auditors and General Managers held in companies included in the scope of consolidation, amount to euro 226,000 for the Directors and euro 113,000 for the Statutory Auditors.

■ EXCHANGE RATES USED TO TRANSLATE FOREIGN CURRENCY FINANCIAL STATEMENTS

| (currency/euro) | Exchange rates at year-end Balance sheet | | | Average exchange rates during the year Statement of income | | |
|-------------------------|---|-------------|-----------|---|-------------|-----------|
| | 12.31.2004 | 12.31.2003 | Changes % | 2004 | 2003 | Changes % |
| Europe | | | | | | |
| Romanian leu | 0.000025387 | 0.000024297 | 4.49 | 0.000024686 | 0.000024297 | 1.60 |
| Pound sterling | 1.418339125 | 1.418842225 | -0.04 | 1.473470170 | 1.445065823 | 1.97 |
| Turkish Lira | 0.000000547 | 0.000000573 | -4.54 | 0.000000566 | 0.000000573 | -1.22 |
| Hungarian forint | 0.004065536 | 0.003809524 | 6.72 | 0.003973677 | 0.003943411 | 0.77 |
| Russian Rouble | 0.026494425 | 0.027082796 | -2.17 | 0.027917482 | 0.027082796 | 3.08 |
| Polish zloty | 0.244828008 | 0.21267998 | 15.12 | 0.220908553 | 0.227321291 | -2.82 |
| Swiss Franc | 0.648130145 | 0.641889723 | 0.97 | 0.647743908 | 0.657388721 | -1.47 |
| Swedish krona | 0.110857371 | 0.110132159 | 0.66 | 0.109596848 | 0.109598650 | 0.00 |
| North of America | | | | | | |
| USA dollar | 0.734160488 | 0.791765637 | -7.28 | 0.803923145 | 0.884102945 | -9.07 |
| South of America | | | | | | |
| Venezuelan bolivar | 0.000382375 | 0.000494854 | -22.73 | 0.000430721 | 0.000494854 | -12.96 |
| Bolivian boliviano | 0.091518354 | 0.101566975 | -9.89 | 0.101429651 | 0.115416399 | -12.12 |
| Costarica Colon | 0.001602621 | 0.001893406 | -15.36 | 0.001835601 | 0.002218858 | -17.27 |
| Peruvian Nuevo sol | 0.223693129 | 0.228339175 | -2.03 | 0.235640093 | 0.254169007 | -7.29 |
| Argentinean Peso | 0.246445030 | 0.270227180 | -8.80 | 0.273243455 | 0.299695509 | -8.83 |
| Chilean Peso | 0.001316880 | 0.001336539 | -1.47 | 0.001319383 | 0.001280799 | 3.01 |
| Colombian Peso | 0.000312409 | 0.000284941 | 9.64 | 0.000306344 | 0.000307495 | -0.37 |
| Brazilian Real | 0.276582328 | 0.274043178 | 0.93 | 0.274776607 | 0.287837706 | -4.54 |
| Mexican Peso | 0.065879451 | 0.070523354 | -6.58 | 0.071241004 | 0.081940817 | -13.06 |
| Asia | | | | | | |
| Hong Kong dollar | 0.094445651 | 0.101989821 | -7.40 | 0.103219307 | 0.113540628 | -9.09 |
| Israeli Shekel | 0.170141524 | 0.180974839 | -5.99 | 0.179628349 | 0.194683960 | -7.73 |
| Japanese Yen | 0.007160759 | 0.007044665 | -3.29 | 0.007438009 | 0.007634808 | -2.58 |
| Singapore dollar | 0.449195939 | 0.466200466 | -3.65 | 0.475836997 | 0.50752662 | -6.24 |
| Africa | | | | | | |
| South African rand | 0.130044085 | 0.120082617 | 8.30 | 0.124856415 | 0.117238655 | 6.50 |

Moreover, pursuant to the provisions of the Italian Civil Code, there were no significant changes in the consolidated economic and financial figures as a result of changes in the foreign exchange rates between the end of the fiscal year and the date of the approval of the draft financial statements by the Board of Directors.

* * *

The following Annexes numbered 1 to 9 are an integral part of these notes.

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■ ANNEX 1

ACCOUNTS RECEIVABLE AND ACCRUED INCOME BY MATURITY AND TYPE

| | 12/31/2004 Amount due | | | | 12/31/2003 Amount due | | | |
|---|--------------------------|------------------------------|-------------------------|---------------|--------------------------|------------------------------|-------------------------|---------------|
| | Within one year | From two to five years | Beyond five years | Total | Within one year | From two to five years | Beyond five years | Total |
| (in millions of euro) | | | | | | | | |
| Accounts receivable in long-term investments | | | | | | | | |
| Unconsolidated subsidiaries | - | 4 | - | 4 | 3 | 2 | - | 5 |
| Affiliated companies | 32 | 28 | - | 60 | 54 | 26 | 37 | 117 |
| Others | 43 | 238 | 57 | 338 | 281 | 90 | 28 | 399 |
| | 75 | 270 | 57 | 402 | 338 | 118 | 65 | 521 |
| Accounts receivable in current assets | | | | | | | | |
| Other financial receivables: | | | | | | | | |
| Unconsolidated subsidiaries | 6 | - | - | 6 | 15 | - | - | 15 |
| Affiliated companies | 1 | - | - | 1 | 15 | - | - | 15 |
| Others | 375 | - | - | 375 | 796 | - | - | 796 |
| | 382 | - | - | 382 | 826 | - | - | 826 |
| Trade accounts receivables: | | | | | | | | |
| Customers | 6,413 | 1 | - | 6,414 | 6,849 | 1 | - | 6,850 |
| Unconsolidated subsidiaries | 7 | - | - | 7 | 12 | - | - | 12 |
| Affiliated companies | 164 | - | - | 164 | 114 | - | - | 114 |
| Others | 81 | - | - | 81 | 104 | - | - | 104 |
| | 6,665 | 1 | - | 6,666 | 7,079 | 1 | - | 7,080 |
| Other receivables: | | | | | | | | |
| Unconsolidated subsidiaries | 1 | - | - | 1 | 3 | - | - | 3 |
| Affiliated companies | 23 | - | - | 23 | 20 | - | - | 20 |
| Tax authorities | 770 | 4 | 4 | 778 | 1,584 | 69 | - | 1,653 |
| Deferred tax assets | 1,931 | 1,509 | 266 | 3,706 | 1,841 | 2,857 | 315 | 5,013 |
| Others | 1,425 | 15 | 3 | 1,443 | 980 | 58 | 6 | 1,044 |
| | 4,150 | 1,528 | 273 | 5,951 | 4,428 | 2,984 | 321 | 7,733 |
| Total accounts receivable | 11,197 | 1,529 | 273 | 12,999 | 12,333 | 2,985 | 321 | 15,639 |
| Accrued income | 431 | - | - | 431 | 495 | - | - | 495 |

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■ ANNEX 2

LIABILITIES AND ACCRUED EXPENSES BY MATURITY AND TYPE

| | 12/31/2004 Amount due | | | | 12/31/2003 Amount due | | | |
|---|--------------------------|------------------------|-------------------|---------------|--------------------------|------------------------|-------------------|---------------|
| | Within one year | From two to five years | Beyond five years | Total | Within one year | From two to five years | Beyond five years | Total |
| (in millions of euro) | | | | | | | | |
| Medium and long-term financial debt | | | | | | | | |
| Debentures | 3 | 14,898 | 14,739 | 29,640 | 6,730 | 10,449 | 12,874 | 30,053 |
| Convertible debentures | 803 | 1,964 | 2,825 | 5,592 | 1,715 | 2,768 | 2,829 | 7,312 |
| Due to banks | 469 | 989 | 41 | 1,499 | 684 | 1,140 | 42 | 1,866 |
| Due to other lenders | 66 | 416 | 889 | 1,371 | 88 | 257 | 413 | 758 |
| Trade accounts payable | 3 | 1 | - | 4 | 5 | 4 | - | 9 |
| Accounts payable to affiliated companies | 5 | 12 | 3 | 20 | 9 | 19 | 4 | 32 |
| Taxes payable | - | - | - | - | 23 | - | - | 23 |
| Other liabilities | 15 | 40 | - | 55 | 35 | 53 | - | 88 |
| | 1,364 | 18,320 | 18,497 | 38,181 | 9,289 | 14,690 | 16,162 | 40,141 |
| Short-term borrowings | | | | | | | | |
| Due to banks | 331 | - | - | 331 | 594 | - | - | 594 |
| Due to other lenders | 252 | - | - | 252 | 254 | - | - | 254 |
| Accounts payable to unconsolidated subsidiaries | 3 | - | - | 3 | 9 | - | - | 9 |
| Accounts payable to affiliated companies | 1 | - | - | 1 | 1 | - | - | 1 |
| Taxes payable | - | - | - | - | 35 | - | - | 35 |
| Other liabilities | 76 | - | - | 76 | 431 | - | - | 431 |
| | 663 | - | - | 663 | 1,324 | - | - | 1,324 |
| Trade accounts payable ⁽¹⁾ | | | | | | | | |
| Accounts payable to suppliers | 6,785 | - | - | 6,785 | 5,848 | - | - | 5,848 |
| Accounts payable to unconsolidated subsidiaries | 1 | - | - | 1 | 3 | - | - | 3 |
| Accounts payable to affiliated companies | 271 | - | - | 271 | 113 | - | - | 113 |
| | 7,057 | - | - | 7,057 | 5,964 | - | - | 5,964 |
| Other payables | | | | | | | | |
| Accounts payable to unconsolidated subsidiaries | 8 | - | - | 8 | 6 | - | - | 6 |
| Accounts payable to affiliated companies | 1 | - | - | 1 | 24 | - | - | 24 |
| Taxes payable | 532 | 10 | - | 542 | 1,416 | 2 | - | 1,418 |
| Contributions to pension and social security institutions | 316 | 940 | 100 | 1,356 | 326 | 1,017 | 171 | 1,514 |
| Other liabilities | 2,726 | 3 | - | 2,729 | 2,761 | 14 | - | 2,775 |
| | 3,583 | 953 | 100 | 4,636 | 4,533 | 1,033 | 171 | 5,737 |
| Total liabilities⁽¹⁾ | 12,667 | 19,273 | 18,597 | 50,537 | 21,110 | 15,723 | 16,333 | 53,166 |
| Accrued expenses | 1,378 | - | - | 1,378 | 1,298 | 6 | 23 | 1,327 |

(1) not including the caption "Advances"

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■ ANNEX 3

RECEIVABLES AND PAYABLES BY GEOGRAPHICAL AREA

| (in millions of euro) | Italy | Rest of Europe | North America | Central and South America | Australia, Africa and Asia | Total |
|--|---------------|----------------|---------------|---------------------------|----------------------------|---------------|
| Receivables from shareholders for capital contributions | 45 | | | | | 45 |
| Accounts receivable in long-term investments: | | | | | | |
| - unconsolidated subsidiaries | 4 | | | | | 4 |
| - affiliated companies | 26 | 29 | | | 5 | 60 |
| - others | 167 | 89 | 1 | 81 | | 338 |
| Total | 197 | 118 | 1 | 81 | 5 | 402 |
| Accounts receivable in current assets: | | | | | | |
| - customers | 4,849 | 566 | 207 | 661 | 131 | 6,414 |
| - unconsolidated subsidiaries | 11 | | | 3 | | 14 |
| - affiliated companies | 170 | 3 | | 10 | 5 | 188 |
| - taxes | 542 | 21 | | 215 | | 778 |
| - others | 1,834 | 33 | 1 | 31 | | 1,899 |
| Total ⁽¹⁾ | 7,406 | 623 | 208 | 920 | 136 | 9,293 |
| Payables | | | | | | |
| - debentures | 7,152 | 22,309 | | 179 | | 29,640 |
| - convertible debentures | 2,825 | 2,767 | | | | 5,592 |
| - due to banks | 569 | 782 | 154 | 225 | 100 | 1,830 |
| - due to other lenders | 611 | 836 | | 30 | 146 | 1,623 |
| - advances | 50 | | | | | 50 |
| - trade accounts payable | 4,961 | 625 | 60 | 1,002 | 141 | 6,789 |
| - accounts payable to unconsolidated subsidiaries | 11 | | | 1 | | 12 |
| - accounts payable to affiliated companies | 288 | | | 5 | | 293 |
| - taxes payable | 424 | 23 | 1 | 91 | 3 | 542 |
| - contributions to pension and social security institutions | 1,340 | 4 | 2 | 10 | | 1,356 |
| - other liabilities | 2,682 | 72 | 1 | 94 | 11 | 2,860 |
| Total | 20,913 | 27,418 | 218 | 1,637 | 401 | 50,587 |

(1) Compared to the total presented in the assets of the balance sheet, this total excludes Deferred tax assets.

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■ ANNEX 4

RECONCILIATION OF THE SHAREHOLDERS' EQUITY AND NET INCOME OF TELECOM ITALIA AND THE CONSOLIDATED FIGURES IN THE FINANCIAL STATEMENTS AT DECEMBER 31, 2003

| (in millions of euro) | TELECOM ITALIA'S INTEREST | | | | MINORITY INTEREST | | | TOTAL |
|--|---------------------------|--------------------------------|-------------------|---------------|----------------------------|-------------------|--------------|---------------|
| | Share capital | Reserves and retained earnings | Net income (loss) | Total | Share capital and reserves | Net income (loss) | Total | |
| Financial statements of Telecom Italia at December 31, 2003 | 8.854 | 4.856 | 2.646 | 16.356 | | | | 16.356 |
| Net income (loss) of consolidated companies for the year | | | 82 | 82 | | 864 | 864 | 946 |
| Share capital and reserves of consolidated companies | | 22.251 | | 22.251 | 3.413 | | 3.413 | 25.664 |
| - carrying value of investments in consolidated companies | | (52.125) | | (52.125) | | | | (52.125) |
| Consolidation adjustments: | | | | | | | | |
| - valuation of investments using the equity method | | (243) | 71 | (172) | 1 | | 1 | (171) |
| - positive differences on purchase of investments | | 28.736 | (1.791) | 26.945 | 231 | (39) | 192 | 27.137 |
| - intragroup dividends | | 608 | (1.957) | (1.349) | 3 | (11) | (8) | (1.357) |
| - losses of subsidiaries included in the results of parent companies and extraordinary writedowns of investments | | 3.221 | 1.817 | 5.038 | (97) | 453 | 356 | 5.394 |
| - gains on sales of investments | | (362) | 188 | (174) | (9) | (10) | (19) | (193) |
| - elimination of intragroup profits included in fixed assets and intangibles | | (150) | 48 | (102) | (10) | 3 | (7) | (109) |
| - elimination of intragroup profits on investments | | (382) | | (382) | (245) | | (245) | (627) |
| - other | | (364) | 88 | (276) | (26) | (24) | (50) | (326) |
| Consolidated financial statements at December 31, 2003 | 8.854 | 6.046 | 1.192 | 16.092 | 3.261 | 1.236 | 4.497 | 20.589 |

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■ ANNEX 4

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| (in millions of euro) | TELECOM ITALIA'S INTEREST | | | | MINORITY INTEREST | | | TOTAL |
|--|---------------------------|--------------------------------|-------------------|---------------|----------------------------|-------------------|--------------|---------------|
| | Share capital | Reserves and retained earnings | Net income (loss) | Total | Share capital and reserves | Net income (loss) | Total | |
| Financial statements of Telecom Italia at December 31, 2004 | 8,865 | 5,811 | 2,135 | 16,811 | | | | 16,811 |
| Net income (loss) of consolidated companies for the year | | | 727 | 727 | | 1,048 | 1,048 | 1,775 |
| Share capital and reserves of consolidated companies | | 25,355 | | 25,355 | 2,072 | | 2,072 | 27,427 |
| - carrying value of investments in consolidated companies | | (56,497) | | (56,497) | | | | (56,497) |
| Consolidation adjustments: | | | | | | | | |
| - valuation of investments using the equity method | | (256) | 113 | (143) | 1 | | 1 | (142) |
| - positive differences on purchase of investments | | 26,989 | (1,530) | 25,459 | 202 | (23) | 179 | 25,638 |
| - intragroup dividends | | 43 | (1,455) | (1,412) | 20 | (34) | (14) | (1,426) |
| - losses of subsidiaries included in the results of parent companies and extraordinary writedowns of investments | | 5,427 | 389 | 5,816 | 1,695 | 3 | 1,698 | 7,514 |
| - gains on sales of investments | | (157) | 88 | (69) | (17) | 11 | (6) | (75) |
| - elimination of intragroup profits included in fixed assets and intangibles | | (102) | 35 | (67) | (7) | 2 | (5) | (72) |
| - elimination of intragroup profits on investments | | (370) | | (370) | (238) | | (238) | (608) |
| - other | | (717) | 279 | (438) | (160) | 114 | (46) | (484) |
| Consolidated financial statements at December 31, 2004 | 8,865 | 5,526 | 781 | 15,172 | 3,568 | 1,121 | 4,689 | 19,861 |

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■ ANNEX 5

STATEMENT OF CHANGES IN CONSOLIDATED SHAREHOLDERS' EQUITY FOR THE YEAR ENDED DECEMBER 31, 2003

| (in millions of euro) | TELECOM ITALIA'S INTEREST | | | | MINORITY INTEREST | | | TOTAL |
|--|---------------------------|--------------------------------|-------------------|---------------|----------------------------|-------------------|--------------|---------------|
| | Share capital | Reserves and retained earnings | Net income (loss) | Total | Share capital and reserves | Net income (loss) | Total | |
| Consolidated financial statements at December 31, 2002 | 8,845 | 3,568 | (773) | 11,640 | 8,517 | 467 | 8,984 | 20,624 |
| Appropriation of 2002 net income: | | | | | | | | |
| - Dividends distributed | | | | | (582) | (467) | (1,049) | (1,049) |
| - Transfer to reserves | | (773) | 773 | | | | | |
| Contribution by shareholders | 20 | 24 | | 44 | | | | 44 |
| Merger effect | | 3,424 | | 3,424 | (3,424) | | (3,424) | |
| Effect of share withdrawals, tender offer, cancellation of treasury stock and shares in current assets | (11) | (168) | | (179) | (938) | | (938) | (1,117) |
| Deconsolidation of Seat Pagine Gialle | | | | | (126) | | (126) | (126) |
| Translation adjustments on the conversion of financial statements in foreign currencies and other | | (29) | | (29) | (186) | | (186) | (215) |
| Net income for the year 2003 | | | 1,192 | 1,192 | | 1,236 | 1,236 | 2,428 |
| Consolidated financial statements at December 31, 2003 | 8,854 | 6,046 | 1,192 | 16,092 | 3,261 | 1,236 | 4,497 | 20,589 |

STATEMENT OF CHANGES IN CONSOLIDATED SHAREHOLDERS' EQUITY FOR THE YEAR ENDED DECEMBER 31, 2004

| (in millions of euro) | TELECOM ITALIA'S INTEREST | | | | MINORITY INTEREST | | | TOTAL |
|---|---------------------------|--------------------------------|-------------------|---------------|----------------------------|-------------------|--------------|---------------|
| | Share capital | Reserves and retained earnings | Net income (loss) | Total | Share capital and reserves | Net income (loss) | Total | |
| Consolidated financial statements at December 31, 2003 | 8,854 | 6,046 | 1,192 | 16,092 | 3,261 | 1,236 | 4,497 | 20,589 |
| Appropriation of 2003 net income | | | | | | | | |
| - Dividends distributed | | (538) | (1,192) | (1,730) | | (1,050) | (1,050) | (2,780) |
| - Transfer to reserves | | | | - | 186 | (186) | | - |
| Contribution by shareholders | 11 | 33 | | 44 | 207 | | 207 | 251 |
| Shares subscribed on capital increases in progress | | 3 | | 3 | 38 | | 38 | 41 |
| Dilution of TIM shares held following stock options | | 66 | | 66 | (66) | | (66) | - |
| Effect of consolidation of TIM shares previously recorded in current assets | | | | - | (20) | | (20) | (20) |
| Translation adjustments on the conversion of financial statements in foreign currencies and other | | (84) | | (84) | (38) | | (38) | (122) |
| Net income for the year 2004 | | | 781 | 781 | | 1,121 | 1,121 | 1,902 |
| Consolidated financial statements at December 31, 2004 | 8,865 | 5,526 | 781 | 15,172 | 3,568 | 1,121 | 4,689 | 19,861 |

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■ ANNEX 6

LIST OF COMPANIES CONSOLIDATED ON A LINE-BY-LINE BASIS

| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|---|-----------------------------|----------|---------------|-------------------|-------------|--|
| Wireline | | | | | | |
| BBEYOND B.V. (telecommunications services) | AMSTERDAM (HOLLAND) | EUR | 18,000 | 100.0000 | | BBNED N.V. |
| BBNED N.V. (telecommunications services) | AMSTERDAM (HOLLAND) | EUR | 82,430,000 | 98.7764 | | TELECOM ITALIA INTERNATIONAL N.V. |
| ELETTRA TLC S.p.A. (services rendered in connection with submarine cable systems for telecommunications) | ROME (ITALY) | EUR | 10,329,200 | 100.0000 | | MEDITERRANEAN NAUTILUS S.A. |
| HANSENET TELEKOMMUNIKATION GmbH (telecommunications services) | HAMBURG (GERMANY) | EUR | 91,521,500 | 100.0000 | | TELECOM ITALIA DEUTSCHLAND HOLDING GmbH |
| INTELCOM SAN MARINO S.p.A. (telecommunications services in San Marino) | REPUBLIC OF SAN MARINO | EUR | 1,550,000 | 99.9999 0.0001 | | TELECOM ITALIA SPARKLE S.p.A. TELECOM ITALIA S.p.A |
| LATIN AMERICAN NAUTILUS ARGENTINA S.A. (installation and maintenance of submarine cable systems) | BUENOS AIRES (ARGENTINA) | ARS | 12,000 | 99.9999 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS BOLIVIA S.r.l. (installation and maintenance of submarine cable systems) | LA PAZ (BOLIVIA) | BOB | 5,110,600 | 99.9980 0.0020 | | LATIN AMERICAN NAUTILUS S.A. LATIN AMERICAN NAUTILUS USA Inc. |
| LATIN AMERICAN NAUTILUS BRASIL Ltda (installation and maintenance of submarine cable systems) | RIO DE JANEIRO (BRAZIL) | BRL | 86,865,371 | 99.9900 0.0100 | | LATIN AMERICAN NAUTILUS S.A. LATIN AMERICAN NAUTILUS USA Inc. |
| LATIN AMERICAN NAUTILUS BRASIL PARTICIPACOES Ltda (holding company) | RIO DE JANEIRO (BRAZIL) | BRL | 86,866,370 | 99.9980 0.0020 | | LATIN AMERICAN NAUTILUS S.A. LATIN AMERICAN NAUTILUS LTD |
| LATIN AMERICAN NAUTILUS CHILE S.A. (installation and maintenance of submarine cable systems) | SANTIAGO (CHILE) | CLP | 7,291,239,671 | 99.9999 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS COLOMBIA Ltda (installation and maintenance of submarine cable systems) | BOGOTÀ (COLOMBIA) | COP | 199,833,000 | 99.9999 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS Ltd (installation and maintenance of submarine cable systems) | DUBLIN (IRELAND) | USD | 1,000,000 | 100.0000 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS MEXICO S.A. (installation and maintenance of submarine cable systems) | MEXICO D.F. (MEXICO) | MXN | 100,000 | 99.9900 0.0100 | | LATIN AMERICAN NAUTILUS S.A. LATIN AMERICAN NAUTILUS USA Inc. |
| LATIN AMERICAN NAUTILUS PANAMA S.A. (installation and maintenance of submarine cable systems) | PANAMA | USD | 10,000 | 100.0000 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS PERÙ S.A. (installation and maintenance of submarine cable systems) | LIMA (PERÙ) | PEN | 36,036,491 | 99.9999 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS S.A. (holding company) | LUXEMBURG | USD | 55,500,000 | 99.9999 | | TELECOM ITALIA S.p.A |
| LATIN AMERICAN NAUTILUS SERVICE Inc. (installation and maintenance of submarine cable systems) | MIAMI (USA) | USD | 10,000 | 100.0000 | | LATIN AMERICAN NAUTILUS USA Inc. |
| LATIN AMERICAN NAUTILUS St. Croix LLC (installation and maintenance of submarine cable systems) | ST. CROIX (USA) | USD | 1,000 | 100.0000 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS USA Inc. (installation and maintenance of submarine cable systems) | MIAMI (USA) | USD | 20,000 | 100.0000 | | LATIN AMERICAN NAUTILUS S.A. |
| LATIN AMERICAN NAUTILUS VENEZUELA C.A. (installation and maintenance of submarine cable systems) | CARACAS (VENEZUELA) | BOB | 21,925,000 | 99.9999 | | LATIN AMERICAN NAUTILUS S.A. |
| LOQUENDO SOCIETÀ PER AZIONI (research, development and marketing of technologies and equipment regarding voice synthesis recognition and/or interaction) | TURIN (ITALY) | EUR | 3,573,741 | 99.9846 | | TELECOM ITALIA S.p.A. |
| MED 1 IC-1 (1999) Ltd (installation and management of submarine cable IC1) | TEL AVIV (ISRAEL) | ILS | 1,000 | 99.9000 0.1000 | | MED-1 SUBMARINE CABLES Ltd MED-1 ITALY S.r.l. |
| MED-1 (NETHERLANDS) B.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 18,151 | 100.0000 | | MED-1 SUBMARINE CABLES Ltd |
| MED-1 ITALY S.r.l. (installation and management submarine cable systems in Italian seas) | ROME (ITALY) | EUR | 548,477 | 100.0000 | | MED-1 (NETHERLANDS) B.V. |

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|---|---------------------------|----------|-----------------|---------------------------------------|-------------|--|
| MED-1 SUBMARINE CABLES Ltd (installation and management of cable Lev) | TEL AVIV (ISRAEL) | ILS | 100,000 | 27.8250 23.1750 | | TELECOM ITALIA INTERNATIONAL N.V. TELECOM ITALIA S.p.A |
| MEDITERRANEAN NAUTILUS BV (holding company) | AMSTERDAM (HOLLAND) | EUR | 18,003 | 100.0000 | | MEDITERRANEAN NAUTILUS Ltd |
| MEDITERRANEAN NAUTILUS GREECE Ltd (installation and maintenance of submarine cable systems) | ATHENS (GREECE) | EUR | 111,600 | 100.0000 | | MEDITERRANEAN NAUTILUS BV |
| MEDITERRANEAN NAUTILUS Inc. (telecommunications services) | DELAWARE (USA) | USD | 3,000 | 100.0000 | | MEDITERRANEAN NAUTILUS BV |
| MEDITERRANEAN NAUTILUS ISRAEL Ltd (TLC services, installation and management of submarine cable systems) | TEL AVIV (ISRAEL) | ILS | 1,000 | 100.0000 | | MEDITERRANEAN NAUTILUS BV |
| MEDITERRANEAN NAUTILUS ITALY S.p.A. (installation and maintenance of submarine cable systems) | ROME (ITALY) | EUR | 3,100,000 | 100.0000 | | MEDITERRANEAN NAUTILUS BV |
| MEDITERRANEAN NAUTILUS Ltd (installation and management of submarine cable systems) | DUBLIN (IRELAND) | USD | 100,000 | 51.0000 | | MEDITERRANEAN NAUTILUS S.A. |
| MEDITERRANEAN NAUTILUS S.A. (holding company) | LUXEMBURG | USD | 326,480,000 | 62.5092 7.4908 | | TELECOM ITALIA S.p.A. TELECOM ITALIA INTERNATIONAL N.V. |
| MEDITERRANEAN NAUTILUS TELEKOMÜNİKASYON HİZMETLERİ TİCARET ANONİM ŞİRKETİ (telecommunications services) | ISTANBUL (TURKEY) | TRL | 350,000,000,000 | 99.9988 0.0003 0.0003 0.0003 | | MEDITERRANEAN NAUTILUS BV MEDITERRANEAN NAUTILUS Ltd MEDITERRANEAN NAUTILUS ITALY S.p.A. MEDITERRANEAN NAUTILUS ISRAEL Ltd MEDITERRANEAN NAUTILUS GREECE Ltd |
| PATH.NET S.p.A. (networking systems and telecommunications) | ROME (ITALY) | EUR | 25,800,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA DEUTSCHLAND HOLDING GmbH (holding company) | HAMBURG (GERMANY) | EUR | 25,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA FRANCE SAS (telecommunications services) | PARIS (FRANCE) | EUR | 20,307,800 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TELECOM ITALIA NETHERLANDS B.V. (telecommunications services) | AMSTERDAM (HOLLAND) | EUR | 18,200 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TELECOM ITALIA SPAIN SL UNIPERSONAL (telecommunications services) | MADRID (SPAIN) | EUR | 2,003,096 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TELECOM ITALIA SPARKLE OF NORTH AMERICA, INC. (telecommunications and promotional services) | NEW YORK (USA) | USD | 15,550,000 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TELECOM ITALIA SPARKLE S.p.A. (public and private telecommunication services management) | ROME (ITALY) | EUR | 200,000,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA SPARKLE SINGAPORE PTE. LTD. (telecommunications services) | SINGAPORE | USD | 500,000 | 99.9998 0.0002 | | TELECOM ITALIA SPARKLE S.p.A. TELECOM ITALIA SPARKLE OF NORTH AMERICA, INC. |
| TELECONTACT CENTER S.p.A. (telemarketing services) | NAPLES (ITALY) | EUR | 770,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELEFONIA MOBILE SAMMARINESE S.p.A. (mobile telephony services) | REPUBLIC OF SAN MARINO | EUR | 78,000 | 51.0000 | | INTELCOM SAN MARINO S.p.A. |
| TELEMEDIA INTERNATIONAL USA Inc. (telecommunications services) | DELAWARE (USA) | USD | 154,022,889 | 100.0000 | | TMI - TELEMEDIA INTERNATIONAL Ltd |
| TI BELGIUM S.P.R.L. - B.V.B.A (telecommunications services) | BRUSSELS (BELGIUM) | EUR | 3,000,000 | 99.9967 | | TELECOM ITALIA SPARKLE S.p.A. |
| TI GERMANY GmbH (telecommunications services) | FRANKFURT (GERMANY) | EUR | 25,000 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TI SWITZERLAND GmbH (telecommunications services) | ZURICH (SWITZERLAND) | CHF | 2,000,000 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TI TELECOM ITALIA (AUSTRIA) TELEKOMMUNICATIONSDIESTE GMBH (telecommunications services) | VIENNA (AUSTRIA) | EUR | 2,735,000 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TI UNITED KINGDOM Ltd (telecommunications services) | LONDON (UK) | GBP | 3,855,000 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |
| TMI - TELEMEDIA INTERNATIONAL Ltd (telecommunications services) | LONDON (UK) | EUR | 3,983,254 | 100.0000 | | TELECOM ITALIA SPARKLE S.p.A. |

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|--|--|----------|----------------|--------------------|-------------------|--|
| Mobile | | | | | | |
| BLAH! INC (ex TIMNET USA INC) (mobile network services) | MIAMI (USA) | USD | 21,664,000 | 100.0000 | | TIM INTERNATIONAL N.V. |
| BLAH! SOCIEDADE ANÔNIMA DE SERVIÇOS E COMÉRCIO (internet services) | RIO DE JANEIRO (BRAZIL) | BRL | 78,000,000 | 100.0000 (*) | | TIM INTERNATIONAL N.V. |
| CORPORACION DIGITEL C.A. (telecommunications services) | CARACAS (VENEZUELA) | VEB | 41,214,946,687 | 100.0000 (*) | | TIM INTERNATIONAL N.V. |
| CRC - CENTRO DE RELACIONAMENTO COM CLIENTES LTDA (ex STARCEL) (call center services) | SAO PAULO (BRAZIL) | BRL | 50,000,000 | 100.0000 (*) | | TIM BRASIL SERVIÇOS E PARTICIPAÇÕES S.A. |
| MAXITEL S.A. (mobile telephony operator) | BELO HORIZONTE (BRAZIL) | BRL | 1,200,769,399 | 100.0000 | | TIM CELULAR S.A. |
| TELECOM ITALIA MOBILE S.p.A. (mobile telephony operator) | TURIN (ITALY) | EUR | 515,728,778 | 55.0800 0.1650 | 55.9400 0.1680 | TELECOM ITALIA S.p.A TELECOM ITALIA FINANCE S.A. |
| TIM BRASIL SERVIÇOS E PARTICIPAÇÕES S.A. (holding company) | RIO DE JANEIRO (BRAZIL) | BRL | 9,280,705,829 | 100.0000 | | TIM INTERNATIONAL N.V. |
| TIM CELULAR S.A. (mobile telephony operator) | SAO PAULO (BRAZIL) | BRL | 8,383,490,152 | 100.0000 (*) | | TIM BRASIL SERVIÇOS E PARTICIPAÇÕES S.A. |
| TIM HELLAS TELECOMMUNICATIONS S.A. (ex STET HELLAS TELECOMMUNICATIONS) (mobile telephony operator) | ATHENS (GREECE) | EUR | 128,331,382 | 80.7407 0.1294 | | TIM INTERNATIONAL N.V. TELECOM ITALIA FINANCE S.A. |
| TIM INTERNATIONAL N.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 555,430,000 | 100.0000 | | TELECOM ITALIA MOBILE S.p.A. |
| TIM ITALIA S.p.A. (mobile telephony operator) | MILAN (ITALY) | EUR | 120,000 | 100.0000 | | TELECOM ITALIA MOBILE S.p.A. |
| TIM NORDESTE TELECOMUNICAÇÕES SA (ex TELPE CELULAR SA) (mobile telephony operator) | JABOATAO DOS GUARARAPES (BRAZIL) | BRL | 508,798,763 | 81.7515 | 94.0891 | TIM PARTICIPAÇÕES S.A. |
| TIM PARTICIPAÇÕES S.A. (ex TELE CELULAR SUL PARTICIPAÇÕES) (holding company for operating companies providing mobile network services)) | CURITIBA (BRAZIL) | BRL | 884,503,728 | 23.7305 | 53.2329 | TIM BRASIL SERVIÇOS E PARTICIPAÇÕES S.A. |
| TIM PERÙ S.A.C. (mobile telephony operator) | LIMA (PERÙ) | PEN | 1,337,542,452 | 100.0000 (*) | | TIM INTERNATIONAL N.V. |
| TIM SUL S.A. (mobile telephony operator) | CURITIBA (BRAZIL) | BRL | 971,469,987 | 81.7305 | 90.6528 | TIM PARTICIPAÇÕES S.A. |
| South America | | | | | | |
| AMERICASKY CORPORATION (telecommunications services) | MIAMI (USA) | USD | 1,000 | 80.0000 20.0000 | | ENTEL USA HOLDINGS INC. ENTEL INTERNATIONAL B.V.I. CORP |
| AMERICATEL CENTROAMÉRICA S.A. (telecommunications services) | CIUDAD DE GUATEMALA (GUATEMALA) | USD | 2,649,608 | 78.6500 | | ENTEL CHILE S.A. |
| AMERICATEL CORP USA (telecommunications services) | MIAMI (USA) | USD | 62,372,553 | 80.0000 | | ENTEL INTERNATIONAL B.V.I. CORP |
| AMERICATEL EL SALVADOR S.A. DE C.V. (telecommunications services) | SAN SALVADOR (EL SALVADOR) | USD | 1,143,572 | 85.0000 15.0000 | | AMERICATEL CENTROAMÉRICA S.A. ENTEL CHILE S.A. |
| AMERICATEL GUATEMALA S.A. (telecommunications services) | CIUDAD DE GUATEMALA (GUATEMALA) | GTQ | 450,000 | 100.0000 | | AMERICATEL CENTROAMÉRICA S.A. |
| AMERICATEL HONDURAS S.A. (telecommunications services) | TEGUCIGALPA (HONDURAS) | HNL | 500,000 | 96.0000 | | AMERICATEL CENTROAMÉRICA S.A. |
| AMERICATEL PERÙ SA (telecommunications services) | LIMA (PERÙ) | PEN | 129,256,053 | 53.4000 46.6000 | | ENTEL INVERSIONES S.A. ENTEL CHILE S.A. |
| CHILE WIRELESS S.A. (holding company) | SANTIAGO (CHILE) | CLP | 120,221,724 | 99.0000 1.0000 | | ENTEL TELEFONÍA LOCAL S.A. ENTEL INVERSIONES S.A. |

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|--|---------------------------|----------|-----------------|--------------------|-------------|---|
| DATAKOM S.A. (data transmission services) | LA PAZ (BOLIVIA) | BOB | 66,938,200 | 100.0000 | | ENTEL BOLIVIA S.A. |
| EMPRESA DE RADIOCOMUNICACIONES INSTA BEEP LTDA. (telecommunications services) | SANTIAGO (CHILE) | CLP | 2,400,246,130 | 99.9000 | | ENTEL TELEFONÍA PERSONAL S.A. |
| EMPRESA NACIONAL DE TELECOMUNICACIONES S.A. - ENTEL CHILE (telecommunications services) | SANTIAGO (CHILE) | CLP | 422,481,690,872 | 54.7642 | | TELECOM ITALIA INTERNATIONAL N.V. |
| ENTEL S.A. - EMPRESA NACIONAL DE TELECOMUNICACIONES - ENTEL BOLIVIA (telecommunications services) | LA PAZ (BOLIVIA) | BOB | 1,280,898,800 | 50.0000 | | ETI N.V. |
| ENTEL CALL CENTER S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 11,209,089,143 | 90.0000 10.0000 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| ENTEL INTERNATIONAL B.V.I. CORP. (telecommunications services) | BRITISH VIRGIN ISLANDS | CLP | 33,567,413,118 | 100.0000 | | ENTEL CHILE S.A. |
| ENTEL INVERSIONES S.A. (holding company) | SANTIAGO (CHILE) | CLP | 3,337,021,555 | 100.0000 (*) | | ENTEL CHILE S.A. |
| ENTEL PCS TELECOMUNICACIONES S.A. (mobile services) | SANTIAGO (CHILE) | CLP | 101,836,530,371 | 99.9000 0.1000 | | ENTEL TELEFONÍA PERSONAL S.A. ENTEL CHILE S.A. |
| ENTEL SERVICIOS TELEFÓNICOS S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 1,142,377,585 | 91.4198 8.5802 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| ENTEL TELEFONÍA LOCAL S.A. (local telecommunications services) | SANTIAGO (CHILE) | CLP | 23,928,757,326 | 99.0000 1.0000 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| ENTEL TELEFONÍA MOVIL S.A. (mobile services) | SANTIAGO (CHILE) | CLP | 1,950,379,510 | 99.9200 0.0800 | | ENTEL TELEFONÍA PERSONAL S.A. ENTEL CHILE S.A. |
| ENTEL TELEFONÍA PERSONAL S.A. (holding company) | SANTIAGO (CHILE) | CLP | 131,742,704,099 | 94.6400 5.3600 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| ENTEL USA HOLDINGS INC. (holding company) | MIAMI (USA) | USD | 1,000 | 100.0000 | | ENTEL INTERNATIONAL B.V.I. CORP |
| ENTEL VENEZUELA C.A. (telecommunications services) | CARACAS (VENEZUELA) | BOB | 709,500,000 | 100.0000 | | ENTEL CHILE S.A. |
| MICARRIER TELECOMUNICACIONES S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 3,347,714,780 | 99.9900 0.0100 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| RED DE TRANSACCIONES ELECTRÓNICAS S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 1,687,204,941 | 93.7600 | | ENTEL CHILE S.A. |
| SATEL TELECOMUNICACIONES S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 2,877,673,405 | 99.9000 0.1000 | | ENTEL CHILE S.A. ENTEL INVERSIONES S.A. |
| Internet and Media | | | | | | |
| BEIGUA S.r.l. (purchase, sale, management and maintenance of installation for the repair and distribution of radio and TV broadcasting) | ROME (ITALY) | EUR | 51,480 | 51.0004 | | TI MEDIA BROADCASTING S.r.l. |
| DATABANK S.p.A. (market information) | MILAN (ITALY) | EUR | 937,300 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| DBK S.A. (market information) | MADRID (SPAIN) | EUR | 99,000 | 99.9967 | | DATABANK S.p.A. |
| FINANZIARIA WEB S.p.A. (financing) | ROME (ITALY) | EUR | 9,606,074 | 60.0000 40.0000 | | TELECOM ITALIA MEDIA S.p.A. ISM S.r.l. |
| GRUPPO BUFFETTI S.p.A. (manufacture of products regarding the paper industry, printing and publishing) | ROME (ITALY) | EUR | 11,817,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| HOLDING MEDIA E COMUNICAZIONE H.M.C. S.p.A. (production, marketing on TV and press) | ROME (ITALY) | EUR | 5,064,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| LA7 TELEVISIONI S.p.A. (purchase, management and maintenance of technical transmission systems for audio and video broadcasting) | ROME (ITALY) | EUR | 6,200,000 | 100.0000 | | HOLDING MEDIA E COMUNICAZIONE H.M.C. S.p.A. |

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|---|--|----------|---------------|------------------------------|-------------------|---|
| MATRIX S.p.A. (Internet services) | MILAN (ITALY) | EUR | 1,100,000 | 66.0000 33.3000 0.7000 | | FINANZIARIA WEB S.p.A. ISM S.r.l. TELECOM ITALIA MEDIA S.p.A. |
| MTV ITALIA S.r.l. (services in the field of radio and TV broadcasting, production and sale of radio, TV and cinema programs) | ROME (ITALY) | EUR | 12,151,928 | 51.0000 | | LA7 TELEVISIONI S.p.A. |
| MTV PUBBLICITÀ S.r.l. advertising agency | MILAN (ITALY) | EUR | 10,400 | 100.0000 | | MTV ITALIA S.r.l. |
| SK DIRECT S.r.l. (graphic arts) | ROME (ITALY) | EUR | 1,570,507 | 100.0000 | | GRUPPO BUFFETTI S.p.A. |
| TELECOM ITALIA MEDIA S.p.A. (management of all activities connected with the handling of information) | ROME (ITALY) | EUR | 111,107,894 | 59.4337 2.0328 | 60.4303 2.0669 | TELECOM ITALIA S.p.A. TELECOM ITALIA FINANCE S.p.A. |
| TELECOM MEDIA NEWS S.p.A. (multimedia journalistic information) | ROME (ITALY) | EUR | 120,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| TELEVOICE S.p.A. (ex GIALLO VOICE) (teleselling, telemarketing and call centers and marketing) | CERNUSCO SUL NAVIGLIO (MILAN - ITALY) | EUR | 1,000,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| TI MEDIA BROADCASTING S.r.l. (purchase, sale, management and maintenance of installation for the repair and distribution of radio and TV broadcasting) | ROME (ITALY) | EUR | 7,140,381 | 100.0000 | | LA7 TELEVISIONI S.p.A. |

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|---|---------------------------|-----|---------------|-------------------|--|--|
| CELL-TEL S.p.A. (telecommunications equipment, installations and systems) | IVREA (TURIN - ITALY) | EUR | 500,000 | 80.0000 | | OLIVETTI TECNOST S.p.A. |
| INNOVIS S.p.A. (computer, online and telecommunications equipments and services) | IVREA (TURIN - ITALY) | EUR | 325,000 | 80.0000 | | OLIVETTI TECNOST S.p.A. |
| OLIVETTI CHILE S.A. (sale and maintenance of office equipment, accessories and software) | SANTIAGO (CHILE) | CLP | 2,574,015,843 | 99.9994 0.0006 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI PERUANA S.A. (in liquidazione) |
| OLIVETTI DE PUERTO RICO, Inc. (office equipment in the United States and Central America) | SAN JUAN (PORTO RICO) | USD | 1,000 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI DO BRASIL S.A. (manufacture and sale of typewriters, accessories, parts and assistance) | SAO PAULO (BRAZIL) | BRL | 111,660,625 | 96.6446 3.3554 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI MEXICANA S.A. |
| OLIVETTI I-JET S.p.A. (manufacture and sale of products and accessories for office equipment) | ARNAD (AOSTA - ITALY) | EUR | 15,000,000 | 100.0000 | | OLIVETTI TECNOST S.p.A. |
| OLIVETTI MEXICANA S.A. (manufacture and sale, import-export of typewriters, adding machines, accessories and parts, technical assistance services) | MEXICO CITY (MEXICO) | MXN | 195,190,636 | 99.9999 0.0001 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI TECNOST S.p.A. |
| OLIVETTI SISTEMA E SERVICOS LIMITADA (sale of typewriters, information systems products and electronic goods and services) | SAO PAULO (BRAZIL) | BRL | 410,000 | 100.0000 | | OLIVETTI DO BRASIL S.A. |
| OLIVETTI TECNOST AFRICA (PTY) Ltd. (sale of office equipment) | SANDTON (SOUTH AFRICA) | ZAR | 601 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST AUSTRIA Ges.m.b.H (sale of office equipment and accessories) | VIENNA (AUSTRIA) | EUR | 36,336 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST de MEXICO S.A. de C.V. (manufacture and sale of office equipment) | MEXICO D.F. (MEXICO) | MXN | 234,895,310 | 99.9999 0.0001 | | OLIVETTI MEXICANA S.A. OLIVETTI TECNOST S.p.A. |
| OLIVETTI TECNOST DEUTSCHLAND GmbH (sale of office equipment and holding company) e gestione di partecipazioni) | NURNBERG (GERMANY) | EUR | 25,600,000 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST ESPANA S.A. (sale and maintenance of office equipment, consulting and telematic network management) | BARCELONA (SPAIN) | EUR | 1,229,309 | 99.9912 | | OLIVETTI TECNOST INTERNATIONAL B.V. |

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List of companies consolidated on a line-by-line basis

| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|--|---------------------------------------|----------|---------------|--------------------|-------------|--|
| OLIVETTI TECNOST FRANCE S.A. (sale of office equipment and software) | PUTEAUX (FRANCE) | EUR | 2,200,000 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST INTERNATIONAL B.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 355,027,092 | 100.0000 | | OLIVETTI TECNOST S.p.A. |
| OLIVETTI TECNOST NEDERLAND B.V. (sale of office equipment and accessories) | LEIDERDORP (HOLLAND) | EUR | 6,468,280 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST PORTUGAL, S.A. (sale of office equipment and accessories) | LISBOA (PORTUGAL) | EUR | 275,000 | 99.9927 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI TECNOST S.p.A. (manufacture and sale of products and accessories for office equipment) | IVREA (TURIN - ITALY) | EUR | 78,000,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| OLIVETTI TECNOST UK Ltd. (sale of office equipment) | MILTON KEYNES (UK) | GBP | 6,295,712 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| TIEMME SISTEMI S.r.l. (electric, electromechanical, electronic equipment and related systems) | CARSOLI (L'AQUILA - ITALY) | EUR | 1,040,000 | 100.0000 | | OLIVETTI TECNOST S.p.A. |
| TIESSE S.c.p.A. (installation and assistance for electromechanical, electronic, computer, telematic and telecommunications equipment) | ROME (ITALY) | EUR | 103,292 | 42.0000 19.0000 | | OLIVETTI TECNOST S.p.A. TIEMME SISTEMI S.r.l. |
| TOP SERVICE S.p.A. (electronic diagnostics and repairs of computer products) | MODUGNO (BARI - ITALY) | EUR | 1,022,500 | 50.3667 | | OLIVETTI TECNOST S.p.A. |
| WIRELAB S.p.A. (repairs, management and assistance of fixed telecommunications and other equipment) | SCARMAGNO (TURIN - ITALY) | EUR | 300,000 | 70.0000 | | OLIVETTI TECNOST S.p.A. |
| YMINDS S.A. (product research and development based on ink-jet technology) | YVERDON LES BAINS (SWITZERLAND) | CHF | 100,000 | 100.0000 | | OLIVETTI I-JET S.p.A. |

Information Technology Market

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|--|----------------------------|-----|----------------|--------------------|---------|---|
| AGRISIAN - Consulenza e Servizi per l'Agricoltura S.C.p.A. (consulting and services in favor of agriculture) | ROME (ITALY) | EUR | 10,330,000 | 50.8600 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| ASPASIEL S.r.l. (information systems) | ROME (ITALY) | EUR | 260,000 | 50.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| BANKSIEL S.p.A. (design, installation, operation and maintenance of information systems for bank, financial and insurance companies) | MILAN (ITALY) | EUR | 10,400,000 | 55.5000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CARISIEL Sistemi Informativi Elettronici per il Settore Creditizio e Finanziario (management of information systems and prod., development and maintenance) | RENDE (COSENZA - ITALY) | EUR | 769,585 | 98.0000 2.0000 | | BANKSIEL S.p.A. FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CENTROSIEL S.p.A. (information systems) | MILAN (ITALY) | EUR | 516,600 | 47.0000 | 51.0000 | BANKSIEL S.p.A. |
| EUSTEMA S.p.A. (design, research, development and marketing of software, information and online systems) | ROME (ITALY) | EUR | 312,000 | 67.3333 | | TELECOM ITALIA S.p.A. |
| FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. (conception and implementation of projects in information technology applications) | ROME (ITALY) | EUR | 59,982,385 | 79.4995 0.6286 | | TELECOM ITALIA S.p.A. FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| FINSIEL ROMANIA S.r.l. (consulting and software development) | BUCHAREST (ROMANIA) | ROL | 11,841,500,000 | 97.9732 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| I.A.K. S.r.l. (advanced information systems for credit) | MILAN (ITALY) | EUR | 1,040,000 | 100.0000 | | BANKSIEL S.p.A. |
| INSIEL - INFEPER SISTEMI LOCALI S.p.A. (information systems) | TRIESTE (ITALY) | EUR | 7,755,000 | 52.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| INTERSIEL S.p.A. (design, installation, operation and maintenance of information systems) | RENDE (COSENZA - ITALY) | EUR | 456,900 | 100.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| KRENESIEL - SOCIETÀ SARDA DI INFORMATICA S.p.A. (information systems) | SASSARI (ITALY) | EUR | 2,582,300 | 41.0000 10.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. INSIEL - INFEPER SISTEMI LOCALI S.p.A. |
| TELE SISTEMI FERROVIARI S.p.A. (information systems) | ROME (ITALY) | EUR | 77,003,670 | 60.9997 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |

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| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|--|-----------------|----------|---------------|--------------------|-------------|--|
| VENEZIA INFORMATICA E SISTEMI - VENIS S.p.A. (information systems for the City of Venice and other public subjects) | VENICE (ITALY) | EUR | 1,549,500 | 30.6000 20.4000 | | INSIEL - INF.PER SIST.ENTI LOCALI S.p.A. FINSEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| WEBRED S.p.A. (information systems) | PERUGIA (ITALY) | EUR | 1,560,000 | 51.0000 | | FINSEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |

Information Technology Group

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|--|---------------|-----|------------|----------|--|-----------------------|
| I.T. TELECOM S.R. L. (other software development and software consulting) | MILAN (ITALY) | EUR | 25,000,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
|--|---------------|-----|------------|----------|--|-----------------------|

Other Activities

| | | | | | | |
|---|-----------------------|-----|---------------|-------------------------------|--|--|
| DOMUS ACADEMY S.p.A. (specialized design courses) | MILAN (ITALY) | EUR | 140,000 | 67.3336 | | TELECOM ITALIA S.p.A. |
| EDOTEL S.p.A. (holding company) | TURIN (ITALY) | EUR | 4,847,193 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| EMSA Servizi S.p.A. (real estate services management) | ROME (ITALY) | EUR | 5,000,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| ETI - EURO TELECOM INTERNATIONAL N.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 50,050 | 100.0000 | | ICH - INTERNATIONAL COMMUNICATION HOLDING N.V. |
| ICH - INTERNATIONAL COMMUNICATION HOLDING N.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 50,000 | 100.0000 | | TELECOM ITALIA INTERNATIONAL N.V. |
| ISM S.r.l. (holding company) | ROME (ITALY) | EUR | 56,010,000 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| O&B COSTRUZIONI GENERALI S.r.l. (real estate purchases, exchanges and sales) | IVREA (TURIN - ITALY) | EUR | 100,000 | 50.1000 | | OLIVETTI MULTISERVICES S.p.A. |
| OFI CONSULTING S.r.l. (administrative consulting) | IVREA (TURIN - ITALY) | EUR | 95,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| OLIVETTI GESTIONI IVREA S.p.A. (real estate services) | IVREA (TURIN - ITALY) | EUR | 1,300,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| OLIVETTI HOLDING B.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 15,882,770 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| OLIVETTI MULTISERVICES S.p.A. (real estate management) | IVREA (TURIN - ITALY) | EUR | 20,337,161 | 100.0000 | | TELECOM ITALIA S.p.A. |
| OLIVETTI SYSTEMS TECHNOLOGY CORPORATION (real estate management) | YOKOHAMA (JAPAN) | JPY | 100,000,000 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| OMS HOLDING B.V. (financing) | AMSTERDAM (HOLLAND) | EUR | 20,000 | 100.0000 | | OLIVETTI MULTISERVICES S.p.A. |
| RUF GESTION S.A.S. (real estate services) | PUTEAUX (FRANCE) | EUR | 266,300 | 100.0000 | | OMS HOLDING B.V. |
| SAIAT SOCIETÀ ATTIVITÀ INTERMEDIE AUSILIARIE TLC PA. (financing) | TURIN (ITALY) | EUR | 35,745,120 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TECNOSERVIZI MOBILI s.r.l. (management of movable assets) | ROME (ITALY) | EUR | 26,000 | 51.0000 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA AMERICA LATINA SA (telecommunications and promotional services) | SAN PAOLO (BRAZIL) | BRL | 43,614,072 | 99.9996 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA AUDIT - SCARL (internal auditing for the Telecom Italia Group) | MILAN (ITALY) | EUR | 2,750,000 | 63.6364 18.1818 18.1818 | | TELECOM ITALIA S.p.A. TELECOM ITALIA MOBILE S.p.A. TELECOM ITALIA MEDIA S.p.A. |
| TELECOM ITALIA CAPITAL SA (financing) | LUSSEMBURGO | EUR | 2,336,000 | 99.9990 0.0010 | | TELECOM ITALIA S.p.A. TELECOM ITALIA FINANCE S.A. |
| TELECOM ITALIA FINANCE S.A. (financing) | LUSSEMBURGO | EUR | 542,090,241 | 100.0000 (*) | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA INTERNATIONAL N.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 2,399,483,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELECOM ITALIA LAB SA (holding company) | LUSSEMBURGO | USD | 163,870 | 99.9939 0.0061 | | TELECOM ITALIA S.p.A. TELECOM ITALIA FINANCE S.A. |

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| Name | Head Office | Currency | Share Capital | % Ownership | % of Voting | Held by |
|--|--------------------|----------|---------------|--------------------|-------------|---|
| TELECOM ITALIA LEARNING SERVICES DO BRASIL LIMITADA (information consulting and services) | SAO PAULO (BRAZIL) | BRL | 174,040 | 99.9989 | | TELECOM ITALIA LEARNING SERVICES S.p.A. |
| TELECOM ITALIA LEARNING SERVICES S.p.A. (professional training) | MILAN (ITALY) | EUR | 1,560,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TELENERGIA S.r.l. (import, export, purchase, sale and exchange of electrical energy) | ROME (ITALY) | EUR | 50,000 | 80.0000 20.0000 | | TELECOM ITALIA S.p.A. TELECOM ITALIA MOBILE S.p.A. |
| TELSI (financing company) | LONDON (UK) | GBP | 496,661,807 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| TELSY ELETTRONICA E TELECOMUNICAZIONI SpA (manufacturing and sale of systems for encrypted telecommunications) | TURIN (ITALY) | EUR | 390,000 | 100.0000 | | TELECOM ITALIA S.p.A. |
| TIAUDIT LATAM S.A. (internal auditing) | SAO PAULO (BRAZIL) | BRL | 1,500,000 | 100.0000 | | TELECOM ITALIA AUDIT - SCARL |

[*] The percentage of ownership includes ordinary shares/quotas held by members of the Board of Directors/Managers, as required by local laws in order to hold the post of Director /Manager, or held by trustees.

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■ ANNEX 7

LIST OF COMPANIES ACCOUNTED FOR BY THE EQUITY METHOD

| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|--|----------------------------------|----------|-----------------------|--------------------|-------------|---|
| Subsidiaries | | | | | | |
| THINX-SM TELEHOUSE INTERNET EXCHANGE S.A. (housing and hosting) | REPUBLIC OF SAN MARINO | EUR | 258,000 | 100.0000 | | INTELCOM SAN MARINO S.p.A. |
| TMI TELEMEDIA INTERNATIONAL DO BRASIL Ltda (telecommunications services) | SAN PAOLO (BRAZIL) | BRL | 2,589,317 | 100.0000 (*) | | TMI - TELEMEDIA INTERNATIONAL Ltd |
| Affiliated Companies | | | | | | |
| 012 GOLDEN LINES INTERNATIONAL COMMUNICATIONS SERVICES Ltd (long distance telephony services) | RAMAT GAN (ISRAEL) | ILS | 3,000,000 | 26.4000 | | TELECOM ITALIA INTERNATIONAL N.V. |
| AREE URBANE S.r.l. (real estate) | MILAN (ITALY) | EUR | 307,717 | 31.6499 0.9700 | | TELECOM ITALIA S.p.A. TELECOM ITALIA MEDIA S.p.A. |
| ASCAI SERVIZI S.r.l. (insurance mediation) | ROME (ITALY) | EUR | 73,337 | 35.2113 | | SAIAT SOCIETÀ ATTIVITÀ INTERMEDIE AUSILIARIE TLC PA. |
| ASSCOM INSURANCE BROKERS S.r.l. (insurance mediation) | MILAN (ITALY) | EUR | 100,000 | 20.0000 | | TELECOM ITALIA S.p.A. |
| AVEA ILETISIM HIZMETLERI A.S. (ex TT&TIM ILETISIM HIZMETLERI AS) (mobile telephony operator) | ISTANBUL (TURKEY) | TRL | 6,628,185,030,970,000 | 40.0000 | | TIM INTERNATIONAL N.V. |
| BALTEA S.r.l. (manufacture and sale of office equipment and computer and telecommunications services) | IVREA (TURIN - ITALY) | EUR | 2,220,000 | 49.0000 | | OLIVETTI TECNOST S.p.A. |
| BROAD BAND SERVICE S.A. (production and sales of multimedia services) | REPUBLIC OF SAN MARINO | EUR | 258,000 | 20.0000 | | INTELCOM SAN MARINO S.p.A. |
| BUENAVENTURA S.A. (telecommunications services) | SANTIAGO (CHILE) | CLP | 1,841,258,210 | 50.0000 | | ENTEL TELEFONÍA PERSONAL S.A. |
| E-UTILE S.p.A. (ICT solutions and services for companies in the field of public utilities) | MILAN (ITALY) | EUR | 482,000 | 51.0000 | | SIEMENS INFORMATICA S.p.A. |
| EISYS S.p.A. (software development) | ROME (ITALY) | EUR | 619,200 | 25.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| Empresa de Telecomunicaciones de Cuba S.A. ETEC-SA (telecommunications services) | HAVANA (CUBA) | USD | 1,717,302,900 | 27.0025 | | TELECOM ITALIA INTERNATIONAL N.V. |
| EUROFLY SERVICE S.p.A. (purchase, sale and chartering of airplanes) | CASELLE TORINESE (TURIN - ITALY) | EUR | 8,275,000 | 24.5500 | | TELECOM ITALIA S.p.A. |
| IM.SER S.p.A. (real estate management) | TURIN (ITALY) | EUR | 889,950 | 40.0000 | | TELECOM ITALIA S.p.A. |
| ITALCOM S.p.A. (multimedia systems and devices) | MILAN (ITALY) | EUR | 103,200 | 100.0000 | | ITALTEL S.p.A. |
| ITALDATA S.p.A. (solutions and services for the web economy) | AVELLINO (ITALY) | EUR | 3,096,000 | 100.0000 | | SIEMENS INFORMATICA S.p.A. |
| ITALTEL A.O. (telecommunications systems) | S.PETERSBUR (RUSSIA) | RUB | 20,000 | 100.0000 | | ITALTEL BV |
| ITALTEL ARGENTINA S.A. (telecommunications systems) | BUENOS AIRES (ARGENTINA) | ARS | 600,000 | 96.0000 4.000 | | ITALTEL BV ITALTEL S.p.A. |
| ITALTEL BV (trading and financial company) | AMSTERDAM (HOLLAND) | EUR | 12,731,200 | 100.0000 | | ITALTEL S.p.A. |
| ITALTEL BRASIL LTDA (trading company) | SAN PAOLO (BRAZIL) | BRL | 2,018,302 | 51.4400 48.5600 | | ITALTEL S.p.A. ITALTEL BV |
| ITALTEL CERM PALERMO S.c.p.A. (scientific and technological research) | PALERMO (ITALY) | EUR | 2,125,000 | 90.0000 10.0000 | | ITALTEL S.p.A. TELECOM ITALIA S.p.A. |
| ITALTEL DEUTSCHLAND GmbH (trading company) | DUSSELDORF (GERMANY) | EUR | 40,000 | 60.0000 40.0000 | | ITALTEL HOLDING S.p.A. ITALTEL BV |
| ITALTEL ESPANA S.A. (telecommunications systems) | MADRID (SPAIN) | EUR | 13,191,950 | 100.0000 | | ITALTEL BV |
| ITALTEL FRANCE S.a.s (trading company) | PARIS (FRANCE) | EUR | 40,000 | 100.0000 | | ITALTEL HOLDING S.p.A. |

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List of companies accounted for by the equity method

| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|--|-------------------------------------|----------|-----------------|-----------------------------|-------------|--|
| ITALTEL INC. LTD (trading company) | DELAWARE (USA) | USD | 100 | 60.0000 40.0000 | | ITALTEL HOLDING S.p.A. ITALTEL BV |
| ITALTEL KENYA LTD (telecommunications systems) | NAIROBI (KENYA) | KES | 500,000 | 99.9800 0.0200 | | ITALTEL BV ITALTEL S.p.A. |
| ITALTEL S.p.A. (telecommunications systems) | SETTIMO MILANESE (MILAN - ITALY) | EUR | 196,830,400 | 100.0000 | | ITALTEL HOLDING S.p.A. |
| ITALTEL TELECOM HELLAS EPE (telecommunications systems) | ATHENS (GREECE) | EUR | 18,000 | 80.0000 20.0000 | | ITALTEL HOLDING S.p.A. ITALTEL S.p.A. |
| ITALTEL HOLDING S.p.A. (holding company) | MILAN (ITALY) | EUR | 115,459,344 | 19.3733 | | TELECOM ITALIA FINANCE S.A. |
| LATINA GIOCHI E SISTEMI S.r.l. (lotteries and telephone and telematic games) | MILAN (ITALY) | EUR | 1,000,000,000 | 25.0000 | | OLIVETTI TECNOST S.p.A. |
| MICRO SISTEMAS S.A. (telecommunications services) | BUENOS AIRES (ARGENTINA) | ARS | 210,000 | 99.9900 0.0100 | | TELECOM ARGENTINA S.A. PUBLICOM S.A. |
| MOVENDA SpA (technological platforms for the development of mobile Internet services) | ROME (ITALY) | EUR | 133,333 | 25.0000 | | TELECOM ITALIA LAB SA |
| NORDCOM S.p.A. (application service provider) | MILAN (ITALY) | EUR | 5,000,000 | 42.0000 | | TELECOM ITALIA S.p.A. |
| NORTEL INVERSORA S.A. (holding company) | BUENOS AIRES (ARGENTINA) | ARS | 78,633,050 | 100.0000 | | SOFORA TELECOMUNICACIONES SA |
| NUCLEO S.A. (telecommunications services) | ASUNCIÓN (PARAGUAY) | PYG | 175,200,000,000 | 67.5000 | | TELECOM PERSONAL S.A. |
| OLI GULF FZCO (marketing of office and computer equipment) | JEBEL ALI (DUBAI - UAE) | AED | 500,000 | 40.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLITECNO S.A DE C.V.(in liquidation) (manufacture and sale of products for the telecommunications industry) | MEXICO D.F. (MEXICO) | MXN | 1,000,000 | 50.0000 | | OLIVETTI MEXICANA S.A. |
| ONE-ANS S.p.A. (supply of information technology services) | MONZA (MILAN - ITALY) | EUR | 1,013,874 | 100.0000 | | ITALTEL S.p.A. |
| PEGASO s.r.l. (purchase, sale, exchange, rent, administration, maintenance of movable goods registered for any use and destination) | CASELLE TORINESE (TURIN - ITALY) | EUR | 20,000 | 24.5500 | | TELECOM ITALIA S.p.A. |
| PUBLICOM S.A. (telecommunications services) | BUENOS AIRES (ARGENTINA) | ARS | 16,000,000 | 99.9900 0.0100 | | TELECOM ARGENTINA S.A. NORTEL INVERSORA S.A. |
| SHARED SERVICE CENTER SCARL (planning, design, installation running of computer services) | MILAN (ITALY) | EUR | 1,756,612 | 40.9091 4.5455 4.5455 | | TELECOM ITALIA S.p.A. TELECOM ITALIA MOBILE S.p.A. OLIVETTI TECNOST S.p.A. |
| SIEMENS INFORMATICA S.p.A. (supply of innovating solutions in the field of electronic and mobile business) | MILAN (ITALY) | EUR | 6,192,000 | 49.0000 | | TELECOM ITALIA S.p.A. |
| SISPI S.p.A. (information systems for the municipality of Palermo and other private and public entities) | PALERMO (ITALY) | EUR | 2,066,000 | 49.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| SOFORA TELECOMUNICACIONES SA (holding company) | BUENOS AIRES (ARGENTINA) | ARS | 439,702,000 | 32.5000 17.5000 | | TELECOM ITALIA S.p.A. TELECOM ITALIA INTERNATIONAL N.V. |
| TELBIO S.p.A. (technological services supporting the health sector) | MILAN (ITALY) | EUR | 4,083,330 | 31.0345 | | TELECOM ITALIA S.p.A. |
| TELECOM ARGENTINA S.A. (telecommunications services) | BUENOS AIRES (ARGENTINA) | ARS | 984,380,978 | 54.7364 | | NORTEL INVERSORA S.A. |
| TELECOM ARGENTINA USA INC. (telecommunications services) | DELAWARE (USA) | USD | 249,873 | 100.0000 | | TELECOM ARGENTINA S.A. |
| TELECOM PERSONAL S.A. (telecommunications services) | BUENOS AIRES (ARGENTINA) | ARS | 310,514,481 | 99.9923 0.0077 | | TELECOM ARGENTINA S.A. PUBLICOM S.A. |
| TELEGONO s.r.l. (real estate management) | ROME (ITALY) | EUR | 1,000,000 | 40.0000 | | TELECOM ITALIA S.p.A. |
| TELELEASING - LEASING DI TELECOMUNICAZIONI E GENERALE S.p.A. (financial leasing of real estate and other assets) | MILAN (ITALY) | EUR | 9,500,000 | 20.0000 | | SAIAT SOCIETÀ ATTIVITÀ INTERMEDIE AUSILIARIE TLC PA. |
| TIGLIO I S.r.l. (real estate management) | MILAN (ITALY) | EUR | 5,255,704 | 45.6991 2.1027 | | TELECOM ITALIA S.p.A. TELECOM ITALIA MEDIA S.p.A. |

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List of companies accounted for by the equity method

| Name | Head Office | Currency | Share Capital | % Ownership | % of Voting | Held by |
|---|------------------------|----------|---------------|-------------|-------------|---|
| TIGLIO II S.r.l. (real estate management) | MILAN (ITALY) | EUR | 14,185,288 | 49.4707 | | TELECOM ITALIA S.p.A. |
| VALUE TEAM S.p.A. (EX WEBEGG) (web solutions) | MILAN (ITALY) | EUR | 33,107,160 | 30.2000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| W.P. WINNER PROJECT B.V. (web solutions) | ROTTERDAM (HOLLAND) | EUR | 18,151 | 100.0000 | | VALUE TEAM S.p.A. |
| WEMACOM TELEKOMMUNIKATION GmbH (telecommunications services) | SCHWERIN (GERMANY) | EUR | 60,000 | 25.0000 | | HANSENET TELEKOMMUNIKATION GmbH |

[*] The percentage of ownership includes ordinary shares/quotas held by members of the Board of Directors/Managers, as required by local laws in order to hold the post of Director /Manager, or held by trustees.

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LIST OF OTHER SUBSIDIARIES AND AFFILIATED COMPANIES

| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|---|-----------------------------|----------|---------------|---------------------------------------|-------------|---|
| Subsidiaries | | | | | | |
| DEDITA S.p.A. (in liquidation) (systems products and services, electronic and electromechanical devices) | IVREA (TURIN - ITALY) | EUR | 250,000 | 100.0000 | | OLIVETTI TECNOST S.p.A. |
| DIASPRON DO BRASIL S.A. (in liquidation) (manufacture and export of typewriters and printers) | SAO PAULO (BRAZIL) | BRL | 5,135,417 | 99.9999 0.0001 | | OLIVETTI DO BRASIL S.A. OLIVETTI SISTEMA E SERVICOS LIMITADA |
| EMAX TRADE S.r.l. - (in liquidation) (Internet site management) | MILAN (ITALY) | EUR | 100,000 | 100.0000 | | MATRIX S.p.A. |
| GIALLO MARKET S.r.l. - (in liquidation) (owner of Virgilio.it) | MILAN (ITALY) | EUR | 10,000 | 90.0000 10.0000 | | MATRIX S.p.A. TELECOM ITALIA MEDIA S.p.A. |
| GIALLO VIAGGI. It S.r.l. (in liquidation) (research, design, development, production of information and telematic products for tourism) | MILAN (ITALY) | EUR | 10,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| HOLDING MEDIA & COMUNICAZIONE S.r.l. (in liquidation) (purchase/sale of advertising space and management of advertising on radio/TV stations/channels) | ROME (ITALY) | EUR | 516,500 | 100.0000 | | HOLDING MEDIA E COMUNICAZIONE H.M.C. S.p.A. |
| IL CENTRO CONTABILE S.p.A. (in liquidation) (retail sale of stationery, books and office supplies) | ROME (ITALY) | EUR | 2,233,507 | 89.7018 | | GRUPPO BUFFETTI S.p.A. |
| IRIDIUM ITALIA S.p.A. (in liquidation) (satellite telecommunications services) | ROME (ITALY) | EUR | 2,575,000 | 65.0000 | | TELECOM ITALIA S.p.A. |
| KMATRIX S.r.l. (in liquidation) (Internet site creation and management) | MILAN (ITALY) | EUR | 100,000 | 100.0000 | | MATRIX S.p.A. |
| MULTIDATA S/A ELETTRONICA INDUSTRIA E COMERCIO (in liquidation) (manufacture and export of typewriters and printers) | MANAUS (BRAZIL) | BRL | 5,583,350 | 99.9999 0.0001 | | OLIVETTI DO BRASIL S.A. OLIVETTI SISTEMA E SERVICOS LIMITADA |
| NETESI S.p.A. (in liquidation) (telecommunications and multimedia services) | MILAN (ITALY) | EUR | 434,715 | 100.0000 | | TELECOM ITALIA S.p.A. |
| OFFICE AUTOMATION PRODUCTS S.r.l. (in liquidation) (wholesale of magnetic supports) | ROME (ITALY) | EUR | 90,000 | 100.0000 | | GRUPPO BUFFETTI S.p.A. |
| OLIVETTI ARGENTINA S.A.C.e.I. (in liquidation) (sale and maintenance of office equipment) | BUENOS AIRES (ARGENTINA) | ARS | 7,590,000 | 99.9999 0.0001 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI PERUANA S.A. (in liquidation) |
| OLIVETTI COLOMBIANA S.A. (in liquidation) (sale of office and industrial equipment) | BOGOTÁ (COLOMBIA) | COP | 2,500,000,000 | 90.5288 9.4700 0.0001 0.0001 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI TECNOST S.p.A. OLIVETTI CHILE S.A. OLIVETTI PERUANA S.A. (in liquidation) |
| OLIVETTI INTERNATIONAL (SERVICE) S.A. (in liquidation) (administrative services) | LUGANO (SWITZERLAND) | CHF | 50,000 | 100.0000 | | TELECOM ITALIA FINANCE S.A. |
| OLIVETTI LEXIKON NORDIC AB (in liquidation) (sale of accessories and office equipment) | STOCKHOLM (SWEDEN) | SEK | 10,100,000 | 100.0000 | | OLIVETTI TECNOST INTERNATIONAL B.V. |
| OLIVETTI PERUANA S.A. (in liquidation) (sale and assistance for office equipment and machines) | LIMA (PERÙ) | PEN | 4,654,920 | 99.9998 0.0002 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI TECNOST S.p.A. |
| OLIVETTI SERVICIOS Y SOLUCIONES INTEGRALES S.A. de C.V. (in liquidation) (hardware maintenance and other services and integration of engineering projects) | MEXICO D.F. (MEXICO) | MXN | 7,025,226 | 99.9999 0.0001 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI TECNOST S.p.A. |
| OLIVETTI TECNOST (H.K.) Ltd. (in liquidation) (sale of equipment and systems in the Pacific area and other areas) | HONG KONG | HKD | 200,000 | 99.5000 0.5000 | | OLIVETTI TECNOST INTERNATIONAL B.V. OLIVETTI TECNOST S.p.A. |
| SATURN VENTURE PARTNERS LLC (holding company) | DELAWARE (USA) | USD | 27,166,000 | 56.9643 17.8482 | | TELECOM ITALIA LAB SA TELECOM ITALIA MOBILE S.p.A. |
| SCS COMUNICAZIONE INTEGRATA S.p.A. (in liquidation) (marketing and communication consulting) | ROME (ITALY) | EUR | 600,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| TECO SOFT ARGENTINA S.A. (in liquidation) (design, development and sale of software) | BUENOS AIRES (ARGENTINA) | ARS | 12,000 | 99.9917 | | TELECOM ITALIA S.p.A. |
| TELECOM MEDIA INTERNATIONAL ITALY-CANADA Inc. (in liquidation) (telecommunications services) | MONTREAL (CANADA) | CAD | 952,100 | 100.0000 | | TMI - TELEMEDIA INTERNATIONAL Ltd |

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| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|---|---------------|----------|---------------|--------------|-------------|-----------------------------|
| TIN WEB S.r.l. (in liquidation) (Internet site development consulting) | MILAN (ITALY) | EUR | 10,000 | 100.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| TRAINET S.p.A. (in liquidation) (development, operation and sales of teleteaching systems) | ROME (ITALY) | EUR | 674,446 | 100.0000 | | TELECOM ITALIA S.p.A. |
| ZD TECH ITALIA S.p.A. - (in liquidation) (Internet site development and management) | MILAN (ITALY) | EUR | 100,000 | 51.0000 | | MATRIX S.p.A. |

Affiliated Companies

| | | | | | | |
|---|-----------------------------------|-----|---------------|--------------------|--|--|
| ARCHEO S.p.A. (in liquidation) (services) (ITALY) | BARI | EUR | 464,400 | 25.0000 | | OFI CONSULTING S.r.l. |
| CABLE INSIGNIA S.A. (in liquidation) (telecommunications services) | ASUNCIÓN (PARAGUAY) | PYG | 1,000,000,000 | 75.0000 | | TELECOM PERSONAL S.A. |
| CARTESIA - CARTOGRAFIA DIGITALE S.p.A. (in liquidation) (design, development, marketing of numeric cartography) | ROME (ITALY) | EUR | 100,000 | 50.0000 | | TELECOM ITALIA S.p.A. |
| CLIPPER S.p.A. (in liquidation) (marketing and communication consulting) | ROME (ITALY) | EUR | 100,000 | 50.0000 | | SCS COMUNICAZIONE INTEGRATA S.p.A. (in liquidation) |
| CROMA S.r.l. (in liquidation) (hardware maintenance) | P. SAN GIOVANNI (PERUGIA - ITALY) | EUR | 41,317 | 50.0012 | | WEBRED S.p.A. |
| IN.VA. CONSULTING S.r.l. (information systems development) | AOSTA (ITALY) | EUR | 75,400 | 55.0000 | | IN.VA. S.p.A. |
| IN.VA. S.p.A. (information systems) | AOSTA (ITALY) | EUR | 520,000 | 40.0000 | | TELECOM ITALIA S.p.A. |
| IN.VA. SISTEMI INFORMATIVI TERRITORIALI S.r.l. (supply of software) | AOSTA (ITALY) | EUR | 75,000 | 55.0000 | | IN.VA. S.p.A. |
| INTERNATIONAL INFORMATION SERVICES (marketing of information systems and software products) | MOSCOW (RUSSIA) | RUB | 1,000,000 | 50.0000 | | OLIVETTI HOLDING B.V. |
| ISCE Investors in Sapient & Cuneo Europe S.A. (investment company) | LUSSEMBURGO | EUR | 4,334,400 | 25.0000 | | TELECOM ITALIA MEDIA S.p.A. |
| LI.SIT. - LOMBARDIA INTEGRATA SERVIZI INFOTELEMATICI PER IL TERRITORIO S.p.A. (information and TLC services and products for the local public administration) | MILAN (ITALY) | EUR | 6,500,000 | 24.2000 11.0000 | | TELECOM ITALIA S.p.A. FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| MESNIL HOLDING S.A. (internet) | LUSSEMBURGO | EUR | 78,000 | 99.9987 | | ISCE Investors in Sapient & Cuneo Europe S.A. |
| MIAECONOMIA S.r.l. (publishing in the field of personal finance) | ROME (ITALY) | EUR | 1,000,000 | 30.0000 | | MATRIX S.p.A. |
| OCN-TRADING S.r.l. (in liquidation) (trading company) | IVREA (TURIN - ITALY) | EUR | 40,800 | 40.0000 | | TELECOM ITALIA S.p.A. |
| PARCO DORA BALTEA S.p.A. (various services connected with the real estate sector) | IVREA (TURIN - ITALY) | EUR | 300,000 | 33.3333 | | OLIVETTI MULTISERVICES S.p.A. |
| UBA-NET S.A. (in liquidation) (teleteaching systems) | BUENOS AIRES (ARGENTINA) | ARS | 12,000 | 50.0000 | | TRAINET S.p.A. (in liquidation) |

Consortium Subsidiaries

| | | | | | | |
|---|--------------|-----|---------|--------------------|--|--|
| CONS. FORM. PROF. MEZZOGIORNO D'ITALIA E PAESI AREA MEDITERRANEA - NAUTILUS (professional training) | ROME (ITALY) | EUR | 30,000 | 31.0000 20.0000 | | TELECOM ITALIA LEARNING SERVICES MEDITERRANEAN NAUTILUS Ltd |
| CONSORZIO ENERGIA GRUPPO TELECOM ITALIA (coordination of power for fixed and mobile networks of consortia) | ROME (ITALY) | EUR | 10,000 | 50.0000 50.0000 | | TELECOM ITALIA TELECOM ITALIA MOBILE |
| CONSORZIO IRIS BENI CULTURALI (filing/recovery of documents and system assistance for the Ministry of Cultural and Environmental Works of Art) | ROME (ITALY) | EUR | 170,431 | 90.9000 9.1000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. TELECOM ITALIA S.p.A. |
| CONSORZIO MAEL (participation in bids and competitions held by public and private entities) | ROME (ITALY) | EUR | 52,000 | 60.0000 40.0000 | | OLIVETTI TECNOST S.p.A. TIEMME SISTEMI S.r.l. |
| CONSORZIO SESIT (in liquidation) (development of the integrated information system for the Ministry of Transport and Navigation) | ROME (ITALY) | EUR | 51,646 | 70.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CONSORZIO TURISTEL (online tourism services) | ROME (ITALY) | EUR | 77,469 | 33.3333 33.3333 | | TELECOM ITALIA S.p.A. FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |

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| Name | Head Office | Currency | Share Capital | % Owner-ship | % of Voting | Held by |
|---|---------------------------|----------|---------------|--------------------|-------------|--|
| Consortium Affiliates | | | | | | |
| CONSORZIO ACCAM (automation of the communication centers of the agencies and operating units of the Air Force) | ROME (ITALY) | EUR | 6,120 | 33.3333 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CONSORZIO CSIA (in liquidation) (information systems for the State agency for the agricultural market) | ROME (ITALY) | EUR | 206,583 | 44.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CONSORZIO DREAM FACTORY (in liquidation) (promotion of new economy development in the weak areas of the country) | ROME (ITALY) | EUR | 20,000 | 20.0000 | | TELECOM ITALIA S.p.A. |
| CONSORZIO E O (in liquidation) (professional training) | ROME (ITALY) | EUR | 19,107 | 50.0000 | | TELECOM ITALIA S.p.A. |
| CONSORZIO IRI TELEMATICA CALABRIA - TELCAL (planning and development of the "Piano Telematico Calabria" project) | CATANZARO (ITALY) | EUR | 877,975 | 24.0000 24.0000 | | INTERSIEL S.p.A. TELECOM ITALIA S.p.A. |
| CONSORZIO LABORATORIO DELLA CONOSCENZA (realization of a research project for innovative remote professional training and platforms in Naples) | NAPLES (ITALY) | EUR | 51,646 | 25.0000 25.0000 | | TELECOM ITALIA S.p.A. TELECOM ITALIA LEARNING SERVICES S.p.A. |
| CONSORZIO OMNIA (in liquidation) (hardware maintenance) | PERUGIA (ITALY) | EUR | 2,582 | 50.0000 | | WEBRED S.p.A. |
| CONSORZIO REISS FORM (training and consulting services for training and management) | ROME (ITALY) | EUR | 51,646 | 50.0000 | | TELECOM ITALIA LEARNING SERVICES S.p.A. |
| CONSORZIO S.I.A.R.C. (in liquidation) (supply of information products and services) | NAPLES (ITALY) | EUR | 25,821 | 30.0000 | | TELECOM ITALIA S.p.A. |
| CONSORZIO SCUOLA SUPERIORE ALTA FORMAZIONE UNIVERSITARIA FEDERICO II (professional training) | NAPLES (ITALY) | EUR | 129,114 | 20.0000 | | TELECOM ITALIA MOBILE S.p.A. |
| CONSORZIO SIMT (information systems for the general management of the civil traffic and transport control authority) | ROME (ITALY) | EUR | 51,646 | 45.0000 | | FINSIEL - CONSULENZA E APPLICAZIONI INFORMATICHE S.p.A. |
| CONSORZIO STOAMED CONSORZIO FORMAZIONE MEDITERRANEO STOA (design and management of high-tech professional training courses) | ERCOLANO (NAPLES - ITALY) | EUR | 10,000 | 30.0000 | | TELECOM ITALIA LEARNING SERVICES S.p.A. |
| CONSORZIO TELEMED (in liquidation) (online social and health assistance activities) | ROME (ITALY) | EUR | 103,291 | 33.3335 | | TELECOM ITALIA S.p.A. |
| NAVIGATE CONSORTIUM (terrestrial and satellite network integration) | MILAN (ITALY) | EUR | 582,716 | 20.0000 | | TELECOM ITALIA S.p.A. |

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OTHER SIGNIFICANT INVESTMENTS IN ACCORDANCE WITH CONSOB RESOLUTION NO. 11971 DATED MAY 14, 1999

| Name | Head Office | Currency | Share Capital | Owner-ship | % of Voting | Held by |
|---|----------------------------------|----------|---------------|------------------|-------------|--|
| ANCITEL S.p.A. (telecommunications services) | ROME (ITALY) | EUR | 1,087,232 | 8.5500 7.1320 | | TELECOM ITALIA S.p.A. INSIEL S.p.A. |
| ATESIA - Telemarketing Comunicazione Telefonica e Ricerche di Mercato S.p.A. (telemarketing) | ROME (ITALY) | EUR | 3,150,406 | 19.9000 | | TELECOM ITALIA S.p.A. |
| CIFRA S.c.a.r.l. (training and advanced research for information systems) | CAGLIARI (ITALY) | EUR | 92,964 | 16.6700 | | KRENESIEL S.p.A. |
| ELETTROCLICK S.p.A. (in bankruptcy) (software production) | MILAN (ITALY) | EUR | 127,420 | 14.7000 | | TELECOM ITALIA MEDIA S.p.A. |
| FIN.PRIV. S.r.l. (financing) | MILAN (ITALY) | EUR | 20,000 | 14.2900 | | TELECOM ITALIA S.p.A. |
| FORTHNET SA (information and telecommunications services) | KALLITHEA (GREECE) | EUR | 19,499,850 | 7.7400 4.4800 | | TELECOM ITALIA INTERNATIONAL N.V. MEDITERRANEAN NAUTILUS S.A. |
| IFM INFOMASTER S.p.A. (planning and development of call center solutions) | GENOA (ITALY) | EUR | 161,765 | 12.0000 | | TELECOM ITALIA LAB S.A. |
| INSULA S.p.A. (telecommunications services) | VENICE-MESTRE (ITALY) | EUR | 2,064,000 | 12.0000 | | TELECOM ITALIA S.p.A. |
| ISTITUTO R.T.M. S.p.A. (study and research of mechanical technologies for automation) | VICO CANAVESE (TURIN - ITALY) | EUR | 1,113,714 | 16.1617 | | OLIVETTI TECNOST S.p.A. |
| ITALBIZ.COM Inc (Internet services) | CALIFORNIA (USA) | USD | 4,720 | 19.5000 | | TELECOM ITALIA MEDIA S.p.A. |
| LEISURE LINK HOLDINGS Ltd (manufacture of gaming and leisure-time machines) | STAFFORDSHIRE (UK) | GBP | 7,809,618 | 10.9476 | | TELECOM ITALIA FINANCE S.A. |
| PAS GROUP - Professional Application Software S.r.l. (software production) | MILAN (ITALY) | EUR | 91,800 | 16.6700 | | EUSTEMA S.p.A. |
| PIEDMONT INTERNATIONAL S.A. (financing) | LUXEMBOURG | USD | 10,507,500 | 17.1300 | 10.3000 | TELECOM ITALIA FINANCE S.A. |
| RETAIL NETWORK SERVICES B.V. (holding company) | AMSTERDAM (HOLLAND) | EUR | 15,129,484 | 13.6500 | | OLIVETTI TECNOST S.p.A. |
| SOLPART PARTICIPACOES S.A. (holding company for investment in Brasil Telecom Participações S.A.) | RIO DE JANEIRO (BRAZIL) | BRL | 1,837,900,000 | 31.5900 | 19.0000 | TELECOM ITALIA INTERNATIONAL N.V. |
| TRADIZIONI ITALIANE S.p.A. (in bankruptcy) (production and sale of food and other) | CIRÒ (CROTONE - ITALY) | EUR | 8,263,111 | 11.3800 | | INTERSIEL S.p.A. |
| TWICE SIM S.p.A. (investment services) | MILAN (ITALY) | EUR | 8,450,000 | 14.2300 | | TELECOM ITALIA MEDIA S.p.A. |
| USABLENET INC (development of software for the analysis of web site usability) | DELAWARE (USA) | USD | 4 | 18.1081 | | TELECOM ITALIA LAB SA |
| WAVEMARKET INC (holding company) | DELAWARE (USA) | USD | 26,043 | 11.4800 | | SATURN VENTURE PARTNERS LLI |

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■ INDEPENDENT AUDITORS' REPORT



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www.ey.com

INDEPENDENT AUDITORS' REPORT pursuant to article 156 of Legislative Decree of February 24, 1998, n. 58 (Translation from the original Italian text)

To the Shareholders
of Telecom Italia S.p.A.

1. We have audited the consolidated financial statements of Telecom Italia S.p.A. as of and for the year ended December 31, 2004. These financial statements are the responsibility of the Telecom Italia S.p.A.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.
2. Our audit was made in accordance with auditing standards and procedures recommended by CONSOB. In accordance with such standards and procedures, we planned and performed our audit to obtain the information necessary to determine whether the consolidated financial statements are materially misstated and if such financial statements, taken as a whole, may be relied upon. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, as well as assessing the appropriateness and correct application of the accounting principles and the reasonableness of the estimates made by management. We believe that our audit provides a reasonable basis for our opinion.

For our opinion on the consolidated financial statements of the prior year, which are presented for comparative purposes as required by the law, reference should be made to our report dated April 15, 2004.

3. In our opinion, the consolidated financial statements of Telecom Italia S.p.A. comply with the Italian regulations governing consolidated financial statements; accordingly, they present clearly and give a true and fair view of the consolidated financial position of Telecom Italia S.p.A. as of December 31, 2004, and the consolidated results of its operations for the year then ended.

Milan, March 16, 2005

Reconta Ernst & Young S.p.A.

Signed by: Felice Persico (Partner)

■ Reconta Ernst & Young S.p.A.
Sede Legale: 00196 Roma - Via G.D. Romagnosi, 18/A
Capitale Sociale € 1.259.500,00 i.v.
Iscritta alla S.O. del Registro delle Imprese presso la C.C.I.A.A. di Roma
Codice fiscale e numero di iscrizione 00434000584
P.I. 00891231003
(vecchio numero R.I. 6697/89 - numero R.E.A. 250904)



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BALANCE SHEETS

ASSETS

(in euro)

| | 12/31/2004 | 12/31/2003 |
|--|-----------------------|-----------------------|
| RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS | | |
| Portion called in | 3,206,226 | |
| Portion not called in | | |
| TOTAL RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS | 3,206,226 | - |
| INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS | | |
| - INTANGIBLE ASSETS | | |
| Start-up and expansion costs | 11,541,727 | 23,008,099 |
| Industrial patents and intellectual property rights | 1,278,654,018 | 882,699,375 |
| Concessions, licenses, trademarks and similar rights | 1,349,772 | 850,025 |
| Goodwill | 3,063,804 | 1,144,583 |
| Work in progress and advances to suppliers | 382,132,313 | 477,639,011 |
| Other intangibles | 168,493,582 | 99,238,269 |
| TOTAL INTANGIBLE ASSETS | 1,845,235,215 | 1,484,579,362 |
| - FIXED ASSETS | | |
| Land and buildings | 1,163,533,198 | 1,106,851,118 |
| Plant and machinery | 9,323,365,395 | 10,050,719,281 |
| Manufacturing and distribution equipment | 14,414,369 | 10,048,945 |
| Other fixed assets | 77,798,067 | 48,846,328 |
| Construction in progress and advances to suppliers | 440,935,714 | 626,257,125 |
| TOTAL FIXED ASSETS | 11,020,046,743 | 11,842,722,798 |
| - LONG-TERM INVESTMENTS | | |
| Equity investments in subsidiaries | 33,771,060,795 | 34,188,394,538 |
| affiliated companies | 245,740,410 | 450,394,506 |
| other companies | 204,537,838 | 220,159,093 |
| Total equity investments | 34,221,339,043 | 34,858,948,137 |
| Advances on future capital contributions | 12,064,440 | 136,237,932 |
| Accounts receivable (*) | | |
| subsidiaries | 4,612,671 | 2,890,502 |
| affiliated companies | 2,840,981 | 95,535 |
| other receivables | 18,974,624 | 68,613,790 |
| Total accounts receivable | 26,428,277 | 71,599,827 |
| Treasury stock (total par value euro 700 thousand at 12/31/2004) | 2,298,156 | 279,015,468 |
| TOTAL LONG-TERM INVESTMENTS | 34,817,480,161 | 35,276,499,693 |
| TOTAL INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS | 47,682,762,119 | 48,603,801,852 |
| CURRENT ASSETS | | |
| - INVENTORIES | | |
| Contract work in process | 31,188,677 | 23,341,218 |
| Finished goods and merchandise | | |
| merchandise | 113,485,810 | 65,194,154 |
| TOTAL INVENTORIES | 144,674,486 | 88,535,372 |
| - ACCOUNTS RECEIVABLE (*) | | |
| Trade accounts receivable | 3,121,009,218 | 3,703,449,847 |
| Accounts receivable from subsidiaries | 2,663,711,114 | 3,075,289,042 |
| Accounts receivable from affiliated companies | 126,474,697 | 96,774,507 |
| Taxes receivable | 494,318,645 | 1,362,329,226 |
| Deferred tax assets | 1,078,918,207 | 2,391,462,536 |
| Other receivables due from | | 2,055,138,575 |
| Government and other public entities for grants and subsidies | 27,128,862 | 30,748,076 |
| other receivables | 1,099,190,612 | 807,653,267 |
| Total other receivables | - | 1,126,319,474 |
| TOTAL ACCOUNTS RECEIVABLE | 9,923,295,683 | 12,306,159,930 |
| - SHORT-TERM FINANCIAL ASSETS | | |
| Equity investments in subsidiaries | 52,323 | 166,190,144 |
| Other equity investments | 7,694 | 21,314 |
| Other securities | 0 | 16,178,765 |
| TOTAL SHORT-TERM FINANCIAL ASSETS | 60,017 | 182,390,223 |
| - LIQUID ASSETS | | |
| Bank and postal accounts | 5,423,499,499 | 204,634,612 |
| Checks | 35,239 | 47,595 |
| Cash and valuables on hand | 524,067 | 568,855 |
| TOTAL LIQUID ASSETS | 5,424,058,806 | 205,251,062 |
| TOTAL CURRENT ASSETS | 15,492,088,993 | 12,782,336,589 |
| ACCRUED INCOME AND PREPAID EXPENSES | | |
| Issue discounts and similar charges | 102,832,115 | 110,621,576 |
| Accrued income and other prepaid expenses | 448,151,668 | 453,188,766 |
| TOTAL ACCRUED INCOME AND PREPAID EXPENSES | 550,983,784 | 563,810,342 |
| TOTAL ASSETS | 63,729,041,122 | 61,949,948,783 |

(*) Amounts due within one year

(**) Amounts due beyond one year

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LIABILITIES AND SHAREHOLDERS EQUITY

(in euro)

| | 12/31/2004 | 12/31/2003 |
|--|-----------------------|-----------------------|
| SHAREHOLDERS' EQUITY | | |
| - SHARE CAPITAL | 8,864,857,176 | 8,853,990,645 |
| - ADDITIONAL PAID-IN CAPITAL | 120,380,400 | 88,376,636 |
| - RESERVES FOR INFLATION ADJUSTMENTS - Law No. 413, 12/30/1991 | 1,128,827 | - |
| - LEGAL RESERVE | 1,953,493,714 | 1,834,686,976 |
| - RESERVE FOR TREASURY STOCK IN PORTFOLIO | 2,298,156 | 2,298,156 |
| - MISCELLANEOUS RESERVES | | |
| Reserve Law No. 488/1992 | 142,365,063 | 118,677,664 |
| Reserve L.D. No. 124/1993, ex art. 13 | 391,352 | 185,808 |
| Reserve D.P.R. No. 917/1986, ex art. 24 | 5,749,710 | 5,749,710 |
| Reserve for capital grants | 510,993,216 | 498,701,503 |
| Other reserves | 4,499,029 | 119,012,282 |
| Merger surplus reserve | 2,188,528,994 | 2,188,528,994 |
| TOTAL MISCELLANEOUS RESERVES | 2,852,527,363 | 2,930,855,961 |
| - RETAINED EARNINGS | 881,028,354 | - |
| - NET INCOME | 2,134,847,902 | 2,645,902,665 |
| TOTAL SHAREHOLDERS' EQUITY | 16,810,561,892 | 16,356,111,039 |
| RESERVES FOR RISKS AND CHARGES | | |
| Reserve for taxes and reserve for deferred taxes | 168,547,308 | 119,410,092 |
| Other reserves | 779,403,253 | 657,917,133 |
| TOTAL RESERVES FOR RISKS AND CHARGES | 947,950,561 | 777,327,225 |
| RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES | 1,042,919,286 | 972,412,757 |
| LIABILITIES | (**) | (**) |
| Debentures | 12,701,250,006 | 8,264,982,800 |
| Convertible debentures | 2,824,946,617 | 2,829,005,585 |
| Due to banks | 489,633,645 | 905,642,738 |
| Due to other lenders | 785,210,733 | 1,044,720,870 |
| Advances | | 462,538,177 |
| Trade accounts payable | 32,583,929 | 781,884,860 |
| Accounts payable to subsidiaries | 2,032,076,394 | 22,723,406 |
| Accounts payable to affiliated companies | 16,722,346,123 | 1,929,794,121 |
| Taxes payable | 4,059,996 | 20,543,520,078 |
| Contributions to pension and social security institutions | 224,858,943 | 84,770,489 |
| Other liabilities | 265,867,920 | 379,080,287 |
| TOTAL LIABILITIES | 400,827,571 | 466,543,787 |
| ACCRUED EXPENSES AND DEFERRED INCOME | 52,805 | 626,768,912 |
| TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY | 1,967,562,657 | 441,373 |
| | 63,296,180,750 | 41,395,472,357 |
| | 1,631,428,633 | 2,448,625,405 |
| | 63,729,041,122 | 61,949,948,783 |

(**) Amounts due beyond one year

MEMORANDUM ACCOUNTS

(in euro)

| | 12/31/2004 | 12/31/2003 |
|--|-----------------------|-----------------------|
| GUARANTEES PROVIDED | | |
| Sureties | | |
| on behalf of subsidiaries | 25,932,062,486 | 29,654,575,978 |
| on behalf of affiliated companies | 149,789,992 | 106,450,253 |
| on behalf of others | 119,420,162 | 153,080,279 |
| TOTAL GUARANTEES PROVIDED | 26,201,272,640 | 29,914,106,510 |
| COLLATERAL PROVIDED | - | - |
| PURCHASES AND SALES COMMITMENTS | 4,264,890,849 | 159,844,095 |
| OTHER MEMORANDUM ACCOUNTS | 64,094,726 | 18,549,141 |
| TOTAL MEMORANDUM ACCOUNTS | 30,530,258,215 | 30,092,499,746 |

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STATEMENTS OF INCOME

(in euro)

| | 2004 | 2003 |
|--|-------------------------|-------------------------|
| PRODUCTION VALUE | | |
| Sales and service revenues | 16,126,291,213 | 16,033,200,607 |
| Changes in inventory of contract work in process | (17,703,175) | 6,431,985 |
| Increases in capitalized internal construction costs | 601,232,263 | 59,848,159 |
| Other revenues and income | | |
| operating grants | 7,659,368 | 8,811,916 |
| other | 204,480,064 | 211,339,575 |
| Total other revenues and income | 212,139,432 | 220,151,491 |
| TOTAL PRODUCTION VALUE | 16,921,959,733 | 16,319,632,242 |
| PRODUCTION COSTS | | |
| Raw materials, supplies and merchandise | 614,505,552 | 378,200,723 |
| Services | 5,394,978,811 | 5,215,924,337 |
| Use of property not owned | 620,892,813 | 639,563,595 |
| Personnel costs | | |
| wages and salaries | 1,837,882,348 | 1,757,078,867 |
| social security contributions | 587,147,217 | 557,588,452 |
| termination indemnities | 137,117,728 | 131,362,346 |
| other costs | 51,994,528 | 50,385,900 |
| Total personnel costs | 2,614,141,821 | 2,496,415,565 |
| Amortization, depreciation and writedowns | | |
| amortization of intangible assets | 671,342,802 | 614,766,202 |
| depreciation of fixed assets | 2,220,634,369 | 2,304,065,561 |
| writedowns of receivables included in current assets and liquid assets | 101,456,333 | 198,983,107 |
| Total amortization, depreciation and writedowns | 2,993,433,504 | 3,117,814,870 |
| Changes in inventory of raw materials, supplies and merchandise | (37,801,087) | (12,398,195) |
| Provisions for risks | 49,137,824 | 14,430,827 |
| Miscellaneous operating costs | | |
| losses on disposals of assets | 17,430,802 | 15,612,246 |
| TLC operating fees | 23,249,802 | 21,817,191 |
| other miscellaneous costs | 397,915,444 | 293,134,325 |
| Total miscellaneous operating costs | 438,596,048 | 330,563,762 |
| TOTAL PRODUCTION COSTS | (12,687,885,287) | (12,180,515,484) |
| OPERATING INCOME | 4,234,074,446 | 4,139,116,758 |
| FINANCIAL INCOME AND EXPENSE | | |
| Income from equity investments | | |
| dividends from subsidiaries | 1,392,082,651 | 1,908,322,292 |
| dividends from affiliated companies | | 5,200,000 |
| dividends from other companies | 8,755,033 | 6,021,771 |
| other income from equity investments | 5,993,068 | 87,165,135 |
| Total income from equity investments | 1,406,830,752 | 2,006,709,198 |
| Other financial income from | | |
| accounts receivable included in long-term investments | | |
| subsidiaries | 3,725,104 | 3,443,158 |
| affiliated companies | 1,789,550 | 6,169,478 |
| other | 7,084,652 | 6,816,902 |
| Total from accounts receivable included in long-term investments | 12,599,306 | 16,429,538 |
| securities, other than equity investments, included in current assets | 240,273 | 1,788,446 |
| other income | | |
| interest and fees from subsidiaries | 25,140,833 | 29,963,561 |
| interest and fees from affiliated companies | 50,519 | 408,523 |
| interest and fees from others and miscellaneous income | 189,070,664 | 68,377,310 |
| Total other income | 214,262,016 | 98,749,394 |
| Total other financial income | 227,101,595 | 116,967,378 |
| Interest and other financial expense | | |
| interest and fees paid to subsidiaries | 770,635,971 | 849,565,365 |
| interest and fees paid to affiliated companies | 445,769 | 305,547 |
| interest and fees paid to others and miscellaneous expense | 1,225,196,564 | 1,669,541,618 |
| Total interest and other financial expense | (1,996,278,304) | (2,519,412,530) |
| Foreign exchange gains and losses | (2,417,782) | (1,773,715) |
| TOTAL FINANCIAL INCOME AND EXPENSE | (364,763,740) | (397,509,668) |

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(in euro)

| | 2004 | 2003 |
|---|----------------------|------------------------|
| VALUE ADJUSTMENTS TO FINANCIAL ASSETS | | |
| Upward adjustments of | | |
| equity investments | 84,506,670 | 76,570,384 |
| Total upward adjustments | 84,506,670 | 76,570,384 |
| Writedowns of | | |
| equity investments | 30,333,749 | 437,583,619 |
| long-term investments, other than equity investments | 95,535 | |
| securities, other than equity investments, included in current assets | - | 127,692 |
| Total writedowns | (30,429,284) | (437,711,311) |
| TOTAL VALUE ADJUSTMENTS TO FINANCIAL ASSETS | 54,077,386 | (361,140,927) |
| EXTRAORDINARY INCOME AND EXPENSE | | |
| Income | | |
| gains on disposals | 58,203,414 | 36,532,312 |
| elimination of tax interference | 932,387 | |
| miscellaneous | 507,682,674 | 1,014,506,842 |
| Total income | 566,818,475 | 1,051,039,154 |
| Expense | | |
| losses on disposals | 3,595,673 | 387,804,138 |
| prior years' taxes | 2,278,747 | 6,749,918 |
| provisions and writedowns of equity investments | 632,312,672 | 1,278,544,563 |
| miscellaneous | 654,450,031 | 1,030,248,282 |
| Total expense | (1,292,637,122) | (2,703,346,901) |
| TOTAL EXTRAORDINARY ITEMS | (725,818,647) | (1,652,307,747) |
| INCOME BEFORE TAXES | 3,197,569,446 | 1,728,158,416 |
| Income taxes, current and deferred | (1,062,721,544) | 917,744,249 |
| NET INCOME | 2,134,847,902 | 2,645,902,665 |

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■ NOTES TO THE FINANCIAL STATEMENTS

■ INTRODUCTION

The statutory financial statements for the year ended December 31, 2004 of Telecom Italia S.p.A. have been prepared in accordance with the provisions of the Italian Civil Code, amended by the introduction of the reform of corporate law pursuant to Legislative Decree No. 6 dated January 17, 2003 and successive amendments, and consist of the balance sheet, the statement of income and these notes to the financial statements. The statement of cash flows, although presented in the Report on Operations, constitutes an integral part of the statutory financial statements pursuant to art. 2423, paragraph 3 of the Italian Civil Code.

Reclassifications to certain captions of the financial statements have also been made to the financial statements at December 31, 2003 for purposes of comparison.

As stated in the comments on the reclassified statement of income, balance sheet and statement of cash flows included in the Report on Operations, the figures for the year 2004, presented in the balance sheet, statement of income and notes to the financial statements, take into account the effects – as from January 1, 2004 for accounting and tax purposes – of the merger by absorption of IT Telecom S.p.A. and EPIClink S.p.A. in Telecom Italia S.p.A., executed on December 31, 2004.

In accordance with the changes in the law introduced by Legislative Decree No. 6 dated January 17, 2003, with reference to the reform of corporate law, and taking into account recent indications on the subject provided by Institutions and Authorities, tax interference relative to accelerated depreciation charges made in prior years exclusively for tax purposes have been eliminated with a contra-entry to extraordinary income.

As a consequence of this law, Telecom Italia has eliminated accelerated depreciation totaling euro 932 thousand, as described in the note on "Fixed assets".

During 2004, the consolidated national tax return procedure became applicable for the first time; Telecom Italia will adhere to it jointly with certain subsidiaries.

The relative regulation, provided by articles 117 to 129 of the new Italian Income Tax Code (T.U.I.R.), involves the computation, for Corporate Income Tax (IRES) purposes, of a single aggregate taxable income amounting to the algebraic sum of the incomes and/or losses of the Parent Company and the subsidiaries adhering to the procedure and, thus, the settlement of a single income tax to be paid or a single overpayment to be refunded or carried forward under the control of the Parent Company. The carryforward of any consolidated losses also rests with the Parent Company.

The consolidated national tax return procedure makes it possible, from 2004, to recognize the losses in the same year as the adhering companies if, and to the extent that, they offset the incomes of the other adhering companies, and to financially compensate the individual receivable and payable positions.

The settlement of the compensation for the benefit transferred from companies with losses to companies with taxable income will be carried out centrally by Telecom Italia in June 2006. Therefore, the financial statements will present the balances with subsidiaries due beyond one year, respectively, with a payable due to subsidiaries which attribute a tax loss and a receivable due from subsidiaries which attribute a taxable income. Moreover, the settlement, by Telecom Italia, of the individual receivable and payable positions which make up the IRES balance that will be paid in June 2005 (calculated on the income which remains after offsetting the losses) entails the booking of short-term net receivables/payables due from/to the subsidiaries adhering the consolidated national tax return procedure which reflect the contra-accounts of the respective positions.

At December 31, 2004, as a result of the application of the consolidated national tax return procedure, Telecom Italia S.p.A., shows a receivable balance for IRES taxes from the Financial Administration due to higher on-account payments compared to the taxes due.

Each subsidiary adhering to the consolidated national tax return procedure will maintain in its financial statements its balance sheet position related to IRES deferred taxes.

During the year, there were no exceptional cases causing recourse to the departures allowed by art. 2423, paragraph 4, of the Italian Civil Code. Lastly, consolidated financial statements are presented together with the statutory financial statements of Telecom Italia S.p.A. as required by the Legislative Decree No. 127/1991.

All amounts are stated in thousands of euro, unless otherwise indicated.

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■ ACCOUNTING POLICIES

■ Intangible assets

Intangible assets are recorded at acquisition or production cost and are amortized using the straight-line method over their estimated period of benefit.

Intangible assets are written down when there is a permanent impairment to below their net book value, in accordance with article 2426, paragraph 1, item 3 of the Italian Civil Code. The original recorded value will be reinstated in subsequent years if the underlying assumptions are no longer correct.

Intangible assets specifically refer to the following:

"Start-up and expansion costs": these are amortized over a period of five years starting from the time the asset produces an economic benefit.

"Industrial patents and intellectual property rights": these are amortized over their estimated period of benefit on a five-year basis (industrial patents) or on a three-year basis (software), starting from the time the asset produces an economic benefit.

"Concessions, licenses, trademarks and similar rights": these refer mainly to satellite utilization rights and are amortized over the contract period.

"Goodwill": this relates to the acquisition of businesses and companies and is amortized over five years.

"Other intangibles": these refer almost entirely to leasehold improvements. Amortization is calculated on the basis of the lesser of the period of future economic benefit or the residual lease period, starting from the time the expenses are incurred or from the time the asset produces an economic benefit.

"Research, development and advertising costs" are charged to income in the year incurred.

■ Fixed assets

Fixed assets are recorded at acquisition or production cost and depreciated using the straight-line method at rates determined on the basis of their estimated remaining useful life and include inflation adjustments.

Fixed assets are written down when there is a permanent impairment to below their net book value, in accordance with article 2426, paragraph 1, item 3 of the Italian Civil Code. The original recorded value will be reinstated in subsequent years if the underlying assumptions are no longer correct.

Construction in progress is stated at the amount of direct costs incurred (materials used for or intended for installations, third-party services, miscellaneous expenses, internal design costs, as well as company labor). The value of fixed assets does not include maintenance costs incurred for their upkeep to guarantee their expected useful life, their original capacity and productivity, and costs borne to repair malfunctions and failures; such expenses are charged to the statement of income in the year incurred.

Depreciation is calculated on the basis of the estimated useful lives of the installations.

Total accumulated depreciation on fixed assets was upwardly adjusted, in the cases provided, according to the above-cited special laws.

The elimination, disposal or sale of fixed assets is recorded in the financial statement by eliminating the cost and accumulated depreciation from the financial statements and booking the related gain or loss in the statement of income.

■ Equity investments

Equity investments considered long-term in nature are recorded in long-term investments or, if acquired for subsequent sale, recorded in short-term financial assets.

For equity investments in long-term investments and short-term financial assets, the cost flows are determined by reference to the "weighted average cost method for each movement".

Acquisition cost is increased by statutory inflation adjustments, as well as the voluntary one made to several investments during the preparation of the financial statements at December 31, 1981, as well as the cancellation deficit, attributed to TIM shares and which arose from the merger of Telecom Italia S.p.A. in Olivetti S.p.A., being the difference between the carrying value of the cancelled shares and the underlying share of net equity of the merged company.

The carrying value of investments recorded in long-term investments is adjusted for any reasonable expectations of a decline in profitability or recoverability in future years.

In the case of a permanent impairment, the value of such equity investments is written down and the impairment in value in excess of the corresponding carrying value is recorded in *"reserves for risks and charges"*.

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Equity investments included under current assets are stated at the lower of the cost of acquisition and estimated realizable value, represented by the year-end prices on the electronic trading market of the Italian stock exchange and the NASDAQ.

The cost of investments in foreign companies has been translated at the historical exchange rates prevailing at the time of acquisition or subscription or at the year-end rate, if lower, in the case the reduction is considered a permanent impairment.

Writedowns of investments, whether included in long-term investments or current assets, will be reversed in subsequent years if the underlying assumptions are no longer correct.

■ Other securities (other than equity investments) recorded in short-term financial assets

Securities recorded in current assets are valued at the lower of cost of acquisition and realizable value based on market prices at year-end; if, in future years, the underlying assumptions for the writedowns are no longer correct, the carrying value will be adjusted to market value up to the amount of original cost.

■ Inventories

Inventories – consisting of goods intended for sale, as well as stock on hand of technical materials and replacement parts to be used in the business during the year and for maintenance – are valued at the lower of cost, calculated using the weighted-average method, and realizable value.

The carrying value of goods in stock is reduced, through appropriate writedowns, for obsolete materials.

Inventories include work on behalf of third parties in progress at the end of the year, valued according to “cost” criteria determined on the basis of the completed contract method.

■ Accounts receivable and liabilities

Accounts receivable are stated at estimated realizable value and classified under long-term investments or current assets. They include – as far as telecommunications services are concerned – the amount of services already rendered to customers, already billed or still to be billed, as well as invoices for the sale of telephone and on-line equipment.

Liabilities are shown at their nominal value.

■ Transactions in foreign currency

Monetary assets and liabilities are accounted for at the exchange rate as of the transaction date and adjusted to the exchange rates prevailing at year-end, taking into account hedging contracts. Unrealized positive and negative differences arising the adjustment of such items to the year-end exchange rate are recorded in the statement of income and any unrealized net exchange gain is set aside in a specific reserve until realization.

■ Securitization

The total amount of receivables sold under securitization transactions commenced in 2001 is reversed from the balance sheet as the contra-entry for the consideration received on the sale; the amount paid is represented by the non-repeatable amount received immediately (without recourse) whereas the deferred portion is recorded in *Other receivables (financial)* in current assets. This balance sheet caption is presented net of the relative allowance account calculated on the basis of estimated realizable value; the change in the allowance account is booked in *Financial expense* in the statement of income. The difference between the carrying value of the receivables sold and the agreed consideration on the sale is recognized in the statement of income in *Miscellaneous operating costs*, for the trading portion, and in *Interest and other financial expense*, for the financial portion.

■ Accruals and deferrals

These items are recorded on the accrual basis. “*Issue discounts and similar charges*” consist of costs in connection with long-term loans, which are charged to the statement of income over the period of the loan in proportion to the accrued interest.

■ Reserves for risks and charges

“For taxes, for deferred taxes”

This reserve includes prudent provisions for estimated tax charges, including any sanctions and late payment interest, on positions not yet agreed or in dispute, and deferred taxes calculated as described in the note on income taxes.

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“Other reserves”

These reserves relate primarily to provisions to cover risks and charges for losses or liabilities of certain or likely existence whose amount or date of occurrence could, however, not be determined at the end of the year. The provisions reflect the best possible estimate, based on the commitments made and on the data available.

■ Reserve for employee termination indemnities

The amount of this reserve is determined in accordance with current laws (in particular Law No. 297 dated May 29, 1982, which provides for fixed and variable cost-of-living adjustments) and collective bargaining agreements. The reserve is adjusted to the liability matured at the end of the year for personnel in force at that date and is net of advances paid.

■ Due to shareholders for loans

“Shareholders” are considered parties which hold directly at least 2% of share capital at the end of the year. At December 31, 2004, shareholders holding at least 2% of the share capital of Telecom Italia had made no loans to the company.

■ Employee benefit obligations under Law No. 58/1992

With regard to Telecom Italia's obligation under Law No. 58/1992 to guarantee a uniform insurance status under the Telephone Workers' Social Security Fund (which became part of the general “Employees Pension Fund” beginning January 1, 2000) to all employees in service as of February 20, 1992 in the companies Stet, Sip, Italcable and Telespazio, as well as those who moved from the Public Administration to Iritel, Article 66, paragraph 1 of Legislative Decree 331/1993 and converted into Law No. 427/1993, specifies that the sums due to the Fund should be recorded in the financial statements and are tax deductible in the years in which the fifteen equal annual deferred installments are paid to discharge this obligation.

At the present time, the amount of the liability, which will be determined by the National Social Security Institute (Istituto Nazionale della Previdenza Sociale - INPS), can be estimated only roughly, due to disagreements relating to the interpretation and application of the social security legislation and to the lack of certain data which only the social security institutions currently possess (at December 31, 2004, INPS had notified the Company of around 98% of the positions which give rise to expenses for Telecom Italia under the uniform insurance status). A dispute concerning the application and interpretation of this law arose with INPS regarding the exclusion from the estimates under Law No. 58/1992 of all employees (except for employees of the former Iritel) who had already filed an application to join pursuant to Law No. 29/1979 before February 20, 1992, even though that application had not been processed by INPS. The position of the Telecom Italia is that the criteria set forth in Law No. 29/1979 – and, therefore, payment of the respective obligations – apply to these employees.

At the present time, the parties have agreed that the differences in interpretation shall be settled through test appeals for a final determination of the correct interpretation of the law in question. While awaiting these decisions, Telecom Italia has agreed to pay, with reservation, the amounts requested by INPS based on the criteria determined by the latter, subject to subsequent equalization adjustments, if the Courts ultimately accept the Company's interpretation.

Having said that, a reasonable estimate of the principal amount of the liability attributable to Telecom Italia (net of the amounts attributed to Group companies for the employees transferred to those companies) could vary between euro 958 million (partial application of Law 29/1979) and euro 1,281 million (full application of Law 58/1992), of which euro 568 million has already been paid, depending on conflicting interpretations and taking into account all personnel involved. In either case, the impact of the charge should definitely be compatible with the income of future years, since, as allowed under Article 5, paragraph 3 of Law No. 58/1992, the payments requested by INPS are made in fifteen equal annual deferred installments (including annual interest of 5%), based on notification of the expenses by INPS.

The remaining liability for obligations under Law No. 58/1992, to be paid in fifteen annual installments on the basis of the positions notified by INPS up to December 31, 2004 and the interpretation of said positions, totals (net of the amounts attributed to Group companies for the employees transferred to those companies) euro 958 million, of which euro 713 million is for the principal amount and euro 245 million for accrued interest.

Moreover, these financial statements at December 31, 2004 include euro 468 million of residual payables to INPS, (net of the amount attributed to Group companies for the employees transferred to those companies), relating to the estimate referring to the employees of the former State Company for Telephone Services (ASST) which the special Ministerial Commission established under Law No. 58/1992 had made upon the transfer of the assets of the Post and Telecommunications Administration to Iritel, and recorded by the latter company in its financial statements at December 31, 1993. As a result, these charges will have no impact on the results of future years, since they were already included in the aforementioned calculation.

The expenses recorded in 2004 in “extraordinary expenses” amount to euro 149 million and include accrued interest. This amount takes into account the above-mentioned expenses paid by Telecom Italia to INPS also on behalf of other Group companies for those employees transferred to them and covered by the obligation of a uniform insurance status under Law No. 58/1992. The recovery from these same companies of the amounts paid is recorded in the statement of income under “extraordinary income” and amounts to euro 2 million.

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■ Grants

Both operating grants (directly credited to the statement of income) and capital grants or grants for installations are recorded in the accounting period in which the paperwork documenting the grants is received, or in the period in which the respective costs are incurred, provided that the certainty of payment is confirmed by established procedures.

Capital grants and grants for installation are recorded under "*deferred income*" and credited to the statement of income in relation to the depreciation taken on the assets to which the grants refer.

■ Revenues and expenses

Revenues and expenses are recorded on an accrual basis. Revenues relating to telecommunications services are shown gross of the amounts due to other carriers which are recorded, for the same amount, in production costs.

Fees for new access lines and line transfers are recorded as income when the service is provided.

Dividends from subsidiaries are recorded on the maturity principle, that is, in the year when the income from which they are paid is earned by the subsidiaries, providing there is a substantial certainty that they will be paid, and, in any event, when the shareholders' resolution declaring the dividend is passed or when the appropriation of net income is set forth in the preliminary financial statements prepared by management of the subsidiaries prior to the Board Meeting of the parent company that resolves upon the financial statements.

Dividends from affiliated companies and other companies, on the other hand, are recognized in the statement of income according to the accrual principle, that is, in the year in which the respective right to the receivable arises, following the declaration of dividends approved by the shareholders' resolution of those companies.

■ Income taxes

Current income taxes are computed on the basis of a realistic estimate of the income tax charge according to the tax laws in force; the related income tax payable is shown net of payments on account, withholding taxes and tax credits in "taxes payable". Any net receivable position is shown in "taxes receivable" under current assets.

Deferred income taxes are calculated on the basis of the temporary differences between the value attributed to the assets and liabilities for statutory purposes and the value attributed to the same assets and liabilities for tax purposes. Deferred tax assets, including benefits from tax loss carryforwards, are booked in "deferred tax assets" in current assets. The tax benefit relating to tax loss carryforwards is recorded only when there is reasonable certainty of recovery.

Deferred tax assets and liabilities are offset, whenever the assumptions for doing so exist. Deferred taxes on tax-deferred reserves and funds are booked if such reserves will be distributed or, in any case, utilized and their distribution or utilization gives rise to a tax charge.

■ Leased assets

Assets purchased under a financial lease are recognized in the financial statements by a method consistent with current legislation, which requires that leasing payments be recorded as operating costs.

■ Memorandum accounts

"*Guarantees provided*" are shown for the amount of the remaining liability or other obligation guaranteed; those provided in foreign currencies are translated at year-end exchange rates.

"*Purchases and sales commitments*" are determined on the basis of the unperformed portion of contracts outstanding at the end of the fiscal year which do not fall under the normal "operating cycle".

■ Derivative financial instruments

Derivative financial instruments are used by Telecom Italia S.p.A. to hedge exposure to interest rate and exchange rate risks.

For derivative financial instruments used to hedge interest rate risks, the interest differentials are recorded in the statement of income in "*financial income and expense*" based on the accrual principle.

For financial instruments used to hedge exchange rate risks, the cost (or "financial component" calculated as the difference between the spot rate at the date of stipulating the contract and the forward rate) is recorded in the statement of income in "financial income and expense" based on the accrual principle.

Premiums relating to option-type financial instruments are recorded in "other liabilities" or "other receivables" and, if exercised, are considered as an incidental charge to the purchase or sale value of the underlying instruments; if the option is not exercised the premium is recorded in the statement of income under financial income (financial expense).

In this manner, the derivative financial instruments are valued consistently with the underlying asset and liability, for each transaction, and any net expense is recognized in the statement of income.

Option-type derivative financial instruments existing at the end of the year are valued at the lower of cost and market value at the balance sheet date.

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BALANCE SHEETS - ASSETS

RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS

euro 3,206 thousand

Receivables from shareholders for capital contributions refer to the portion of stock options exercised and subscribed but not yet paid.

INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS

INTANGIBLE ASSETS

euro 1,845,235 thousand

(euro 1,484,579 thousand at December 31, 2003)

A summary of the changes in intangible assets during the year is presented below:

| | |
|--|----------------|
| (in thousands of euro) | 2004 |
| - IT Telecom and EPIClink merger | 98,210 |
| - additions | 1,030,650 |
| - amortization | (671,343) |
| - eliminations | (11,720) |
| - contribution from IT Telecom S.p.A. to IT Telecom S.r.l. | (87,407) |
| - other movements | 2,266 |
| Total | 360,656 |

An analysis of the composition and the changes in intangible assets during the year is presented in the following tables:

| 12/31/2003 | | | | | |
|--|------------------|--------------------|------------|--------------------------|------------------|
| (in thousands of euro) | Cost | Upward adjustments | Writedowns | Accumulated amortization | Total |
| Start-up and expansion costs | 152,755 | | | (129,747) | 23,008 |
| Industrial patents and intellectual property rights | 4,102,823 | | | (3,220,124) | 882,699 |
| Concessions, licenses, trademarks and similar rights | 92,506 | | | (91,656) | 850 |
| Goodwill | 1,335 | | | (190) | 1,145 |
| Work in progress and advances to suppliers | 477,639 | | | | 477,639 |
| Other intangibles (*) | 416,696 | | | (317,458) | 99,238 |
| Total | 5,243,754 | | | (3,759,175) | 1,484,579 |
| (*) of which: | | | | | |
| Leasehold improvements | 416,295 | | | (317,057) | 99,238 |

CHANGES DURING THE YEAR

| (in thousands of euro) | IT Telecom and EPIClink merger | Additions | Reclassifications | Sales/Retirements/Other movements | Amortization | Total |
|--|--------------------------------|------------------|-------------------|-----------------------------------|------------------|----------------|
| Start-up and expansion costs | 91 | | | | (11,557) | (11,466) |
| Industrial patents and intellectual property rights | 75,745 | | 1,022,969 | (75,887) | (626,872) | 395,955 |
| Concessions, licenses, trademarks and similar rights | 104 | | 569 | | (173) | 500 |
| Goodwill | 3,822 | | | | (1,903) | 1,919 |
| Work in progress and advances to suppliers | 2,365 | 1,030,650 | (1,119,873) | (8,649) | | (95,507) |
| Other intangibles (*) | 16,083 | | 96,335 | (12,325) | (30,838) | 69,255 |
| Total | 98,210 | 1,030,650 | 0 | (96,861) | (671,343) | 360,656 |
| (*) of which: | | | | | | |
| Leasehold improvements | 16,083 | - | 96,335 | (12,382) | (30,838) | 69,198 |

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(a) Broken down as follows:

| | Cost | Upward adjustments | Writedowns | Accumulated amortization | Net value |
|---|------------------|-----------------------|------------|-----------------------------|-----------------|
| Industrial patents and intellectual property rights | (382,018) | | | 306,131 | (75,887) |
| - of which contribution to IT Telecom S.r.l. | (225,949) | | | 148,631 | (77,318) |
| Work in progress and advances to suppliers | (8,649) | | | | (8,649) |
| - of which contribution to IT Telecom S.r.l. | (1,823) | | | | (1,823) |
| Other intangibles | (111,883) | | | 99,558 | (12,325) |
| - of which contribution to IT Telecom S.r.l. | (21,501) | | | 13,235 | (8,266) |
| Total | (502,550) | | | 405,689 | (96,861) |
| - of which contribution to IT Telecom S.r.l. | (249,273) | | | 161,866 | (87,407) |

12/31/2004

| (in thousands of euro) | Cost | Upward adjustments | Writedowns | Accumulated amortization | Total |
|--|------------------|-----------------------|------------|-----------------------------|------------------|
| Start-up and expansion costs | 153,277 | | | (141,735) | 11,542 |
| Industrial patents and intellectual property rights | 5,024,534 | | | (3,745,880) | 1,278,654 |
| Concessions, licenses, trademarks and similar rights | 96,408 | | | (95,058) | 1,350 |
| Goodwill | 9,516 | | | (6,452) | 3,064 |
| Work in progress and advances to suppliers | 382,132 | | | 0 | 382,132 |
| Other intangibles (*) | 450,816 | | | (282,323) | 168,493 |
| Total | 6,116,683 | - | - | (4,271,448) | 1,845,235 |
| (*) of which: | | | | | |
| Leasehold improvements | 450,415 | - | - | (281,922) | 168,493 |

In particular:

"Start-up and expansion costs" consist primarily of underwriting commissions paid in connection with share capital increases.

"Industrial patents and intellectual property rights" consist almost entirely of applications software purchased outright and user licenses for an indefinite time period.

"Goodwill" relates to the acquisition, by Telecom Italia, of the "administrative services" business segments from Holding Media e Comunicazioni, TIM, Finsiel and Telecom Italia Media. The caption also includes the goodwill on acquisition, by the merged company IT Telecom, in 2002, of the companies Telesoft and Netsiel and, in 2003, of the Enterprise business from Finsiel.

"Work in progress and advances to suppliers" mainly refer to software projects for network and operating program applications. All acquisitions of intangibles are managed through specific work orders and recorded in this caption.

"Other intangibles" refer to leasehold improvements made to properties owned by third parties and include the costs incurred to meet the operating requirements of the Company in the rented premises.

Reclassifications refer to assets that came into use during the year.

In 2004, the purchases of intangibles from subsidiaries and affiliated companies amount to euro 118,931 thousand and mainly refer to software from Italtel (euro 94,897 thousand), Siemens Informatica (euro 10,330 thousand) and Shared Service Center (euro 6,473 thousand).

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■ FIXED ASSETS

euro 11,020,047 thousand

(euro 11,842,723 thousand at December 31, 2003)

A summary of the changes in fixed assets during the year is presented as follows:

| (in thousands of euro) | 2004 |
|--|------------------|
| - IT Telecom and EPIClink merger | 200,256 |
| - additions | 1,299,047 |
| - depreciation | (2,220,635) |
| - disposals | (20,837) |
| - contribution from IT Telecom S.p.A. to IT Telecom S.r.l. | (79,570) |
| - other movements | (937) |
| Total | (822,676) |

An analysis of the composition and the changes in fixed assets during the year is presented in the following tables:

12/31/2003

| (in thousands of euro) | Cost | Upward adjustments | Writedowns | Accumulated depreciation | Total |
|---|-------------------|--------------------|------------------|--------------------------|-------------------|
| Land and buildings | 1,920,352 | 393,067 | (4,827) | (1,201,741) | 1,106,851 |
| - non-industrial | 21,281 | 792 | | (1,189) | 20,884 |
| - industrial | 1,899,071 | 392,275 | (4,827) | (1,200,552) | 1,085,967 |
| Plant and machinery | 46,662,097 | 730,392 | (727,730) | (36,614,039) | 10,050,720 |
| Manufacturing and distribution equipment | 767,876 | 2,693 | | (760,520) | 10,049 |
| Other fixed assets | 554,247 | 4,251 | | (509,652) | 48,846 |
| Construction in progress and advances to supplies | 626,257 | | | | 626,257 |
| Total | 50,530,829 | 1,130,403 | (732,557) | (39,085,952) | 11,842,723 |

CHANGES DURING THE YEAR

| (in thousands of euro) | IT Telecom and EPIClink merger | Additions | Reclassifications | Sales/Retirements/Other movements(a) | Writedowns/Writebacks | Depreciation | Total |
|---|--------------------------------|------------------|-------------------|--------------------------------------|-----------------------|--------------------|------------------|
| Land and buildings | | | | | | | |
| - non-industrial | | | 94 | (1,039) | | (148) | (1,093) |
| - industrial | 64,480 | | 84,706 | (12,102) | | (79,309) | 57,775 |
| | 64,480 | 0 | 84,800 | (13,141) | 0 | (79,457) | 56,682 |
| Plant and machinery | 119,754 | | 1,373,671 | (115,095) | | (2,105,685) | (727,355) |
| Manufacturing and distribution equipment | 1,626 | | 11,011 | (682) | | (7,589) | 4,366 |
| Other fixed assets | 12,717 | | 20,579 | 23,560 | | (27,904) | 28,952 |
| Construction in progress and advances to supplies | 1,679 | 1,299,047 | (1,490,061) | 4,014 | | | (185,321) |
| Total | 200,256 | 1,299,047 | 0 | (101,344) | | (2,220,635) | (822,676) |

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(a) Broken down as follows:

| | Cost | Upward adjustments | Writedowns | Accumulated depreciation | Net value |
|---|------------------|--------------------|------------|--------------------------|------------------|
| Land and buildings | | | | | |
| - non-industrial | (1,326) | (51) | | 338 | (1,039) |
| - industrial | (16,705) | (1,809) | 176 | 6,236 | (12,102) |
| | (18,031) | (1,860) | 176 | 6,574 | (13,141) |
| - of which contribution to IT Telecom S.r.l. | (1,411) | | | 339 | (1,072) |
| Plant and machinery | (1,373,199) | (7,325) | | 1,265,429 | (115,095) |
| - of which contribution to IT Telecom S.r.l. | (260,485) | | | 186,201 | (74,284) |
| Manufacturing and distribution equipment | (240,389) | (3) | | 239,710 | (682) |
| - of which contribution to IT Telecom S.r.l. | (916) | | | 284 | (632) |
| Other fixed assets | 826,348 | (15) | | (802,773) | 23,560 |
| - of which contribution to IT Telecom S.r.l. | (4,825) | | | 1,243 | (3,582) |
| Construction in progress and advances to supplies | 4,014 | | | | 4,014 |
| Total | (801,257) | (9,203) | 0 | 708,940 | (101,344) |
| - of which contribution to IT Telecom S.r.l. | (267,637) | 0 | 0 | 188,067 | (79,570) |

12/31/2004

| (in thousands of euro) | Cost | Upward adjustments | Writedowns | Accumulated depreciation | Total |
|---|-------------------|--------------------|------------------|--------------------------|-------------------|
| Land and buildings | | | | | |
| - non-industrial | 20,049 | 741 | | (999) | 19,791 |
| - industrial | 2,049,955 | 390,466 | (4,651) | (1,292,028) | 1,143,742 |
| | 2,070,004 | 391,207 | (4,651) | (1,293,027) | 1,163,533 |
| Plant and machinery | 47,731,935 | 723,067 | (727,730) | (38,403,907) | 9,323,365 |
| Manufacturing and distribution equipment | 542,185 | 2,690 | | (530,460) | 14,415 |
| Other fixed assets | 1,429,455 | 4,236 | | (1,355,893) | 77,798 |
| Construction in progress and advances to supplies | 440,936 | | | | 440,936 |
| Total fixed assets | 52,214,515 | 1,121,200 | (732,381) | (41,583,287) | 11,020,047 |

All fixed asset purchases are managed using specific work orders and recorded in "construction in progress and advances to suppliers". Reclassifications refer to fixed assets that came into use during the year.

In 2004, purchases of fixed assets from subsidiaries and affiliated companies amount to euro 216.952 thousand and refer principally to the acquisition of telephone exchanges from Italtel (euro 202,090 thousand).

Accumulated depreciation at December 31, 2004 is considered sufficient in relation to the remaining period of utilization of the assets and is determined on the basis of the estimated useful lives of the installations making up the domestic telecommunications network. Depreciation is calculated at the rates used in the previous year. Accumulated depreciation, net of writedowns, covers 79.1% of fixed assets at December 31, 2004 compared to 76.9% at December 31, 2003 post-merger.

In accordance with the contract signed January 16, 2004 by Telecom Italia and Fintecna S.p.A., containing reciprocal options for the purchase and sale (put/call) of seven properties owned by Fintecna S.p.A., at a total price of euro 72,000 thousand, on June 22, 2004, Telecom Italia, after exercising the option in April 2004, signed the deed for the purchase of the seven properties for the contractually agreed price.

Moreover, in accordance with the changes introduced by Legislative Decree No. 6 dated January 17, 2003, with reference to the reform of corporate law, as well as the principles issued on the subject by the Italian Accounting Board, tax interference relative to accelerated depreciation charges (euro 932 thousand) made in prior years by the merging company Olivetti, in accordance with tax laws, has been eliminated with a contra-entry to extraordinary income; the relevant reserve for deferred taxes was booked with a contra-entry to other extraordinary expenses (prior years' taxes).

■ Assets purchased under finance lease contracts

The Company has fixed assets under sale and leaseback transactions and under finance lease contracts. These are accounted for using the operating method by which lease payments are charged to costs under the use of property not owned caption. Any gains on the sale of assets under sale and leaseback transactions are recognized immediately in the statement of income. Had the finance lease contracts been

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accounted for using the finance method, entries would have been made in the statement of income for the interest on the financed principal and for the depreciation charge of the value of the assets purchased by lease; additionally, entries would have been made in the balance sheet to record the fixed assets under assets and the residual debt under liabilities. Furthermore, use of this method would also have resulted in the deferral, on a straight-line basis, of any gains on sale and leaseback transactions over the finance lease term.

The effects of this accounting treatment are described in the following table:

| BALANCE SHEET EFFECT AT DECEMBER 31, 2004 | | (in millions of euro) |
|---|--|-----------------------|
| a) Outstanding contracts | | |
| Assets under finance lease contracts at December 31, 2003, net of writedowns of euro 26 million and accumulated depreciation of euro 232 million | | 1,510 |
| Assets under new finance lease contracts in 2004 (+) | | 34 |
| Assets purchased under finance lease contracts in 2004 (-) | | 4 |
| Depreciation charge in 2004 (-) | | 120 |
| Writedowns/writebacks on assets under finance lease contracts in 2004 (+ / -) | | - |
| Assets under finance lease contracts at December 31, 2004, net of writedowns of euro 26 million and accumulated depreciation of euro 344 million | | 1,419 |
| b) Assets purchased in 2004 | | |
| Total higher value of assets purchased, calculated according to the finance method, compared to their accounting net book value | | - |
| c) Prepaid expenses at December 31, 2004 | | |
| d) Liabilities | | |
| Implicit liabilities for finance lease transactions at December 31, 2003 (of which euro 82 million due within one year, euro 311 million due between two and five years and euro 1,392 million due beyond five years) | | 1,785 |
| Implicit liabilities arising in 2004 (+) | | 1 |
| Repayment of principal and assets purchased in 2004 (-) | | 94 |
| Implicit liabilities for finance lease transactions at December 31, 2004 (of which euro 108 million due within one year, euro 301 million due between two and five years and euro 1,319 million due beyond five years) | | 1,728 |
| e) Total gross effect at December 31, 2004 (a + b + c - d) | | (309) |
| f) Tax effect | | (75) |
| g) Balance sheet effect at December 31, 2004 of leasing transactions recognized using the finance method (e - f) | | (234) |

| STATEMENT OF INCOME EFFECT FOR THE YEAR 2004 | | (in millions of euro) |
|---|--|-----------------------|
| Reversal of installments on finance lease transactions | | (237) |
| Recognition of financial expenses on finance lease transactions | | 144 |
| Recognition of: | | |
| - depreciation charge: | | |
| • on outstanding contracts | | 123 |
| • on assets purchased | | |
| - writedowns/writebacks of assets under finance lease contracts | | |
| Effect on income before taxes | | (30) |
| Recognition of tax effect | | (11) |
| Statement of income effect for the year 2004 of leasing transactions recognized using the finance method | | (19) |

Had the sale and leaseback transactions resulting in a finance lease been accounted for using the finance method, shareholders' equity would have been lower by euro 239 million at December 31, 2004 and the net income for the year would have been lower by euro 20 million.

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■ LONG-TERM INVESTMENTS

euro 34,817,480 thousand

(euro 35,276,500 thousand at December 31, 2003)

Details are as follows:

| (in thousands of euro) | 12/31/2003 | 12/31/2004 |
|---|-------------------|-------------------|
| Equity investments in: | | |
| • subsidiaries | 33,188,395 | 33,771,061 |
| • affiliated companies | 450,394 | 245,740 |
| • other companies | 220,159 | 204,538 |
| | 34,858,948 | 34,221,339 |
| Advances on future capital contributions | 136,238 | 12,064 |
| Accounts receivable: | | |
| • subsidiaries | 67,098 | 448,326 |
| • affiliated companies | 54,490 | 25,544 |
| • other receivables | 157,428 | 107,909 |
| | 279,016 | 581,779 |
| Treasury stock | 2,298 | 2,298 |
| Total | 35,276,500 | 34,817,480 |

■ Equity investments

euro 34,221,339 thousand

Annexes 1 and 2 present the changes in each investment during 2004 and the corresponding values at the beginning and the end of the year, as well as the list of investments held in subsidiaries and affiliated companies in accordance with point 5 of art. 2427 of the Italian Civil Code.

The effects of the merger include the contribution of the investments held by the merged company IT Telecom at December 31, 2003 (euro 47,820 thousand).

In summary, investments in subsidiaries, affiliates and other companies decreased by euro 637,609 thousand compared to December 31, 2003, as illustrated in the following tables:

| INCREASES: | (in thousands of euro) |
|---|------------------------|
| • Acquisition of the following equity investments at January 1, 2004, subsequent to the merger by absorption of IT Telecom S.p.A. in Telecom Italia S.p.A.: Webegg (46,595), Shared Services Center (613), Eustema (465), Telecom Italia Media (102), Consorzio Turistel (26), Consorzio Iris (15), Path.NET (3) and Added (1) | 47,820 |
| • Contribution of the Data Center business segment to IT Telecom S.r.l. by IT Telecom S.p.A. | 132,743 |
| • Subscription to capital increases, recapitalizations and loss coverage of: Telecom Italia Media (71,616), Latin American Nautilus (40,801), Sky Italia (19,315), Teco Soft Argentina (6,671), Telecom Italia Learning Services (6,406), Telesoft Zao Russia (4,148), Edotel (1,459), EUROFLY SERVICES (1,334), Iridium (945), Shared Services Center (306), IT Telecom S.r.l. (30), Consorzio S.I.A.R.C (1), IM.SER (125), Telbios (993), Consorzio ABI LAB (1), Consorzio DISTRETTO AUDIOVISIVO and ICT (5) | 154,156 |
| • Subscription to capital increase by Telecom Italia Finance through the contribution of the investment in Edotel and advances on future capital contributions of Edote | 1,500,824 |
| • Definitive capital increase from advances on future capital contributions relating to IT Telecom (110,440), Sky Italia (43,780), Edotel (1,200) and Netesi (435) | 155,855 |
| • Writebacks of value di Olivetti Tecnost (49,274), Iridium (775) and Edotel (46) | 50,095 |
| • Reclassification of TIM ordinary shares in current assets to long-term investments | 198,255 |
| Total increases | (A) 2,239,748 |

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DECREASES:

(in thousands of euro)

| | |
|---|------------------------|
| <ul style="list-style-type: none"> • Sales/reductions of shares/quotas in: Sky Italia (87,859), Mirror International Holding (54,689), Webegg (46,595), Atesia (2,665), Siosistemi (1,600), Pirelli Real Estate (15,199) and TILAB GP (9) | (208,616) |
| <ul style="list-style-type: none"> • Distribution of reserves of: Telecom Italia International (1,800,000), Tiglio I (72,206), Tiglio II (24,735) and Olivetti Gestioni Ivrea (4,849) | (1,901,790) |
| <ul style="list-style-type: none"> • Cancellation of the investment in IT Telecom following the merger by absorption of the same company | (167,090) |
| <ul style="list-style-type: none"> • Writedowns for losses of value charged to the statement of income of: Telecom Italia International (256,990), Telecom Italia Media (112,416), Finsiel (138,680), Latin American Nautilus (42,774), Telecom Italia Learning Services (6,406), LI.SIT. (5,993), Telbios (3,178), Olivetti Gestione Ivrea (euro 508), PAR.FIN (256), Netesi (79), Cartesia (50), TILAB SA (48), TILAB GP (12) and Med-1 (5) | (567,395) |
| <ul style="list-style-type: none"> • Writedowns for losses of value covered by the reserve for losses of subsidiaries and affiliates of: Eurofly Service (2,028), IM.SER (168), Consorzio S.I.A.R.C. (1), Consorzio CO.TIM (2), Consorzio CI.MARK (3), Consorzio di BIOINGEGNERIA ED INFORMATICA MEDICA (15), Consorzio GE.SE.CE.DI. (73), Consorzio NETTUNO (41) and Added (1) | (2,332) |
| <ul style="list-style-type: none"> • Writedowns for losses of value covered by the allowance for doubtful accounts of Sky Italia (19,315), Teco Soft Argentina (6,671) and Telesoft Zao Russia (4,148) | (30,134) |
| Total decreases | (B) (2,877,357) |
| Net change for the year | (A-B) (637,609) |

In particular, the following should be mentioned:

- on February 20, 2004, the Shareholders' Meetings of Olivetti International S.A. and Telecom Italia Finance approved the plan for the merger of Olivetti International S.A. in Telecom Italia Finance. Following this transaction, Telecom Italia Finance issued 30,000,000 new shares to Telecom Italia (the sole shareholder of Olivetti International S.A.) in exchange for the shares of the merged company. The merger is effective for accounting purposes as from January 1, 2004;

- on September 28, 2004, Telecom Italia sold its 19.9% interest in Sky Italia to the NewsCorp group. Consideration on the sale was euro 88 million. The transaction resulted in a gain over the carrying value at June 30, 2004 of euro 31.4 million which offsets the effect of the writedown made in the first half of the year. Accordingly, the economic impact of the transaction for Telecom Italia is basically nil;

- under the second stage of the Tiglio project (which calls for an end to the process of appreciating the real estate assets held by Tiglio I and Tiglio II by contributing the assets to real estate funds or concluding individual sale transactions), the affiliated company Tiglio I contributed real estate assets: i) to "TECLA - FONDO UFFICI" made up of 65 properties for a total market value of about euro 926 million, to which a 15% discount was applied by virtue of their transfer en masse, in addition to a cash contribution of euro 25 million and ii) to "CLOE FONDO UFFICI", made up of 39 properties for a total market value of euro 877 million, to which a 15% discount was applied by virtue of their transfer en masse.

With reference to "TECLA - FONDO UFFICI", its placement was concluded on March 1, 2004. The total placement offer, net of indebtedness of 60% of the value contributed, was equal to euro 288 million. 10% of this amount – as a voluntary gesture – was kept by Tiglio I, 2% was subscribed by Pirelli & C. Real Estate Sgr S.p.A., as manager of the fund, while the remaining 88% was entirely placed on the market.

As for "CLOE - FONDO UFFICI", placed on the market on June 29, 2004, the offer totaled euro 298 million. 5% was subscribed by Pirelli & C Real Estate Sgr S.p.A. as manager of the fund, while the remaining 95% was entirely placed with Italian investors for about 70%, and foreign investors for about 30%.

On October 7, 2004, the company "Tiglio II" signed a deed for the contribution of three properties to "FONDO SHOPS OLINDA - a closed-end investment fund". The placement of the shares of this Fund – directed to professional investors and the public at large – ended on December 6, 2004 and was officially listed on December 9, 2004. The Fund was entirely placed with European investors.

The companies Tiglio I and Tiglio II also contributed to the "CLARICE LIGHT INDUSTRIAL" Fund, placed with European investors on December 16, 2004, 27 properties and 43 properties, respectively, for a total market value of euro 221 million, to which a 9% discount was applied by virtue of their transfer en masse. The contribution value was thus equal to euro 201 million and the value of the Fund, after taking into account a financial indebtedness of approx. 55% of the contribution value, was about euro 90 million.

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Following these transactions, in 2004, Tiglio I and Tiglio II proceeded to distribute cash to Telecom Italia in the form of a reimbursement of capital (additional paid-in capital), respectively, for euro 72,206 thousand and euro 24,735 thousand;

- for purposes of bringing Telecom Italia Finance's financial position into equilibrium, by transferring liquidity from Telecom Italia International, the following transactions took place during the month of September 2004:
 - purchase, by Telecom Italia, of 40% of the investment in Edotel held by TIM for euro 1,939 thousand. After this transaction, Telecom Italia's holding in Edotel rose from 60% to 100%;
 - distribution of additional paid-in capital by Telecom Italia International to Telecom Italia for euro 1,800,000 thousand;
 - advance on future capital contribution for euro 1,500,000 thousand made by Telecom Italia to Edotel.

In October 2004, Telecom Italia subscribed to Telecom Italia Finance's capital increase by contributing the investment in Edotel;

- December 31, 2004 marked the date of the execution of the merger of the wholly-owned subsidiaries IT Telecom S.p.A. and EPIClink S.p.A. in Telecom Italia. This plan falls under a broader reorganization of the Information Technology Group area.

The merger is effective for accounting and tax purposes as from January 1, 2004.

On December 30, 2004, IT Telecom S.p.A. conferred its Data Center business segment to a newly formed company called IT Telecom S.r.l.. The value of the company complex transferred was equal to euro 132,743 thousand;

- some investments in subsidiaries and affiliated companies are recorded at a amount in excess of the corresponding share of the underlying shareholders' equity, net of dividends and after consolidation adjustments. These investments are maintained at their carrying values since they are expected to show future earnings and their assets are worth more than their respective book values. In particular, with regard to the investment in TIM, the higher carrying value compared to the underlying net equity and the stock market price is due to the allocation of the merger deficit on the Olivetti - Telecom Italia merger. However, taking into account the current strategic positioning of the business as well as its potential for further growth, it is believed, consistent with a recent valuation conducted by an external consultant, that the carrying value is aligned to the effective value of the investment.

A comparison between the market price of listed shares at December 31, 2004 and their carrying value shows an unrealized loss of euro 1,368,716 thousand (of which euro 1,437,105 thousand can be ascribed to the investment held in TIM). Further details are given in Annex 3.

■ Advances on future capital contributions euro 12,064 thousand

Advances on future capital contributions decreased by euro 124,174 thousand, compared to December 31, 2003, and are shown net of the relative allowance accounts of euro 4,140 thousand.

The decrease since December 31, 2003 is principally attributable to the cancellation of the advances on future capital contributions made to IT Telecom (euro 110,440 thousand) and EPIClink (euro 10,938 thousand).

This caption includes advances made to Telegono (8,840 thousand) and Loquendo (euro 3,224 thousand).

■ Accounts receivable euro 581,779 thousand

Accounts receivable increased by euro 302,763 thousand compared to December 31, 2003. Details are as follows:

| | 12/31/2003 | Changes during the year | | | | 12/31/2004 |
|------------------------|----------------|--------------------------------------|--------------------|---------------------|------------------|----------------|
| | | IT Telecom and EPIClink merger | Disburse- ments | Reimbur- sements | Other changes | Total |
| (in thousands of euro) | | | | | | |
| Accounts receivables: | | | | | | |
| • subsidiaries | 67,098 | | 4,302 | - | 376,926 | 381,228 |
| • affiliated companies | 54,490 | | 1,569 | (21,578) | (8,936) | (28,945) |
| • other receivables | 157,428 | 8,654 | 21,456 | (78,431) | (1,199) | (49,520) |
| | 279,016 | 8,654 | 27,327 | (100,009) | 366,791 | 302,763 |
| | | | | | | 581,779 |

Subsidiaries euro 448,326 thousand

Accounts receivables from subsidiaries refer mainly to TIM (euro 376,308 thousand) – as a result of the adoption of the consolidated national tax return procedure – and loans made to *TIM Hellas, for the acquisition of the UMTS license (euro 60,000 thousand)* and to *Mediterranean Nautilus (euro 10,470 thousand)*, to meet financial requirements.

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Affiliated companies

euro 25,544 thousand

Accounts receivable from affiliated companies refer mainly to loans made to the companies Aree Urbane (euro 20,074 thousand), Telegono (euro 2,800 thousand) and Tiglio II (euro 2,628 thousand) for the purchase of properties.

Other receivables

euro 107,909 thousand

Other receivable mainly refer to:

- the remaining loans receivable from employees (euro 54,941 thousand);
- the prepayment of the tax on the reserve for employee termination indemnities (euro 48,905 thousand), required under Law No. 662 dated December 23, 1996, revalued as set forth by law;
- security deposits of euro 3,517 thousand.

As regards accounts receivable included in long-term investments, the portion due within and beyond five years is presented in the attached Annex 4.

■ Treasury stock

euro 2,298 thousand

Treasury stock remains unchanged compared to December 31, 2003. Treasury stock refers to 1,272,014 ordinary shares originally held by ex-Olivetti.

* * *

As required by Article 10 of Law No. 72/1983 the table below sets forth a breakdown of upward adjustments by type of asset held at December 31, 2004.

| Description (in thousands of euro) | Fixed assets | | | | | Equity investments | | |
|---|--------------------|---------------------|--|--------------------|--|--------------------|-------------------|----------------|
| | Land and buildings | Plant and machinery | Manufacturing and distribution equipment | Other fixed assets | Construction in progress and advances to suppliers | Total | Subsidiaries | Affiliates |
| Historical cost of additions to 12/31/2004: | | | | | | | | |
| - Upward adjustments under special laws | 685,133 | 1,958,393 | 3,451 | 7,900 | - | 2,654,877 | 762,440 | 2,417 |
| - Not revalued | 1,384,871 | 45,773,542 | 538,734 | 1,421,555 | 440,936 | 49,559,638 | 37,009,048 | 280,623 |
| Total | 2,070,004 | 47,731,935 | 542,185 | 1,429,455 | 440,936 | 52,214,515 | 37,771,488 | 283,040 |
| Upward adjustments: | | | | | | | | |
| - under Law No. 74 of 2/11/1952 | 210 | - | - | - | - | 210 | 374 | - |
| - under Law No. 823 of 12/19/1973 | 1,007 | - | - | - | - | 1,007 | 546 | - |
| - under Law No. 576 of 12/2/1975 | 20,399 | 26,985 | 299 | 481 | - | 48,164 | 11,801 | - |
| - under Law No. 72 of 3/19/1983 | 160,601 | 696,082 | 2,391 | 3,755 | - | 862,829 | 65,603 | 1,424 |
| - under Law No. 413 of 12/30/1991 | 208,990 | - | - | - | - | 208,990 | - | - |
| - Voluntary revaluation 1981 | - | - | - | - | - | - | 17,436 | - |
| Total | 391,207 | 723,067 | 2,690 | 4,236 | - | 1,121,200 | 95,760 | 1,424 |
| Grand total | 2,461,211 | 48,455,002 | 544,875 | 1,433,691 | 440,936 | 53,335,715 | 37,867,248 | 284,464 |

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CURRENT ASSETS

■ INVENTORIES

euro 144,675 thousand

(euro 88,535 thousand at December 31, 2003)

Inventories consist of the following:

| (in thousands of euro) | 12/31/2003 | 12/31/2004 |
|--------------------------|---------------|----------------|
| Contract work in process | 23,341 | 31,189 |
| Merchandise | 65,194 | 113,486 |
| Total | 88,535 | 144,675 |

Inventories increased by euro 56,140 thousand compared to December 31, 2003 principally due to higher inventories connected with the marketing of Aladino cordless phones and videophones.

In 2004, the "contract work in process" of the merged company IT Telecom was reclassified to "increases in capitalized internal construction costs".

■ ACCOUNTS RECEIVABLE

euro 9,923,296 thousand

(euro 12,306,160 thousand at December 31, 2003)

Accounts receivable decreased by euro 2,382,864 thousand compared to December 31, 2003. A breakdown and the changes that occurred during the year are provided in the table below:

| | 12/31/2003 | Changes during the year | | | | | 12/31/2004 |
|--|-------------------|--------------------------------------|---------------|------------------|--------------------|--------------------|------------------|
| (in thousands of euro) | | IT Telecom and EPIClink merger | Utilizations | Provisions | Other | Total changes | |
| Trade accounts receivable | 4,021,325 | 34,697 | | | (588,242) | (553,545) | 3,467,780 |
| allowance for doubtful accounts | (317,875) | (14,981) | 87,541 | (101,456) | | (28,896) | (346,771) |
| Total trade accounts receivable | 3,703,450 | 19,716 | 87,541 | (101,456) | (588,242) | (582,441) | 3,121,009 |
| Accounts receivable from subsidiaries | 3,078,742 | (183,874) | - | - | (231,156) | (415,030) | 2,663,712 |
| allowance for doubtful accounts of subsidiaries | (3,453) | | - | - | 3,453 | 3,453 | - |
| Total accounts receivable from subsidiaries | 3,075,289 | (183,874) | - | - | (227,703) | (411,577) | 2,663,712 |
| - of which financial receivables | 823,919 | (266,221) | - | - | 149,254 | (116,967) | 706,952 |
| Accounts receivable from affiliated companies | 123,574 | 4,719 | - | - | (1,818) | 2,901 | 126,475 |
| allowance for doubtful accounts of affiliated companies | (26,800) | - | - | 26,800 | 26,800 | - | |
| Total accounts receivable from affiliated companies | 96,774 | 4,719 | - | - | 24,982 | 29,701 | 126,475 |
| - of which financial receivables | 13,718 | - | - | (13,605) | (13,605) | 113 | |
| Taxes receivable | 1,362,329 | 10,797 | - | - | (878,808) | (868,011) | 494,318 |
| Deferred tax assets | 3,229,916 | 665 | - | - | (839,118) | (838,453) | 2,391,463 |
| Other receivables | 838,402 | 10,510 | - | - | 277,407 | 287,917 | 1,126,319 |
| Government and other public entities | | | | | | | |
| for grants and subsidies | 30,748 | 1,043 | - | - | (4,662) | (3,619) | 27,129 |
| Other receivables | 860,176 | 9,467 | - | - | 265,491 | 274,958 | 1,135,134 |
| allowance for doubtful accounts | (52,522) | - | - | - | 16,578 | 16,578 | (35,944) |
| Total | 12,306,160 | (137,467) | 87,541 | (101,456) | (2,231,482) | (2,382,864) | 9,923,296 |

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■ Trade accounts receivable

euro 3,121,009 thousand

Trade accounts receivable decreased by euro 582,441 thousand compared to December 31, 2003 and are shown net of the relative allowance accounts (euro 346,771 thousand, of which euro 101,456 thousand was provided during the year). The caption includes euro 605,380 thousand of receivables due from other wireline and mobile telecommunications operators.

The change from December 31, 2003 is chiefly due to transactions for the sale of accounts receivable to factoring companies during 2004, described in the following paragraphs.

Accounts receivable securitization and factoring transactions show that:

Securitization

The program for the securitization of trade accounts receivable generated by services rendered to Telecom Italia Wireline clientele begun during 2001 has continued in 2004.

During 2004, the total amount of trade accounts receivable sold under the securitization program was equal to euro 8,821 million and refers to Telecom Italia's receivables from consumer and microbusiness customers. At December 31, 2004, receivables sold amount to euro 808,961 thousand (euro 874,368 thousand at December 31, 2003), of which euro 773,000 thousand is not yet due.

The securitization transaction led to a reduction in net financial indebtedness of euro 785,946 thousand at December 31, 2004 (euro 851,302 thousand at December 31, 2003).

Furthermore, Telecom Italia posted a short-term financial payable (euro 211,660 thousand) for loans made by TI Securitisation Vehicle S.r.l. out of the excess liquid resources generated by the securitization transaction.

Factoring

In 2004, trade accounts receivable without recourse were sold to leading factoring companies for a total amount of euro 877,950 thousand (euro 379,271 thousand at December 31, 2003). Factoring transactions by Telecom Italia led to a reduction in net financial indebtedness at December 31, 2004 of euro 912,258 thousand (euro 334,909 thousand at December 31, 2003).

■ Accounts receivable from subsidiaries

euro 2,663,712 thousand

Accounts receivable from subsidiaries include trade, financial and other receivables and decreased by euro 411,577 thousand, compared to December 31, 2003, partly on account of the cancellation of the receivables from IT Telecom.

Financial receivables, equal to euro 706,952 thousand, reflect current account transactions carried out at market rates for cash management purposes and loans. They principally include accounts receivable from *Olivetti Tecnost* (euro 460,000 thousand), *Telecom Italia Media* (euro 173,180 thousand) and *Telecom Italia Learning Services* (euro 27,210 thousand). Trade accounts receivable (euro 493,728 thousand) relate to TLC services rendered mainly to *TIM* (euro 204,364 thousand), *Telecom Italia Sparkle* (euro 69,555 thousand), *Finsiel* (euro 24,761 thousand), *Telecom Italia Media* (euro 49,870 thousand), *Olivetti Tecnost* (euro 20,814 thousand), *Path.Net* (euro 16,781 thousand) and *Telecom Italia Learning Services* (euro 26,254 thousand) and management fees receivable from *Telecom Italia International* (euro 22,929 thousand). Other receivables (euro 1,463,032 thousand) mainly include the accrual for dividends from subsidiaries (euro 1,382,278 thousand), details of which are presented in the note on "income from equity investments" in the statement of income and receivables connected with the Group's VAT settlement system, specifically from *TIM* (euro 20,899 thousand) and *Telecom Italia Sparkle* (euro 27,877 thousand).

■ Accounts receivable from affiliated companies

euro 126,475 thousand

Accounts receivable from affiliated companies include trade, financial and other receivables and increased by euro 29,701 thousand compared to December 31, 2003.

Financial receivables total euro 113 thousand. Trade accounts receivable (euro 114,444 thousand) refer in particular to *Teleleasing* (euro 66,891 thousand) for the sale of TLC products and services and *LI.SIT* (euro 30,953 thousand) for the supply of health cards to the Lombardy Region. Other receivables (euro 11,918 thousand) mainly refer to transactions with *Tiglio I* (euro 7,035 thousand) and *LI.SIT* (euro 4,594 thousand).

In 2004, the allowance for doubtful accounts was completely utilized following the waiver of receivables due by the Telecom Italia Group from Sky Italia, sold on September 28, 2004.

■ Taxes receivable

euro 494,318 thousand

Taxes receivable decreased by euro 868,011 thousand, compared to December 31, 2003, mainly due to the sale of IRPEG receivables of euro 1,294,000 thousand to TIM to be used to pay the 2004 on-account payment for IRES taxes.

They specifically include:

- direct income taxes receivable, euro 452,827 thousand, of which euro 431,032 thousand is the result of the adoption of the consolidated national tax return procedure;
- VAT receivable, euro 11,961 thousand;
- other indirect taxes receivable, euro 18,483 thousand.

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■ Deferred tax assets

euro 2,391,463 thousand

These are shown net of the reserve for deferred taxes (euro 26,243 thousand).

The nominal tax rates in Italy are 33% for the Corporate Income Tax (IRES), introduced beginning January 1, 2004 by Legislative Decree No. 344/2003, and 4.25% for the Regional Tax on Production Activities (IRAP), calculated on a different taxable base.

Deferred tax assets and liabilities at December 31, 2004 take into account these rates.

The balance of deferred tax assets and liabilities is made up as follows:

| (in thousands of euro) | 12/31/2003 Amounts due | | | | 12/31/2004 Amounts due | | | |
|----------------------------|---------------------------|-------------------------|-------------------|-----------|---------------------------|-------------------------|-------------------|-----------|
| | Within 1 year | From 2 to 5 years | Beyond 5 years | Total | Within 1 year | From 2 to 5 years | Beyond 5 years | Total |
| Deferred tax assets | 1,187,523 | 2,065,247 | - | 3,252,769 | 1,329,119 | 1,088,587 | - | 2,417,706 |
| Reserve for deferred taxes | (12,745) | (10,109) | - | (22,854) | (16,575) | (9,668) | - | (26,243) |
| Net receivable balance | 1,174,778 | 2,055,138 | - | 3,229,916 | 1,312,544 | 1,078,919 | - | 2,391,463 |

Details of the major components, divided by nature, constituting the net receivable balance of deferred tax assets and changes from the prior year are presented in the following table:

| (in thousands of euro) | 12/31/2003 | Benefit Stmt. of Income | Charge Stmt. of Income | 12/31/2004 |
|---|------------|----------------------------|---------------------------|------------|
| Deferred tax assets, details: | | increase | decrease | |
| Reserves for risks and charges | 153,640 | 32,277 | (89,027) | 96,890 |
| Allowance for doubtful accounts | 101,365 | 37,547 | (56,012) | 82,900 |
| Investment writedowns and other | 2,446,720 | 98,115 | (814,020) | 1,730,815 |
| Tax losses | 505,671 | 212,487 | (267,552) | 450,606 |
| Other deferred tax asset items | 45,373 | 50,109 | (38,988) | 56,494 |
| Deferred tax liabilities, details: | | decrease | increase | |
| Deferred tax gains | (21,491) | 12,406 | (4,071) | (13,156) |
| Dividends | (439) | 0 | (763) | (1,202) |
| Accumulated accelerated depreciation | (318) | 318 | 0 | 0 |
| Other deferred tax liability items | (605) | 3,608 | (14,888) | (11,885) |
| Total: | | | | |
| Net balance in balance sheet | 3,229,916 | 446,867 | (1,285,321) | 2,391,463 |
| Net effect | | (838,454) | | |
| of which: | | | | |
| - booked to statement of income | | (941,112) | | |
| - booked to balance sheet | | +102,658 | | |

Specifically, the main items which give rise to deferred taxes are the investment writedowns made in 2002 and 2003 as a result of applying Legislative Decree 209/2002, as well as the residual tax losses from 2003 which at December 31, 2004 amount to euro 1,365,486 thousand and led to the posting of deferred tax assets since their utilization by 2008 (the year in which utilization of the losses expire) is considered reasonably certain.

At December 31, 2004, some euro 201,723 thousand of deferred tax assets have not been booked in the financial statements since their recoverability is not reasonable assured.

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The main items, divided by nature, which constitute deferred tax assets that have not been booked are as follows:

| (in thousands of euro) | 12/31/2004 |
|---|----------------|
| Inventories | 3,754 |
| Reserves for risks and charges | 69,905 |
| Allowance for doubtful accounts | 28,490 |
| Sundry writedowns | 60,445 |
| Accumulated depreciation accounts exceeding tax limit | 9,433 |
| Other deferred tax asset items | 29,696 |
| Total | 201,723 |

At December 31, 2004, the company has tax-deferred capital reserves which are subject to taxation in the event of distribution and/or utilization for euro 2,352,930 thousand. No taxes have been set aside on these tax-deferred reserves since no transactions are expected to be entered into that would warrant their distribution or utilization.

■ Other receivables

euro 1,126,319 thousand

Other receivables amount to euro 1,126,319 thousand and particularly refer to the receivable from the Financial Administration for the accrual of prior period income relating to the TLC license fee and the relative interest paid by Telecom Italia for the year 1999 (euro 410,838 thousand) as a result of the decision handed down by the TAR of Lazio No. 47/2005 of January 4, 2005, which upheld the appeal filed by Telecom Italia and cancelled the Ministerial Decree dated March 21, 2000 regarding the TLC fee instituted by Law 448/1998 declaring it to be illegal.

Other receivables also include:

credit positions (net of the relative allowance account) due from TI Securitisation Vehicle S.r.l. for the deferred portion of trade accounts receivable securitization transactions (euro 262,327 thousand), receipts from customers in transit with the banking and postal systems (euro 78,029 thousand), employee-related receivables (euro 61,593 thousand), receivables from the Ministry of Industry, Commerce and Handicrafts, the European Union and the Ministry of Instruction, University and Research for grants in respect of research and training projects (euro 27,129 thousand) and advances to suppliers (euro 24,403 thousand).

In 2004, Telecom Italia sold receivables for interest accrued on IRPEG receivables from the Ministry of Finance which had been sold to primary factoring companies, for a total amount of euro 30,471 thousand.

* * *

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of receivables by geographical area is presented in Annex 6.

■ SHORT-TERM FINANCIAL ASSETS

euro 60 thousand

(euro 182,390 thousand at December 31, 2003)

The composition and changes during the year are shown in the following table:

| | 12/31/2003 | Changes during the year | | | | 12/31/2004 |
|------------------------------------|----------------|-------------------------|--|--------------------------------|------------------|------------|
| | | Acquisitions | Sales/ reimburse- ments/other movements | Writed- owns/ Writebacks | Total changes | |
| (in thousands of euro) | | | | | | |
| Equity investments in subsidiaries | 166,190 | 5 | (198,255) | 32,112 | (166,138) | 52 |
| Other equity investments | 21 | - | - | (13) | (13) | 8 |
| Other securities | | | | | | |
| - sundry | 16,179 | - | (16,179) | - | (16,179) | - |
| Total | 182,390 | 5 | (214,434) | 32,099 | (182,330) | 60 |

At December 31, 2004, short-term financial assets total euro 60 thousand and include euro 52 thousand for Telecom Italia Media savings shares and euro 8 thousand for Portal Software shares both purchased for trading purposes.

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In 2004, the 38,192,000 TIM shares were revalued by euro 32,119 thousand to adjust them to market value, and later reclassified to long-term financial assets.

Further details are provided in Annex 3.

■ LIQUID ASSETS

euro 5,424,059 thousand

(euro 205,251 thousand at December 31, 2003)

Liquid assets are composed of the following:

| | 12/31/2003 | Changes during the year | | | 12/31/2004 |
|----------------------------|----------------|--------------------------------------|--------------------|------------------|------------------|
| | | IT Telecom and EPIClink merger | Other movements | Total changes | |
| (in thousands of euro) | | | | | |
| Bank and postal accounts | 204,635 | 262 | 5,218,603 | 5,218,865 | 5,423,500 |
| Checks | 47 | - | (12) | (12) | 35 |
| Cash and valuables on hand | 569 | 14 | (59) | (45) | 524 |
| Total | 205,251 | 276 | 5,218,532 | 5,218,808 | 5,424,059 |

Liquid assets total euro 5,424,059 thousand and increased by euro 5,218,808 thousand following the increase of cash resources in Italian and foreign bank accounts partly as a result of the loans received in October from Telecom Italia Capital. The choice of the type of investment of the liquidity was essentially due to the need to have liquid resources available for the partial payment of the price on the shares tendered under the cash tender offer for TIM shares.

ACCRUED INCOME AND PREPAID EXPENSES

euro 550,984 thousand

(euro 563,811 thousand at December 31, 2003)

Accrued income and prepaid expenses decreased by euro 12,827 thousand compared to December 31, 2003, and include the following:

| | 12/31/2003 | Changes during the year | | | 12/31/2004 |
|--|----------------|--------------------------------------|------------------|------------------|----------------|
| | | IT Telecom and EPIClink merger | Other changes | Total changes | |
| (in thousands of euro) | | | | | |
| Issue discounts and similar charges | 110,622 | - | (7,790) | (7,790) | 102,832 |
| Accrued income | | | | | |
| - financial | 20,423 | - | 40,049 | 40,049 | 60,472 |
| - other | 275 | - | 4,394 | 4,394 | 4,669 |
| | 20,698 | - | 44,443 | 44,443 | 65,141 |
| Other prepaid expenses | | | | | |
| - trade | 90,299 | 2,285 | (5,172) | (2,887) | 87,412 |
| - financial | 325,261 | - | (54,751) | (54,751) | 270,510 |
| - other | 16,931 | - | 8,158 | 8,158 | 25,089 |
| | 432,491 | 2,285 | (51,765) | (49,480) | 383,011 |
| Accrued income and other prepaid expenses | 453,189 | 2,285 | (7,322) | (5,037) | 448,152 |
| Total | 563,811 | 2,285 | (15,112) | (12,827) | 550,984 |

■ Issue discounts and similar charges

euro 102,832 thousand

"Issue discounts and similar charges" refer to incidental costs on loans (euro 62,581 thousand) and costs relating to the issue of bonds (euro 40,251 thousand).

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■ Accrued income and other prepaid expenses

euro 448,152 thousand

Accrued financial income (euro 60,472 thousand) mainly includes euro 53,086 thousand of income on derivative financial instruments, euro 3,917 thousand of sundry financial income from banks, as well as euro 1,326 thousand of interest income subsidized until 1991 by the government under Law No. 67/1988, equivalent to three percentage points of the cost of the loans which replaced those assigned to the Company, through Cassa Depositi e Prestiti, under Law No. 887/1984.

Prepaid expenses (euro 383,011 thousand) mainly pertain to building rents (euro 37,060 thousand); financial expenses (euro 270,510 thousand) for the portion of the premium on the redemption of convertible bonds relating to future years, fees regarding facilities (euro 27,433 thousand), insurance premiums (euro 32,258 thousand) and rental and maintenance charges (euro 9,229 thousand).

* * *

A breakdown of receivables and accrued income by maturity and type is presented in Annex 4.

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■ BALANCE SHEETS - LIABILITIES AND SHAREHOLDERS' EQUITY

SHAREHOLDERS' EQUITY

euro 16,810,562 thousand

(euro 16,356,111 thousand at December 31, 2003)

Shareholders' equity includes the following:

| (in thousands of euro) | 12/31/2003 | 12/31/2004 |
|--|-------------------|-------------------|
| Share capital | 8,853,991 | 8,864,857 |
| Additional paid-in capital | 88,377 | 120,380 |
| Reserves for inflation adjustments - Law No. 413, 12/30/1991 | - | 1,129 |
| Legal reserve | 1,834,687 | 1,953,494 |
| Reserve for treasury stock in portfolio | 2,298 | 2,298 |
| Miscellaneous reserves | | |
| - Reserve Law No. 488/1992 | 118,678 | 142,365 |
| - Reserve L.D. 124/1993, ex art. 13 | 185 | 391 |
| - Reserve DPR No. 917/1986, ex art. 74 | 5,750 | 5,750 |
| - Reserve for capital grants | 498,701 | 510,993 |
| - Other reserves | 119,012 | 4,499 |
| - Merger surplus reserve | 2,188,529 | 2,188,529 |
| Retained earnings | - | 881,029 |
| Net income | 2,645,903 | 2,134,848 |
| Total | 16,356,111 | 16,810,562 |

■ SHARE CAPITAL

euro 8,864,857 thousand

The share capital of Telecom Italia S.p.A. at December 31, 2004 amounts to euro 8,864,857 thousand and consists of 10,322,001,069 ordinary shares and of 5,795,921,069 savings shares, all with a par value of euro 0.55 each.

Share capital increased by euro 10,866 thousand compared to December 31, 2003 due to the following movements:

- conversion of 2,588,322 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption" for the issue of 1,220,399 new shares for a par value of euro 671 thousand;
- exercise of 5,615,768 stock options set aside for employees of the company for the issue of 18,536,927 new shares for a par value of euro 10,195 thousand.

■ ADDITIONAL PAID-IN CAPITAL

euro 120,380 thousand

Additional paid-in capital amounts to euro 120,380 thousand at December 31, 2004, with an increase of euro 32,003 thousand compared to December 31, 2003. The change in this caption is due to the additional paid-in capital on the foregoing capital increases.

■ RESERVES FOR INFLATION ADJUSTMENTS - LAW NO. 413, 12/30/1991

euro 1,129 thousand

This reserve for inflation adjustments, which showed a nil balance at December 31, 2003 following its complete utilization to cover the loss for the year 2002 of the merging company Olivetti, was replenished at June 30, 2004, pursuant to the resolution passed by the Shareholders' Meeting on May 6, 2004.

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■ LEGAL RESERVE

euro 1,953,494 thousand

The legal reserve amounts to euro 1,953,494 at December 31, 2004 and shows an increase of euro 118,807 thousand compared to December 31, 2003 due to the reclassification from "Other reserves" to adjust the legal reserve to the amount required by law following any share capital increases as a result of either the exercise of stock options or the conversion of bonds.

■ RESERVE FOR TREASURY STOCK IN PORTFOLIO

euro 2,298 thousand

This reserve amounts to euro 2,298 thousand at December 31, 2004 and is unchanged from December 31, 2003.

■ MISCELLANEOUS RESERVES

euro 2,852,527 thousand

Miscellaneous reserves total euro 2,852,527 thousand at December 31, 2004, with a decrease of euro 78,329 thousand from December 31, 2003. The various components of miscellaneous reserves are analyzed in the following paragraphs.

■ Reserve Law No. 488/1992:

this reserve, equal to euro 142,365 thousand, increased by euro 23,687 thousand compared to December 31, 2003 as a result of the appropriation of net income for the year 2003, as voted by the Shareholders' Meeting on May 6, 2004, in order to obtain the benefits stated in Law 488/92 under the projects for investments in the south of Italy.

■ Reserve L.D. 124/1993, ex art. 13:

this reserve, equal to euro 391 thousand at December 31, 2004, increased by euro 205 thousand compared to December 31, 2003 due to the reclassification from Other reserves in order to replenish the tax-deferred reserves of the merged companies.

■ Reserve DPR No. 917/1986, ex art. 74:

this reserve, equal to euro 5,750 thousand at December 31, 2004, is unchanged from December 31, 2003.

■ Reserve for capital grants:

this reserve, equal to euro 510,993 thousand at December 31, 2004, increased by euro 12,291 thousand compared to December 31, 2003 due to the transfer from the "reserves for risks and charges" of the portion of grants that became available during the year.

■ Other reserves:

these reserves, equal to euro 4,499 thousand at December 31, 2004, consist solely of the Reserve for payments for future capital increases. The reduction of euro 114,513 thousand compared to December 31, 2003 is due to a combination of the following:

- payments relating to stock options exercised at December 2004 with the issue of shares in January 2005 (euro 3,206 thousand);
- conversions, made in December 2004, of convertible bonds 2001-2010, with effect in January 2005 (euro 1,293 thousand);
- the aforementioned reclassification of euro 205 thousand to the Reserve 124/1993, ex art. 13;
- the aforementioned reclassification of euro 118,807 thousand to the Legal reserve.

■ Merger surplus reserve:

this reserve, equal to euro 2,188,529 thousand at December 31, 2004, is unchanged compared to December 31, 2003.

■ RETAINED EARNINGS

euro 881,029 thousand

Retained earnings refer to the appropriation of net income for the year 2003 of euro 881,029 thousand, pursuant to the resolution passed by the Shareholders' Meeting of May 6, 2004

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In order to complete disclosure on shareholders' equity, the following statements are presented:

- statement showing the reserves subject to restrictions for statutory purposes and the tax treatment applicable in the event of distribution;
- statement prepared according to ex art. 2427, paragraph 7 - bis, showing the items in shareholders' equity separately according to their source, possibility of utilization and distribution, in addition to their utilization in prior years;
- statement of changes in shareholders' equity during the prior year and in 2004.

RESERVES IN SHAREHOLDERS' EQUITY - STATUTORY RESTRICTIONS AND TAX REGIME FOR PURPOSES OF INCOME TAXES

| | Amounts not subject to statutory restrictions | Amounts subject to statutory restrictions | December 31, 2004 | Amounts of reserves which, in the event of distribution, form part of the taxable income of the company | Amounts of other income reserves | Amount of reserves which, in the event of distribution, do not form part of the taxable income of the company |
|---|--|--|----------------------------------|--|---|--|
| (in thousands of euro) | (a) | (b) | (c) = (a + b) = = (d + e + f) | (d) | (e) | (f) |
| Reserves and retained earnings | | | | | | |
| Additional paid-in capital | 120,380 | - | 120,380 | - | - | 120,380 |
| Legal reserve | 180,523 | 1,772,971 | 1,953,494 | 1,834,667 | 643 | 118,184 |
| Reserve for treasury stock in portfolio | - | 2,298 | 2,298 | - | 2,298 | - |
| Merger surplus reserve | 2,176,987 | 11,542 | 2,188,529 | - | - | 2,188,529 |
| Reserve Law No. 488/92 | - | 142,365 | 142,365 | - | 122,090 | 20,275 |
| Reserve, L.D. No. 124/93, ex art. 13 | 391 | - | 391 | 391 | - | - |
| Reserve D.P.R. No. 917/86 ex art. 74 | 5,750 | - | 5,750 | 5,750 | - | - |
| Reserve for capital grants | 510,993 | - | 510,993 | 510,993 | - | - |
| Revaluation reserve Law No. 413/91 | 1,129 | - | 1,129 | 1,129 | - | - |
| Payments for future capital increases | - | 4,499 | 4,499 | - | - | 4,499 |
| Retained earnings | 881,029 | - | 881,029 | - | 881,029 | - |
| Total reserves and retained earnings | 3,877,182 | 1,933,675 | 5,810,857 | 2,352,930 | 1,006,060 | 2,451,867 |

The amount of distributable reserves without tax charges to be borne by the Company is equal to euro 3,297,223 thousand.

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STATEMENT EX ART. 2427, PARAGRAPH 7-BIS OF THE ITALIAN CIVIL CODE

| Nature/description | Amount | Possibility of utilization | Amount available | Summary of the amounts utilized during the last three years | |
|---|------------------|----------------------------|------------------|---|-------------------|
| | | | | for absorption of losses | for other reasons |
| (in thousands of euro) | | | | | |
| Share capital | 8,864,857 | | | 0 | 10,961 |
| Capital reserves: | | | | | |
| Additional paid-in capital | 120,380 | A, B, C | 120,380 | 3,700,751 | 0 |
| Legal reserve | 1,953,494 | A, B, C | 180,523 | 920,810 | 0 |
| Reserve Law No. 488/92 | 20,275 | A, B | 20,275 | 0 | 0 |
| Reserve, L.D. No. 124/93, ex art. 13 | 391 | A, B, C | 391 | 0 | 0 |
| Reserve D.P.R. No. 917/86 ex art. 74 | 5,750 | A, B, C | 5,750 | 0 | 0 |
| Reserve for capital grants | 510,993 | A, B, C | 510,993 | 0 | 0 |
| Payments for future capital increases | 4,499 | A, B | 4,499 | 0 | 0 |
| Miscellaneous reserves | 0 | A, B, C | 0 | 28,816 | 0 |
| Merger surplus reserve | 2,188,529 | A, B, C | 2,188,529 | 0 | 0 |
| Income reserves: | | | | | |
| Revaluation reserve Law No. 413/91 | 1,129 | A, B, C | 1,129 | 1,129 | 0 |
| Reserve for treasury stock in portfolio | 2,298 | - | 0 | 0 | 0 |
| Reserve Law No. 488/92 | 122,090 | A, B | 122,090 | 0 | 0 |
| Retained earnings | 881,029 | A, B, C | 881,029 | 0 | 0 |
| Total | | | 4,035,588 | 4,651,505 | 10,961 |
| Amount not distributable ⁽¹⁾ | | | 158,406 | | |
| Remaining amount distributable | | | 3,877,182 | | |

Key:

A: for share capital increase

B: for absorption of losses

C: for distribution to shareholders

(1) Represents the amount not distributable as a result of reserve Law No. 488/1992 (euro 142,365 thousand), for the part set aside to cover unamortized intangible assets according to ex art. 2426, paragraph 5 (euro 11,542 thousand), as well as the reserve for the Payments of future capital increases (euro 4,499 thousand).

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Statement of changes in shareholders' equity

| | Share capital | Capital increases awaiting registration in Companies Register | Additional paid-in capital | Additional paid-in capital on capital increases awaiting registration in Companies Register | Revaluation reserve Law No. 413/91 | Legal reserve | Reserve for treasury stock in portfolio | Reserve Law No. 488/92 | Reserve L.D. No. 124/93, ex art. 13 | Reserve D.P.R. No. 917/86 ex art. 74 | Special reserve | Reserve for capital grants | Payments for future capital increases | Miscellaneous reserves | Retained earnings | Retained earnings | Net income for the year | Total |
|--|---------------|---|----------------------------|---|------------------------------------|---------------|---|------------------------|-------------------------------------|--------------------------------------|-----------------|----------------------------|---------------------------------------|------------------------|-------------------|-------------------|-------------------------|------------|
| (in thousands of euro) | | | | | | | | | | | | | | | | | | |
| Balance at January 1, 2003 | 8,845,240 | 200 | 3,765,365 | 127 | 1,129 | 920,810 | 2,298 | | | | 1,888,261 | | 0 | 147,828 | (299,930) | (6,239,963) | 9,031,365 | |
| Appropriation of 2002 profit: | | | | | | | | | | | | | | | | | | |
| - Absorption of loss for the year (as voted by the Shareholders' Meeting of May 26, 2003) | | | (3,400,820) | (127) | (1,129) | (920,810) | | | | | (1,888,261) | | | (28,816) | | 6,239,963 | 0 | |
| Other changes: | | | | | | | | | | | | | | | | | | |
| - Absorption of the accumulated deficit (as voted by the Shareholders' Meeting of May 26, 2003) | | | (299,930) | | | | | | | | | | | | | 299,930 | | 0 |
| - Changes connected with the Olivetti - Telecom Italia merger | (10,961) | | | | | 20 | | | | | | | | | 4,633,630 | | | 4,622,689 |
| - Reclassification of merger surplus | | | | | | 1,834,667 | | 118,678 | 186 | 5,750 | | 485,821 | | (2,445,101) | | | | 0 |
| - Conversion of 385,731 "Telecom Italia 1.5% 2001-2004 convertible bonds with a premium on redemption" and 19,623,810 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption" | 13,456 | | 7,170 | | | | | | | | | | | | | | | 20,626 |
| - Exercise of stock options | 6,055 | | 16,592 | | | | | | | | | | | | | | | 22,647 |
| - Transfer from the "Reserves for risks and charges" of the portion of grants which became available during the year | | | | | | | | | | | | 12,880 | | | | | | 12,880 |
| - Other changes | 200 | (200) | | | | | | | | | | | | | | | | 0 |
| Net income for the year 2003 | | | | | | | | | | | | | | | | | 2,645,903 | 2,645,903 |
| Balance at December 31, 2003 | 8,853,991 | 0 | 88,377 | 0 | 0 | 1,834,687 | 2,298 | 118,678 | 186 | 5,750 | 0 | 498,701 | 0 | 119,012 | 2,188,529 | 0 | 2,645,903 | 16,356,111 |
| Appropriation of 2003 profit (as voted by the Shareholders' Meeting of May 6, 2004) | | | | | | | | | | | | | | | | | | |
| - Declaration of dividends (euro 0.1041 per ordinary share; euro 0.1151 per savings share) | | | | | | | | | | | | | | | | (1,740,058) | (1,740,058) | |
| - Other appropriations | | | | | 1,129 | | | 23,687 | | | | | | | 881,029 | (905,845) | | 0 |
| Other changes: | | | | | | | | | | | | | | | | | | |
| - Conversion of 3,881,157 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption" | 671 | | 1,916 | | | | | | | | | | 1,293 | | | | | 3,880 |
| - Exercise of stock options | 10,195 | | 30,087 | | | | | | | | | | | 3,206 | | | | 43,488 |
| - Exercise of warrants for ordinary shares of Telecom Italia ex Olivetti 1999-2004 | | | | | | | | | | | | | | | | | | 0 |
| - Transfer from the "Reserves for risks and charges" of the portion of grants which became available during the period | | | | | | | | | | | | 12,292 | | | | | | 12,292 |
| - Reclassification following the replenishment of the tax-deferred reserves of the merged company IT Telecom S.p.A. and the addition to the legal reserve | | | | | | 118,807 | | | 205 | | | | | -119,012 | | | | |
| Net income for the year 2004 | | | | | | | | | | | | | | | | | 2,134,848 | 2,134,848 |
| Balance at December 31, 2004 | 8,864,857 | 0 | 120,380 | 0 | 1,129 | 1,953,494 | 2,298 | 142,365 | 391 | 5,750 | 0 | 510,993 | 4,499 | 0 | 2,188,529 | 881,029 | 2,134,848 | 16,810,562 |

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Subsequent to December 31, 2004, on January 3 and 4, 2005, 1,304,947 shares of par value euro 718 thousand were issued plus additional paid-in capital of euro 1,967 thousand against requests presented previously to exercise 395,355.64 options of the ex-Telecom Italia "Stock Option Plan 1999". The rights relating to the remaining options of this Plan expired on December 31, 2004.

As far as future potential changes in share capital are concerned, at December 31, 2004, the following are still outstanding:

- 2,387,465,140 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption" (formerly known as "Olivetti 1.5% 2001-2010 convertible bonds with a premium on redemption"), including 1,292,835 bonds for which conversion into shares had already been requested on December 31, 2004, with the consequent reduction in the quantity of bonds still convertible with a contra-entry for a liability with future shareholders (the corresponding 609,625 ordinary shares for a par value of euro 335 thousand plus additional paid-in capital of euro 958 thousand were issued on January 14, 2005).
Such bonds originally allowed conversion into Olivetti shares, in a ratio of one Olivetti share for every bond converted.
As a result of the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital of the merging company and in light of the ratio indicated above, such bonds now allow the conversion to Telecom Italia shares in a ratio of 0.471553 Telecom Italia ordinary shares for every bond converted.
Against the above bonds that can still be converted, therefore, besides the above 609,625 shares, a further maximum 1,125,206,724 Telecom Italia ordinary shares could be issued, for a total par value of euro 618,864 thousand, plus additional paid-in capital of euro 1,767,309 thousand.
- 10,699,996 options of the ex-Telecom Italia "Stock Option Plan 2002".
Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at the price of euro 13.815 for every option exercised.
Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute share capital and on the basis of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about euro 4.185 per share.
Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 35,319,216 new Telecom Italia ordinary shares could be issued, for a total par value of euro 19,426 thousand, plus additional paid-in capital of euro 128,394 thousand.
- 31,980,000 options of the ex-Telecom Italia "Stock Option Plan 2001" .
Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 10.488 for every option exercised.
Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about euro 3.177 per share.
Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 105,561,230 new Telecom Italia ordinary shares could be issued, for a total par value of euro 58,059 thousand, plus additional paid-in capital of euro 277,346 thousand.
- 10,500,000.98 options of the ex-Telecom Italia "Stock Option Plan 2002 Top" .
Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 9.203 for every option exercised.
Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about 2.788 per share.
Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 34,659,130 new Telecom Italia ordinary shares could be issued, for a total par value of euro 19,063 thousand, plus additional paid-in capital of euro 77,569 thousand.
- 23,536,501.09 options of the ex-Telecom Italia "Stock Option Plan 2002", net of 53,999.69 options exercised against requests that had been received by December 31, 2004 (on January 4, 2005, the corresponding 178,246 shares were issued for a par value of euro 98 thousand, plus additional paid-in capital of euro 424 thousand).

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Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at the following prices for each option held: 22,556,501.01 options at a price of euro 9.665, 780,000.08 options at a price of euro 7.952 and 200,000.00 options at a price of euro 7.721.

Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of, respectively, about euro 2.928, about euro 2.409 and about euro 2.339 per share.

Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary and the different subscription prices, in addition to the above 178,246 shares, a further maximum 77,690,515 new Telecom Italia ordinary shares could be issued, for a total par value of euro 42,730 thousand, plus additional paid-in capital of euro 183,024 thousand.

The Shareholders' Meeting of May 6, 2004 also conferred the Board of Directors with the right (which, to date, has not been exercised), for a maximum period of five years beginning May 6, 2004, to increase against payment, at one or more times, the share capital for a maximum total amount of euro 880,000,000, through the issue of a maximum of 1,600,000,000 ordinary shares, in whole or in part

- (i) to be offered as option rights to the shareholders and convertible bondholders, or
- (ii) to be offered for subscription to the employees of Telecom Italia S.p.A. or to the companies which it controls, with the exclusion of the option rights, pursuant to the combined provision of art. 2441, last paragraph, of the Italian Civil Code, and art. 134, second paragraph, of Legislative Decree 58/1998.

The resolutions for capital increases passed by the Board of Directors in exercising the aforementioned right shall establish the subscription price (including any additional paid-in capital) and shall fix a specific deadline for the subscription of the shares; they may also provide that, in the event the increase voted by the Board is not subscribed to by the deadline set each time for that purpose, the capital shall be increased for an amount equal to the subscriptions received up to that deadline date.

RESERVES FOR RISKS AND CHARGES

euro 947,950 thousand

(euro 777,327 thousand at December 31, 2003)

The reserves for risks and charges increased by euro 170,623 thousand compared to December 31, 2003. The composition and changes in these reserves are described as follows:

| | 12/31/2003 | Changes during the year | | | | | 12/31/2004 |
|---|----------------|--------------------------------------|----------------|------------------|-----------------------|----------------------------------|------------------|
| (in thousands of euro)) | | IT Telecom and EPIClink merger | Provisions | Utilizations | Released to income | Reclassi- fications/ Other | Total changes |
| Reserve for taxes, reserve for deferred taxes | 119,410 | 500 | - | (26,841) | - | 75,478 | 49,137 |
| Other reserves | 657,917 | 35,033 | 325,784 | (197,559) | (15,934) | (25,838) | 121,485 |
| Reserve for litigation | 113,489 | 7,066 | 32,688 | (27,042) | (140) | - | 12,572 |
| Reserve for capital grants | 88,876 | - | - | - | - | (12,292) | (12,292) |
| Reserve for losses of subsidiaries and affiliates | 10,264 | 4,978 | 88,616 | (6,541) | (2,292) | - | 84,761 |
| Reserve for corporate restructuring | 121,144 | 6,094 | - | (75,442) | (3,345) | (500) | (73,193) |
| Reserve for contractual risks and other risks | 324,144 | 16,895 | 204,480 | (88,534) | (10,157) | (13,046) | 109,638 |
| Total | 777,327 | 35,533 | 325,784 | (224,400) | (15,934) | 49,640 | 170,623 |
| | | | | | | | 947,950 |

■ Reserve for taxes, reserve for deferred taxes

These reserves amount to euro 168,547 thousand and increased by euro 49,137 thousand compared to December 31, 2003. The utilizations refer to the payment of the tax amnesty for the income taxes for the year 2002 (ex Law 289/2002); reclassifications refer to adjustments made to the reserve during the year.

■ Other reserves

Other reserves amount to euro 779,403 thousand and decreased by euro 121,486 thousand compared to December 31, 2003.

In particular:

- the provision to the reserve for losses of subsidiaries and affiliates of euro 88,616 thousand is principally in reference to losses in excess of the carrying values of Mediterranean Nautilus, euro 46,447 thousand, Latin American Nautilus, euro 21,752 thousand, and Med 1, euro 13,249 thousand;
- the provision to the reserve for contractual risks and other risks mainly regards the sanction levied by the Antitrust Authority for the alleged abuse of a dominant position (euro 152,000 thousand).

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RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES

euro 1,042,919 thousand

(euro 972,413 thousand at December 31, 2003)

The reserve for employee termination indemnities increased by euro 70,506 thousand compared to December 31, 2003. The amount and changes during the year are presented below:

| | |
|--|------------------|
| (in thousands of euro) | |
| Balance at December 31, 2003 - Telecom Italia | 972,413 |
| IT Telecom and EPIClink merger | 57,939 |
| Changes during the year: | |
| – Provisions charged to income for amounts to fund employee termination indemnities accrued in favor of employees during the year plus the fixed and variable cost-of-living adjustments required under Law No. 297/1982 | 137,118 |
| – Utilizations for: | |
| • Indemnities paid to employees who took retirement or resigned during the year | (75,251) |
| • Advances | (15,407) |
| • Supplementary benefits (Telemaco) | (18,211) |
| • Equalization tax on the revaluation of the reserve | (3,069) |
| – Transfers to/from subsidiaries and other movements | (12,613) |
| Balance at December 31, 2004 | 1,042,919 |

LIABILITIES

euro 43,296,181 thousand

(euro 41,395,472 thousand at December 31, 2003)

Liabilities increased by euro 1,900,709 thousand compared to December 31, 2003. Details are as follows:

| | 12/31/2003 | Changes during the year | | | 12/31/2004 |
|---|-------------------|--------------------------------------|------------------|------------------|-------------------|
| | | IT Telecom and EPIClink merger | Other changes | Total changes | |
| (in thousands of euro) | | | | | |
| Debentures | 9,764,983 | - | 2,936,267 | 2,936,267 | 12,701,250 |
| Convertible debentures | 4,159,570 | - | (1,334,623) | (1,334,623) | 2,824,947 |
| Due to banks | 1,191,094 | 1,167 | (286,618) | (285,451) | 905,643 |
| Due to other lenders | 781,885 | - | 262,836 | 262,836 | 1,044,721 |
| Advances | 22,723 | 121 | 9,740 | 9,861 | 32,584 |
| Trade accounts payable | 1,929,794 | 397,975 | (295,673) | 102,282 | 2,032,076 |
| Accounts payable to subsidiaries | 20,543,520 | (522,125) | 706,911 | 184,786 | 20,728,306 |
| Accounts payable to affiliated companies | 84,771 | 30,743 | 109,345 | 140,088 | 224,859 |
| Taxes payable | 379,080 | 9,146 | (122,358) | (113,212) | 265,868 |
| Contributions to pension and social security institutions | 626,769 | 11,955 | (70,359) | (58,404) | 568,365 |
| Other liabilities | 1,911,283 | 53,646 | 2,633 | 56,279 | 1,967,562 |
| | 41,395,472 | (17,372) | 1,918,081 | 1,900,709 | 43,296,181 |

■ Debentures

euro 12,701,250 thousand

Debentures include the following:

- notes for euro 6,935,588 thousand issued under the “Global Note Program” as follows:
 - notes for euro 2,500,000 thousand, issued on February 1, 2002, divided into two tranches of euro 1,250,000 thousand each, at annual fixed rates, respectively, with a coupon of 5.625% maturing on February 1, 2007 and a coupon of 6.25% maturing on February 1, 2012. The issue is part of the “Global Medium Term Note Program”;

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- notes for euro 3,000,000 thousand, issued on January 29, 2004, divided into three tranches: the first, for euro 1,000,000 thousand, with an annual coupon indexed to the 3-month Euribor +0.33 basis points, maturing October 29, 2007; the second, for euro 750,000 thousand, with an annual fixed-rate coupon of 4.50%, maturing on January 28, 2011; the third, for euro 1,250,000 thousand, with an annual fixed-rate coupon of 5.375%, maturing on January 29, 2019;
- notes for euro 110,000 thousand issued on April 8, 2004 with a quarterly coupon equal to the 3-month Euribor rate +0.60%, maturing March 30, 2009;
- notes for GBP 850,000 thousand (equivalent to euro 1,205,588 thousand) issued on June 24, 2004, with a coupon of 6.375%, maturing June 24, 2019;
- notes for euro 120,000 thousand issued on November 23, 2004 with a quarterly coupon equal to the 3-month Euribor + 0.66%, maturing November 23, 2015;
- 2002-2022 notes for euro 215,662 thousand reserved for subscription by employees, in service and retired, of companies, directly and indirectly, controlled by Telecom Italia with headquarters in Italy. The 20-year notes, with a face value of euro 50 each, issued at face value, are not listed and can only be traded with Telecom Italia at face value. The semiannual interest is payable in arrears on January 1 and July 1 of every year and is indexed to the 6-month Euribor;
- 2002-2012 notes for euro 2,500,000 thousand originally subscribed to by the subsidiary Olivetti Finance N.V. (merged in Telecom Italia Finance effective June 1, 2004), with a fixed-rate coupon of 7.375% (issued June 26, 2002):
- 2002-2012 notes for euro 1,400,000 thousand originally subscribed to by the subsidiary Olivetti Finance N.V. (merged in Telecom Italia Finance effective June 1, 2004), with a fixed-rate coupon of 6.625% (issued December 23, 2002):
- 2001-2011 notes for euro 1,500,000 thousand subscribed to by Telecom Italia Finance, with a fixed-rate coupon of 7.250% (issued May 31, 2001):
- 2001-2011 notes for euro 150,000 thousand subscribed to by Telecom Italia Finance, with a fixed-rate coupon of 6.875% (issued December 28, 2001).

■ Convertible debentures

euro 2,824,947 thousand

Details are as follows:

| | 12/31/2003 | Changes during the year | 12/31/2004 |
|---|------------------|-------------------------|------------------|
| (in thousands of euro) | | | |
| Telecom Italia 1.5% 2001-2004 convertible bonds with a premium on redemption | | | |
| - Residual face value | 1,266,268 | (1,266,268) | - |
| - Premium on redemption | 64,296 | (64,296) | - |
| Total | 1,330,564 | (1,330,564) | - |
| Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption | | | |
| - Residual face value | 2,389,802 | (3,629) | 2,386,173 |
| - Premium on redemption | 439,204 | (430) | 438,774 |
| Total | 2,829,006 | (4,059) | 2,824,947 |
| Total | 4,159,570 | (1,334,623) | 2824,947 |

Telecom Italia 1.5% 2001-2004 convertible bonds with a premium on redemption were fully repaid on January 1, 2004.

Moreover, on December 31, 2004, requests were presented for the conversion of 1,292,835 bonds to shares. The corresponding 609,625 ordinary shares were issued on January 14, 2005.

■ Due to banks

euro 905,643 thousand

Due to banks decreased by euro 285,451 thousand compared to December 31, 2003. They include medium/long-term debt totaling euro 670,066 thousand and short-term borrowings amounting to euro 235,577 thousand, relating to bank overdrafts.

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■ Due to other lenders euro 1,044,721 thousand

Due to other lenders decreased by euro 262,836 thousand compared to December 31, 2003. They consist of medium/long-term financing totaling euro 833,061 thousand and short-term loans payable amounting to euro 211,660 thousand.

Medium/long-term financing principally refers to liabilities for transactions in derivatives (euro 632,465 thousand) put into place with various banks to hedge loans made by subsidiaries, loans made by Cassa Depositi e Prestiti (euro 139,847 thousand) and by the Fondo per l'innovazione tecnologica (euro 51,564 thousand).

Short-term loans refer almost entirely to loans made by TI Securitisation Vehicle S.r.l. deriving from excess cash resources generated by securitization transactions.

■ Trade accounts payable euro 2,032,076 thousand

Trade accounts payable increased by euro 102,282 thousand compared to December 31, 2003. The balance includes euro 284,530 thousand due to other telecommunications operators.

■ Accounts payable to subsidiaries euro 20,728,306 thousand

Accounts payable to subsidiaries increased by euro 184,786 thousand compared to December 31, 2003. They consist of financial payables, trade accounts payable and other payables. Financial payables (euro 19,545,102 thousand) refer to current account transactions negotiated at market rates for cash management purposes and mainly include loans payable to *Telecom Italia Finance* (euro 12,974,679 thousand), *Telecom Italia Capital* (euro 5,602,642 thousand), *TIM* (euro 633,719 thousand) and *Telecom Italia Sparkle* (euro 197,805 thousand). Trade accounts payable (euro 553,755 thousand) mainly consist of accounts payable to *TIM* (euro 186,330 thousand), *Telecom Italia Sparkle* (euro 183,770 thousand) and *Telecom Italia Media* (euro 42,263 thousand) for the portion of TLC services invoiced by Telecom Italia to customers, and *Olivetti Tecnost* (euro 32,978 thousand) and *Telecom Italia Learning Services* (euro 21,580 thousand) for supply transactions. Other payables (euro 629,449 thousand) mainly refer to the adoption of the consolidated national tax return procedure (euro 583,493 thousand) and due to *TIM* (euro 428,200 thousand), *Telecom Italia Media* (euro 99,076 thousand), *Olivetti Tecnost* (euro 21,836 thousand) and *LA 7* (euro 19,806 thousand). They also include payables for capital contributions particularly to *Path.Net* (euro 18,076 thousand) and *sundry payables to Telecom Italia Sparkle* (euro 7,991 thousand).

■ Accounts payable to affiliated companies euro 224,859 thousand

Accounts payable to affiliated companies increased by euro 140,088 thousand compared to December 31, 2003. They consist of financial payables, trade accounts payable and other payables. Financial payables (euro 5,898 thousand) refer to current account transactions negotiated at market rates for cash management purposes mainly due to *Share Service Center - SSC* (euro 5,414 thousand). Trade accounts payable (euro 218,183 thousand) mainly refer to supply transactions with *Italtel* (euro 139,917 thousand), *Siemens Informatica* (euro 33,504 thousand), *Service Center* (euro 27,048 thousand) and *Teleleasing* (euro 9,560 thousand). Other payables refer to the tenths of share capital payable to *Telbios* (euro 745 thousand).

■ Taxes payable euro 265,868 thousand

Taxes payable decreased by euro 113,212 thousand, compared to December 31, 2003, and refer to:

- VAT payable of euro 155,723 thousand;
- Income taxes payable of euro 20,700 thousand;
- withholding taxes payable to the Italian Treasury as the substitute taxpayer of euro 77,175 thousand;
- local other taxes payable of euro 12,270 thousand.

■ Contributions to pension and social security institutions euro 568,365 thousand

Contributions to pension and social security institutions decreased by euro 58,404 thousand compared to December 31, 2003. They include amounts owed to social security and health institutions with regard to personnel. These specifically comprise euro 467,595 thousand payable to INPS for the estimated charges assessed pursuant to Law No. 58/1992, described under the accounting policies.

■ Other liabilities euro 1,967,562 thousand

Other liabilities increased by euro 56,279 thousand compared to December 31, 2003. They include, in particular, liabilities for:

- customer-related items totaling euro 1,140,938 thousand, comprising, among other things, deposits by subscribers against telephone conversations and pre-billed basic charges;
- employee-related items amounting to euro 441,947 thousand;
- lease installments amounting to euro 31,531 thousand.

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ACCRUED EXPENSES AND DEFERRED INCOME

euro 1,631,429 thousand

(euro 2,448,626 thousand at December 31, 2003)

Accrued expenses and deferred income decreased by euro 817,197 thousand compared to December 31, 2003, and include the following:

| | 12/31/2003 | Changes during the year | | | 12/31/2004 |
|---|------------------|--------------------------------------|------------------|------------------|------------------|
| | | IT Telecom and EPIClink Merger | Other changes | Total changes | |
| (in thousands of euro) | | | | | |
| Accrued expenses | | | | | |
| - trade | 89 | 16 | (19) | (3) | 86 |
| - financial | 1,828,233 | 90 | (800,817) | (800,727) | 1,027,506 |
| - other | - | - | | | - |
| | 1,828,322 | 106 | (800,836) | (800,730) | 1,027,592 |
| Deferred income | | | | | |
| - trade | 504,084 | 725 | (2,120) | (1,395) | 502,689 |
| - financial | 3,880 | 509 | 20 | 529 | 4,409 |
| - other | 112,340 | 1,872 | (17,473) | (15,601) | 96,739 |
| - of which capital grants (unavailable portion) | 110,532 | 1,872 | (20,835) | (18,963) | 91,569 |
| | 620,304 | 3,106 | (19,573) | (16,467) | 603,837 |
| Total | 2,448,626 | 3,212 | (820,409) | (817,197) | 1,631,429 |

Accrued financial expenses mainly regard interest on long-term loans from subsidiaries (euro 505,386 thousand) relating to *Telecom Italia Finance*, interest on bonds (euro 484,847 thousand), as well as interest on derivative financial transactions (euro 25,074 thousand).

Deferred income mainly includes pre-billed basic subscriber charges, rentals and maintenance of telephone equipment (euro 398,069 thousand), interconnecting fees and line lease revenues from *Telecom Italia Sparkle* (euro 44,764 thousand) and *TIM* (euro 23,211 thousand), the unavailable portion of capital grants received after December 31, 1992 and financial items principally connected with loans to employees.

* * *

An analysis of liabilities and accrued expenses by maturity and type is provided in Annex 5.

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of liabilities by geographical area is presented in Annex 6.

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■ MEMORANDUM ACCOUNTS

Memorandum accounts total euro 30,530,258 thousand at December 31, 2004 and can be analyzed as follows:

■ GUARANTEES PROVIDED

euro 26,201,273 thousand

Guarantees provided consist of sureties (net of counter-guarantees received totaling euro 1,183,200 thousand), of which euro 25,932,062 thousand are provided on behalf of subsidiaries, euro 149,790 thousand on behalf of affiliated companies and euro 119,421 thousand on behalf of others. The guarantees are given mainly in respect of the notes issued by Telecom Italia Finance (under the Global Medium Term Note Program) for euro 19,989,198 thousand, by Telecom Italia Capital for euro 5,695,639 thousand, and other medium/long-term financial transactions, supply contracts and guarantees on bids to acquire licenses abroad.

■ PURCHASES AND SALES COMMITMENTS

euro 4,264,891 thousand

This item consists of commitments for purchases of euro 4,263,318 thousand and commitments for sales of euro 1,573 thousand.

Commitments for purchases particularly include:

- 9- to 21-year future lease obligations on buildings equal to euro 4,079,733 thousand;
- other future lease obligations, increased by the purchase option (euro 157,714 thousand).

Commitments for sales refer to the sale of the investment in LI.SIT. to Lombardia Informatica for euro 1,573 thousand, at the expiry of the contract (September 15, 2009).

■ OTHER MEMORANDUM ACCOUNTS

euro 64,094 thousand

Other memorandum accounts specifically refer to assets of third parties on loan, on deposit for safekeeping and securities of third parties held as guarantees.

* * *

Moreover:

- the Company issued weak letters of patronage totaling euro 668,396 thousand, chiefly on behalf of subsidiaries and affiliated companies to guarantee insurance policies, lines of credit and overdraft arrangements;
- assets held by third parties on loan, on deposit for safekeeping or for similar purposes amount to euro 247,888 thousand, and mainly consist of equipment leased to customers;
- guarantees provided by others for company obligations amount to euro 839,029 thousand to guarantee the proper performance of non-financial contractual obligations;
- the shares of employees and shareholders deposited at December 31, 2004 with Telecom Italia, and therefore subdeposited with Monte Titoli S.p.A., are equal to euro 219,266 thousand, whereas those awaiting assignment or in the process of being replaced total euro 84 thousand;
- the expense fund to safeguard the holders of savings shares, set up by resolution of the Shareholders' Meeting of June 21, 1999, amounts to euro 2,087 thousand at December 31, 2004.

■ DERIVATIVE FINANCIAL INSTRUMENTS

Transactions in derivative financial instruments at December 31, 2004 include combined cross currency & interest rate swaps (to covert some loan contracts in British pounds, US dollars and Japanese yen to euro) and interest rate swaps (to covert loans originally at floating interest rates to fixed interest rates and to convert the indexing of debt linked with domestic parameters to the 6-month Euribor). The following table shows the notional values of the derivatives hedging medium/long-term debt at December 31, 2004.

| DESCRIPTION | Notional amount in millions of euro |
|---|-------------------------------------|
| Floating to fixed IRS transactions put into place by Telecom Italia S.p.A. | 6 |
| Floating to floating IRS transactions put into place by Telecom Italia S.p.A. | 148 |
| CCIRS transactions put into place by Telecom Italia S.p.A. | 5,193 (*) |
| Totale | 5,347 |

(*) The protection structure is conditional on the loans being maintained performing by Telecom Italia S.p.A. for euro 345 million.

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- The floating to fixed IRS transactions (4.71%) put into place by Telecom Italia S.p.A. for a notional amount of euro 6 million refer to EIB loans at floating rates.
 - The floating to floating IRS transactions put into place by Telecom Italia S.p.A. for a notional amount of euro 148 million refer to indexed loans at domestic parameters (Rendint, Rolint, Robot) with conversion to the 6-month Euribor.
 - CCIRS transactions put into place by Telecom Italia S.p.A. amounting to euro 5,193 million refer:
 - for *euro 3,409 million*, to the floating rate infragroup loan in USD, received from the subsidiary Telecom Italia Capital S.A. following the bonds issued in October 2003 for a total amount of USD 4,000 million, equivalent to euro 2,937 million at December 31, 2004, with conversion of the loan to:
 - quarterly floating rate in euro maturing November 2008 for euro 851 million;
 - semiannual average 5.04% fixed rate in euro maturing November 2013 for euro 1,707 million, of which euro 470 million through two distinct and linked transactions;
 - semiannual 5.99% fixed rate in euro maturing November 2033 for euro 851 million.
- Moreover, against the issue of fixed rate bonds for USD 4,000 million (euro 2,937 million at the euro/USD exchange rate of December 31, 2004), Telecom Italia Capital S.A. put into place IRS contracts converting the semiannual 4% fixed rate coupon on USD 1,000 million maturing November 2008, the 5.25% rate on USD 2,000 million maturing November 2013, the 6.38% rate on USD 1,000 million maturing November 2033 to quarterly floating rates in USD.
- for *euro 174 million*, with reference to the Dual Currency loan with a notional principal of JPY 20 billion with a 5% fixed interest rate with a step-up of +0.45% in USD maturing October 2029, originally received by Olivetti International Finance N.V., equivalent to euro 143 million at December 31, 2004, now carried by Telecom Italia Finance S.A., the following was put into place
 - by Telecom Italia S.p.A., a CCIRS in which Telecom Italia S.p.A., with regard to the infragroup loan in JPY, receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is conditional on the loan being maintained performing by Telecom Italia S.p.A.;
 - by Telecom Italia S.p.A., an IRS with the conversion of the semiannual floating rate in euro to a 6.94% fixed rate up to maturity.
 - for *euro 171 million* with reference to the bonds 2002/2032 of JPY 20 billion with a 3.55% fixed rate coupon maturing May 2032 originally issued by Olivetti Finance N.V., equivalent to euro 143 million at December 31, 2004, Telecom Italia S.p.A. put into place a CCIRS contract on a floating rate infragroup loan in JPY in which Telecom Italia S.p.A. receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is conditional on the loan being maintained performing by Telecom Italia S.p.A..
 - for *euro 150 million*, CCIRSs linked to an EIB loan in USD, equivalent to euro 132 million at December 31, 2004, with conversion to a floating rate in euro.
 - for *euro 1,289 million*, with regard to bonds 2004/2019 with an annual 6.375% fixed rate in GBP maturing June 2019, equivalent to euro 1,206 million at December 31, 2004), CCIRSs with three-year maturities with conversion to the semiannual Euribor.

At December 31, 2004, Telecom Italia S.p.A. has exchange rate transactions put into place for treasury management purposes for a notional amount of euro 122 million.

Consistent with the accounting principles disclosed previously, the negative difference, if any, on the valuation of the above described derivative financial instruments at fair value, is recognized in the statement of income under financial expenses

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■ STATEMENTS OF INCOME

PRODUCTION VALUE

(euro 16,319,632 thousand in 2003)

euro 16,921,960 thousand

Production value includes the following captions:

■ Sales and service revenues

euro 16,126,291 thousand

Sales and service revenues increased by euro 93,090 thousand compared to 2003 mainly as a result of the contribution to revenues by the merged companies IT Telecom and EPIClink (euro 74,157 thousand). Revenues are shown gross of the amount due to other operators (euro 3,024,020 thousand), which are included in costs for "services".

The breakdown of revenues by business segment, expressly required by art. 2427, point 10, of the Italian Civil Code, is presented in the following table, while the breakdown of revenues by geographical area, also required by the same article of the Italian Civil Code, is presented in Annex 6:

Breakdown by business segment

| (in thousands of euro) | 2004 | 2003 | Change |
|------------------------------|-------------------|-------------------|------------------|
| Sales: | | | |
| - telephone products | 726,292 | 425,948 | 300,344 |
| - other goods | 8,529 | 765 | 7,764 |
| | 734,821 | 426,713 | 308,108 |
| Services: | | | |
| - Traffic | 6,536,700 | 6,797,759 | (261,059) |
| - Basic subscription charges | 7,917,676 | 7,937,422 | (19,746) |
| - Fees | 385,068 | 323,643 | 61,425 |
| - Miscellaneous income | 552,026 | 547,664 | 4,362 |
| | 15,391,470 | 15,606,488 | (215,018) |
| Total | 16,126,291 | 16,033,201 | 93,090 |

Traffic revenues are detailed as follows:

| (in thousands of euro) | 2004 | 2003 | Change |
|--------------------------------------|------------------|------------------|------------------|
| • Retail traffic: | | | |
| - phone | 4,558,466 | 4,726,314 | (167,848) |
| - internet (online dial-up and ADSL) | 529,233 | 474,890 | 54,343 |
| - VAS and data | 666,253 | 882,805 | (216,552) |
| | 5,753,952 | 6,084,009 | (330,057) |
| • National wholesale traffic | 782,748 | 713,750 | 68,998 |
| Total | 6,536,700 | 6,797,759 | (261,059) |

Revenues from basic subscription charges are detailed below:

| (in thousands of euro) | 2004 | 2003 | Change |
|---|------------------|------------------|-----------------|
| • Retail subscription charges: | | | |
| - phone | 4,929,937 | 5,057,459 | (127,522) |
| - ADSL | 367,444 | 221,797 | 145,647 |
| - VAS and data | 1,532,292 | 1,504,217 | 28,075 |
| | 6,829,673 | 6,783,473 | 46,200 |
| • National wholesale subscription charges | 1,088,003 | 1,153,949 | (65,946) |
| Total | 7,917,676 | 7,937,422 | (19,746) |

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Revenues from fees to activate service are detailed below:

| (in thousands of euro) | 2004 | 2003 | Change |
|---------------------------|----------------|----------------|---------------|
| • Retail fees: | | | |
| - phone | 155,085 | 136,560 | 18,525 |
| - ADSL | 76,195 | 12,528 | 63,667 |
| - VAS and data | 55,577 | 47,960 | 7,617 |
| | 286,857 | 197,048 | 89,809 |
| • National wholesale fees | 98,211 | 126,595 | (28,384) |
| Total | 385,068 | 323,643 | 61,425 |

Revenues from sales (euro 734,821 thousand) increased by euro 308,108 thousand compared to 2003, mainly driven by the commercial emphasis on both specific contracts and the launch of new products (particularly Aladino cordless phones and Videophones). As for the marketing of products, there was an increase in the sales of phone products (+ euro 157,693 thousand), products for data service (+ euro 61,798 thousand) and VAS products (+ euro 73,982 thousand).

Transactions for revenues from sales and services with subsidiaries and affiliated companies total euro 1,358,813 thousand. In particular, they refer to:

- TIM (euro 633,724 thousand) - revenues for mobile-fixed interconnections and fees for lines leased;
- Telecom Italia Media (euro 154,172 thousand) - telecommunications services;
- Teleleasing (euro 200,430 thousand) - sales of telecommunications products and services;
- Path.Net (euro 118,717 thousand) - TLC services and infrastructures dedicated to the public administration;
- Telecom Italia Sparkle (euro 74,320 thousand) - telecommunications services;
- LI.SIT. (euro 24,069 thousand) - supply of health cards to the Lombardy Region.

■ Changes in inventory of contract work in process

– euro 17,703 thousand

Changes in inventory of contract work in process represents the increase for new work (in particular, for LI.SIT. relating to the sanitary paper for the Lombardy Region) and the decrease mainly as a result of the reclassification to "Increases in capitalized internal construction costs" – after the IT Telecom and EPIClink merger – of the contracts in the process of completion by IT Telecom for Telecom Italia (euro 25,551 thousand).

■ Increases in capitalized internal construction costs

euro 601,232 thousand

These consist entirely of capitalized labor costs. Increases in capitalized internal construction costs amount to euro 541,384 thousand compared to 2003 and for the most part are due to the work previously carried out by IT Telecom and EPIClink (euro 505,382 thousand), which is now performed internally, and the aforementioned reclassification from "Changes in inventory of contract work in process".

■ Other revenues and income

euro 212,140 thousand

Other revenues and income decreased by euro 8,011 thousand compared to 2003. They include the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|---|----------------|----------------|----------------|
| Operating grants | 7,660 | 8,812 | (1,152) |
| Gains on disposal of assets used in the production process | 4,914 | 4,551 | 363 |
| Reimbursements of costs for employees on loan at Group companies | 23,725 | 30,643 | (6,918) |
| Capital grants recorded in income | 19,524 | 24,372 | (4,848) |
| Late payment fees | 76,302 | 79,078 | (2,776) |
| Indemnification, reimbursements and recoveries and other miscellaneous income | 80,015 | 72,695 | 7,320 |
| Total | 212,140 | 220,151 | (8,011) |

Transactions involving other revenues and income with subsidiaries and affiliated companies total euro 51,274 thousand. They refer to the recovery of costs for personnel on loan and sundry services, mainly in respect of:

- TIM (euro 20,781 thousand);
- Telecom Italia Sparkle (euro 10,221 thousand);
- Finsiel (euro 3,745 thousand).

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PRODUCTION COSTS

(euro 12,180,515 thousand in 2003)

euro 12,687,885 thousand

Production costs include the following:

■ Raw materials, supplies and merchandise

euro 614,505 thousand

Raw materials, supplies and merchandise increased by euro 236,304 thousand, compared to 2003 (euro 378,201 thousand), mainly on account of higher purchases of telephone equipment for sale to customers.

They principally include "costs for purchases of telephone equipment to be resold to customers" for euro 313,453 thousand, "costs for purchases of inventory materials" for euro 226,100 thousand, "costs for purchases of materials for the management of corporate assets" for euro 28,098 thousand and "costs for purchases of supply materials" for euro 25,269 thousand.

Raw materials, supplies and merchandise costs include transactions with subsidiaries and affiliated companies of euro 40,266 thousand mainly in reference to Teleleasing (euro 13,238 thousand), Olivetti Tecnost (euro 6,204 thousand), Siemens Informatica (euro 4,784 thousand), Italtel (euro 3,940 thousand) and TIM (euro 3,223 thousand).

■ Services

euro 5,394,979 thousand

Costs for services increased by euro 179,055 thousand compared to 2003. They consist of the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|-------------------------------------|------------------|------------------|----------------|
| Advertising and promotion | 154,617 | 145,698 | 8,919 |
| Selling expenses | 268,898 | 252,441 | 16,457 |
| Maintenance | 219,696 | 266,571 | (46,875) |
| Professional and consulting fees | 544,910 | 169,868 | 375,042 |
| Electricity and water | 166,156 | 157,294 | 8,862 |
| Telephone bill mailing expenses | 42,971 | 43,002 | (31) |
| Interconnection costs | 211,845 | 325,311 | (113,466) |
| Insurance | 34,993 | 45,551 | (10,558) |
| Amounts due to other operators | 27,896 | 27,423 | 473 |
| Selling expenses | 3,024,020 | 3,079,902 | (55,882) |
| Distribution and logistics expenses | 49,359 | 51,571 | (2,212) |
| Other services | 649,618 | 651,292 | (1,674) |
| Total | 5,394,979 | 5,215,924 | 179,055 |

In particular, professional and consulting fees increased by euro 375,042 thousand mainly as a result of the costs of the merged companies IT Telecom and EPIClink (euro 369,168 thousand). This increment was compensated by the reduction in outsourcing costs (– euro 113,466 thousand) after eliminating the costs incurred by Telecom Italia with respect to IT Telecom and EPIClink (euro 157,449 thousand).

Service costs include euro 2,047,451 thousand of transactions with subsidiaries and affiliated companies. They mainly regard:

- TIM (euro 992,979 thousand) - telecommunications services and interconnection costs;
- Telecom Italia Sparkle (euro 385,725 thousand) - telecommunications services and interconnection costs;
- Telecom Italia Media (euro 178,837 thousand) - telecommunications services and selling expenses;
- Telenergia (euro 131,259 thousand) - electricity;
- Share Service Center (euro 99,947 thousand) - performance of services;
- Atesia (euro 21,058 thousand) - outsourcing costs for call center and assistance activities.

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■ Use of property not owned

euro 620,893 thousand

Use of property not owned decreased by euro 18,671 thousand, compared to 2003.

These costs consist of:

| (in thousands of euro) | 2004 | 2003 | Change |
|------------------------|----------------|----------------|-----------------|
| Rentals | 471,401 | 450,860 | 20,541 |
| Hires | 120,783 | 172,064 | (51,281) |
| Lease installments | 21,713 | 14,317 | 7,396 |
| Other | 6,996 | 2,323 | 4,673 |
| Total | 620,893 | 639,564 | (18,671) |

This item comprises euro 183,907 thousand of costs for the use of property not owned relating to transactions with subsidiaries and affiliated companies, specifically with Tiglio I (euro 52,784 thousand) and Tiglio II (euro 24,464 thousand) for building rentals, Telecom Italia Sparkle (euro 84,159 thousand) for line leases, Teleleasing (euro 6,771 thousand) for hire and leasing installments

■ Personnel costs

euro 2,614,142 thousand

Personnel costs increased by euro 117,727 thousand compared to 2003 mainly for the personnel costs of IT Telecom and EPIClink (euro 206,657 thousand).

They comprise "wages and salaries" (euro 1,837,882 thousand), "social security contributions" (euro 587,147 thousand), "employee termination indemnities" (euro 137,118 thousand) and "other costs" (euro 51,995 thousand). Personnel costs include the costs of employees on loan to other Group companies (euro 23,725 thousand) and recovered from the same Group companies; the income from the recovery of such costs is recorded in "Other revenues and income".

A comparative breakdown of the average number of employees by professional category in 2004 is presented as follows:

| | 2004 | 2003 |
|-------------------|---------------|---------------|
| Executives | 1,005 | 928 |
| Middle management | 2,573 | 1,902 |
| Clerical staff | 49,848 | 46,940 |
| Technicians | 233 | 3,360 |
| Total | 53,659 | 53,130 |

■ Amortization, depreciation and writedowns

euro 2,993,433 thousand

Details of this caption are provided as follows:

Amortization of intangible assets

euro 671,343 thousand

Amortization of intangible assets increased by euro 56,577 thousand, compared to 2003, and refers to the following assets:

| (in thousands of euro) | 2004 | 2003 | Change |
|--|----------------|----------------|---------------|
| Start-up and expansion costs | 11,557 | 27,488 | (15,931) |
| Industrial patents and intellectual property rights | 626,872 | 557,618 | 69,254 |
| Concessions, licenses, trademarks and similar rights | 173 | 9,959 | (9,786) |
| Goodwill | 1,903 | 186 | 1,717 |
| Other intangibles | 30,838 | 19,515 | 11,323 |
| Total | 671,343 | 614,766 | 56,577 |

Depreciation of fixed assets

euro 2,220,635 thousand

Depreciation of fixed assets decreased by euro 83,431 thousand compared to 2003. The average depreciation rate referring to assets being depreciated is equal to 8.1%.

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The following table shows the depreciation charge for each asset category in 2004 and the related depreciation rate.

| (in thousands of euro) | 2004 | | 2003 | | Change |
|--|-------|------------------|-------|------------------|-----------------|
| Land and building | 3.3% | 79,457 | 3.3% | 79,228 | 229 |
| Plant and machinery | 8.3% | 2,105,685 | 8.8% | 2,168,708 | (63,023) |
| Manufacturing and distribution equipment | 19.9% | 7,589 | 18.7% | 10,594 | (3,005) |
| Other fixed assets | 24.9% | 27,904 | 25% | 45,536 | (17,632) |
| Total | | 2,220,635 | | 2,304,066 | (83,431) |

Writedowns of receivables included in current assets and liquid assets

euro 101,456 thousand

This caption includes the provision to the allowance for doubtful trade accounts receivables from customers which decreased by euro 97,527 thousand compared to 2003 (euro 198,983 thousand). The decrease is principally due to the reduction in receivables as a result of discounting transactions.

■ **Changes in inventory of raw materials, supplies and merchandise**

– euro 37,801 thousand

The changes reflect the purchases of equipment destined for sale and goods for maintenance that were not used and also takes into account writedowns for obsolete materials and materials with diminished utilization. The amount primarily refers to inventories connected with the marketing of Aladino cordless phones and videophones.

■ **Provisions for risks**

euro 49,138 thousand

Provisions for risks refer to provisions made to the “reserve for litigation” to cover expenses connected with the potential outcome of disputes with third parties (euro 25,487 thousand) and provisions connected with transactions with other TLC operators in respect of matters concerning interconnection (euro 22,600 thousand).

■ **Miscellaneous operating costs**

euro 438,596 thousand

Miscellaneous operating costs increased by euro 108,033 thousand, compared to 2003, and include the following:

Losses on disposal of assets

euro 17,431 thousand

These losses mainly refer to the disposal of fixed assets.

TLC operating fees

euro 23,250 thousand

TLC operating fees mainly include the fee for the assignment of telephone numbers (euro 8,824 thousand) and the fee for the use of radio frequencies (euro 8,665 thousand) provided by the Ministerial Decree of February 5, 1998, in addition to the fee for the operation of the Regulatory Body (euro 5,320 thousand).

Other miscellaneous costs

397,915 thousand

Other miscellaneous costs increased by euro 104,781 thousand, compared to 2003, and include the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|--|----------------|----------------|----------------|
| Other indirect duties and annual taxes, relating mainly to local property taxes, local duties, stamp and register tax, vehicle tax, production and electrical energy consumption taxes and permits and government concession taxes | 93,386 | 94,690 | (1,304) |
| Association dues and membership fees | 15,307 | 17,056 | (1,749) |
| Losses due to settlements | 104,839 | 38,265 | 66,574 |
| Losses on the sale of receivables | 89,231 | 69,357 | 19,874 |
| Other costs, essentially relating to compensation due to customers for delays in hookups or line transfers, damages paid to third parties for line installations and maintenance | 95,152 | 73,766 | 21,386 |
| Total | 397,915 | 293,134 | 104,781 |

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FINANCIAL INCOME AND EXPENSE

– euro 364,763 thousand

(– euro 397,509 thousand in 2003)

Financial income and expense shows an expense balance of euro 364,763 thousand. Details are as follows:

| (in thousands of euro) | | 2004 | 2003 | Change |
|--------------------------------------|------------------------|------------------|------------------|---------------|
| Income from equity investments | (A) | 1,406,831 | 2,006,709 | (599,878) |
| Other financial income | (B) | 227,102 | 116,968 | 110,134 |
| Interest and other financial expense | (C) | (1,996,278) | (2,519,412) | 523,134 |
| Foreign exchange gains and losses | (D) | (2,418) | (1,774) | (644) |
| Total | (A + B + C + D) | (364,763) | (397,509) | 32,746 |

Income from equity investments refers to the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|---|------------------|------------------|------------------|
| Dividends from subsidiaries, affiliated companies and other companies | 1,400,838 | 1,919,544 | (518,706) |
| Other income from equity investments: | | | |
| • tax credits on dividends | - | 83,323 | (83,323) |
| • other income from equity investments | 5,993 | 3,842 | 2,151 |
| | 1,406,831 | 2,006,709 | (599,878) |

Dividends can be analyzed as follows:

| (in thousands of euro) | 2004 | | | 2003 | | | Change |
|-------------------------------------|-----------|----------|-----------|-----------|----------|-----------|-----------|
| Dividends from subsidiaries | Accrued | Received | Total (a) | Accrued | Received | Total (b) | |
| - Telecom Italia | | | | | 511,245 | 511,245 | (511,245) |
| - Oliv. Finanz. Industriale | | | | | | - | |
| - Oli. Multiservices | | | | | 346 | 346 | (346) |
| - Olivetti Gestioni Ivrea | | | | 106 | 650 | 756 | (756) |
| - TIM | 1,337,378 | 9,805 | 1,347,183 | 1,205,435 | 82,591 | 1,288,026 | 59,157 |
| - Finsiel | | | | | 3,097 | 3,097 | (3,097) |
| - Atesina | | | | 9,898 | | 9,898 | (9,898) |
| - Saiat | | | | | | - | |
| - Emsa | | | | | | - | |
| - Tecnoservizi Mobili | | | | 204 | | 204 | (204) |
| - Telecom Italia Gmbh | | | | | | - | |
| - PathNet | 6,200 | | 6,200 | 4,850 | | 4,850 | 1,350 |
| - Telsy | 700 | | 700 | 500 | | 500 | 200 |
| - TELIMM | | | | | | | |
| - Telecom Italia Sparkle | 38,000 | | 38,000 | 89,400 | | 89,400 | (51,400) |
| | 1,382,278 | 9,805 | 1,392,083 | 1,310,393 | 597,929 | 1,908,322 | (516,239) |
| Dividends from affiliated companies | | Received | Total (a) | | Received | Total (b) | |
| - Telegono | | - | - | | 5,200 | 5,200 | (5,200) |
| | | - | - | | 5,200 | 5,200 | (5,200) |

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| (in thousands of euro) | 2004 | | 2003 | | Change |
|--------------------------------|-----------|--------|-----------|---------|---------------------|
| Dividends from other companies | Received | Total | Received | Total | |
| - MCC | 770 | 770 | 1,539 | 1,539 | (769) |
| - Mediobanca | 5,647 | 5,647 | 2,541 | 2,541 | 3,106 |
| - Tredicimarzo | | | - | - | |
| - Eurofly Services | | | - | - | |
| - Datalogic | | | 34 | 34 | (34) |
| - Intelsat | | | - | - | |
| - Pirelli Real Estate | 1,145 | 1,145 | 1,013 | 1,013 | 132 |
| - SIA | 307 | 307 | 307 | 307 | - |
| - UBAE | | | 88 | 88 | (88) |
| - Emittenti Titoli | 100 | 100 | 148 | 148 | (48) |
| - Azienda Esercizio Gas | | | 1 | 1 | (1) |
| - FIN. PRIV. | 786 | 786 | 351 | 351 | 435 |
| | 8,755 | 8,755 | 6,022 | 6,022 | 2,733 |
| Total | 1,382,278 | 18,560 | 1,310,393 | 609,151 | 1,919,544 (518,706) |

Dividends from subsidiaries, affiliated companies and other companies decreased by euro 518,706 thousand compared to 2003 mainly following the receipt, in 2003, of pre-merger Olivetti/Telecom Italia dividends by the merged company Telecom Italia (euro 511,245 thousand).

Other income from equity investments refers to the recovery of the *share premium from the company LI.SIT.* and decreased by euro 81,172 thousand as a result of the elimination of the tax credit on dividends following the tax reform introduced by Legislative Decree No. 344/2003.

Other financial income includes the following:

| (in thousands of euro) | Included in long-term investments | 2004 Included in current assets | Total | 2003 | Change |
|--|-----------------------------------|------------------------------------|---------|---------|---------|
| Interest and fees on: | | | | | |
| • accounts receivable | | | | | |
| - from subsidiaries | 3,725 | 25,141 | 28,866 | 33,407 | (4,541) |
| - from affiliated companies | 1,789 | 51 | 1,840 | 6,579 | (4,739) |
| - other | 7,085 | - | 7,085 | 6,817 | 268 |
| • securities | - | 240 | 240 | 1,788 | (1,548) |
| • bank and postal accounts | - | 38,114 | 38,114 | 13,931 | 24,183 |
| | 12,599 | 63,546 | 76,145 | 62,522 | 13,623 |
| Income on derivative financial instruments | | | 130,153 | 27,052 | 103,101 |
| Other income ¹ | | | 20,804 | 27,394 | (6,590) |
| | | | 227,102 | 116,968 | 110,134 |

Other financial income includes euro 30,816 thousand of interest and fees on receivables from subsidiaries and affiliated companies, almost all of which refers to accrued interest on current accounts for cash management purposes, mainly with:

- Olivetti Tecnost (euro 12,146 thousand);
- Telecom Italia Finance (euro 3,337 thousand, financial fees);
- Telecom Italia Media (euro 2,872 thousand);
- TIM (euro 1,961 thousand).

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Interest and other financial expense can be analyzed as follows:

| (in thousands of euro) | 2004 | | | 2003 | Change |
|--|-----------------------|-----------------------|------------------|------------------|------------------|
| | Medium/long-term debt | Short-term borrowings | Total | | |
| Interest and fees paid to subsidiaries | 610,423 | 160,213 | 770,636 | 849,566 | (78,930) |
| Interest and fees paid to affiliated companies | - | 446 | 446 | 306 | 140 |
| Interest and fees paid to others and miscellaneous expense | | | | | |
| • on due to banks | 17,770 | 9,334 | 27,104 | 112,957 | (85,853) |
| • on debentures | 809,274 | - | 809,274 | 1,276,421 | (467,147) |
| • on due to other lenders | 10,639 | 14,490 | 25,129 | 39,883 | (14,754) |
| • on other items | | | | | |
| - Accrued portion of issue discounts and similar charges on loans | 54,722 | - | 54,722 | 56,841 | (2,119) |
| - Provision to the allowance for doubtful accounts for the "Deferred Purchasing Price" | - | 23,015 | 23,015 | 16,644 | 6,371 |
| - Expenses on derivative financial instruments | 214,886 | - | 214,886 | 79,656 | 135,230 |
| - Other financial expense | 30,917 | 40,149 | 71,066 | 87,138 | (16,072) |
| Total | 1,748,631 | 247,647 | 1,996,278 | 2,519,412 | (523,134) |

Interest on debentures (euro 809,274 thousand) includes interest to Telecom Italia Finance (euro 396,204 thousand) for bonds subscribed to by this company and described in a specific note.

Interest and other financial expense includes euro 1,167,311 thousand of interest and fees on payables to subsidiaries and affiliated companies principally with regard to:

- Telecom Italia Finance (euro 979,508 thousand, including the above interest on bonds), Telecom Italia Capital (euro 99,133 thousand) and TIM (euro 36,733 thousand) - interest expenses accrued on current accounts for cash management purposes.

Foreign exchange gains and losses include the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|-------------------------|----------------|----------------|--------------|
| Foreign exchange gains | | | |
| - from amounts realized | 6,147 | 12,849 | (6,702) |
| - from adjustments | 6,926 | 17 | 6,909 |
| Total (A) | 13,073 | 12,866 | 207 |
| Foreign exchange losses | | | |
| - from amounts realized | 6,700 | 4,629 | 2,071 |
| - from adjustments | 8,791 | 10,011 | (1,220) |
| Total (B) | 15,491 | 14,640 | 851 |
| Total (A-B) | (2,418) | (1,774) | (644) |

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VALUE ADJUSTMENTS TO FINANCIAL ASSETS

euro 54,077 thousand

(– euro 361,141 thousand in 2003)

Value adjustments to financial assets include upward adjustments (euro 84,507 thousand) and writedowns (euro 30,430 thousand), including writedowns of equity investments (euro 30,334 thousand).

Upward adjustments refer to the following:

| (in thousands of euro) | 2004 | 2003 | Change |
|--|---------------|---------------|--------------|
| Included in long-term investments | | | |
| Olivetti Tecnost | 49,274 | - | 49,274 |
| Iridium Italia | 1,905 | - | 1,905 |
| Telesoft Zao Russia | 830 | - | 830 |
| Telecom Italia America Latina | 332 | - | 332 |
| Edotel | 46 | - | 46 |
| Telecom Italia Finance | - | 66,902 | (66,902) |
| Trainet | - | 7,522 | (7,522) |
| Included in short-term financial assets | | | |
| TIM | 32,120 | 2,146 | 29,974 |
| | 84,507 | 76,570 | 7,937 |

The writedowns of equity investments refer to the following companies:

| | 2004 | | | 2003 | Change |
|---|-------------------------------------|--|--------|---------|-----------|
| | Writedowns to carrying values | Writedowns recorded in the reserve for losses of subsidiaries and affiliates | Total | | |
| (in thousands of euro) | | | | | |
| Recorded in long-term investments | | | | | |
| - IT Telecom | - | - | - | 114,871 | (114,871) |
| - Olivetti Tecnost | - | - | - | 53,722 | (53,722) |
| - Olivetti Finance | - | - | - | 3,200 | (3,200) |
| - Olivetti International | - | - | - | 80,461 | (80,461) |
| - Sky Italia (ex Stream) | - | - | - | 95,504 | (95,504) |
| - Edotel | - | - | - | 6,798 | (6,798) |
| - Netesi | - | - | - | 2,032 | (2,032) |
| - TILAB S.A. | 48 | 3,112 | 3,160 | 6,920 | (3,760) |
| Telecom Italia Learning Services | 13,021 | 2,834 | 15,855 | 63,213 | (47,358) |
| - Trainet | | 752 | 752 | - | 752 |
| - Telbios | 3,178 | | 3,178 | - | 3,178 |
| - Telecom Italia America Latina | | | | 3,796 | (3,796) |
| - LI.SIT | 5,993 | | 5,993 | 3,257 | 2,736 |
| - Siosistemi | | | | 1,705 | (1,705) |
| - Other companies | 906 | 470 | 1,376 | 1,924 | (548) |
| | (A) | 23,146 | 7,168 | 30,314 | 437,403 |
| | | | | | (407,089) |
| Recorded in short-term financial assets | | | | | |
| - Datalogic | - | - | - | 3 | (3) |
| - Biesse | - | - | - | 121 | (121) |
| - Telecom Italia Media | 7 | - | 7 | 30 | (23) |
| - Portal Software | 13 | - | 13 | 26 | (13) |
| | (B) | 20 | - | 20 | 180 |
| | | | | | (160) |
| Total | (A + B) | 23,166 | 7,168 | 30,334 | 437,583 |
| | | | | | (407,249) |

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EXTRAORDINARY INCOME AND EXPENSE

– euro 725,819 thousand

(– euro 1,652,308 thousand in 2003)

The balance is detailed as follows:

| (in thousands of euro) | 2004 | 2003 | Change |
|---|------------------|--------------------|--------------------|
| Income | | | |
| - gains on disposals | 58,203 | 36,532 | 21,671 |
| - elimination of tax interference | 932 | - | 932 |
| - recovery and release of liabilities and reserve for risks in respect of TLC license fee Law 448/98 | 410,838 | 921,872 | (511,034) |
| - income tax refunds | 24,707 | - | 24,707 |
| - recoveries under Law 58/1992 and damage compensation | 10,369 | 8,976 | 1,393 |
| - other | 61,770 | 83,659 | (21,889) |
| (A) | 566,819 | 1,051,039 | (484,220) |
| Expense | | | |
| - expenses under Law 58/1992 | 149,377 | 151,776 | (2,399) |
| - loss on sale of Seat Pagine Gialle | - | 347,703 | (347,703) |
| - loss on sale of buildings | - | 40,101 | (40,101) |
| - provisions and writedowns of equity investments | 632,313 | 1,278,545 | (646,232) |
| - provision for Antitrust sanction | 152,000 | - | 152,000 |
| - expenses and provisions for corporate restructuring (employee reduction plans, territorial and other layoffs, CIGS) | 145,819 | 195,786 | (49,967) |
| - prior period expenses for telephone cards | - | 56,434 | (56,434) |
| - expenses on Olivetti/Telecom Italia merger and sale of Nuova Seat | - | 181,372 | (181,372) |
| - expenses on Telecom Italia/TIM merger | 19,365 | - | 19,365 |
| - expenses for Pagine Italia settlement | - | 55,000 | (55,000) |
| - writeoffs of prior years' receivables | 46,384 | 191,747 | (145,363) |
| - expenses for damages by third parties | 36,959 | 32,642 | 4,317 |
| - expenses for liability items | 27,013 | 35,459 | (8,446) |
| - adjustment on contribution to TI Sparkle | - | 49,166 | (49,166) |
| - provisions for corporate-related transactions | 24,315 | 13,023 | 11,292 |
| - other | 59,093 | 74,593 | (15,500) |
| (B) | 1,292,638 | 2,703,347 | (1,410,709) |
| Total | (A-B) | (1,652,308) | (926,489) |

Extraordinary income, equal to euro 566,819 thousand, decreased by euro 484,220 thousand compared to 2003. This reduction is mainly due to prior period income for the difference between nonexistent liabilities recorded in 2003 as a result of the cancellation of the TLC license fee relating to the years 2000, 2001 and 2002 (Euro 921,872 thousand) and the prior period income relating to the same fee paid for 1999 and the relative interest (euro 410,838 thousand) recorded in 2004 as a result of the decision handed down by the TAR of Lazio No. 47/2005 of January 4, 2005, which upheld the appeal filed by Telecom Italia and cancelled the Ministerial Decree dated March 21, 2000 regarding the TLC fee instituted by Law 448/1998 declaring it to be illegal.

Besides the above prior period income relating to the 1999 TLC license fee, extraordinary income also includes the following:

- the gains (euro 58,203 thousand) realized mainly on the sale of the equity investments in Pirelli & C. Real Estate (euro 9,044 thousand) and Mirror International Holding (euro 17,973 thousand), the sale of 80.1% of Atesia (euro 1,897 thousand), the sale of the "Maintenance" and "Environmental Services" (euro 3,500 thousand) and "Document Management" (euro 1,000 thousand) business segments and the sale of the "Development" business segment by the merged company IT Telecom (euro 23,000 thousand);
- the income tax refund for ILOR paid in 1991 (euro 24,707 thousand) relating to the reinvestment of earnings in the south of Italy for which the exemption was requested in the 1992 tax return, pursuant to art. 102 of D.P.R. No. 218 dated March 6, 1978;

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- the recovery of expenses from companies of the Group relating to Law 58/1992 (euro 1,920 thousand) and from third parties for damage compensation (euro 8,449 thousand);
- the elimination of prior period tax interference (euro 932 thousand), pursuant to Legislative Decree No. 6 dated January 17, 2003, introducing the Corporate Law Reform, following accelerated depreciation taken in prior years by the acquiring company Olivetti as allowed by tax laws;
- other prior period income of euro 61,770 thousand.

Extraordinary expenses, equal to euro 1,292,638 thousand, decreased by euro 1,410,709 thousand compared to 2003 in which the following items had been booked:

- loss on the sale of Nuova Seat Pagine Gialle (euro 347,703 thousand);
- expenses connected with the Olivetti/Telecom Italia merger and the sale of the company Nuova Seat Pagine Gialle (euro 181,372 thousand);
- writedowns of the equity investments in Telecom Italia Media (+euro 378,174 thousand), Telecom Italia International (+euro 146,123 thousand), Latin American Nautilus (+euro 172,358 thousand), EPIClink (euro 110,093 thousand) and Loquendo (euro 7,866 thousand) and provisions for guarantees provided upon the sales of the satellite consortia (euro 30,000 thousand);
- expenses relating to the settlement with Pagine Italia (euro 55,000 thousand).

Extraordinary expenses include:

- writedowns of the equity investments in Telecom Italia International (euro 256,990 thousand) to adjust the investments in Entel Chile and Etec S.A. to market value, Telecom Italia Media (euro 112,416 thousand) for the loss of value following the settlement with the De Agostini group, Finsiel (euro 138,680 thousand) to adjust the investment to its estimated sales value, Latin American Nautilus (euro 64,526 thousand), Mediterranean Nautilus (euro 46,447 thousand) and Med 1 (euro 13,254 thousand);
- provision for the sanction levied by the Antitrust Authority for the alleged abuse of a dominant position (euro 152,000 thousand);
- expenses under Law 58/1992 (euro 149,377 thousand) to cover employees under the former fund "Telephone Employees Pension Fund" (FPT), which became part of the general "Employees Pension Fund", in accordance with the 2000 Finance Bill;
- expenses (euro 145,819 thousand) for corporate restructuring relating to employees cutbacks and layoffs;
- prior period expenses for the writeoff of prior years' receivables balances (euro 46,384 thousand) made necessary by the actions verifying credit transactions with customers;
- expenses for damages caused to the company's assets as a result of natural events or brought about by third parties (euro 36,959 thousand);
- expenses for the recognition of liabilities referring to prior years (euro 27,013 thousand), principally in respect of matters concerning interconnection as a result of tests conducted with the interested operators;
- provisions (euro 24,315 thousand) connected with corporate-related transactions;
- expenses connected with the Telecom Italia - TIM merger (euro 19,365 thousand);
- other prior period expenses and extraordinary expenses euro 59,093 thousand.

INCOME TAXES

euro 1,062,722 thousand

Income taxes consist of current taxes of euro 121,958 thousand and deferred taxes of euro 940,764 thousand.

The total amount can be divided into Corporate Income Taxes (IRES) of euro 716,831 thousand and the Regional Tax on Production Activities (IRAP) of euro 345,891 thousand.

The statement of income benefits from euro 224,498 thousand of compensation for the transfer to the consolidated national tax return of the losses deriving from the consolidation adjustments.

Dividends, as a result of the tax reform introduced by Legislative Decree 344/2003 dated January 1, 2004, no longer carry the relative tax credit and, in view of adhering to the consolidated national tax return procedure, are basically excluded from the formation of the income of the company.

Income taxes also include the effects deriving from the filing of the 2003 tax return, as well as the booking of deferred tax assets and liabilities relating to the merged companies.

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The reconciliation between theoretical taxes, deriving from the application of the nominal rate, and taxes effectively booked in the statement of income, is presented in the following table:

| (in thousands of euro) | IRES | IRAP | Total |
|--|------------------|----------------|------------------|
| Income before taxes | 3,197,569 | (*) | 3,197,569 |
| Theoretical taxes | 1,055,198 | 297,930 | 1,353,128 |
| Permanent differences: | | | |
| - permanent increases | 331,147 | 33,368 | 364,515 |
| - dividends posted to statement of income | (461,493) | 0 | (461,493) |
| - permanent decreases | (57,867) | (2,081) | (59,948) |
| Tax adjustments | (150,154) | 16,674 | (133,480) |
| Taxes booked to statement of income | 716,831 | 345,891 | 1,062,722 |

(*) Irapp calculated on taxable income of euro 7,010,127 thousand.

* * *

The following Annexes numbered 1 to 6 are an integral part of these notes.

OTHER INFORMATION

■ REMUNERATION TO DIRECTORS, STATUTORY AUDITORS AND GENERAL MANAGERS

In compliance with art. 78 giving effect to Legislative Decree 58 dated February 24, 1998, adopted by Consob under resolution No. 11971 of May 14, 1999, the following table presents the remuneration to which all the individuals were entitled who held posts in 2004, even for a part of the year, as a director, statutory auditor and general manager of Telecom Italia S.p.A..

In particular:

- the column "Fees for the post held in the company preparing the financial statements" shows the fees, by period of reference, voted by the Shareholders' Meeting of Telecom Italia S.p.A. and the remuneration ex art. 2389, paragraph 3, of the Italian Civil Code;
- the column "Non-cash benefits" refer to fringe benefits subject to taxes based on current tax laws;
- the column "Bonuses and other incentives" include one-off remuneration;
- the column "Other remuneration" includes: (i) fees due for posts held in listed and unlisted subsidiaries; (ii) employee compensation (gross of the employees' portion of social security charges and taxes, excluding the employers' portion of obligatory social security contributions and expenses for employee termination indemnities).

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BOARD OF STATUTORY AUDITORS' REPORT

| Individual | Description of post | Period during which post was held | Remuneration (in thousands of euro) | | | |
|--------------------------|---|-----------------------------------|--|-------------------|------------------------------|---------------------|
| | | | Fees for the post held in the company preparing the financial statements | Non-cash benefits | Bonuses and other incentives | Other compensation |
| Marco TRONCHETTI PROVERA | Chairman of the Board of Directors | 1/1-12/31/2004 | 2,121 ⁽¹⁾ | | 1,000 ⁽²⁾ | |
| Gilberto BENETTON | Deputy Chairman | 1/1-12/31/2004 | 110 | | | |
| Carlo Orazio BUORA | Managing Director | 1/1-12/31/2004 | 2,073 ⁽¹⁾ | | 1,250 ⁽³⁾ | 80 ⁽⁴⁾ |
| Riccardo RUGGIERO | Managing Director General Manager | 1/1-12/31/2004 | 550 ^{(1) (5)} | 9 | 5,817 | 946 ⁽⁶⁾ |
| Paolo BARATTA | Director | 5/7-12/31/2004 | 110 ⁽⁷⁾ | | | |
| John Robert Sotheby BOAS | Director | 5/7-12/31/2004 | 76 | | | |
| Umberto COLOMBO | Director | 1/1-06/05/2004 | 34 | | | |
| Giovanni CONSORTE | Director | 1/1-12/31/2004 | 110 | | | |
| Francesco DENOZZA | Director | 1/1-12/31/2004 | 152 ⁽⁸⁾ | | | |
| Domenico DE SOLE | Director | 5/7-12/31/2004 | 123 ⁽⁹⁾ | | | |
| Luigi FAUSTI | Director | 1/1-12/31/2004 | 180 ⁽¹⁰⁾ | | | |
| Guido FERRARINI | Director | 1/1-12/31/2004 | 183 ⁽¹¹⁾ | | | |
| Jean Paul FITOUSSI | Director | 5/7-12/31/2004 | 76 | | | |
| Natale IRTI | Director | 1/1-06/05/2004 | 52 ⁽¹²⁾ | | | |
| Gianni MION | Director | 1/1-12/31/2004 | 110 ⁽¹³⁾ | | | 146 ⁽¹⁴⁾ |
| Pietro MODIANO | Director | 1/1-06/05/2004 | 34 ⁽¹⁵⁾ | | | |
| Massimo MORATTI | Director | 1/1-12/31/2004 | 110 | | | |
| Marco ONADO | Director | 5/7-12/31/2004 | 123 ⁽⁹⁾ | | | |
| Renato PAGLIARO | Director | 5/7-12/31/2004 | 76 ⁽¹⁶⁾ | | | |
| Pasquale PISTORIO | Director | 5/7-12/31/2004 | 116 ⁽¹⁷⁾ | | | |
| Carlo A. PURI NEGRI | Director | 1/1-12/31/2004 | 110 | | | |
| Luigi ROTH | Director | 5/7-12/31/2004 | 76 | | | |
| Pier Francesco SAVIOTTI | Director | 1/1-06/05/2004 | 52 ⁽⁷⁾ | | | |
| Giuseppe SALA | General Manager | 1/1-12/31/2004 | = | 5 | 2,400 | 691 ⁽⁶⁾ |
| Ferdinando SUPERTI FURGA | Chairman of the Board of Statutory Auditors | 1/1-12/31/2004 | 184 ⁽¹⁸⁾ | | | |
| Rosalba CASIRAGHI | Acting Auditor | 1/1-12/31/2004 | 128 | | | |
| Paolo GOLIA | Acting Auditor | 1/1-12/31/2004 | 128 | | | |
| Salvatore SPINIELLO | Acting Auditor | 1/1-12/31/2004 | 128 | | | 21 ⁽¹⁹⁾ |
| Gianfranco ZANDA | Acting Auditor | 1/1-12/31/2004 | 128 | | | 92 ⁽²⁰⁾ |

(1) The amount includes the remuneration ex art. 2389, section 3, of the Italian Civil Code.

(2) This refers to variable remuneration ex art. 2389 paragraph 3 of the Italian Civil Code for the year 2003, paid in 2004 since it was subject to reaching a consolidated EBIT 2003 budget target, in the presence of a positive EVA change. With regard to 2004, the Board of Directors has anticipated additional remuneration of euro 1,400,000.00, the payment of which in 2005 is subject to reaching a consolidated EBIT 2004 budget target, in the presence of a positive EVA change.

(3) This refers to variable remuneration ex art. 2389 paragraph 3 of the Italian Civil Code for the year 2003, paid in 2004 since it was subject to reaching a consolidated EBIT 2003 budget target, in the presence of a positive EVA change. With regard to 2004, the Board of Directors has anticipated additional remuneration of euro 1,250,000.00, the payment of which in 2005 is subject to reaching a consolidated EBIT 2004 budget target, in the presence of a positive EVA change.

(4) Remuneration for the post of Chairman of Telecom Italia Mobile S.p.A., not received but paid over to Telecom Italia S.p.A..

(5) The amount relating to remuneration ex art. 2389, section 1, of the Italian Civil Code (equal to about euro 110,000.00) is not paid to the person.

(6) Employment income.

(7) The amount includes the remuneration paid as a member of the Remuneration Committee.

(8) The amount includes the remuneration paid as a member of the Internal Control and Corporate Governance Committee for the period 5/7 - 12/31/2004.

(9) The amount includes the remuneration paid as a member of the Internal Control and Corporate Governance Committee and the remuneration paid as a member of the Strategies Committee for the period 9/9 - 12/31/2004.

(10) The amount includes the remuneration paid as Chairman of the Remuneration Committee and the remuneration paid as a member of the Internal Control and Corporate Governance Committee for the period 1/1 - 5/6/2004.

(11) The amount includes the remuneration paid as Chairman of the Internal Control and Corporate Governance Committee and the remuneration paid as a member of the Supervisory Panel Legislative Decree 231/2001 for the period 5/7 - 12/31/2004.

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- (12) The amount includes the remuneration paid as a member of the Internal Control and Corporate Governance Committee.
- (13) Remuneration not received but paid over to Edizione Holding.
- (14) Remuneration for the posts of Director of Telecom Italia Media S.p.A. and Deputy Chairman of Telecom Italia Mobile S.p.A., not received but paid over to Edizione Holding S.p.A.
- (15) Remuneration not received but paid over to Unicredito.
- (16) Remuneration not received but paid over to Mediobanca.
- (17) The amount includes the remuneration paid as a member of the Remuneration Committee and the remuneration paid as a member of the Strategies Committee for the period 9/9 - 12/31/2004.
- (18) The amount includes the remuneration paid as a member of the Supervisory Panel Legislative Decree 231/2001 for the period 5/7 - 12/31/2004.
- (19) Remuneration for the post of Acting Statutory Audit in Telecom Italia Media S.p.A.
- (20) Remuneration for the post of Chairman of the Board of Statutory Auditors of IT Telecom S.p.A. and Acting Statutory Auditor in the companies Finsiel S.p.A. and Telecom Italia Mobile S.p.A..

In conformity with the format established by the regulation implementing the Legislative Decree of February 24, 1998, adopted by Consob under Resolution No. 11971 of May 14, 1999 and later changes and supplements, the following table summarizes the key features of the stock option plans for Directors and General Managers:

STOCK OPTION PLANS FOR DIRECTORS AND GENERAL MANAGERS

| | | Options held at the beginning of 2004 | | | Options granted during 2004 | | | Options exercised during 2004 | | | Options expired in 2004 | Options held at the end of 2004 | | |
|-----------------------------|-----------|---------------------------------------|------------------------|-------------------------|-----------------------------|------------------------|-------------------------|-------------------------------|------------------------|----------------------------------|-------------------------|---------------------------------|------------------------|-------------------------|
| (A) | (B) | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) | (11) = 1+4-7-10 | (12) | (13) |
| Name | Post held | Number of options | Average exercise price | Average expiration date | Number of options | Average exercise price | Average expiration date | Number of options | Average exercise price | Average market price during year | Number of options | Number of options | Average exercise price | Average expiration date |
| Riccardo Ruggiero M.D./G.M. | | 750,000 | 3.177343 | 2007 | | | | | | | | 750,000 | 3.177343 | 2007 |
| | | 150,000 | 2.788052 | 2008 | | | | 150,000 | 2.788052 | 2.910 | | = | = | |
| | | 150,000 | 2.788052 | 2009 | | | | 150,000 | 2.788052 | 2.910 | | = | = | |
| | | 200,000 | 2.788052 | 2010 | | | | | | | | 200,000 | 2.788052 | 2010 |

Note:

Each option corresponds to the subscription or purchase of one share.

| | | Options held at the beginning of 2004 | | | Options granted during 2004 | | | Options exercised during 2004 | | | Options expired in 2004 | Options held at the end of 2004 | | |
|---------------|-----------------|---------------------------------------|------------------------|---|-----------------------------|------------------------|-------------------------|-------------------------------|------------------------|----------------------------------|-------------------------|---------------------------------|------------------------|-------------------------|
| (A) | (B) | (1) | (2) | (3) | (4) | (5) | (6) | (7) | (8) | (9) | (10) | (11) = 1+4-7-10 | (12) | (13) |
| Name | Post held | Number of TIM options | Average exercise price | Average expiration date | Number of options | Average exercise price | Average expiration date | Number of options | Average exercise price | Average market price during year | Number of options | Number of TIM options | Average exercise price | Average expiration date |
| Giuseppe Sala | General Manager | 480,000 | 5.07 | 1/3 until May 2008, 1/3 until May 2009 and 1/3 until May 2010 | = | = | = | 480,000 | 5.07 | 5.49 | = | = | = | |

Note:

Each option corresponds to the subscription or purchase of one share.

These refer to TIM options relating to a stock option plan granted as the director of Finance and Control at TIM.

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■ ANNEX N. 1

LONG-TERM INVESTMENTS AND ADVANCES ON CAPITAL CONTRIBUTIONS OF SUBSIDIARIES AND AFFILIATED COMPANIES

| | 12.31.2003 | | | | Changes during the year | | | | | | 12.31.2004 | | | | |
|---|------------|----------------------------|-------------|---------------------|--|----------------------------------|----------------------------------|---------------------|--|--------------------------------|-------------|------------|----------------------------|-------------|-------------------|
| | | Upward adjust- ments | Writedowns | Carrying value | Contribut. merged companies at 12.31.2003 | Purchases/ Sub- scriptions | Reclassi- fications | Disposals (1) | Writedowns(-) Writebacks of value(+) | Capital Replenish- ments | Total | Cost | Upward adjust- ments | Writedowns | Carrying value |
| (in thousands of euro) | Cost | | | | | | | | | | | | | | |
| Equity investments in subsidiaries | | | | | | | | | | | | | | | |
| ATESIA | 3,707 | - | - | 3,707 | | | (1,042) | (2,665) | | | (3,707) | - | - | - | - |
| DOMUS ACCADEMY | 2,400 | - | - | 2,400 | | | | | | | - | 2,400 | - | - | 2,400 |
| EDOTEL | 9,056 | - | (6,914) | 2,142 | | 1,459 | (3,647) | - | 46 | | (2,142) | - | - | - | - |
| EMSA SERVIZI | 5,000 | - | - | 5,000 | | | | | | | - | 5,000 | - | - | 5,000 |
| EPIClink | 450 | - | (450) | - | | | - | | | | - | - | - | - | - |
| EUSTEMA | - | - | - | - | 465 | | | | | | 465 | 465 | - | - | 465 |
| FINSIEL | 364,680 | - | (115,000) | 249,680 | | | | | (138,680) | | (138,680) | 364,680 | - | (253,680) | 111,000 |
| IT TELECOM SPA | 171,521 | - | (114,871) | 56,650 | | | (56,650) | - | | | (56,650) | - | - | - | - |
| IT TELECOM SRL | - | - | - | - | | 30 | 132,743 | | | | 132,773 | 132,773 | - | - | 132,773 |
| INTELCOM SAN MARINO | - | - | - | - | | | | | | | - | - | - | - | - |
| IRIDIUM ITALIA (in liquidation) | 775 | - | (775) | - | | 945 | | | 775 | | 1,720 | 1,720 | - | - | 1,720 |
| LATIN AMERICAN NAUTILUS S.A. | 5,241 | - | (3,268) | 1,973 | | 40,801 | | | (42,774) | | (1,973) | 46,042 | - | (46,042) | - |
| LOQUENDO | 7,820 | - | (7,820) | - | | | | | | | - | 7,820 | - | (7,820) | - |
| MED-1 Submarine Cables | 5 | - | - | 5 | | | | | (5) | | (5) | 5 | - | (5) | - |
| MEDITERRANEAN NAUTILUS S.A. | 14,352 | - | - | 14,352 | | | | | | | - | 14,352 | - | - | 14,352 |
| NETESI (in liquidation) | 14,745 | - | (14,745) | - | | | 435 | - | (79) | | 356 | 435 | - | (79) | 356 |
| OFI CONSULTING | 78,940 | - | (43,831) | 35,109 | | | | | | | - | 78,940 | - | (43,831) | 35,109 |
| OLIVETTI GESTION I IVREA | 7,516 | - | - | 7,516 | | | | (4,849) | (508) | | (5,357) | 2,667 | - | (508) | 2,159 |
| OLIVETTI INTERNATIONAL | 442,740 | - | (162,177) | 280,563 | | | (280,563) | | | | (280,563) | - | - | - | - |
| OLIVETTI MULTISERVICES | 41,042 | - | (639) | 40,403 | | | | | | | - | 41,042 | - | (639) | 40,403 |
| OLIVETTI TECNOST | 78,000 | - | (27,749) | 50,251 | | | | | 49,274 | | 49,274 | 99,525 | - | - | 99,525 |
| PATH.NET | 25,820 | - | - | 25,820 | 3 | | | | | | 3 | 25,823 | - | - | 25,823 |
| SAIAT | 34,743 | 11,616 | - | 46,359 | | | | | | | - | 34,743 | 11,616 | - | 46,359 |
| TECNO SERVIZI MOBILI | 53 | - | - | 53 | | | | | | | - | 53 | - | - | 53 |
| TECO SOFT ARGENTINA (in liquid.) | - | - | - | - | - | 6,671 | (6,671) | | | | - | 6,685 | - | (6,685) | - |
| TELECOM ITALIA AMERICA LATINA | 13,220 | - | (13,220) | - | | | | | | | - | 13,220 | - | (13,220) | - |
| TELECOM ITALIA AUDIT | 1,750 | - | - | 1,750 | | | | | | | - | 1,750 | - | - | 1,750 |
| TELECOM ITALIA CAPITAL SA | 2,388 | - | - | 2,388 | | | | | | | - | 2,388 | - | - | 2,388 |
| TELECOM ITALIA DEUTSCHLAND HOLDING | 243,201 | - | - | 243,201 | | | | | | | - | 243,201 | - | - | 243,201 |
| TELECOM ITALIA INTERNATIONAL | 7,851,463 | - | (3,545,848) | 4,305,615 | | | | (1,800,000) | (256,990) | | (2,056,990) | 4,629,735 | - | (2,381,110) | 2,248,625 |
| TELECOM ITALIA LEARNING SERVICES | 1,560 | - | (1,560) | - | | 4,846 | | - | (6,406) | 1,560 | - | 1,560 | - | (1,560) | - |
| TELECOM ITALIA MEDIA | 1,974,913 | - | (1,227,787) | 747,126 | 102 | 71,616 | | | (112,416) | | (40,698) | 2,046,631 | - | (1,340,203) | 706,428 |
| TELECOM ITALIA MOBILE | 27,182,687 | 84,144 | - | 27,266,831 | | | 198,255 | | | | 198,255 | 27,380,942 | 84,144 | - | 27,465,086 |
| TELECONTACT CENTER | 110 | - | - | 110 | | | 379 | | | | 379 | 489 | - | - | 489 |
| TELENERGIA | 40 | - | - | 40 | | | | | | | - | 40 | - | - | 40 |
| TELESOFT ZAO RUSSIA | - | - | - | - | - | 4,148 | (4,148) | - | | | - | - | - | - | - |
| TELSY | 14,512 | - | - | 14,512 | | | | | | | - | 14,512 | - | - | 14,512 |
| TI FINANCE | 607,507 | 38,057 | (645,564) | - | | | 1,786,234 | - | | | 1,786,234 | 1,786,234 | - | - | 1,786,234 |
| TI LAB GENERAL PARTNER (in liquid.) | 33 | - | (12) | 21 | | | | (9) | (12) | | (21) | - | - | - | - |
| TI LAB SA | 131 | - | (83) | 48 | | | | | (48) | | (48) | 131 | - | (131) | - |
| TI SPARKLE | 784,765 | - | - | 784,765 | | | | | | | - | 784,765 | - | - | 784,765 |
| TRAINET (in liquidation) | 674 | - | (674) | - | | | | | | | - | 674 | - | (674) | - |
| WEBEGG | - | - | - | - | 46,595 | | (46,595) | | | | - | - | - | - | - |
| Consorzio IRIS | - | - | - | - | 15 | | | | | | 15 | 15 | - | - | 15 |
| Consorzio Energia Gruppo Telecom Italia | 5 | - | - | 5 | | | | | | | - | 5 | - | - | 5 |
| Consorzio TURISTEL | - | - | - | - | 26 | | | | | | 26 | 26 | - | - | 26 |
| | 39,987,565 | 133,817 | (5,932,987) | 34,188,395 | 47,206 | 130,516 | 1,765,325 | (1,854,118) | (507,823) | 1,560 | (417,334) | 37,771,488 | 95,760 | (4,096,187) | 33,771,061 |
| (1) | ATESIA | EDOTEL | IT TELECOM | NETESI (in liquid.) | OLIVETTI GESTION I IVREA | TELECOM ITALIA INTERNAT. | TELECOM ITALIA LEARNING SERVICES | TELESOFT ZAO RUSSIA | TELECOM ITALIA FINANCE | TILAB GP (in liquid.) | WEBEGG | | | | |
| Cost | 2,665 | 6,868 | 114,871 | 15,960 | 4,849 | 3,221,727 | 6,406 | 4,638 | 645,564 | 33 | 80,269 | | | | |
| Writedowns | - | (6,868) | (114,871) | (15,960) | - | (1,421,727) | (6,406) | (4,638) | (645,564) | (24) | (33,674) | | | | |
| | 2,665 | - | - | - | - | 4,849 | 1,800,000 | - | - | 9 | 46,595 | | | | |

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|---|----------------|----------------------------|--------------------------------|-------------------|--|----------------------------------|------------------------|------------------|--|--------------------------------|-------------------------------------|----------------|----------------------------|-----------------|-------------------|
| | Cost | Upward adjust- ments | Writedowns | Carrying value | Contribut. merged companies at 12.31.2003 | Purchases/ Sub- scriptions | Reclassi- fications | Disposals (1) | Writedowns(-) Writebacks of value(+) | Capital Replenish- ments | Total | Cost | Upward adjust- ments | Writedowns | Carrying value |
| Equity investments in affiliated companies | | | | | | | | | | | | | | | |
| AREE URBANE | 5,589 | - | - | 5,589 | | | | | | | - | 5,589 | - | - | 5,589 |
| ASSCOM INSURANCE BROKERS | 20 | - | - | 20 | | | | | | | - | 20 | - | - | 20 |
| CARTESIA (in liquidation) | 50 | - | - | 50 | | | | | (50) | | (50) | 50 | - | (50) | - |
| EUROFLY SERVICE | - | - | - | - | | | - | | | | - | 2,304 | - | (2,304) | - |
| IM.SER | 399 | - | - | 399 | | | (168) | - | | 125 | (43) | 356 | - | - | 356 |
| IN.VA. | 206 | - | (45) | 161 | | | | | | | - | 206 | - | (45) | 161 |
| LI.SIT. | 37,400 | - | (3,258) | 34,142 | | | | | (5,993) | | (5,993) | 37,400 | - | (9,251) | 28,149 |
| LOCALPORT | 145 | - | (145) | - | | | | - | | | - | - | - | - | - |
| MIRROR INTERNATIONAL HOLDING | 124,689 | - | (70,000) | 54,689 | | | | (54,689) | | | (54,689) | - | - | - | - |
| NORDCOM | 29,045 | - | (26,902) | 2,143 | | | | | | | - | 29,045 | - | (26,902) | 2,143 |
| OCN TRADING (in liquidation) | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| PEGASO | - | - | - | - | | | 7 | | | | 7 | 8 | - | (1) | 7 |
| SHARED SERVICES CENTER | - | - | - | - | 613 | 306 | | | | | 919 | 919 | - | - | 919 |
| SIEMENS INFORMATICA | 2,417 | 1,424 | - | 3,841 | | | | | | | - | 2,417 | 1,424 | - | 3,841 |
| SINOPIA INFORMATICA (in failure) | - | - | - | - | | | | | | | - | - | - | - | - |
| SIOSISTEMI | 3,305 | - | (1,705) | 1,600 | | | | (1,600) | | | (1,600) | - | - | - | - |
| SKY ITALIA | 282,358 | - | (238,279) | 44,079 | | 19,315 | 24,465 | (87,859) | | | (44,079) | - | - | - | - |
| SOFORA TELECOMUNICACIONES S.A. | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| TELBIO | 3,375 | - | - | 3,375 | | | | - | (3,178) | 993 | (2,185) | 1,267 | - | (77) | 1,190 |
| TELEGONO | 413 | - | - | 413 | | | | | | | - | 413 | - | - | 413 |
| TIGLIO I | 227,273 | - | - | 227,273 | | | | (72,206) | | | (72,206) | 155,067 | - | - | 155,067 |
| TIGLIO II | 72,070 | - | - | 72,070 | | | | (24,735) | | | (24,735) | 47,335 | - | - | 47,335 |
| VOICE MAIL INTERNATIONAL (in liq.) | 3,801 | - | (3,801) | - | | | | - | | | - | - | - | - | - |
| Consorzio ARS (in liquidation) | - | - | - | - | | | | - | | | - | - | - | - | - |
| Consorzio DREAM FACTORY (in liquid.) | 89 | - | (89) | - | | | | | | | - | 89 | - | (89) | - |
| Consorzio EO (in liquidation) | 16 | - | - | 16 | | | | | | | - | 16 | - | - | 16 |
| Consorzio LABORATORIO DELLA CONOSCENZA | 14 | - | (4) | 10 | | | | | | | - | 14 | - | (4) | 10 |
| Consorzio NAVIGATE CONSORTIUM | 300 | - | - | 300 | | | | | | | - | 300 | - | - | 300 |
| Consorzio S.I.A.R.C. (in liquidation) | 1 | - | - | 1 | | 1 | (1) | - | | | - | 1 | - | - | 1 |
| Consorzio TELCAL | 211 | - | - | 211 | | | | | | | - | 211 | - | - | 211 |
| Consorzio TELEMED (in liquidation) | 10 | - | - | 10 | | | | | | | - | 10 | - | - | 10 |
| | 793,198 | 1,424 | (344,228) | 450,394 | 613 | 19,622 | 24,303 | (241,089) | (9,221) | 1,118 | (204,654) | 283,039 | 1,424 | (38,723) | 245,740 |
| | | | | | | | | | | | | | | | |
| (1) | IM.SER | LOCAL- PORT | MIRROR INTERNAT. HOLDING | SIOSISTEMI | SKY ITALIA | TELBIO | TIGLIO I | TIGLIO II | VOICE MAIL (in liquid.) | Cons. ARS (in liquid.) | Cons. S.I.A.R.C. (in liquid.) | | | | |
| Cost | 168 | 145 | 124,689 | 3,305 | 345,453 | 3,101 | 72,206 | 24,735 | 3,801 | - | 1 | | | | |
| Writedowns | (168) | (145) | (70,000) | (1,705) | (257,594) | (3,101) | - | - | (3,801) | - | (1) | | | | |
| | - | - | 54,689 | 1,600 | 87,859 | - | 72,206 | 24,735 | - | - | - | | | | |

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|---|-------------------------|----------------------------|-----------------------|--------------------------------------|--|----------------------------------|---|--------------------------|--|--------------------------------|------------|------------|----------------------------|-------------|-------------------|
| (in thousands of euro) | Cost | Upward adjust- ments | Writedowns | Carrying value | Contribut. merged companies at 12.31.2003 | Purchases/ Sub- scriptions | Reclassi- fications | Disposals (1) | Writedowns(-) Writebacks of value(+) | Capital Replenish- ments | Total | Cost | Upward adjust- ments | Writedowns | Carrying value |
| Equity investments in other companies | | | | | | | | | | | | | | | |
| ADDED (in liquidation) | - | - | - | - | 1 | | (1) | - | | | - | - | - | - | - |
| ANCITEL | 93 | - | - | 93 | | | | | | | - | 93 | - | - | 93 |
| ATESIA | - | - | - | - | | | 663 | | | | 663 | 663 | - | - | 663 |
| AZIENDA ESERCIZIO GAS | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| BIOINDUSTRY PARK DEL CANAVESE | 52 | - | - | 52 | | | | | | | - | 52 | - | - | 52 |
| CAF ITALIA 2000 | - | - | - | - | | | | | | | - | - | - | - | - |
| CERM L'AQUILA | 266 | - | - | 266 | | | | | | | - | 266 | - | - | 266 |
| CONSORTIUM | 19,527 | - | - | 19,527 | | | | | | | - | 19,527 | - | - | 19,527 |
| DIOMEDEA (in liquidation) | 6 | - | - | 6 | | | | | | | - | 6 | - | - | 6 |
| EDINDUSTRIA | 44 | - | (6) | 38 | | | | | | | - | 44 | - | (6) | 38 |
| EMITTENTI TITOLI | 424 | - | - | 424 | | | | | | | - | 424 | - | - | 424 |
| EUROFLY SERVICE | 978 | - | (277) | 701 | | 1,334 | (2,035) | | | | (701) | - | - | - | - |
| FIN. PRIV. | 15,375 | - | - | 15,375 | | | | | | | - | 15,375 | - | - | 15,375 |
| Fratelli ALINARI | 2,974 | - | (2,273) | 701 | | | | | | | - | 2,974 | - | (2,273) | 701 |
| FUNIVIE DEL PICCOLO S. BERNARDO | - | - | - | - | | | | | | | - | - | - | - | - |
| IDROENERGIA | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| IMSER 60 | 59 | - | - | 59 | | | | | | | - | 59 | - | - | 59 |
| INSULA | 248 | - | - | 248 | | | | | | | - | 248 | - | - | 248 |
| IST. ENCICLOPEDIA ITALIANA G. TRECCANI | 5,256 | - | (1,424) | 3,832 | | | | | | | - | 5,256 | - | (1,424) | 3,832 |
| ISTUD | 6 | - | - | 6 | | | | | | | - | 6 | - | - | 6 |
| ITALTEL CERM PALERMO | 217 | - | (24) | 193 | | | | | | | - | 217 | - | (24) | 193 |
| ITALTEL CERM S. MARIA CAPUA VETERE | 255 | - | (63) | 192 | | | | | | | - | 255 | - | (63) | 192 |
| MCC | 36,018 | - | - | 36,018 | | | | | | | - | 36,018 | - | - | 36,018 |
| MEDIOBANCA | 113,119 | - | - | 113,119 | | | | | | | - | 113,119 | - | - | 113,119 |
| MIX | 10 | - | - | 10 | | | | | | | - | 10 | - | - | 10 |
| MONTEROSA | 20 | - | - | 20 | | | | | | | - | 20 | - | - | 20 |
| PAR. FIN. (in failure) | 256 | - | - | 256 | | | | | (256) | | (256) | 256 | - | (256) | - |
| PILA | 6 | - | - | 6 | | | | | | | - | 6 | - | - | 6 |
| PIRELLI RE | 15,199 | - | - | 15,199 | | | | (15,199) | | | (15,199) | - | - | - | - |
| S.A.G.I.T. | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| SIA | 11,278 | - | - | 11,278 | | | | | | | - | 11,278 | - | - | 11,278 |
| SODETEL | 4 | - | - | 4 | | | | | | | - | 4 | - | - | 4 |
| UBAE | 1,898 | - | - | 1,898 | | | | | | | - | 1,898 | - | - | 1,898 |
| Consorzio ABI LAB | - | - | - | - | | 1 | | | | | 1 | 1 | - | - | 1 |
| Consorzio C.I. MARK | 3 | - | - | 3 | | | (3) | - | | | (3) | - | - | - | - |
| Consorzio CAISI (in liquidation) | - | - | - | - | | | | - | | | - | - | - | - | - |
| Consorzio CEFRIEL | 36 | - | - | 36 | | | | | | | - | 36 | - | - | 36 |
| Consorzio CIES | 26 | - | - | 26 | | | | | | | - | 26 | - | - | 26 |
| Consorzio CO.TIM (in liquidation) | 4 | - | (2) | 2 | | | (2) | - | | | (2) | - | - | - | - |
| Consorzio COREP | 10 | - | - | 10 | | | | | | | - | 10 | - | - | 10 |
| Consorzio CRATI | - | - | - | - | | | | - | | | - | - | - | - | - |
| Consorzio BIOINGEGNERIA INFORMATICA MEDICA | 15 | - | - | 15 | | | (15) | - | | | (15) | - | - | - | - |
| Consorzio DISTRETTO AUDIOVISIVO E dell'ICT | - | - | - | - | | 5 | | | | | 5 | 5 | - | - | 5 |
| Consorzio DISTRETTO TECNOLOGICO CANAVESE | 117 | - | - | 117 | | | | | | | - | 117 | - | - | 117 |
| Consorzio ELIS | 3 | - | - | 3 | | | | | | | - | 3 | - | - | 3 |
| Consorzio ENERGIA FIERA DISTRICT | 2 | - | - | 2 | | | | | | | - | 2 | - | - | 2 |
| Consorzio GE.SE.CE.DI. | 73 | - | - | 73 | | | (73) | - | | | (73) | - | - | - | - |
| Consorzio MULTIMEDIA | - | - | - | - | | | | - | | | - | - | - | - | - |
| Consorzio Nazionale Imballaggi - CONAI | 1 | - | - | 1 | | | | | | | - | 1 | - | - | 1 |
| Consorzio NETTUNO | 41 | - | - | 41 | | | (41) | - | | | (41) | - | - | - | - |
| Consorzio QUALITAL | - | - | - | - | | | | | | | - | - | - | - | - |
| Consorzio TECHNAPOLI | 206 | - | - | 206 | | | | | | | - | 206 | - | - | 206 |
| Consorzio TOPIX | 100 | - | - | 100 | | | | | | | - | 100 | - | - | 100 |
| | 224,228 | - | (4,069) | 220,159 | 1 | 1,340 | (1,507) | (15,199) | (256) | - | (15,621) | 208,584 | - | (4,046) | 204,538 |
| Total Equity investments | 41,004,991 | 135,241 | (6,281,284) | 34,858,948 | 47,820 | 151,478 | 1,788,121 | (2,110,406) | (517,300) | 2,678 | (637,609) | 38,263,111 | 97,184 | (4,138,956) | 34,221,339 |
| (1) | ADDED (in liquidaz.) | PIRELLI RE | Consorzio C.I.MARK | Consorzio CAISI (in liquidaz.) | Consorzio COTIM (in liquidaz.) | Consorzio CRATI | Consorzio BIOINGEGNERIA INFORMATICA | Consorzio GE.SE.CE.DI | Consorzio MULTIMEDIA | Consorzio NETTUNO | | | | | |
| Cost | 1 | 15,199 | 3 | - | 4 | - | 15 | 73 | - | 41 | | | | | |
| Writedowns | (1) | - | (3) | - | (4) | - | (15) | (73) | - | (41) | | | | | |
| | - | 15,199 | - | - | - | - | - | - | - | - | | | | | |

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■ ANNEX N. 2

LIST OF EQUITY INVESTMENTS IN SUBSIDIARIES AND AFFILIATED COMPANIES AT 12.31.2004

| (in thousands of euro) | Registered office | Share capital (1) | Shareholders' equity (1) (2) | Net income/ (loss) (1) | Percentage owner-ship (%) | Share of net equity (A) (3) | Carrying value (B) (4) | Difference (B-A) |
|---|--|--------------------|------------------------------|------------------------|---------------------------|----------------------------------|------------------------|-------------------|
| Equity investments in subsidiaries | | | | | | | | |
| DOMUS ACCADEMY | Milan | 140 | 529 | (237) | 67.33% | 356 | 2,400 | 2,044 |
| EMSA SERVIZI | Rome | 5,000 | 6,579 | 20 | 100.00% | 6,579 | 5,000 | (1,579) |
| EUSTEMA | Rome | 312 | 2,266 | 118 | 67.33% | 1,526 | 465 | (1,061) |
| FINSIEL | Rome | 59,982 | 185,477 | (279) | 79.50% | 136,779 ⁽⁶⁾ | 111,000 | (25,779) |
| IT TELECOM SRL | Milan | 25,000 | 132,773 | - | 100.00% | 132,773 | 132,773 | - |
| INTELCOM SAN MARINO | San Marino | 1,550 | 2,014 | (1,652) | 0.0001% | - | - | - |
| IRIDIUM ITALIA (in liquidation) | Rome | 2,575 | 3,321 | 7,088 | 65.00% | 2,159 | 1,720 | (439) |
| LATIN AMERICAN NAUTILUS S.A. | Luxemburg US\$ (,000)55,500 | (29,628) 40,746 | (81,120) (21,752) | - (59,555) | - 99.99% | - (21,752) ^{(6) (5)} | - - | - 21,752 |
| LOQUENDO | Turin | 3,574 | 3,547 | 321 | 99.98% | 3,546 | 3,224 | (322) |
| MED-1 Submarine Cables | Tel Aviv (Israel) NIS (,000) | 100 17 | (171,782) (29,227) | (80,087) (13,626) | - 23.17% | - (6,699) ^{(6) (5)} | - - | - 6,699 |
| MEDITERRANEAN NAUTILUS S.A. | Luxemburg US\$ (,000)326,480 | 42,987 239,689 | (290,216) 31,559 | (213,065) | 62.51% | 19,728 | 14,352 | (5,376) |
| NETESI (in liquidation) | Milan | 435 | 245 | (189) | 100.00% | 245 ⁽⁵⁾ | 356 | 111 |
| OFI CONSULTING | Ivrea (To) | 95 | 40,694 | 2,295 | 100.00% | 40,694 | 35,109 | (5,585) |
| OLIVETTI GESTION IIVREA | Ivrea (To) | 1,300 | 2160 | (15) | 100.00% | 2,160 | 2,159 | (1) |
| OLIVETTI MULTISERVICES | Ivrea (To) | 20,337 | 38,618 | 625 | 100.00% | 38,618 | 40,403 | 1,785 |
| OLIVETTI TECNOST | Ivrea (To) | 78,000 | 99,524 | 49,274 | 100.00% | 69,367 ⁽⁶⁾ | 99,525 | 30,158 |
| PATH.NET | Rome | 25,800 | 34,884 | 6,578 | 100.00% | 28,684 | 25,823 | (2,861) |
| SAIAT | Turin | 35,745 | 43,099 | 1,074 | 100.00% | 43,099 | 46,359 | 3,260 |
| TECNO SERVIZI MOBILI | Rome | 26 | 1,304 | 654 | 51.00% | 665 | 53 | (612) |
| TECO SOFT ARGENTINA (in liquidation) | Bueno Aires Pesos Arg. (,000) (Argentina) | 12 3 | (1,225) (302) | (1,060) (261) | 99.99% | (302) ⁽⁵⁾ | - | 302 |
| TELECOM ITALIA AMERICA LATINA | San Paolo R \$ (,000) (Brazil) | 43,614 12,063 | 2,433 673 | 3,648 1,009 | 99.99% | - 673 | - - | - (673) |
| TELECOM ITALIA AUDIT | Milan | 2,750 | 2,545 | (46) | 63.64% | 1,620 ⁽⁵⁾ | 1,750 | 130 |
| TELECOM ITALIA CAPITAL SA | Luxemburg | 2,336 | 3,380 | 676 | 99.99% | 3,380 | 2,388 | (992) |
| TELECOM ITALIA DEUTSCHLAND HOLDING | Amburgo (Germany) | 25 | 253,177 | 8,224 | 100.00% | 253,177 | 243,201 | (9,976) |
| TELECOM ITALIA INTERNATIONAL | Amsterdam (Holland) | 2,399,483 | 2,248,625 | (256,990) | 100.00% | 2,248,625 | 2,248,625 | - |
| TELECOM ITALIA LEARNING SERVICES | Milan | 1,560 | (2,833) | (15,854) | 100.00% | (2,833) ⁽⁵⁾ | - | 2,833 |
| TELECOM ITALIA MEDIA ⁽⁷⁾ | Rome | 111,108 | 435,374 | (21,351) | 59.43% | 186,885 ⁽⁶⁾ | 706,428 | 519,543 |
| TELECOM ITALIA MOBILE | Turin | 515,729 | 9,764,632 | 2,821,781 | 55.08% | 2,881,623 ⁽⁶⁾ | 27,465,086 | 24,583,463 |
| TELECONTACT CENTER | Naples | 770 | 5,306 | 315 | 100.00% | 5,306 | 489 | (4,817) |
| TELENERGIA | Rome | 50 | 1,578 | 1,288 | 80.00% | 1,262 | 40 | (1,222) |
| TELSY | Turin | 390 | 11,763 | 1,833 | 100.00% | 11,063 | 14,512 | 3,449 |
| TI FINANCE | Luxemburg | 542,090 | 1,857,076 | (185,256) | 99.99% | 1,857,076 | 1,786,234 | (70,842) |
| TI LAB SA | Luxemburg US\$ (,000)164 | (4,272) | (4,333) | - | - | - | - | - |
| | | 120 | (3,136) | (3,181) | 99.99% | (3,136) ⁽⁵⁾ | - | 3,136 |
| TI SPARKLE | Rome | 200,000 | 921,993 | 59,563 | 100.00% | 817,652 ⁽⁶⁾ | 784,765 | (32,887) |
| TRAINET (in liquidation) | Rome | 674 | (1,203) | (725) | 100.00% | (1,203) ⁽⁵⁾ | - | 1,203 |
| Consorzio Energia Gruppo Telecom Italia | Rome | 10 | 10 | - | 50.00% | 5 | 5 | - |
| Consorzio IRIS | Rome | 170 | 170 | - | 9.10% | 15 | 15 | - |
| Consorzio TURISTEL | Rome | 77 | 77 | - | 33.33% | 26 | 26 | - |
| | | | | | | | 33,774,285 | 25,014,844 |

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| (in thousands of euro) | Registered office | Share capital (1) | Shareholders' equity (1) (2) | Net income/ (loss) (1) | Percentage owner-ship (%) | Share of net equity (A) (3) | Carrying value (B) (4) | Difference (B-A) |
|---|---|--------------------|------------------------------|------------------------|---------------------------|-----------------------------|------------------------|------------------|
| Equity investments in affiliated companies | | | | | | | | |
| AREE URBANE | Milan | 308 | 17,394 | (688) | 31.65% | 5,505 ⁽⁵⁾ | 5,589 | 84 |
| ASSCOM INSURANCE BROKERS | Milan | 100 | 431 | 331 | 20.00% | 86 | 20 | (66) |
| CARTESIA (in liquidation) | Rome | 100 | (1,643) | (2,090) | 50.00% | (822) ⁽⁵⁾ | - | 822 |
| EUROFLY SERVICE | Caselle Torinese (Turin) | 8,275 | 6,052 | (1,688) | 24.55% | 1,486 | - | (1,486) |
| IM.SER | Turin | 890 | 578 | (314) | 40.00% | 231 ⁽⁵⁾ | 356 | 125 |
| IN.VA. | Aosta | 520 | 1,367 | 190 | 40.00% | 547 | 161 | (386) |
| LI.SIT. | Milan | 6,500 | 45,849 | (25,801) | 24.20% | 11,095 | 28,149 | 17,054 |
| NORDCOM | Milan | 5,000 | 5,545 | 143 | 42.00% | 2,329 | 2,143 | (186) |
| OCN TRADING (in liquidation) | Ivrea (TO) | 41 | (34) | 9 | 40.00% | (13) ⁽⁵⁾ | 1 | 14 |
| PEGASO | Caselle Torinese (Turin) | 20 | 20 | | 24.55% | 5 | 7 | 2 |
| SHARED SERVICES CENTER | Milan | 1,040 | 1,267 | | 40.91% | 878 ^{(8) (5)} | 919 | 41 |
| SIEMENS INFORMATICA | Milan | 6,192 | 28,652 | (5,321) | 49.00% | 14,039 | 3,841 | (10,198) |
| SINOPIA INFORMATICA (in failure) | Bologna | 157 | | | 21.31% | - | - | - |
| SOFORA TELECOMUNICACIONES S.A. | Buenos Aires Pesos Arg.(,000) (Argentina) | 439,702 108,365 | 323,702 79,776 | (116,000) (28,588) | 32.50% | - 25,927 | 1 | - (25,926) |
| TELBIO | Milan | 2,948 | 884 | (2,095) | 31.03% | 1,268 ⁽⁸⁾ | 1,190 | (78) |
| TELEGONO | Rome | 1,000 | (312) | (2,516) | 40.00% | 8,715 ^{(8) (5)} | 9,253 | 538 |
| TIGLIO I | Milan | 5,256 | 361,632 | (12,523) | 45.70% | 145,612 ⁽⁸⁾ | 155,067 | 9,455 |
| TIGLIO II | Milan | 14,185 | 160,897 | 3,562 | 49.47% | 54,860 ⁽⁸⁾ | 47,335 | (7,525) |
| Consorzio DREAM FACTORY (in liquidation) | Rome | 20 | (28) | (23) | 20.00% | (6) ⁽⁵⁾ | - | 6 |
| Consorzio EO (in liquidation) | Rome | 19 | 12 | (8) | 50.00% | 6 ⁽⁵⁾ | 16 | 10 |
| Consorzio LABORATORIO DELLA CONOSCENZA | Naples | 52 | 31 | (10) | 25.00% | 8 ⁽⁵⁾ | 10 | 2 |
| Consorzio NAVIGATE CONSORTIUM | Milan | 583 | 586 | | 20.00% | 117 ⁽⁵⁾ | 300 | 183 |
| Consorzio S.I.A.R.C. (in liquidation) | Napoli | 26 | 22 | (4) | 30.00% | 7 | 1 | (6) |
| Consorzio TELCAL | Catanzaro | 878 | 878 | | 24.00% | 211 | 211 | 0 |
| Consorzio TELEMED (in liquidation) | Rome | 103 | 21 | (7) | 33.33% | 7 ⁽⁵⁾ | 10 | 3 |
| | | | | | | | 254,580 | (17,518) |

(1) Data taken from the latest approved financial statements.

(2) Includes net income (loss).

(3) Net of dividends paid.

(4) Includes advances on future capital contributions of subsidiaries and affiliated companies.

(5) Covered by reserve for losses of subsidiaries and affiliated companies.

(6) Data taken from the consolidated financial statements.

(7) Does not include stock included in short-term financial assets.

(8) "Share of net equity" is taken from the latest approved financial statements, only restated of the operations on share capital in 2004, to let a comparison to carrying value.

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■ ANNEX N. 3

COMPARISON OF THE CARRYING VALUE OF LISTED SHARES WITH MARKET PRICES AT DECEMBER 31, 2004

| STATEMENT OF FINANCIAL POSITION - BALANCE SHEET - 31 DECEMBER 2017 | | | | | | | |
|--|--------------------------|-------------------------|---------------------------------|-------------------------|---------------------------------|-------------------------|---------------------------------|
| | Number of shares held | Market value | | Carrying value | | Difference | |
| | | Unit price (in euro) | Total (thousands of euro) | Unit price (in euro) | Total (thousands of euro) | Unit price (in euro) | Total (thousands of euro) |
| | | (A) | | (B) | | (A-B) | |
| Equity investments | | | | | | | |
| MEDIOBANCA | 14,118,350 | 11.91 | 168,150 | 8.01 | 113,119 | 3.90 | 55,031 |
| TELECOM ITALIA MOBILE | | | | | | | |
| - ordinary shares | 4,734,081,519 | 5.50 | 26,027,980 | 5.80 | 27,465,086 | (0.30) | (1,437,106) |
| TELECOM ITALIA MEDIA | | | | | | | |
| - ordinary shares | 2,201,183,545 | 0.33 | 719,787 | 0.32 | 706,428 | 0.01 | 13,359 |
| Short - term financial assets | | | | | | | |
| TELECOM ITALIA MEDIA | | | | | | | |
| - saving shares | 195,236 | 0.27 | 52 | 0.27 | 52 | - | - |
| PORTAL SOFTWARE INC. | 4,000 | 1.92 | 8 | 1.92 | 8 | - | - |

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■ ANNEX N. 4

ACCOUNTS RECEIVABLE AND ACCRUED INCOME BY MATURITY AND TYPE

| (in thousands of euro) | 12.31.2004 Amounts due | | | | 12.31.2003 Amounts due | | | |
|---|---------------------------|------------------------|-------------------|------------------|---------------------------|------------------------|-------------------|-------------------|
| | Within one year | From two to five years | Beyond five years | Total | Within one year | From two to five years | Beyond five years | Total |
| Accounts receivable in long-term investments | | | | | | | | |
| subsidiaries | 4,613 | 443,713 | | 448,326 | 2,891 | 64,207 | | 67,098 |
| affiliated companies | 2,841 | 22,703 | | 25,544 | 95 | 17,363 | 37,031 | 54,489 |
| others | | | | | | | | |
| - customers | | | | 0 | 269 | 67 | | 336 |
| - employees | 7,092 | 34,878 | 12,971 | 54,941 | 14,981 | 23,255 | 9,249 | 47,485 |
| - security deposits | 7 | 3,139 | 371 | 3,517 | 262 | 3,110 | 12,566 | 15,938 |
| - time deposit on behalf of Getronics | | | | 0 | 32,067 | | | 32,067 |
| - miscellaneous | 11,876 | 36,629 | 946 | 49,451 | 21,035 | 40,568 | | 61,603 |
| | 26,429 | 541,062 | 14,288 | 581,779 | 71,600 | 148,570 | 58,846 | 279,016 |
| Accounts receivable in current assets | | | | | | | | |
| Other financial receivables from | | | | | | | | |
| subsidiaries | 706,952 | | | 706,952 | 823,919 | | | 823,919 |
| affiliated companies | 113 | | | 113 | 13,718 | | | 13,718 |
| others | 345,876 | | | 345,876 | 366,594 | | | 366,594 |
| | 1,052,941 | | | 1,052,941 | 1,204,231 | | | 1,204,231 |
| Trade accounts receivable from | | | | | | | | |
| customers | 3,121,009 | | | 3,121,009 | 3,703,450 | | | 3,703,450 |
| subsidiaries | 493,728 | | | 493,728 | 679,507 | | | 679,507 |
| affiliated companies | 114,444 | | | 114,444 | 70,955 | | | 70,955 |
| others | 78,030 | | | 78,030 | 87,984 | | | 87,984 |
| | 3,807,211 | | | 3,807,211 | 4,541,896 | | | 4,541,896 |
| Other receivables from | | | | | | | | |
| subsidiaries | 1,463,032 | | | 1,463,032 | 1,571,863 | | | 1,571,863 |
| affiliated companies | 11,918 | | | 11,918 | 12,101 | | | 12,101 |
| taxes receivable | 494,318 | | | 494,318 | 1,362,329 | | | 1,362,329 |
| deferred tax assets | 1,312,544 | 1,078,919 | | 2,391,463 | 1,174,778 | 2,055,138 | | 3,229,916 |
| miscellaneous: | | | | | | | | |
| - Government and other public entities for grants subsidies | 27,129 | | | 27,129 | 30,748 | | | 30,748 |
| - miscellaneous | 675,284 | | | 675,284 | 353,076 | | | 353,076 |
| | 3,984,225 | 1,078,919 | | 5,063,144 | 4,504,895 | 2,055,138 | | 6,560,033 |
| Total accounts receivable in current assets | 8,844,377 | 1,078,919 | | 9,923,296 | 10,251,022 | 2,055,138 | | 12,306,160 |
| Accrued income | | | | | | | | |
| financial | 60,472 | | | 60,472 | 20,423 | | | 20,423 |
| trading | | | | | 275 | | | 275 |
| miscellaneous | 4,669 | | | 4,669 | | | | |
| | 65,141 | 0 | 0 | 65,141 | 20,698 | 0 | 0 | 20,698 |

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■ ANNEX N. 5

LIABILITIES AND ACCRUED EXPENSES BY MATURITY AND TYPE

| (in thousands of euro) | 12.31.2004 Amounts due | | | | 12.31.2003 Amounts due | | | |
|---|---------------------------|------------------------|-------------------|-------------------|---------------------------|------------------------|-------------------|-------------------|
| | Within one year | From two to five years | Beyond five years | Total | Within one year | From two to five years | Beyond five years | Total |
| Medium and long-term financial debt | | | | | | | | |
| Debentures | | 2,360,000 | 10,341,250 | 12,701,250 | 1,500,000 | 1,250,000 | 7,014,983 | 9,764,983 |
| Convertible debentures | | | 2,824,947 | 2,824,947 | 1,330,564 | | 2,829,006 | 4,159,570 |
| Due to banks | 180,433 | 488,874 | 759 | 670,066 | 393,819 | 286,508 | 279 | 680,606 |
| Due to other lenders | 47,850 | 348,875 | 436,336 | 833,061 | 77,552 | 213,131 | 249,407 | 540,090 |
| Accounts payable to subsidiaries | 2,008,332 | 10,494,415 | 6,074,574 | 18,577,321 | 2,434,000 | 8,431,867 | 639,267 | 11,505,134 |
| Accounts payable to affiliated companies | 1,353 | 4,060 | | 5,413 | | | | |
| Taxes payable | | | | 0 | 23,430 | | | 23,430 |
| | 2,237,968 | 13,696,224 | 19,677,866 | 35,612,058 | 5,759,365 | 10,181,506 | 10,732,942 | 26,673,813 |
| Short-term borrowings | | | | | | | | |
| Due to banks | 235,577 | | | 235,577 | 510,488 | | | 510,488 |
| Due to other lenders | 211,660 | | | 211,660 | 241,795 | | | 241,795 |
| Accounts payable to subsidiaries | 967,781 | | | 967,781 | 7,798,130 | | | 7,798,130 |
| Accounts payable to affiliated companies | 485 | | | 485 | 1,027 | | | 1,027 |
| Other payables | 46,176 | | | 46,176 | 62,245 | | | 62,245 |
| | 1,461,679 | | | 1,461,679 | 8,613,685 | | | 8,613,685 |
| Trade accounts payable | | | | | | | | |
| Accounts payable to suppliers | 2,032,076 | | | 2,032,076 | 1,929,794 | | | 1,929,794 |
| Accounts payable to subsidiaries | 553,755 | | | 553,755 | 1,148,987 | | | 1,148,987 |
| Accounts payable to affiliated companies | 218,201 | | | 218,201 | 59,405 | | | 59,405 |
| | 2,804,032 | | | 2,804,032 | 3,138,186 | | | 3,138,186 |
| Other payables ⁽¹⁾ | | | | | | | | |
| Accounts payable to subsidiaries | 476,092 | 153,357 | | 629,449 | 91,269 | | | 91,269 |
| Accounts payable to affiliated companies | 760 | | | 760 | 24,339 | | | 24,339 |
| Taxes payable | 265,868 | | | 265,868 | 355,650 | | | 355,650 |
| Contributions to pension and social security institutions | 167,538 | 302,165 | 98,662 | 568,365 | 160,225 | 295,942 | 170,602 | 626,769 |
| Other liabilities | 1,921,333 | 53 | | 1,921,386 | 1,848,597 | 441 | | 1,849,038 |
| | 2,831,591 | 455,575 | 98,662 | 3,385,828 | 2,480,080 | 296,383 | 170,602 | 2,947,065 |
| Total liabilities ⁽¹⁾ | 9,335,270 | 14,151,799 | 19,776,528 | 43,263,597 | 19,991,316 | 10,477,889 | 10,903,544 | 41,372,749 |
| Accrued expenses | | | | | | | | |
| financial | 1,027,506 | | | 1,027,506 | 1,763,589 | 64,644 | | 1,828,233 |
| trading | 86 | | | 86 | 89 | | | 89 |
| miscellaneous | | | | 0 | | | | |
| | 1,027,592 | 0 | 0 | 1,027,592 | 1,763,678 | 64,644 | 0 | 1,828,322 |

(1) Not including the caption "Advances".

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■ ANNEX N. 6

ACCOUNTS RECEIVABLES AND LIABILITIES AT DECEMBER 31, 2004 - GEOGRAPHICAL AREA (CUSTOMER/SUPPLIER LOCATION)

| (in thousands of euro) | Italia | Rest of Europe | North America | Central and South America | Other areas | TOTAL |
|---|-------------------|-------------------|---------------|---------------------------|--------------|-------------------|
| Accounts receivable in long-term investments | | | | | | |
| subsidiaries | 377,856 | 70,470 | - | - | - | 448,326 |
| affiliated companies | 25,544 | - | - | - | - | 25,544 |
| others | 107,909 | - | - | - | - | 107,909 |
| Total | 511,309 | 70,470 | - | - | - | 581,779 |
| Accounts receivable in current assets (*) | | | | | | |
| customers | 3,062,863 | 44,170 | 3,482 | 8,899 | 1,595 | 3,121,009 |
| subsidiaries | 2,611,735 | 45,445 | - | 5,159 | 1,373 | 2,663,712 |
| affiliated companies | 123,425 | - | - | 2,455 | 595 | 126,475 |
| taxes receivable | 493,939 | - | - | 379 | - | 494,318 |
| others | 1,126,319 | - | - | - | - | 1,126,319 |
| | 7,418,281 | 89,615 | 3,482 | 16,892 | 3,563 | 7,531,833 |
| Liabilities | | | | | | |
| Debentures | 7,151,250 | 5,550,000 | - | - | - | 12,701,250 |
| Convertible debentures | 2,824,947 | - | - | - | - | 2,824,947 |
| Due to banks | 510,091 | 395,552 | - | - | - | 905,643 |
| Due to other lenders | 495,241 | 549,480 | - | - | - | 1,044,721 |
| Advances | 32,584 | - | - | - | - | 32,584 |
| Accounts payable to suppliers | 1,976,590 | 45,772 | 5,690 | 1,609 | 2,415 | 2,032,076 |
| Accounts payable to subsidiaries | 2,150,985 | 18,577,321 | - | - | - | 20,728,306 |
| Accounts payable to affiliated companies | 224,859 | - | - | - | - | 224,859 |
| Taxes payable | 265,818 | - | - | 50 | - | 265,868 |
| Contributions to pension and social security institutions | 568,355 | - | - | 10 | - | 568,365 |
| Other liabilities | 1,967,562 | - | - | - | - | 1,967,562 |
| Total | 18,168,282 | 25,118,125 | 5,690 | 1,669 | 2,415 | 43,296,181 |

REVENUES 9 MONTHS TO DECEMBER 31, 2004 - GEOGRAPHICAL AREA (CUSTOMER LOCATION)

| | | | | | | |
|-----------------------------------|-------------------|---------------|--------------|--------------|------------|-------------------|
| SALES AND SERVICE REVENUES | 16,069,768 | 51,160 | 1,545 | 3,133 | 165 | 16,126,291 |
|-----------------------------------|-------------------|---------------|--------------|--------------|------------|-------------------|

(*) Not including the caption "Deferred tax assets".

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■ INDEPENDENT AUDITORS' REPORT



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INDEPENDENT AUDITORS' REPORT pursuant to article 156 of Legislative Decree of February 24, 1998, n. 58 (Translation from the original Italian text)

To the Shareholders
of Telecom Italia S.p.A.

1. We have audited the financial statements of Telecom Italia S.p.A. as of and for the year ended December 31, 2004. These financial statements are the responsibility of the Telecom Italia S.p.A.'s management. Our responsibility is to express an opinion on these financial statements based on our audit.
2. Our audit was made in accordance with auditing standards and procedures recommended by CONSOB. In accordance with such standards and procedures, we planned and performed our audit to obtain the information necessary to determine whether the financial statements are materially misstated and if such financial statements, taken as a whole, may be relied upon. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, as well as assessing the appropriateness and correct application of the accounting principles and the reasonableness of the estimates made by management. We believe that our audit provides a reasonable basis for our opinion.

For our opinion on the financial statements of the prior year, which are presented for comparative purposes as required by the law, reference should be made to our report dated April 15, 2004.

3. In our opinion, the financial statements of Telecom Italia S.p.A. comply with the Italian regulations governing financial statements; accordingly, they present clearly and give a true and fair view of the financial position of Telecom Italia S.p.A. as of December 31, 2004 and the results of its operations for the year then ended.
4. We draw your attention to the information presented in the explanatory notes, "Summary of significant accounting policies", regarding the accounting criteria utilized for the employee benefit obligations as required by Law no. 58/1992.

Milan, March 16, 2005

Reconta Ernst & Young S.p.A.

Signed by: Felice Persico (Partner)

■ Reconta Ernst & Young S.p.A.
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■ REPORT OF THE BOARD OF AUDITORS TO THE SHAREHOLDERS' MEETING OF TELECOM ITALIA S.p.A. PURSUANT TO ARTICLE 153 OF LEGISLATIVE DECREE 48/1998

Dear Shareholders,

During the year ended 31 December 2004 the Board of Auditors of Telecom Italia S.p.A. (the "Company") performed the supervisory activities required by law, taking into account the standards recommended by the Italian accounting profession and the indications of Consob concerning controls and the activity of the Board of Auditors.

We obtained the information we needed for the performance of our duties by holding hearings with managers in the relevant structures and by receiving data and information in the meetings of the Board of Directors, which we always attended. In this respect it should be noted that with the system of corporate governance the Company has put in place it is up to the Board of Directors acting in its collegial capacity – and therefore in the presence of the Board of Auditors – to examine transactions likely, in view of their nature, strategic importance or size, to have a substantial impact on the Company's activity, even though they theoretically fall within the scope of the delegated powers of the executive directors. It should also be noted that the Board of Directors must always give advance approval to transactions with related parties, including intra-group transactions, apart from those of a customary nature to be concluded at standard conditions.

Lastly, it is worth recalling that the Company has adopted self-regulatory measures to ensure that the Board of Auditors receives sufficient information on the action taken by the executive directors using their delegated powers and on the implementation of transactions approved by the Board of Directors. In particular, the Telecom Italia has created a procedure for the collection and transmission of information on: the activity carried out by the Company; the transactions of greatest significance for its profitability, financial position and assets and liabilities; transactions with related parties (including intra-group transactions); and atypical and unusual transactions.

- On the basis of the information we received and the specific analyses we performed, the transactions having major economic, financial and balance-sheet effects entered into by the Company, including those entered into through direct or indirect affiliates, were essentially the following:
 - in January 2004 Telecom Italia International N.V. executed a private placement agreement under which it disposed of its remaining interest in Telekom Austria, equal to 14.78% of that company's share capital;
 - in February 2004 the merger of IS Tim with Aycell was completed with the transfer of the two companies' assets and liabilities to ITT, which, upon completion of the merger, changed its name to TT & TIM İletişim Hizmetleri A.Ş. The company is owned by Tim International N.V. (40%), Turk Telekomunikasyon A.Ş. (40%) and IS Bank Group (20%);
 - in March 2004 IT Telecom S.p.A. (a wholly-owned Telecom Italia subsidiary) transferred its "Sviluppo" division to Tim S.p.A. The transaction was part of the plan for the reorganization of the Group's information technology activities;
 - in March 2004, again as part of the plan for the reorganization of the Group's information technology activities, the "S.I. - Sistemi Informatici - Sistemi Amministrativi" division of Tim S.p.A. (development and maintenance of SAP applications), was transferred to Shared Service Center S.c.r.l. (SSC), a limited liability consortium company affiliated with the Telecom Italia Group;
 - in March 2004 a new three-year euro 6.5 billion loan facility was arranged that replaced the syndicated loan that Olivetti had raised in connection with the merger in 2003, of which the first tranche (euro 4.5 million) was scheduled to fall due in April 2004. The loan agreement does not require the borrower to comply with particular balance sheet ratios and the commitment entered into by the banks guarantees the unconditional availability of the funds in question;
 - in April 2004 a settlement was reached with the minority shareholders of Digitel, whereby Tim International undertook to acquire the holdings of all the other shareholders (corresponding to 32.88% of the Venezuelan company's share capital). Under the agreement, executed on 1 July 2004, Tim International acquired the 1,480,562 million shares owned by the minority shareholders of Digitel. The agreement was consummated after the contractual conditions for the protection of Tim International and Digitel itself had been verified. Accordingly, as of 1 July 2004, Tim has owned 100% of the Venezuelan mobile operator's capital through Tim International;

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- in June 2004 a settlement was reached in the dispute concerning the framework agreement concluded on 20 September 2000 between Seat Pagine Gialle S.p.A. (now Telecom Italia Media S.p.A.) and its subsidiaries on the one hand and companies belonging to the De Agostini Group on the other. Under the terms of the settlement, De Agostini Invest transferred its entire equity interest in Finanziaria Web to Telecom Italia Media (which already controlled the company with a 60% interest) for a consideration of euro 287 million, in place of the price of euro 700 million originally stipulated. In addition to the purchase price, it was agreed that euro 38 million would be paid as reimbursement for expenses incurred by De Agostini Invest in making good Finanziaria Web's losses and recapitalizing the company from July 2001 on;
- in June 2004 IT Telecom S.p.A., a wholly-owned Telecom Italia subsidiary, executed an agreement with Value Partners S.p.A. for the purchase of the latter's 69.8% interest in Webegg S.p.A. In July 2004, after the Antitrust Authority had authorized the transaction, the agreement was consummated with the payment of the agreed consideration;
- in July 2004 Telecom Italia sold the interest in Finanziaria Web acquired from De Agostini Invest to Vertico (a wholly-owned indirect subsidiary of Telecom Italia that already owned a 33.3% interest in Matrix);
- in July 2004 the Boards of Directors of Tele Celular Sul Participações S.A. and Tele Nordeste Celular Participações S.A., both controlled by Tim Brasil, approved the plan for the merger of Tele Nordeste Celular Participações S.A. into Tele Celular Sul Participações S.A. (a transaction that had already commenced on 28 May 2004). In August 2004 the extraordinary shareholders' meetings of Tele Nordeste Celular Participações and Tele Celular Participações approved the merger. Contemporaneously, Tele Celular Sul Participações changed its name to Tim Participações S.A. Following completion of the transaction, Tim holds 23.73% of the share capital of Tim Participações S.A. through Tim Brasil;
- in September 2004 the extraordinary shareholders' meeting of Telecom Italia Media approved a cash increase in capital by means of a rights issue of approximately euro 120 million (including the share premium); the increase was fully subscribed;
- in September 2004 Telecom Italia sold its 19.9% interest in Sky Italia to the NewsCorp group;
- in September 2004, as part of the process of simplifying the structure of the Group, Tim International transferred its interest in Maxitel to Tim Brasil. The Board of Directors of Tim Brasil approved the transaction after obtaining the necessary authorizations from the competent authorities. On 28 October 2004 Tim Brasil transferred the interest in Maxitel to Tim Celular by way of an increase in capital;
- in September 2004 the Board of Directors of Telecom Italia S.p.A. approved the plan for the merger into Telecom Italia of the wholly-owned subsidiaries IT Telecom S.p.A. and Epiclink S.p.A. This transaction was part of the broader plan for the reorganization of the Group's information technology activities. The merger became effective on 31 December 2004 and was effective for accounting and tax purposes as of 1 January 2004;
- in September 2004 Telecom Italia S.p.A. purchased Tim S.p.A.'s 40% interest in Edotel S.p.A. The transaction was part of the plan to rationalize the Telecom Italia Group's equity investments;
- in September 2004 IT Telecom S.p.A. resolved to transfer two divisions ("ERP Solution" and "Application Operations - Administration & Finance") to Shared Service Center S.c.r.l. (SSC). The latter company effected a capital increase with a share premium. IT Telecom S.p.A. paid for its new shares in kind with the contribution of the above-mentioned divisions; the other shareholders (Pirelli & C. S.p.A., Tim S.p.A. and Olivetti Tecnost S.p.A.) paid for their new shares in cash. Upon completion of the transaction, the percentage holdings of the various shareholders were unchanged;
- in November 2004 a preliminary agreement was concluded with CANTV (Compañía Anónima Nacional Teléfonos de Venezuela) for the sale of 100% of Digitel's share capital. The consummation of the transaction, probably by the end of the first half of 2005, is subject to the execution of the definitive agreement and the issue of the necessary authorizations by the competent Venezuelan authorities;

* * *

- in 2004 Telecom Italia made four new note issues as part of the Euro Medium-Term Note Program approved for a total of euro 10 billion by the Board of Directors of Telecom Italia on 10 October 2003:
 - on 29 January 2004 for a total of euro 3 billion, divided into three tranches: euro 1,000 million, coupon 3-month Euribor + 0.33%, issue price 99.927, maturity 29 October 2007; euro 750 million, coupon 4.50%, issue price 99.56, maturity 28 January 2011; and euro 1,250 million, coupon 5.375%, issue price 99.07, maturity 29 January 2019;
 - on 8 April 2004 for a total of euro 110 million in a private placement, variable rate, coupon 3-month Euribor + 0.60%, issue price 100, maturity 30 March 2009;
 - on 24 June 2004 for a total of £850 million, issue price 98.85, fixed rate, coupon 6.375%, maturity 24 June 2019;
 - on 23 November 2004 for a total amount of euro 120 million, coupon 3-month Euribor + 0.66%, issue price 100, maturity 23 November 2015;

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- in 2004 Telecom Italia redeemed note issues amounting to euro 2,831, specifically: euro 1,331 million on 1 January 2004, in connection with the 2001-04 convertible note issue; and euro 1,500 million on 22 March 2004, in connection with the note issue maturing on 21 June 2005, repaid early by exercising the faculty provided for in the terms and conditions of the issue;
- in October 2004 Telecom Italia Capital made a multi-tranche fixed rate note issue guaranteed by Telecom Italia S.p.A. for a total of \$3.5 billion. The issue is divided into three tranches, as follows:
 - A Series, for a total of \$1,250 million (equal to euro 918 million) with a fixed annual coupon of 4%, maturity 15 January 2010;
 - B Series, for a total of \$1,250 million (equal to euro 918 million) with a fixed annual coupon of 4.95%, maturity 30 September 2014;
 - C Series, for a total of \$1,000 million (equal to euro 734 million) with a fixed annual coupon of 6%, maturity 30 September 2034;
- in December 2004 Telecom Italia Finance S.A. issued new notes called "Telecom Italia Finance S.A. Euro 499,717,000 Guaranteed Floating Rate Extendable Notes Due 2006", maturity 14 December 2006. This issue follows the 2002-05 note issue for a total of euro 500 million, with a variable quarterly coupon equal to 3-month Euribor + 130 basis points, which gave noteholders the right to extend the maturity by 21 months each time up to a maximum total maturity of 10 years (the final maturity is 14 March 2012). At 14 March 2004 holders of notes amounting to euro 283,000 had renounced their right to extend the maturity in accordance with the terms and conditions of the issue. For noteholders who decided to extend the maturity of notes amounting to euro 499,717,000, the above-mentioned issue was made with the "new" maturity of 14 December 2006;

* * *

- in January and February 2005 applications were received in relation to the convertible notes 2001-2010 issued by Telecom Italia S.p.A. (formerly Olivetti S.p.A.) for the conversion of 1,406,391,362 notes, corresponding to 663,188,066 Telecom Italia ordinary shares;
- in January 2005 Telecom Italia S.p.A., via its subsidiary Telecom Italia International N.V., concluded an agreement with Almendral S.A. for the sale of its 54.76% interest in the capital of the Chilean company Entel Chile S.A. It is expected that the agreement will be consummated in the first half of 2005;
- in February 2005, after examining the offers received for the sale of the interest in Finsiel S.p.A., Telecom Italia's Board of Directors accepted the offer of the COS Group. It is expected that the transaction will be consummated by the end of May 2005.

All the above transactions are described in the Directors' Report on Operations and/or the notes to the financial statements of Telecom Italia S.p.A. and the consolidated financial statements for 2004.

We verified that the above transactions were carried out in conformity with the law, the bylaws and the principles of correct management and that they were not manifestly imprudent or reckless, nor in contrast with the resolutions approved by the shareholders' meeting or such as to compromise the integrity of the Company's patrimony.

2. We did not find evidence of atypical and/or unusual transactions entered into with third parties or related parties (including intra-group transactions) during 2004 or subsequent to the balance-sheet date.

With regard to transactions potentially involving a conflict of interest, the directors list the main transactions with Group companies and other related parties in the section of the Report on Operations devoted to transactions with related parties and in their observations on the individual items of Telecom Italia S.p.A.'s financial statements. Reference should also be made to these sections for a description of the features of the transactions and a discussion of their economic effects.

We verified, where appropriate with the assistance of the audit firm, Reconta Ernst & Young, that Telecom Italia S.p.A. adopts specific practices to control that the transactions in question are concluded in the interest of the Company and/or the Group, are part of the ordinary course of business and, when not concluded at standard conditions or on specific terms prescribed by statutory or regulatory provisions, are settled at arm's length conditions.

In 2004 Telecom Italia continued to apply the "Rules of Conduct for Transactions with Related Parties" that it had introduced to ensure transparency and procedural and substantial fairness in deciding on and implementing such transactions. More details on how Telecom Italia's Board of Directors applies the Rules are to be found in the Corporate Governance section of the Report on Operations. It should be noted that the Company has commenced a revision of the Rules and is preparing a procedure based on the use, for every transaction to be carried out, of an expert system that will automatically provide indications on how it is to be handled (with regard to decision-making powers, internal information flows for reporting purposes, and the need for an external opinion in evaluating the congruousness of transactions), as explained in the section on Corporate Governance.

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3. The information given in the Report on Operations and in the notes to the financial statements of Telecom Italia and the consolidated financial statements regarding the Company's transactions with related parties and intra-group transactions is adequate in relation to the size and structure of the Company and the Group.

4. On 16 March 2005 the audit firm, Reconta Ernst & Young, issued the reports pursuant to Article 156 of Legislative Decree 58/1998 attesting that the financial statements of Telecom Italia S.p.A. and the consolidated Group financial statements for the year ended 31 December 2004 had been drawn up clearly and gave a clear and fair view of the balance-sheet situation, financial position and results for the year. The report on the Company's financial statements contains an emphasis of matter paragraph concerning the accounting treatment of the pension totalization costs regulated by Law 58/1992.

5. In 2004 we received two complaints pursuant to Article 2408 of the Civil Code concerning: (i) the failure to call a special meeting of the savings shareholders of the "new" Telecom Italia (the name taken on by the absorbing company, Olivetti S.p.A., upon completion of the merger into Olivetti S.p.A. of its subsidiary Telecom Italia S.p.A.). According to the complainant, upon completion of the merger there was a new category of savings shareholders with the consequent need to call a special meeting to elect the common representative and to establish the amount of the fund for expenses. The complainant also claimed that the appointment as common representative by the special meeting of 26 October 2004 of the person who had held the same position in the "old" Telecom Italia could not be considered as legally remedying the omission and that the conditions did not exist in the case in question for any hypothesis of prorogatio; and (ii) the allegedly misleading nature and falseness of statements contained in press releases published by Telecom Italia in connection with the tender offer for ordinary and savings shares of the subsidiary Tim, with special reference to the tender offer for savings shares. We also inform you that we received some complaints, all from the same shareholder, basically requesting data and clarifications aimed at satisfying the complainant's specific informational needs in relation to some corporate transactions effected by Telecom Italia in 2004 (we refer, in particular, to those involving MP Facility S.p.A. and Shared Service Centre (SSC) and the counterparties in some derivative transactions). We carried out the appropriate inquiries on all the complaints without finding omissions, censurable facts or irregularities to report to the shareholders' meeting.

6. During the year we also received fourteen petitions (or groups of petitions, dealt with together when more than one was received from the same person, even at different times), basically concerning technical, commercial and accounting problems. We carried out the appropriate inquiries on all the petitions without finding irregularities to report to the shareholders' meeting.

7. As already indicated in our report to the shareholders' meeting called to approve the 2003 annual report, the Board of Directors has charged the Board of Auditors with acting as Telecom Italia's Audit Committee for purposes of the US securities legislation applicable to the Company as a company registered with the Securities and Exchange Commission with securities listed by means of an ADR programme on the New York Stock Exchange. Readers are referred to that earlier report for a detailed analysis of the Board's tasks and duties in its capacity of Audit Committee.
In accordance with applicable Italian law and in the light of the additional tasks entrusted to the Board of Auditors as the Company's Audit Committee, in 2004 we expressed a favorable opinion on the proposal to engage the audit firm Reconta Ernst & Young to audit the annual financial statements of Telecom Italia S.p.A. and the Group consolidated financial statements and to perform a limited review of Telecom Italia's company and consolidated half-yearly report for the three years 2004-06. During the 2004 fiscal year the Company engaged Reconta Ernst & Young to perform several services other than the statutory audit (so-called "audit services" and "audit-related services"). The table below shows the fees for this work, excluding out-of-pocket expenses and VAT. These fees appear appropriate in relation to the scope, complexity and characteristics of the work carried out.

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| Auditing of expenditure accounts to be submitted to the European Union for the disbursement of research grants under the Sixth Framework Programme | 82,000.00 |
| Tests of compliance and analysis of Telecom Italia's Sustainability Report for the three years 2004-06 | (*) 36,000.00 |
| Tests on the financial reports of Telecom Italia S.p.A.'s Interbusiness Service for the three years 2004-06 | (*) 14,000.00 |
| Audit procedures for 2004 comparative data prepared by applying the IAS/IFRS accounting standards | 240,000.00 |
| Audit procedures for the issue of comfort letters in connection with the "Telecom Italia S.p.A. Issue of euro 1,000,000,000 Floating Rate Notes due 2007, euro 750,000,000 4.50 per cent. Notes due 2011 and euro 1,250,000,000 5.375 per cent. Notes due 2019 under the euro 10,000,000,000 Euro Medium Term Note Programme" | 15,000.00 |
| Audit procedures for the issue of comfort letters in connection with the "Telecom Italia Issue of £850,000,000 6.375% Notes due 2019 under the euro 10,000,000,000 Euro Medium Term Note Programme" | 115,000.00 |
| Audit procedures for the financial statements and/or reporting packages of Group companies previously not included in the audit plan | 55,000.00 |
| Agreed test procedures for communications to be submitted to the Inland Revenue Authority and Ministry of Finance of Singapore in relation to the company Getronics Solutions Pte Ltd., formerly Olivetti Pte Ltd | 15,000.00 |
| Review activity (including post-report review procedures) in relation to the preparation and filing of Form F-4 with a view to the listing on US markets of the privately placed U.S.\$4 billion bond issue | 360,000.00 |
| Agreed test procedures to be applied to the affiliate Telecom Argentina in connection with the audit rights attributed to shareholders and governed by shareholders' agreements | 100,000.00 |
| Accounting assistance and advice in relation to the review conducted by the Securities and Exchange Commission on Telecom Italia's 2003 Form 20-F: euro 148,000.00 Reconta Ernst & Young euro 18,000.00 Capital Markets Division of Ernst & Young | 166,000.00 |
| Total | 1,198,000.00 |

(*) Fee for each of the three years.

8. In 2004 the Company had some services performed by persons linked to Reconta Ernst & Young by continuous work relationships and/or companies belonging to the Ernst and Young Global network (in particular Ernst & Young Financial - Business Advisors S.p.A.). The fees for this work, excluding out-of-pocket expenses and VAT, are summarized below:

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| Agreed procedures in the field of regulatory accounting following Resolution 152/02/CONS: assistance provided in the "Adaptation of the systems and process of regulatory accounting to the requirements concerning the certifiability, traceability and integrity of data" | 449,850.00 |
| Adaptation of the regulatory reporting process: assistance in adapting the external reporting process to legal requirements; assistance in producing internal reports | 145,000.00 |
| Definition of the model of integration between IT Telecom and Purchasing Informatica for planning IT purchases in the "IT Telecom Business Unit" | 350,000.00 |
| Total | 944,850.00 |

9. During the year we gave our opinion to the Board of Directors concerning the remuneration of the Chairman and the Managing Directors, pursuant to Article 2389, third paragraph of the Civil Code.
10. In 2004 the Board of Directors of the Company held 12 meetings, in all of which we participated.
The Internal Control and Corporate Governance Committee met 9 times and the Remuneration Committee 4 times. The Strategy Committee (established on 9 September 2004) met once.
The Board of Auditors met 14 times and participated in all of the meetings held by the Internal Control and Corporate Governance Committee, either in joint meetings or represented by its Chairman or another auditor designated by him, depending on the subjects to be discussed.
We participated in the ordinary and extraordinary shareholders' meetings of the Company held on 6 May 2004 and the Board of Auditors was represented by its Chairman in the special meeting of Telecom Italia savings shareholders held on 26 October 2004.
11. For matters within its sphere of authority, the Board of Auditors monitored compliance with the principles of correct management by carrying out direct checks and investigations, gathering information from the heads of functional units, and holding meetings with the person responsible for internal control at the Company, the Internal Control and Corporate Governance Committee and the audit firm,

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Reconta Ernst & Young (in the latter case for the exchange of data and information relevant for the performance of their respective duties, in accordance with Article 150.2 of Legislative Decree 58/1998).

More specifically, as regards the decision-making of the Board of Directors, we verified, by participating in the directors' meetings, the compliance with the law and the bylaws of the operational decisions taken. We also checked that the resolutions in question were backed by analyses and opinions – produced internally or when necessary by external experts – concerning the economic and financial suitability of transactions and their consequent correspondence with the Company's interest.

We express a basically positive opinion on the corporate governance mechanisms adopted by the Company over time; many of them are an effective means of ensuring compliance with the principles of correct management of operations.

12. We acquired information and monitored the adequacy of the Company's organizational structure through direct checks, hearings, reports from managers in the relevant structures and meetings with the persons responsible for the internal and external audit functions.

The Group's organizational structure was further simplified during the year and now comprises Central Functions (responsible for the management and functioning of the Group) and Business Units (responsible for the development of the Group's business and the coordination of its market-related activities), whose coordination is divided between Telecom Italia's Chairman and one of its managing directors.

The integration of the Group is based primarily on the notion of Professional Families. Coordinated by the corresponding Central Functions, these families link the human resources with homogeneous professional know-how, are spread out at various hierarchical levels across the organization and promote the development, utilization and coordination of the special skills present in the Group, without prejudice to the responsibility of the individual Business Units for results in terms of profitability and markets. It is up to the individual Central Functions, instead, to control and guarantee the quality of the processes and results and to verify that operations are carried out in compliance with the instructions given.

There are also activities organized on a Group-wide basis, such as the Administrative Services Centre, which handles all the administrative and accounting functions of Telecom Italia and the main Business Units.

As regards the guidance and control role played directly by the executive directors, the Chairman heads the General Counsel, Communication and Image, Brand Enrichment, Human Resources, and Public and Economic Affairs Central Functions, as well as the Telecom Italia Lab division and the Wireline, Mobile and Internet & Media Business Units. The Chairman also heads Telecom Italia Latam, which acts as the "delocalized" Corporate Function in Latin America, without prejudice to the responsibility of the Wireline and Mobile Business Units for the results of the companies they respectively control. The Managing Director, Mr. Carlo Buora, heads the other Central Functions and the following Business Units: Information Technology Market and Olivetti Tecnost.

In order to provide support for top management's guidance and control role and ensure the effective overall management of the business, a series of Group Committees have been set up for liaison and coordination purposes. The most important are:

- the Management Committee, which coordinates the Group's activities and ensures a unitary approach to the development and implementation of business strategies;
- the Investment Committee, which is entrusted with approving investments that exceed the thresholds established in delegated powers;
- the "Telecom 2007" Steering Committee, which directs and approves the Group's activity concerning innovation, efficiency and development and monitors the progress made, with a view to ensuring correct and prompt implementation of the planned integration between Telecom Italia and Tim, in accordance with the resolutions adopted by the Boards of Directors of the two companies on 7 December 2004;
- the "Project 404" Steering Committee, which is responsible for the project, which is Group-wide in scope and intended to equip the Company with the means and mechanisms that will ensure the traceability of transactions and full compliance with Section 404 of the Sarbanes-Oxley Act as regards the attestations to be made on internal controls over financial reporting,
- the Purchasing Committee, which coordinates this function throughout the Group with the aim of maximizing the Group's purchasing power and the economies of scale obtainable;
- the Group IT Security Committee, which ensures an integrated approach to the management of IT security within the Group.

Business Reviews are also conducted to check the results achieved by the individual operating units against forecasts and plan remedial action where necessary.

Among the main changes made in 2004 to the Group's macro organizational structure it is worth noting the superseding of the role of general manager at the Mobile Business Unit, which led to a reshuffling of the Functions reporting directly to Managing Director of Tim S.p.A., who now has responsibility for some operational units (Tim Brasil, Tim Perù and Tim Hellas).

Lastly, it is worth noting that for some time the Company has had a procedure for the appointment of the governing bodies of subsidiary and affiliated companies.

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13. The Board of Auditors monitors the adequacy of the Company's internal control system, among other things, through meetings with the person responsible for internal control and the Internal Control and Corporate Governance Committee and by examining documents. It did not find any serious weaknesses.

Since 2002 the performance of the internal audit function within the Company and the Group has been entrusted to a consortium company set up by companies belonging to the Group and called Telecom Italia Audit S.c.a.r.l., whose primary object is the impartial and independent performance, on behalf of the members of the consortium and the Group as a whole, of "internal auditing", i.e. the activities aimed at checking and improving the effectiveness and efficiency of the internal control and risk management system. In view of the activity carried out by Telecom Italia Audit, Telecom Italia (in the same way as the other companies belonging to the Group) has made the internal audit consortium company, in the person of the director designated by the Company, the "person responsible for internal control".

Telecom Italia Audit works in collaboration with Mr. Buora, the Managing Director responsible for deciding on proposals for remedial action, the Board of Auditors and the Internal Control and Corporate Governance Committee.

The activity of the person responsible for internal control is based on annual programmes (comprising interventions identified autonomously by the person responsible for internal control himself or following indications received from the Company's management, the control bodies or the audit firm). The existence of an annual plan obviously does not exclude ad hoc unplanned interventions in response to requests from the Company or the control bodies or made necessary by problems that arise during the year. The person responsible for internal control reports periodically on the results obtained to top management and the control bodies.

The internal control system is completed by TI Audit Latam, charged with overseeing the auditing of the business of Group companies in Latin America. We consider that the reorganization of the internal audit function, including the creation of the new structure for Latin America referred to above, is in the Company's interest.

Further progress was made in implementing two "transversal" projects involving the internal control system of the entire Group:

- the Administrative Systems Checkup project, aimed at verifying the effectiveness of the methods used in producing and controlling accounting data for internal use and disclosure to the market. The implementation of this project has advanced further following the launch of the "404 Project", which, starting from the results of the Checkup project, aims at equipping the Company with the means and mechanisms that will ensure the traceability of transactions and full compliance with Section 404 of the Sarbanes-Oxley Act as regards the attestations to be made on internal controls over financial reporting;
- the Control Risk Self-Assessment project, aimed at providing management with support in the monitoring, analysis and assessment of the main operational risks encountered in the Group's various businesses and identifying appropriate remedial measures. The project led during 2004 to the use of the methodology on a regular basis following its inclusion in the Group's planning and control system. The methodology will be progressively applied at every level of the business and eventually in the companies not covered in the initial phase of the project. In addition Telecom Italia Audit has defined specific action plans with regard to the operational approach it has adopted in terms of organization, methods, professional standards and the level of assurance provided.

As part of the check on the ability of the internal control system to ensure compliance with applicable legislation, especially the provisions of Legislative Decree 231/2001 regarding administrative liability for offences committed by employees and collaborators, we remind you that in 2003 the Company adopted an "Organizational Model" based on "Rules of conduct for dealings with governmental bodies" and "internal control checklists" listing the main phases of every process, the offences that can be committed in connection with individual processes and the control activities serving to forestall the related risks. Monitoring of the functioning of the model and compliance is performed by a Supervisory Panel made up of a member of the Board of Auditors, an independent director on the Internal Control and Corporate Governance Committee and the person responsible for the internal control system. A special unit has been created within Telecom Italia Audit to provide operational support to the Supervisory Panels of Group companies by handling reports of violations of the organizational model and conducting compliance audits on the basis of the data received by way of the information flows that have been put in place.

14. We monitored the adequacy of the administrative and accounting system and its reliability in correctly representing transactions. We performed this task by obtaining information from the heads of the competent organizational structures, examining company documents and analyzing the results of the work carried out by the audit firm, Reconta Ernst & Young.

As regards the procedures used by management to value and verify the fairness of the book values of the Group's equity investments, we examined the results of the checks made by the audit firm, Reconta Ernst & Young, and followed the work of the Company's Internal Control and Corporate Governance Committee with regard to the correct application of the accounting standards adopted and their

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uniformity for the purpose of preparing the consolidated financial statements. We also examined the foreseeable impact from an economic and a financial perspective of the transition to the IAS/IFRS accounting standards and the timetable the Company has prepared for their application.

15. We examined the instructions issued by Telecom Italia to its subsidiaries pursuant to Article 114.2 of Legislative Decree 58/1998 and deemed that they were adequate for the purpose of fulfilling the Company's disclosure obligations under that law. It should be noted in this respect that Telecom Italia has formal procedures governing the flow of information from subsidiaries to its top management on corporate events and other major transactions. In the case of price-sensitive information, the Company has a special procedure for its disclosure to the market (discussed in more detail in point 17). Among other things, the procedure specifies the information that subsidiaries must send to the parent company to enable it to fulfill its disclosure obligations.
16. We checked – through direct verification and information obtained from the audit firm, Reconta Ernst & Young – the Company's compliance with the rules and regulations governing the layout and preparation of the financial statements of Telecom Italia S.p.A., the consolidated financial statements for the Telecom Italia Group and the Report on Operations. In particular, the Group results by business sector and geographical area are presented taking account of Consob Communication No. 98084143 of 27 October 1998. We also took note of the checks and analyses carried out by Reconta Ernst & Young on the Sustainability Report.
17. The Company complies – through its Self-Regulatory Code, which was last amended in October 2003 at the time of the merger of Telecom Italia into Olivetti – with the principles and recommendations contained in the Code of Conduct (known as the Preda Code) drawn up at the initiative of Borsa Italiana by the Committee for the Corporate Governance of Listed Companies.
The Company's Board of Directors (made up of 19 directors) has 16 non-executive directors, 10 of whom qualify as independent. The Board has established an Internal Control and Corporate Governance Committee and a Remuneration Committee, both of which are made up entirely of independent directors. The role of the independent directors has been strengthened by the creation in September 2004 of the position of Lead Independent Director (in the person of the Chairman of the Internal Control and Corporate Governance Committee), who is authorized to call "Independent Directors' Executive Sessions", i.e. special meetings of the independent directors to discuss issues related to operations or the working of the Board.
The Company has not established a Nominating Committee since the slate voting system laid down in the bylaws for the election of the Board of Directors ensures the presence of directors chosen from minority slates.
In September 2004 Telecom Italia established an additional committee (the Strategy Committee) charged with assisting the Board of Directors in making strategic choices in the light of competitive developments. More details on the composition and tasks of this committee are to be found in the Corporate Governance section of the Report on Operations.
In earlier parts of this Report we have referred to most of the corporate governance mechanisms adopted by the Company, which are described more fully in the Section of the Report on Operations devoted to corporate governance. At this point it appears desirable to elaborate a little on the Procedure for the Disclosure of Price-Sensitive Information. Updated in July 2004, this identifies the organizational structures involved in the disclosure process, governs the flow of information from subsidiaries to the parent company and lays down rules for the conduct to be followed in the event of rumours or requests for information from those responsible for operating and supervising the markets. The Procedure also specifies the measures to be adopted on the occasion of meetings with financial analysts and the press with the aim of preventing selective disclosure.
As required by Borsa Italiana, the Company has also adopted a Code of Conduct for Insider Dealing, which imposes conduct and disclosure obligations on the persons specified in the Code with regard to transactions involving listed securities of the Group that are qualitatively and quantitatively more stringent than those prescribed by the market operating company.
We inform you further that the Company has continued to comply with the transparency and disclosure requirements deriving from the SEC's adoption of the rules implementing the Sarbanes-Oxley Act of 2002. In addition to making the Board of Auditors the Company's Audit Committee within the meaning of the applicable US legislation, Telecom Italia has also established a Disclosure Committee consisting of the heads of the competent Central Functions and the person responsible for internal control to assist the Board of Directors and top management in matters concerning corporate communications (annual, half-yearly and quarterly reports, Form 20-F filings, information documents and prospectuses, etc.) and price-sensitive information. The Committee verifies the adequacy and efficiency of the procedures

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and controls put in place by the Company for the collection, analysis and handling of information to be disclosed to the market. It also monitors the application and assesses the need for updating of the Procedure for the Disclosure of Price-Sensitive Information and supervises the layout and updating of the Company's website. The Committee has recently been charged with the task of preparing a procedure based on an expert system to enhance the effectiveness of the "Rules of Conduct for Transactions with Related Parties".

To conclude, we inform you that we were constantly involved in the analysis and implementation of Telecom Italia's system of corporate governance, on which we pass a favourable judgement.

18. The oversight, monitoring and control activities we carried out as described above did not bring to light any significant facts or circumstances that needed to be mentioned in this Report or reported to the Company's control bodies or the supervisory authorities. Nor did we find any objections in the reports issued, pursuant to Articles 153 and 156 of Legislative Decree 58/1998, by the boards of auditors and audit firms of the subsidiaries listed on the markets organized and managed by Borsa Italiana S.p.A. (Tim and Telecom Italia Media) or of the Business Units set up as separate companies (Finsiel and Olivetti Tecnost).
19. As for the matter of Telekom Serbia (arising from the Telecom Italia Group's purchase of a 29% interest in the Serbian company in 1997), to supplement the news we have already provided, most recently in our report to the shareholders' meeting of 6 May 2004, we inform you that in September 2004 we received a letter from the Parliamentary Committee of Inquiry into the Telekom Serbia Affair announcing the definitive termination of the Committee's activity. We accordingly held additional hearings with the heads of the corporate functions concerned to learn of the possibility of new material facts emerging from the Committee's reports and were assured of its inexistence.
20. We now turn to the Antitrust Authority's investigation into Telecom Italia (the subject of a detailed description in the Disputes, Litigation and Legal Proceedings Pending section of the Report on Operations), which led to the imposition of a very heavy fine on the Company for alleged abuses of dominant position. Together with the Internal Control and Corporate Governance Committee, we have continuously monitored the steps taken by the Company to comply with the order issued by the Authority at the close of its investigation.. The complexity of the Antitrust Authority's order and the difficulty of determining the conduct actually required made it appear desirable to obtain the opinions of outside experts and to engage an antitrust lawyer to verify the legal aspects of the steps taken to give effect to the order. We have been able to verify the scale of the staff and resources assigned to the question and the reasonableness of the operational choices made by management in conformity with the opinions of acknowledged experts. We intend to continue to focus our attention on these matters, taking into account any decisions adopted by the administrative court and the Antitrust Authority itself.
21. On 7 December 2004 the Boards of Directors of Telecom Italia and Tim approved a plan for the combination of the two companies that is intended: to satisfy a series of business needs deriving from the progressive integration between fixed and mobile communications platforms, simplify the Group's ownership structure and optimize the balance sheet and financial structure of the company resulting from the merger. The plan envisages: (i) a partial voluntary tender offer by Telecom Italia for 2,456,534,241 Tim ordinary shares, equal to two thirds of the corresponding free float, and a tender offer for 132,069,163 Tim savings shares, corresponding to all the company's savings share capital (completed on 28 January 2005 with the payment of the consideration); and (ii) the merger of Tim with and into Telecom Italia upon completion of the spin-off to a company wholly owned by Tim of the latter's domestic mobile telephony business. The merger will be consummated after the dividend has been paid. To finance the part of the tender offer consideration not paid by drawing on its own funds, Telecom Italia entered into a loan agreement under English law for up to euro 12 billion with a syndicate of Italian and international banks. The loan is divided into three repayment tranches with different maturities and with Telecom Italia having the option to extend the maturities of the first two tranches: (i) a first tranche of euro 3 billion with a maturity of 12 months, extendable by another 12 months; (ii) a second tranche of euro 6 billion with a maturity of 36 months, extendable by another 9 months; and (iii) a third tranche of euro 3 billion with a maturity of 60 months.

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We have found that in adopting the resolutions concerning the business combination referred to above, the Board of Directors of the Company has taken all the necessary and desirable precautions for a transaction of this kind and acted in compliance with the self-regulatory rules and procedures the Company has put in place. In particular, adequate reasons have been given as to why the transaction is in the Company's interest, the rules governing transactions with related parties have been complied with, fairness opinions have been obtained from the financial advisors chosen by the management and, in line with best international practice, from an additional advisor, nominated by the Internal Control and Corporate Governance Committee, serving to guarantee the process from an independent perspective.

We have verified the Company's compliance with the requirements concerning the disclosure of information, the calling of shareholders' meetings and the filing of documentation in connection with the merger transaction. We have also checked that the documents prepared for purposes of the merger in question conform with the applicable laws and regulations.

22. After examining the Company's financial statements for the year ended 31 December 2004, we have no objections to the resolutions proposed by the Board of Directors regarding the allocation of the net income for the year or the size of the dividend to be paid.

Milan, 16 March 2005

Chairman of the Board of Auditors

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■ RESOLUTIONS

APPROVAL OF THE MERGER PLAN OF TELECOM ITALIA MOBILE S.p.A. INTO TELECOM ITALIA S.p.A. - RELATED AND CONSEQUENT RESOLUTIONS

Proposal

The meeting of ordinary shareholders of Telecom Italia S.p.A. (the Absorbing Company),

- having seen the plan for the merger by incorporation into Telecom Italia S.p.A. of Tim S.p.A. (the Company to be Absorbed) filed with the Milan and Turin Company Registers on 25 January 2005 (the Merger Plan);
- having examined the Directors' Reports on the merger transaction (the Merger);
- having taken note of the balance sheets at 30 September 2004 of the companies participating in the Merger;
- having taken note of the reports on the fairness of the exchange ratios prepared by the auditing firms Mazars & Guerard S.p.A. for Telecom Italia and Reconta Ernst & Young S.p.A. for Tim;
- having taken note of the timely filing of the documentation required under applicable law;
- having taken note of the Board of Auditors' attestation that the present share capital is fully paid up;

resolves

1. to approve the Merger Plan and consequently to proceed – with the accounting and tax effects starting on 1 January of the year in which the Merger becomes effective, as provided for in the Merger Plan – with the merger by incorporation of Tim into Telecom Italia on the basis of the following exchange ratios:
 - 1.73 Telecom Italia ordinary shares with a par value of euro 0.55 each for every Tim ordinary share with a par value of euro 0.06;
 - 2.36 Telecom Italia savings shares with a par value of euro 0.55 each for every Tim savings share with a par value of euro 0.06;
2. to increase the share capital by up to euro 1,420,690,865.55 through the issuance of up to 2,291,344,587 ordinary shares and up to 291,729,714 savings shares, with a par value of euro 0.55 each and normal entitlement to the rights pertaining thereto, for the exchange of Tim ordinary and savings shares held at the effective date of the Merger by shareholders other than Telecom Italia, who will be provided with a service to handle any fractions of shares, at market prices and at no cost in terms of expenses, stamp duty or commissions, that will permit the number of newly issued shares to which they are entitled to be rounded up or down to the nearest whole number;
3. to amend Article 5 of the bylaws accordingly by introducing a new paragraph to the effect that:

The shareholders' meeting held on [–]approved an increase in the share capital of up to euro 1,420,690,865.55 through the issuance of up to 2,291,344,587 ordinary shares and up to 291,729,714 savings shares, with a par value of euro 0.55 each and normal entitlement to the rights pertaining thereto, for the merger by incorporation of Tim S.p.A.;
4. to increase the share capital – for Tim's outstanding stock option plans, to the extent they are still effective, taking into account the exchange ratio planned for Tim ordinary shareholders in connection with the Merger and with effect from the effective date of the Merger – by up to euro 38,655,832.60 through the issuance of up to 70,283,332 ordinary shares with a par value of euro 0.55 per share, divided into the following tranches:
 - (i) an increase of up to euro 11,705,656.05 for the exercise of stock options already granted by Tim under its "2000-2002 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 21,283,011 Telecom Italia ordinary shares with a par value of euro 0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim ordinary shares for purposes of the Merger at a price of euro 6.42 for each option held (i.e. euro 3.710983 for each newly issued share);

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- (ii) an increase of up to euro 1,132,285 for the exercise of stock options already granted by Tim under its "2001-2003 Stock-Option Plans", to be implemented by 31 December 2005 through the issuance of up to 2,058,700 Telecom Italia ordinary shares with a par value of euro 0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim ordinary shares for purposes of the Merger at a price of euro 8.671 for each option held (i.e. euro 5.012139 for each newly issued share);
 - (iii) an increase of up to euro 474,798.50 for the exercise of stock options already granted by Tim under its "2001-2003 Supplementary Plans", to be implemented by 31 December 2005 through the issuance of up to 863,270 Telecom Italia ordinary shares with a par value of euro 0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim ordinary shares for purposes of the Merger at a price of euro 7.526 for each option held (i.e. euro 4.350289 for each newly issued share);
 - (iv) an increase of up to euro 22,150,920 for the exercise of stock options already granted by Tim under its "2002-2003 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 40,274,400 Telecom Italia ordinary shares with a par value of euro 0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim ordinary shares for purposes of the Merger at a price of euro 5.67 for each option held (i.e. euro 3.277457 for each newly issued share);
 - (v) an increase of up to euro 3,192,173.05 for the exercise of stock options already granted by Tim under its "2003-2005 Stock-Option Plans", to be implemented through the issuance of up to a total of 5,803,951 shares with a par value of euro 0.55 per share, by 31 December 2008 for the first lot, by 31 December 2009 for the second lot and by 31 December 2010 for the third lot. The shares will be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim ordinary shares for purposes of the Merger at a price of euro 5.07 for each option held (i.e. euro 2.930636 for each newly issued share).
5. to further amend, with effect from the effective date of the Merger, Article 5 of the bylaws as formulated in the text attached to the Merger Plan and that is by inserting after the fourth paragraph the following new fifth paragraph:
The shareholders' meeting held on [-] also approved an increase in the share capital of up to euro 38,655,832.60 through the issuance of up to 70,283,332 ordinary shares with a par value of euro 0.55 per share, divided into the following tranches:
- 1. *an increase of up to euro 11,705,656.05 for the "2000-2002 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 21,283,011 ordinary shares with a par value of euro 0.55 per share to be offered for subscription at a price of euro 6.42 for each option held (i.e. euro 3.710983 for each newly issued share);*
 - 2. *an increase of up to euro 1,132,285 for the "2001-2003 Stock-Option Plans", to be implemented by 31 December 2005 through the issuance of up to 2,058,700 ordinary shares with a par value of euro 0.55 per share to be offered for subscription at a price of euro 8.671 for each option held (i.e. euro 5.012139 for each newly issued share);*
 - 3. *an increase of up to euro 474,798.50 for the "2001-2003 Supplementary Plans", to be implemented by 31 December 2005 through the issuance of up to 863,270 ordinary shares with a par value of euro 0.55 per share to be offered for subscription at a price of euro 7.526 for each option held (i.e. euro 4.350289 for each newly issued share);*
 - 4. *an increase of up to euro 22,150,920 for "2002-2003 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 40,274,400 ordinary shares with a par value of euro 0.55 per share to be offered for subscription at a price of euro 5.67 for each option held (i.e. euro 3.277457 for each newly issued share);*
 - 5. *an increase of up to euro 3,192,173.05 for the "2003-2005 Stock-Option Plans", to be implemented by 31 December 2008 for the first lot, by 31 December 2009 for the second lot and by 31 December 2010 for the third lot through the issuance of up to a total of 5,803,951 shares with a par value of euro 0.55 per share to be offered for subscription at a price of euro 5.07 for each option held (i.e. euro 2.930636 for each newly issued share);*
6. to grant severally to the Chairman, the Deputy Chairman and each of the Managing Directors the powers needed:
- (a) to complete all the formalities required for the resolutions adopted to obtain all the necessary authorizations, with the right to introduce into such resolutions, the Merger Plan and the bylaws of the Absorbing Company annexed thereto any amendments, additions or deletions that may be requested on the occasion of filings with the Company Register;
 - (b) to execute, *inter alia* by having ad hoc recourse to attorneys or agents, in conformity with the resolution of point 1, the public merger deed and any other act serving to recognize, supplement or amend that should prove necessary or desirable, defining every condition, clause, time limit and procedure thereof in conformity with and in implementation of the Merger Plan;

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- (c) to complete and amend when executing the merger deed the numbers contained in Article 5 of the bylaws of the Absorbing Company in accordance with the principles and criteria described above and in relation to the number of shares that will be issued for the Merger;
- (d) to make any amendments to the terms and conditions of Tim's stock-option plans referred to in point 4 rendered necessary by the change described in the subscription ratio, with special reference to the rounding down of the number of shares that can be subscribed for when options are exercised;
- (e) to make, as and when necessary, the changes to Article 5 of the bylaws of the Absorbing Company consequent on the implementation of the increases in capital referred to above, and to that end to complete all the formalities and publish all the notices required by law;
- (f) to do – *inter alia* by having ad hoc recourse to attorneys or agents – whatever else may be necessary for and conducive to the complete implementation of the foregoing resolutions, authorizing entries, transcriptions, annotations, amendments and corrections in public registers and every other competent seat.

FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2004 - RELATED AND CONSEQUENT RESOLUTIONS

Dear shareholders,

The draft financial statements submitted for your approval show net income of euro 2,134,847,901.71, which permits last year's dividend policy to be improved on. Accordingly, we propose the distribution of a dividend per ordinary share of euro 0.1093 (+ 5% with respect to the dividend distributed in May 2004) and a dividend per savings share of euro 0.1203.

The total amount of dividends distributed will depend on the number of shares with dividend entitlement outstanding on the dividend payment day, excluding treasury shares and taking into account shares that could be subscribed for in connection with capital increases pursuant to Article 5 of the bylaws and actually issued by that date.

The proposed allocation of net income includes the setting aside in a special reserve of euro 103,083,000.00 in connection with investment plans presented by the Company in 2004 with applications for financial support under Law 488/1992. In this respect it should be noted that the contribution of equity by the Company serves to maintain the support granted by the Ministry for Productive Activities.

Lastly, in approving the draft financial statements, the Meeting is invited to take note of the reclassification of the shareholders' equity item "miscellaneous reserves", partly to replenish in Telecom Italia's balance sheet the reserves subject to restrictions previously present in the balance sheet of IT Telecom S.p.A. (merged into Telecom Italia with effect for accounting purposes from 1 January 2004) and partly to supplement the legal reserve, so that it will continue to exceed the legal minimum requirement following the potential increase in the Company's capital as a consequence of capital increases pursuant to Article 5 of the bylaws.

Accordingly, the Board of Directors invites you to approve the following

Resolution

The Shareholders' Meeting of Telecom Italia S.p.A.,

- having examined the Company's financial statements for the year ended 31 December 2004;
- having seen the Board of Directors' report on operations;
- having taken note of the reports of the Board of Auditors and the independent auditors, Reconta Ernst & Young S.p.A.;
- considering that the total number of shares with dividend entitlement at the proposed dividend payment date will be equal to a maximum of 11,701,139,181 ordinary shares and 5,795,921,069 savings shares, net of 1,272,014 treasury ordinary shares in the Company's portfolio and taking into account the shares that could be subscribed for by that date under Article 5 of the bylaws;
- taking into account the requests for financial support presented by the Company in 2004 under Law 488/1992, which require euro 103,083,000.00 of the Company's equity to be set aside for investment programmes totaling euro 113,500,000.00;

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resolves

1. to approve the Board of Directors' report on operations, the balance sheet, the statement of income and the notes to the statutory financial statements of Telecom Italia S.p.A. for the year ended 31 December 2004, which record net income of euro 2,134,847,901.71 and the reclassification of the shareholders' equity item "miscellaneous reserves" by means of the transfer of
 - euro 118,806,738.27 to the legal reserve; and
 - euro 205,543.95 (which came from the tax deferred reserves in the financial statements of the merged company IT Telecom S.p.A.) to the reserve set up under Article 13 of Legislative Decree 124/1993;
2. with regard to the net income for the year,
 - a. to allocate up to euro 1,976,183,809.32 to the distribution of dividends to shareholders, calculated on the basis of the following amounts per share, which will be applied to the ordinary and savings shares that they own (excluding the treasury shares in the Company's portfolio) on the ex dividend day:
 - euro 0.1093 per ordinary share,
 - euro 0.1203 per savings share,
 gross of the withholdings required by law. It is to be understood that net income not distributed as dividends will be allocated to retained earnings;
 - b. to allocate euro 103,083,000.00 to the reserve under Law 488/1992 for the whole duration of the programmes receiving financial support, of which:
 - euro 30,897,000.00 for project no. 12836-13 (Puglia region),
 - euro 6,888,000.00 for project no. 82333-12 (Sardinia region),
 - euro 32,280,000.00 for project no. 82337-12 (Sicily region),
 - euro 33,018,000.00 for project no. 82336-12 (Campania region);
 - c. to carry forward the remaining amount (equal to euro 55,581,092.39);
3. to authorize the Board of Directors – and on its behalf its Chairman and the Managing Director, Carlo Buora – to determine in due course, on the basis of the actual number of shares for which dividends are paid, the amount of net income distributed to shareholders and the amount carried forward as retained earnings.
4. to pay the above dividends starting on 21 April 2005, ex dividend on 18 April 2005.

EXPANSION OF THE BOARD OF DIRECTORS - RESOLUTIONS

- To redetermine the number of directors
- To redetermine the total annual remuneration of the Board
- To appoint two directors

Dear shareholders,

The merger of Tim into Telecom Italia, submitted for your approval in the Extraordinary Meeting, makes it desirable to propose an extension of the Board of Directors of the "new" Telecom Italia to include proven experience, competence and professionalism in the management of the mobile telephony business.

To this end, two members of Tim's Board of Directors have been selected who have performed different functions in the management of that company since respectively 1999 and 2001: Marco De Benedetti (Managing Director) and Enzo Grilli (director).

Mr. De Benedetti is an executive director and Professor Grilli a director who qualifies as independent on the basis of the requirements laid

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down in the Self-Regulatory Code. The appointment of Professor Grilli (after increasing the total number of directors from 19 to 21) also results in the independent directors continuing to be in a majority on the Board.

It should be noted that the proposed resolution to extend the Board of Directors does not provide for the application of the slate system for electing directors, which the bylaws require to be used only in the case of the renewal of the entire Board.

As a consequence of the extension of the Board, it is also necessary to revise the amount of the directors' annual remuneration, previously determined by the Shareholders' Meeting held on 6 May 2004 (when the number of directors was fixed at 19) at euro 2.7 million gross, to be divided in accordance with the criteria adopted by the Board itself. At present these annually provide for:

- euro 114,000 to be paid to each director in office;
- an additional euro 63,000 to be paid to each of the four members of the Internal Control and Corporate Governance Committee (Guido Ferrarini, Francesco Denozza, Domenico De Sole and Marco Onado);
- an additional euro 52,000 to be paid to each of the three members of the Remuneration Committee (Luigi Fausti, Paolo Baratta and Pasquale Pistorio);
- an additional euro 20,000 to be paid to each of the three members of the Strategy Committee other than the Chairman of the Board and the Managing Director Carlo Buora (Domenico De Sole, Marco Onado and Pasquale Pistorio);
- an additional euro 20,000 to be paid to the director appointed to the Supervisory Panel set up under Legislative Decree 231/2001 (Guido Ferrarini).

In order to be able to pay the new directors consistently with the amounts indicated above and to leave a margin of flexibility for future organizational needs of the Board (it should be noted, for example, that the decision to set up a Strategy Committee was taken some months after the Board was seated), it is proposed that, pursuant to Article 2389, first paragraph, of the Italian Civil Code, the total annual gross amount of the directors' remuneration be increased from euro 2.7 million to euro 3 million.

Accordingly, the Board of Directors invites you to approve the following

resolution

The Shareholders' Meeting of Telecom Italia S.p.A.,

- having seen the resolutions concerning the composition and remuneration of the Board of Directors adopted in the Shareholders' Meeting held on 6 May 2004;
- considering the applicable provisions of law and the bylaws;

resolves

1. to fix the number of directors at 21;
2. to fix, exclusively for the second and third years of the present Board's mandate, the maximum total annual gross amount of the directors' remuneration, pursuant to Article 2389, first paragraph, of the Italian Civil Code, at euro 3,000,000, to be divided in accordance with the criteria adopted by the Board itself;
3. to appoint Marco De Benedetti and Enzo Grilli to the Company's Board of Directors for the duration of the present Board's mandate, that is for two years terminating on the date of the Shareholders' Meeting called to approve the financial statements for the year ending on 31 December 2006.

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■ USEFUL INFORMATION

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The numbers are to disposal for information and help to shareholders

E-mail

corporate.affairs@telecomitalia.it

Internet

User of the world wide can access the
Annual Report 2004 and obtain information
about Telecom Italia and its products and
services at the following address:
<http://www.telecomitalia.it>

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TELECOM ITALIA

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