UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F

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

OR

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

For the fiscal year ended: December 31, 2001

OR

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

For the transition period from N/A to N/A

Commission file number: 1-13882

Telecom Italia S.p.A.

(Exact name of Registrant as specified in its charter)

Italy

(Jurisdiction of incorporation or organization)

Corso d' Italia 41, 00198 Rome, Italy

(Address of principal executive offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act.

Title of each class	**Name of each exchange on which registered**
American Depositary Shares, each representing 10 Ordinary Shares of €0.55 par value each	The New York Stock Exchange
Ordinary Shares of €0.55 par value each (the "Shares")..............................	The New York Stock Exchange*
American Depositary Shares, each representing 10 Savings Shares of €0.55 par value each	The New York Stock Exchange
Savings Shares of €0.55 par value each (the "Savings Shares")	The New York Stock Exchange*

* Not for trading, but only in connection with the registration of American Depositary Shares representing such Shares or Savings Shares, as the case may be, pursuant to the requirements of the Securities and Exchange Commission.

Securities registered or to be registered pursuant to Section 12(g) of the Act.

None

(Title of Class)

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act.

None

(Title of Class)

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

Not applicable

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes **[X]** No **[ ]** Not applicable **[ ]**

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 **[ ]** Item 18 **[X]**

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INTRODUCTION

Telecom Italia S.p.A. (the "Company") is incorporated as a joint stock company under the laws of Italy.

Unless otherwise indicated, the financial information contained in this Annual Report has been prepared in conformity with the Italian law governing consolidated financial statements interpreted and integrated by the accounting principles established or adopted by the Italian Accounting Profession ("Italian GAAP"), which, as described in Note 26 of Notes to the Consolidated Financial Statements, differ in certain material respects from generally accepted accounting principles in the United States ("U.S. GAAP"). Unless otherwise indicated, any reference in this Annual Report to Consolidated Financial Statements is to the Consolidated Financial Statements of the Group (including the notes thereto) included herein.

"Group" and "Telecom Italia" as used herein means Telecom Italia and its consolidated subsidiaries.

Cautionary Statement for Purposes of the "Safe Harbor" Provisions of the United States Private Securities Litigation Reform Act of 1995. The Private Securities Litigation Reform Act of 1995 provides a "safe harbor" for forward-looking statements. This Annual Report contains certain forward-looking statements, including, but not limited to, the discussion of the changing dynamics of the marketplace, including liberalization of the telecommunications industry, the opening to competition of public voice telephone services, the Company's outlook for growth in the telecommunications industry both within and outside of Italy, including sources of increasing revenues to offset the impact of increasing competition and the Company's outlook regarding the impact of tariff rebalancing on the telecommunications industry. Such statements include, but are not limited to, statements under the following headings: (i) "Item 3. Key Information—Risk Factors", (ii) "Item 4. Information on the Company—Business—Significant Developments during 2001—New Strategy and Business Plan", (iii) "Item 4. Information on the Company—Regulation", (iv) "Item 5. Operating and Financial Review and Prospects", (v) "Item 8. Financial Information—Legal Proceedings" and (vi) "Item 11. Quantitative and Qualitative Disclosures About Market Risk", including statements regarding the likely effect of matters discussed therein. Actual results may differ materially from those projected or implied in the forward-looking statements. Such forward-looking information involves risks and uncertainties, which are outside the Company's control, that could significantly affect expected results and are based on certain key assumptions.

The following important factors could cause the Group's actual results to differ materially from those projected or implied in any forward-looking statements:

- the continuing impact of increased competition in a liberalized market, including competition from global and regional alliances formed by other telecommunications operators in Telecom Italia's core domestic fixed-line and wireless markets;
- Telecom Italia's ability to introduce new services to stimulate increased usage of its fixed and wireless networks to offset declines in its fixed-line business due to market share loss and pricing pressures generally;
- Telecom Italia's ability to achieve cost-reduction targets in the time frame established or to continue the process of rationalizing its non-core assets;
- the impact of regulatory decisions and changes in the regulatory environment;
- the impact of the economic crisis in Argentina, the slowdown generally in Latin American economies and the slow recovery of economies generally on Telecom Italia's international business focused on Latin America and on its foreign investments and capital expenditures;
- the continuing impact of rapid changes in technologies;
- the impact of political and economic developments in Italy and other countries in which the Group operates;

- the impact of fluctuations in currency exchange and interest rates;
- Telecom Italia' s ability to implement successfully its 2002-2004 Industrial Plan, including the rationalization of its corporate structure and the disposition of Telecom Italia' s interests in various companies;
- Telecom Italia' s ability to successfully achieve its debt reduction targets;
- Telecom Italia' s ability to successfully roll out its UMTS networks and services and to realize the benefits of its investment in UMTS licenses and related capital expenditures;
- Telecom Italia' s ability to realize the benefits of the merger of SEAT and Tin.it;
- SEAT' s ability to successfully implement its internet strategy;
- Telecom Italia' s ability to achieve the expected return on the significant investments and capital expenditures it has made in Latin America and in Europe;
- the amount and timing of any future impairment charges for Telecom Italia' s licences, goodwill or other assets; and
- the impact of litigation or decreased mobile communications usage arising from actual or perceived health risks or other problems relating to mobile handsets or transmission masts.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. Telecom Italia undertakes no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events. See the related cautionary statement under "Item 5. Operating and Financial Review and Prospects".

KEY DEFINITIONS

The following terms appearing in this Annual Report have the meanings set forth below.

Company	means Telecom Italia S.p.A.
CSELT...	means Centro Studi e Laboratori Telecomunicazioni S.p.A., Telecom Italia subsidiary on study, research, experimentation and qualification in the field of Telecommunications and Information Technology which in 2001 was renamed TILAB.
DCS 1800 Decree	means Law Decree No. 415 of December 12, 1997, approved by the Parliament in February 1998, concerning allocation of frequencies and the testing of DCS 1800 services.
Draghi Law	means Legislative Decree No. 58 of February 24, 1998 and the specific implementing regulations issued by CONSOB.
EU	means the European Union.
Finsiel	means Finsiel-Consulenza e Applicazioni Informatiche S.p.A., the Group' s principal subsidiary operating in information technology software and services.
Finsiel Group	means Finsiel and its subsidiaries.
Framework Law	means Law No. 481 of November 14, 1995, which provides for, among other things, the definition of a transparent tariff system based on the "price cap" method.
Istat	means Istituto Nazionale di Statistica (National Statistic and Census Bureau).
Italtel..	means Italtel S.p.A., the former Group company operating in the telecommunications equipment business.
Maccanico Law	means Law No. 249 of July 31, 1997, which established the formation of the National Regulatory Agency for regulating the communications industry and implemented the Framework Law.
Merger..	means the merger of Old Telecom Italia with and into STET effective July 18, 1997.
National Regulatory Agency.............	means the independent body, responsible in Italy for the regulation of the telecommunications, radio and television broadcasting sector, established by the Maccanico Law.
Old Telecom Italia	means Telecom Italia (and its predecessor companies) prior to the Merger, which was the main operating subsidiary of STET.
Olivetti..	means Olivetti S.p.A., the holding company and controlling shareholder of Telecom Italia.
PCS	means personal communications services.
RIO	means the Reference Interconnection Offer published by Telecom Italia.
Savings Shares	means the savings shares, €0.55 par value each, of Telecom Italia.
SEAT	means SEAT-Pagine Gialle S.p.A.
Shares	means the ordinary shares, €0.55 par value each, of Telecom Italia.
STET...	means STET—Societá Finanziaria Telefonica—per Azioni, the

	holding company for various businesses, principally telecommunications businesses, of the Group prior to the Merger.
Telecom Italia	means Telecom Italia S.p.A., the operating company for fixed telecommunications services and the holding company for various businesses, principally telecommunications, and includes STET, the surviving company in the Merger which was renamed Telecom Italia, and Old Telecom Italia.
Telecom Merger.................................	means the merger of five telecommunications companies, including the principal providers of domestic and international telephony services, which in 1994 created Old Telecom Italia as the single Italian integrated public telephony services provider.
Telecommunications Regulations	means the telecommunications regulations (approved by Presidential Decree No. 318 of September 19, 1997 which became effective on October 7, 1997, 15 days after its publication) adopted to implement a number of EU directives in the telecommunications sector.
TILAB	means Telecom Italia Lab S.p.A. (formerly CSELT), Telecom Italia' s subsidiary for evaluating, developing and managing new business opportunities.
TIM..	means Telecom Italia Mobile S.p.A., the Group' s subsidiary operating in the mobile telecommunications business.
TIM Demerger...................................	means the demerger which separated mobile telecommunications services from Old Telecom Italia effective July 14, 1995.
Tin.it	means Telecom Italia Net S.p.A., the Group' s subsidiary providing Internet access which was combined with SEAT in November 2000.

PART I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not Applicable

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable

Item 3. KEY INFORMATION

RISK FACTORS

Continuing competition in a fully liberalized market may further reduce Telecom Italia's market share of domestic and international traffic and may cause further reductions in prices and margins.

Domestic competition exists in all of the principal telecommunications business areas in which Telecom Italia operates, including, most significantly, fixed-line and mobile voice telecommunications services, which were liberalized and have been opened to competition since 1998 for fixed-line services and since 1995 for mobile services. As a result, the Company and TIM have faced intensifying competition in Italy, including competition from foreign telecommunications operators, particularly with respect to medium-sized and large business customers. In the last few years the Company and TIM are facing an increased number of competitors due to the entry of global and regional alliances formed by other telecommunications operators in Telecom Italia's core fixed and wireless markets. As of June 2002, there were a number of significant competitors offering fixed-line services and three other operators offering mobile services in the Italian domestic market. This increased competition has led to declines in the Company's market shares, as well as to downward pressure on prices. Continuing pressures on prices due to competition and further erosion in market shares could adversely affect Telecom Italia's results of operations. Additional changes in the regulatory regime, including carrier preselection, number portability and local loop unbundling could further increase competition for the services Telecom Italia provides which could also adversely affect its business.

Telecom Italia's business may be adversely affected if it is unable to continue the introduction of new services to stimulate increased usage of its fixed and wireless networks.

In order to offset revenues lost due to increased competition and lower prices, Telecom Italia's strategy has been to introduce new services in both its fixed-line and wireless services to increase traffic on its networks and find alternative revenue sources. These services include non-voice services such as Internet and data traffic and value added services such as interactive mobile services allowing users to receive news or engage in simple banking transactions. Alternative revenue sources also include increased interconnection traffic from other operators using the Company's fixed-line network. In addition to the steps taken in recent years, Telecom Italia continues to develop new products and services, such as new data services for business customers, broadband services, enhanced communication services and new voice packages, in order to attract and retain customers, particularly business customers, and to stimulate usage of its fixed and wireless telecommunications network. Telecom Italia is also investing in new infrastructure and technologies to enable it to introduce new products and services. Telecom Italia expects that these strategic initiatives will require substantial expenditures and commitment of human resources. Telecom Italia may not be able to introduce commercially these new products and services, and even if it introduces them, they may not be successful.

Telecom Italia' s business will be adversely affected if it is unable to successfully implement the business plans proposed by its new management. Factors beyond Telecom Italia' s control may prevent Telecom Italia from successfully implementing its plan.

On February 14, 2002 the company announced the 2002-2004 business plan (the "2002-2004 Plan"). The 2002-2004 Plan is intended to rationalize Telecom Italia' s structure and portfolio by providing for divestitures of non-strategic holdings valued at approximately €5 billion. The 2002-2004 Plan provides that Telecom Italia' s activities will be highly focused on its core businesses, with the objective of further enhancing its strong market position in Europe.

Factors beyond Telecom Italia' s control that could affect the implementation and completion of the 2002-2004 Plan include:

- Telecom Italia' s ability to manage costs;
- Telecom Italia' s ability to attract and retain highly-skilled and qualified personnel;
- Telecom Italia' s ability to divest non-core businesses and the adequacy of the returns of such divestitures;
- difficulties in developing and introducing new technologies;
- the need to establish and maintain strategic relationships;
- declining prices for some of Telecom Italia' s services;
- the effect of future acquisitions on Telecom Italia' s financial condition and results of operations;
- the effect of adverse economic trends on Telecom Italia' s principal markets; and
- the effect of foreign exchange fluctuations on Telecom Italia' s results of operations.

Regulatory decisions and changes in the regulatory environment could adversely affect Telecom Italia' s business.

Telecom Italia' s fixed and mobile telecommunications operations, as well as its broadband services businesses, are subject to extensive regulatory requirements in Italy and its international operations and investments are subject to regulation in their host countries. In Italy, the Company is the only operator subject to universal service obligations, including the provision of fixed public voice telecommunications services in non-profitable areas, publication of telephone directories and provision of subscriber information services at affordable prices and provision of public payphones. In addition, the National Regulatory Agency has identified the Company as an operator having significant market power in all relevant markets. As a result, the Company is subject to a number of regulatory constraints, including:

- a requirement to conduct its business in a transparent and non-discriminatory fashion;
- a requirement to have its prices for fixed-line telecommunications services approved by the National Regulatory Agency prior to implementation in accordance with a price cap mechanism; and
- a requirement to provide interconnection services, leased lines and access to the local loop to other operators at cost-oriented prices. These services include allowing other operators to interconnect to the Company' s network and transport traffic through the network and offering certain services relating to its local access network, or local loop, on an unbundled basis to other operators to enable these operators to access directly end users by leasing the necessary components from Telecom Italia.

As a member of the European Economic Area, or EEA, Italy is additionally required to adapt its regulatory framework to the legislative and regulatory framework established by the EU for the regulation of the European telecommunications market as far as the directives are made relevant to the EEA Agreement. The EU regulators approved revised telecommunications regulation in March 2002. Implementation of such regulation through Italian law is expected by July 2003. The implementation of the revised telecommunications regulation and possible future decisions relating thereto may change the regulatory accounting system currently used by Telecom Italia in a manner adverse to Telecom Italia. Please see "Item 4.—Information on the Company—Regulation" in this report for more information on the regulatory requirements to which Telecom Italia is subject.

Telecom Italia is unable to predict the impact of any proposed or potential changes in the regulatory environment in which it operates both in Italy and internationally. Changes in laws, regulation or government policy could adversely affect Telecom Italia's business and competitiveness. In particular, Telecom Italia's ability to compete effectively in its existing or new markets could be adversely affected if regulators decide to expand the restrictions and obligations to which Telecom Italia is subject or extend them to new services and markets. In addition, changes in tax laws in countries in which Telecom Italia operates could adversely affect its results of operations. Finally, decisions by regulators regarding the granting, amendment or renewal of licenses, to Telecom Italia or to third parties, could adversely affect Telecom Italia's future operations in Italy and in other countries where it operates.

The costs of providing universal services could adversely affect Telecom Italia.

Telecom Italia, through its domestic fixed network, is required to provide universal service throughout Italy. The net cost of such obligation is required to be shared by Telecom Italia and by the other telecommunication operators which derive benefits from such universal service if the National Regulatory Agency determines that the net cost of the universal service represents an unfair burden on Telecom Italia. An independent committee is responsible for the audit of the net cost of providing universal service and for evaluation of the indirect benefits that Telecom Italia may accrue from providing such universal service. The net costs approved by the independent committee are then shared among operators, including Telecom Italia. Differences between Telecom Italia's estimates of the net cost and the outcome of the audit processes, where Telecom Italia's estimates exceeded the outcome of the audit processes, as well as the allocation of any net costs among other operations, may adversely affect Telecom Italia.

Telecom Italia may not be able to achieve the expected return on the significant investments and capital expenditures it has made in Latin America and in Europe due to the competitive environment in these markets. Returns from the sale of non-core international assets may be lower than expected.

In recent years Telecom Italia pursued a significant strategic acquisition program in Latin America and Europe aimed at achieving a stronger competitive position and balancing the loss of market share in its domestic market. During the past 18 months Telecom Italia has reconsidered this strategy. Telecom Italia's strategy is now focused on:

- consolidating its international presence in Latin America;
- developing its international investments in high-growth market segments, such as wireless, data and Internet;
- strengthening its role of strategic partner in existing investments by increasing the transfer of its technological expertise and marketing know-how; and
- rationalizing its existing international portfolio by divesting minority participations in non-strategic geographical markets.

As a result of this change in strategy, Telecom Italia is seeking to divest certain international non-strategic assets. Due to the current market situation, the general economic conditions and the high level of competition, the actual returns from the announced divestment of non-strategic European assets may be lower than the ones originally expected.

Continuing rapid changes in technologies could increase competition or require Telecom Italia to make substantial additional investments.

The services Telecom Italia offers are technology-intensive and the development of new technologies may render its services non-competitive. Telecom Italia is already making and may have to make substantial additional investments in new technologies to remain competitive. The new technologies Telecom Italia chooses may not prove to be commercially successful. In addition, Telecom Italia may not receive the necessary licenses to provide services based on new technologies in Italy or abroad. As a result, Telecom Italia could lose customers, fail to attract new customers or incur substantial costs in order to maintain its customer base.

The value of Telecom Italia's operations and investments may be adversely affeted by political and economic developments in Italy or other countries.

Telecom Italia's business is dependent on general economic conditions in Italy, including levels of interest rates and inflation. A significant deterioration in these conditions could adversely affect Telecom Italia's business and results of operations. Telecom Italia may also be adversely affected by political and economic developments in other countries where it has made significant equity investments in telecommunications operators. Some of these countries have political, economic and legal systems that are unpredictable. Political or economic upheaval or changes in laws or their application in these countries may harm the operations of the companies in which Telecom Italia has invested and impair the value of these investments. A significant risk of operating in emerging market countries is that foreign exchange restrictions could be established. This could effectively prevent Telecom Italia from receiving profits from, or from selling its investments in, these countries.

Fluctuations in currency exchange and interest rates may adversely affect Telecom Italia's reported results.

Because Telecom Italia has made substantial international investments, primarily in U.S. dollars, and has significantly expanded its operations outside the euro zone, movements in the exchange rates of the euro against other currencies could have an adverse effect on Telecom Italia's revenues and operating results. A rise in the value of the euro relative to other currencies in certain countries in which Telecom Italia operates or has made investments would reduce the relative value of the revenues or assets of Telecom Italia's operations in those countries and, therefore, may adversely affect Telecom Italia's operating results or financial position. In addition, Telecom Italia has raised, and may raise in an increasing proportion in the future, financing in currencies other than the euro, principally the U.S. dollar. Accordingly, the value of those liabilities will be affected by the fluctuation of the euro against the currency in which the financing is denominated. Telecom Italia generally enters into a number of forward currency transactions, swaps and options to manage foreign currency risk exposure with respect to its non-euro denominated liabilities. However, Telecom Italia can give no assurances that it will be successful in managing foreign currency risk exposure.

In addition, to finance its international expansion as well as the payment of the 2000 dividend, the Group's total net indebtedness at year end 2001 was €21,942 million compared with €17,233 million (giving pro forma effect to the consolidation of the Nortel Inversora group on an equity basis at year end 2000). A substantial portion of this indebtedness bears interest at floating rates. Telecom Italia generally enters into interest rate swaps and interest rate options to manage its exposure to floating interest rates. However, Telecom Italia can give no assurance that fluctuations in interest rates will not adversely affect its results of operations.

Telecom Italia may not be able to realize the benefits of its investment in UMTS licenses and related capital expenditures.

Through TIM and other subsidiaries, Telecom Italia has acquired a third generation mobile telephone, or UMTS, license to commence operations of UMTS services in Italy, Greece and Austria. In addition, TIM has made and may be required to make during the next several years substantial investments in Latin America to acquire additional UMTS licenses, to build out UMTS networks and develop related products and services. As of June 10, 2002, TIM has committed to pay €2,417 million (of which €2,183 million have already been paid) for its UMTS license in Italy and, through its international subsidiaries and affiliated companies, a further €319 million for UMTS licenses in Greece and Austria (of which approximately €275 million has already been paid). The suppliers of the handsets and other equipment which Telecom Italia and its competitors intend to use in providing such products and services have not yet fully developed the technology for new UMTS products and service s. Developing UMTS technology may take longer than Telecom Italia anticipated and may prove not to be superior to existing or future technologies. The size of the market for these products and services is unknown and may fall short of the industry' s expectations. Telecom Italia cannot be certain that the demand for such services will justify the related costs. In some locations, the investments, although required under the licenses, may not be commercially desirable. In addition, Telecom Italia has a number of significant competitors in each of its geographic markets.

Telecom Italia expects to roll out its UMTS networks at the same time as its competitors expect to roll out their own UMTS networks throughout Europe. This, combined with the limited number of suppliers of UMTS network equipment, is likely to create high demand for such equipment, and may extend delivery times, which may cause delays in the construction of UMTS networks. Given the substantial costs of upgrading Telecom Italia' sexisting networks to support UMTS and the uncertainty regarding the commercial adoption of UMTS, Telecom Italia may not be able to recoup its investment according to its estimates, if at all. Furthermore, Telecom Italia' scompetitors may be able to build out their UMTS networks more economically than Telecom Italia. This could place Telecom Italia at a competitive disadvantage in providing UMTS services in the relevant market. Telecom Italia has entered into and intends to enter into arrangements with other operators to share the costs and infrastructure of its planned UMTS networks. However, Telecom Italia cannot give any assurance that it will succeed in concluding the necessary agreements with other operators on satisfactory terms. Moreover, while network sharing is intended to reduce costs, Telecom Italia cannot give any assurance that this will be the case or that it will be able to make such network sharing work commercially or technically.

Devaluations of telecom assets and write-downs could adversely affect Telecom Italia' s financial condition and results of operations.

Recent events in the market for telecom stocks and credit ratings of market participants, as well as Telecom Italia' s ongoing review and refinement ofits business plan, has resulted and may result in substantial impairment write-downs of Telecom Italia' s assets at any time. Telecom Italia has recognizedin its financial statements extraordinary write-downs on its assets of €2,381 million under Italian GAAP in 2001. Further charges of €2,641 million and €7,966 million were recognized under U.S. GAAP in 2001 and 2000.

Accounting standards relating to asset valuations and impairment may be refined to require the use of new criteria or methodology. Starting in fiscal year 2002, under U.S. GAAP goodwill has to be valued pursuant to SFAS 142 "Goodwill and Other Intangible Assets". In accordance with the provisions of SFAS 142, goodwill will no longer be amortized, but will be subject to annual impairment tests which are based on a fair value approach such as discounted cash flows. Upon adoption of SFAS 142 in 2002, recognition of impairments of tangible, intangible and financial assets could adversely affect Telecom Italia' sU.S. GAAP results and financial condition.

Growth in the traditional mobile telecommunications industry has slowed significantly during the last year and our revenues may not grow as rapidly as in the past.

In recent years, Telecom Italia' s revenues have grown in large part because of the rapid growth in the mobile communications business. This growth has been driven largely by the rapid expansion of the mobile telecommunications market in Italy. However, as a result of this growth, mobile phone use in the Italian market is approaching saturation levels.

Continued growth in the mobile telecommunications markets in which Telecom Italia operates depends on a number of factors, many of which are outside Telecom Italia' scontrol. These factors include:

- the activities of TIM' s competitors, including consolidation and continuedcompetitive tariff reductions and handset subsidies;
- the development and introduction of new and alternative technologies for mobile telecommunications products and services and the attractiveness of these to customers;

- customer usage habits;
- general economic conditions; and
- health risks or safety concerns associated with mobile telephones and transmission equipment.

If the mobile telecommunications markets in which TIM operates do not continue to expand, or TIM is unable to retain its existing customers or is unable to stimulate increases in customer usage, Telecom Italia' s financial condition and results of operations may be harmed.

Actual or perceived health risks or other problems relating to mobile handsets or transmission masts could lead to litigation or decreased mobile communications usage.

Various reports have alleged that certain radio frequency emissions from wireless handsets and transmission equipment may be linked to various health concerns and may interfere with various electronic devices. Telecom Italia cannot rule out that exposure to electromagnetic fields or other emissions originating from wireless handsets will be identified as a health risk in the future. Telecom Italia' smobile communications business may be harmed as a result of these alleged health risks. For example, this could result in a lower number of customers, reduced usage per customer or potential consumer liability for Telecom Italia. In addition, these concerns may cause regulators to impose greater restrictions on the construction of base station towers or other infrastructure, which may hinder the completion of network build-outs and the commercial availability of new services.

Telecom Italia may be adversely affected if SEAT fails to implement successfully its Internetstrategy.

SEAT' s ability to develop successfully its Internet operations and its strategy to provide a full-range of Internet services to consumers and small and medium-sized companies may be adversely affected if:

- Internet usage in Italy grows more slowly than anticipated, for reasons such as changes in Internet users' preferences;
- the Internet is not accepted as an advertising and commerce medium, for reasons such as the lack of on-line payment methods, low levels of credit card use and on-line security concerns;
- competition by Internet companies increases, for reasons such as the entry of new competitors or consolidation in the industry;
- Internet services become subject to burdensome governmental regulation; and
- SEAT experiences any network interruptions or related problems with network infrastructure.

Any of the above factors may adversely affect SEAT' s, as well as Telecom Italia' s, business and results of operations.

Risk Relating to Olivetti' s Interest in Telecom Italia.

Olivetti has effective control over Telecom Italia, which may limit other shareholders' influence in voting matters.

Olivetti currently has a 54.95% interest in Telecom Italia' s ordinary shares. As a result, Olivetti is able to elect the majority of the members of Telecom Italia' s board of directors, who have substantial involvement in the day-to-day activities of Telecom Italia and will have a significant influence on all matters to be decided by a vote of shareholders, including resolutions relating to:

- corporate reorganizations;
- mergers;

- amendments to the Telecom Italia's bylaws; and
- the payment of dividends.

The interests of Olivetti in deciding these matters could be different from the interests of Telecom Italia's other ordinary shareholders. In addition, Olivetti's interest in Telecom Italia may allow it to prevent the acquisition of Telecom Italia by any third party without Olivetti's approval. In 2001 Olimpia S.p.A. ("Olimpia") acquired the stake in Olivetti previously held by Bell S.A., a Luxembourg holding company ("Bell") and became Olivetti's largest shareholder. See "Item 4. Information on the Company—Business—Significant Developments during 2001—The Pirelli-Olimpia Transaction."

Olivetti's debt level may restrain Telecom Italia's financial flexibility.

In connection with the tender offer Olivetti launched for Telecom Italia, Olivetti and its subsidiaries incurred a substantial amount of debt to finance the consideration paid to tendering shareholders. As of December 31, 2001, Olivetti's total net debt was approximately €16.3 billion. Olivetti's financial position may adversely affect Telecom Italia's financial flexibility and its cost of capital because some lenders and other providers of capital currently view Olivetti's and Telecom Italia's financial position on a consolidated basis. Please see "Item 4. Information on the Company—Business".

RATES OF EXCHANGE

Beginning with the fiscal year 2001, Telecom Italia has published its consolidated financial statements in euros. References to "€", "euro" and "Euro" are to the euro, the currency of 12 member states of the European Union, including Italy and references to "lire", "lira" and "Lit." are to Italian lire, the former Italian non-decimal denomination of the euro, and references to "U.S. dollars", "dollars", "U.S.$" or "$" are to U.S. dollars, the currency of the United States.

For convenience only (except where noted otherwise), certain euro figures have been translated into dollars at the rate (the "Euro/Dollar Exchange Rate") of €1.00 = U.S.$ 0.8901, using the noon buying rate in The City of New York for cable transfers in foreign currencies as announced by the Federal Reserve Bank of New York for customs purposes (the "Noon Buying Rate") on December 31, 2001. These translations should not be construed as a representation that the euro amounts actually represent such dollar amounts or have been or could be converted into dollars at the rate indicated.

For the purpose of this Annual Report, "billion" means a thousand million.

Exchange Rates

Effective January 1, 1999, the following 11 European Union member states adopted the euro as a common currency: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, The Netherlands, Portugal and Spain. They also established fixed conversion rates between their respective sovereign currencies and the euro. On January 1, 2001, Greece (together, with the 11 European Union member states referred to in the previous sentence, the "Member States") joined the European Economic and Monetary Union. The exchange rate at which the lira was irrevocably fixed against the euro is Lit.1,936.27 = €1.00. On January 1, 2002, the Member States began issuing new euro-denominated bills and coins for use in cash transactions. As of March 1, 2002, the Member States withdrew the bills and coins denominated in their respective currencies from circulation, and they are no longer legal tender for any transactions.

The Federal Reserve Bank of New York no longer quotes a Noon Buying Rate for the legacy currencies of any of the Member States.

At the extraordinary stockholders' meeting held on May 3, 2001, Telecom Italia's share capital was converted from lire into euros by rounding up the par value of the shares, from Lit. 1,000 (approximately €0.52) to €0.55 partially through the cancellation of 112,998,070 Savings Shares held in treasury.

The following table sets forth, for the years 1997 and 1998, certain information regarding the Noon Buying Rate for the lira expressed in lira per U.S.$1.

Calendar Period	High	Low	Average(1)	At Period End
1997	1,841	1,516	1,712	1,769
1998	1,828	1,592	1,737	1,654

(1) Average of the rates for the last business day of each month in the relevant period.

The following table sets forth for the years 1999 to 2001 and for the beginning of 2002 certain information regarding the Noon Buying Rate for Dollars expressed in U.S.$ per €1.00.

Calendar Period	High	Low	Average(1)	At Period End
1999	1.1812	1.0016	1.0588	1.0070
2000	1.0335	0.8270	0.9207	0.9388
2001	0.9535	0.8425	0.8909	0.8901
2002 (through June 20, 2002)	0.9646	0.8594	0.8966	0.9646
Monthly Amounts				
January 2002	0.9031	0.8594	0.8832	0.8594
February 2002	0.8778	0.8613	0.8707	0.8658
March 2002	0.8836	0.8652	0.8766	0.8717
April 2002	0.9028	0.8750	0.8860	0.9002
May 2002	0.9373	0.9022	0.9170	0.9339
June 2002 (through June 20, 2002)	0.9646	0.9390	0.9462	0.9646

(1) Average of the rates for the last business day of each month in the relevant period except for 2002 for which the date used is June 20, 2002.

Beginning January 4, 1999, the Shares and Savings Shares commenced trading on *Mercato Telematico Azionario* ("Telematico"), managed by Borsa Italiana S.p.A. ("Borsa Italiana") in euro. Fluctuations in the exchange rate between the euro and the U.S. dollar will affect the U.S. dollar equivalent of the euro price of the Shares and the Savings Shares and the price of the American Depositary Shares ("ADSs") and the Savings Share American Depositary Shares ("Savings Share ADSs"), on the New York Stock Exchange ("NYSE"). Cash dividends were paid by Telecom Italia in lire until 2001 and in euro in 2002. Exchange rate fluctuations will affect the U.S. dollar amounts received by owners of ADSs and Savings Share ADSs upon conversion by the Depositary of cash dividends paid in euro on the underlying Telecom Italia Shares and Telecom Italia Savings Shares. See "Item 10. Additional Information—Description of American Depositary Receipts".

SELECTED FINANCIAL AND STATISTICAL INFORMATION

The selected financial data below should be read in conjunction with the Consolidated Financial Statements and notes thereto included elsewhere in this Annual Report. The selected financial data (other than the 2000 pro forma data) for each of the five years in the period ended December 31, 2001, are extracted or derived from the consolidated financial statements of the Company, which have been audited by the following independent auditors: Reconta Ernst & Young S.p.A. (only for the year ended December 31, 2001), PricewaterhouseCoopers S.p.A. (only for the year ended December 31, 2000) and Arthur Andersen S.p.A., for all other periods. In accordance with Italian law, the financial statements of the parent company Telecom Italia have been approved by the shareholders of Telecom Italia at its Annual Meeting of Shareholders held on May 7, 2002. The Group's Consolidated Financial Statements included herein have been approved by the Telecom Italia Board of Directors.

	Year ended December 31,						
	1997(1)	1998(1)	1999(1)	2000(1)	2000 pro forma (1) (2)	2001(1)	2001
	(millions of Euro, except per share and per ADS amounts)						(millions of U.S. dollars, except per share and per ADS amounts) (3)
Statement of Operations Data:							
Operating revenues	23,236(4)	25,052(4)	27,104	28,911	27,169	30,818	27,431
Other income	460	560	516	426	402	417	371
Total revenues	23,696(4)	25,612(4)	27,620	29,337	27,571	31,235	27,802
Cost of materials	2,389	2,342	2,477	2,259	2,132	1,972	1,755
Salaries and social security contributions	5,032	4,992	4,977	5,025	4,745	4,666	4,153
Depreciation and amortization	5,842	5,412	5,339	5,647	5,209	6,275	5,585
Other external charges	7,306(4)	9,065(4)	9,586	10,790	10,130	12,171	10,833
Changes in inventories	(286)	135	(130)	(277)	(255)	58	52
Capitalized internal construction costs	(902)	(1,078)	(1,062)	(912)	(831)	(581)	(517)
Total operating expenses	19,381(4)	20,868(4)	21,187	22,532	21,130	24,561	21,861
Operating income	4,315	4,744(4)	6,433	6,805	6,441	6,674	5,941
Financial income	518	815	555	847	806	1,076	958
Financial expense	(849)	(868)	(1,466)	(2,470)	(2,261)	(5,031)	(4,478)
Of which write-downs and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies, net	*(69)*	*(178)*	*(565)*	*(1,025)*	*(1,011)*	*(1,665)*	*(1,482)*
Other income and expense, net	(487)	69(4)	(507)	(214)	(184)	(3,452)	(3,073)
Income (loss) before income taxes	3,497	4,760	5,015	4,968	4,802	(733)	(652)
Income taxes	(1,716)	(2,048)	(2,606)	(2,020)	(1,910)	(925)	(823)
Net income (loss) before minority interests	1,781	2,712	2,409	2,948	2,892	(1,658)	(1,475)
Minority interest	(434)	(734)	(672)	(920)	(864)	(410)	(365)
Net income (loss)	1,347	1,978	1,737	2,028	2,028	(2,068)	(1,840)
Net income (loss) per Share(5)	0.1787	0.2634	0.2309	0.2741	0.2741	(0.2858)	(0.2544)
Net income (loss) per Share ADS(5)	1.7869	2.6339	2.3086	2.7410	2.7410	(2.8581)	(2.5440)
Dividends per Share	0.0981	0.1446	0.3114	0.3125	0.3125	0.3125(6)	(0.2782)
Dividends per Savings Share	0.1085	0.1549	0.3218	0.3238	0.3238	0.3237(6)	(0.2881)
Amounts in accordance with U.S. GAAP							
Total revenues	23,696(4)	25,612(4)	27,620	27,938	--	31,017	27,607
Operating income (loss)	4,444	4,662(4)	6,153	(1,926)	--	2,272	2,022
Income (loss) before income taxes	3,554	4,419	4,774	7,058	--	(3,379)	(3,008)
Net income (loss)	621	1,526	1,505	3,522	--	(4,039)	(3,595)
Net income (loss) per Share—Basic (7)	0.0954	0.2026	0.1998	0.4731	--	(0.5553)	(0.4943)
Net income (loss) per Share—Diluted (7)	0.0954	0.2026	0.1997	0.4717	--	(0.5553)	(0.4943)
Net income (loss) per Share ADS—Basic (7)	0.9539	2.0255	1.9982	4.7307	--	(5.5531)	(4.9427)
Net income (loss) per Share ADS—Diluted (7)	0.9539	2.0255	1.9966	4.7173	--	(5.5531)	(4.9427)

	Year ended December 31,						
	1997(1)	1998(1)	1999(1)	2000(1)	2000 pro forma (1) (2)	2001(1)	2001
	(millions of Euro except ratios and other data)						(millions of U.S. dollars) (3)
Balance Sheet Data							
Total current assets	11,822	12,186(8)	12,749	16,395	15,673	16,736	14,897
Total fixed assets, net	24,591	23,584	23,508	23,425	20,721	21,757	19,366
Intangible assets, net	1,674	1,884	2,737	16,037	15,571	16,197	14,417
Total assets	42,134	44,870(8)	46,058	65,515	61,985	62,670	55,783
Total short-term debt	3,775	4,824	4,969	15,136	14,745	9,114	8,112
Total current liabilities	15,022	16,865	17,448	27,482	26,510	21,945	19,533
Total long-term debt	6,194	5,598	5,166	8,268	6,733	16,083	14,315
Total liabilities	25,073	26,440(8)	26,270	39,986	37,293	43,361	38,596
Total stockholders' equitybefore minority interest	15,448	16,346	17,045	18,821	18,821	13,522	12,036
Total stockholders' equity	17,061	18,430	19,788	25,529	24,692	19,309	17,187
Amounts in accordance with U.S. GAAP							
Total current assets	12,228	12,660	12,984	15,366	--	16,944	15,081
Total fixed assets, net	23,995	23,172	23,150	22,823	--	23,883	21,258
Intangible assets, net	5,335	5,292	5,894	24,084	--	22,506	20,032
Total assets	45,482	48,108	49,263	71,528	--	72,518	64,547
Total current liabilities	15,022	16,865	17,448	26,207	--	21,487	19,125
Total long-term debt	6,194	5,598	5,166	12,466	--	21,906	19,498
Total liabilities	25,303	26,908	26,908	44,848	--	52,332	46,579
Stockholders' equity (9)	18,569	19,145	19,659	19,118	--	12,457	11,088
Financial Ratios							
Gross operating margin (Gross operating profit/operating revenues)(%) (10)	47.5	47.2	45.1	45.4	45.0	44.2	44.2
Operating income/operating revenues (ROS) (%)	18.6	18.9	23.7	23.5	23.7	21.7	21.7
Return on equity (ROE) (%)	10.9	15.3	12.6	13.0	13.0	n.s.	n.s.
Return on investments (ROI) (%)	18.4	18.5	23.6	18.8	18.4	16.0	16.0
Net debt/Net invested capital (debt ratio) (%)	31.7	30.7	29.1	42.7	41.1	53.2	53.2
Statistical Data:							
Subscriber fixed lines (thousands) (11)	25,698	25,986	26,502	27,153	27,153	27,353	
ISDN equivalent lines (thousands) (12)	897	1,735	3,049	4,584	4,584	5,403	
TIM lines in Italy (thousands) (13)	9,278	14,299	18,527	21,601	21,601	23,946	
Subscriber fixed lines per full-time equivalent employee (14)	317	332	354	409	409	448	
Page views Virgilio (millions)	--	--	505	2,218	2,218	3,945	
Active Users (at year-end, thousands)	--	--	1,104	1,656	1,656	1,804	

(1) Beginning from the consolidated financial statements for the year ended December 31, 2001, under Italian GAAP, Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group), which in 2000 were consolidated proportionally, have been accounted for using the equity method. Prior to 2000 the Nortel Inversora group was accounted for on the equity method. Under U.S. GAAP, the Nortel Inversora group is accounted for using the equity method. These differences in accounting treatment for 2000 did not affect net income and stockholders' equity buthad an impact on other line items, such as operating revenues and operating expenses, as well as a number of balance sheet line items.

(2) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(3) For the convenience of the reader, Euro amounts for 2001 have been translated into U.S. dollars using the Euro/Dollar Exchange Rate in effect on December 31, 2001 of €1.1235 = U.S.$1.00.

(4) Beginning in 1999 Telecom Italia changed the way in which it accounted for revenues from telecommunications services, calculating such revenues gross of interconnection and service charges payable to other operators and service providers and accounting for such interconnection and service charges as an operating expense (other external charges). In prior fiscal years, revenues from telecommunications services were accounted for net of interconnection and service charges. Due to this change, operating revenues from telecommunications services and other external charges increased by the same amount: €1,123 million and €1,571 million in 1997 and 1998, respectively. This accounting change had no impact on reported net income for 1997 and 1998. In 1998, the item "other external charges" also takes into account additional expenses (€10 million) included in "other income and expense, net" in the consolidated financial statements in Telecom Italia's 1998 Annual Report on Form 20-F. Such additional expenses, which have not been reclassified for previous years, amounted to €10 million in 1997.

(5) Net income per Share in 1997 and 1998 is calculated on the basis of 7,421,251,726 Shares and Savings Shares outstanding. Net income per Share in 1999 is calculated on the basis of 7,426,157,226 Shares and Savings Shares outstanding. Net income per share in 2000 is calculated on the basis of 7,321,179,156 Shares and Savings Shares outstanding; Savings Shares are net of 104,978,070 shares of treasury stock acquired during 2000. Net income (loss) per share in 2001 is calculated on the basis of 7,314,655,506 Shares and Savings Shares outstanding. The increase in Shares and Savings Shares outstanding in 1999 is due to the issuance of 4,905,500 new Shares in connection with the Stock Option Plan. The decrease in Shares and Savings Shares outstanding in 2001 is due to the cancellation of 112,998,070 Savings Shares of treasury stock following the re-denomination of the share capital into Euro and the issuance of 1,496,350 new Shares in connection with the Stock Option Plan. The calculations take into account the requirement that holders of Savings Shares are entitled to an additional dividend equal to 2% of the par value of Savings Shares above dividends paid on the Shares. Prior to 2000 the par value of the Savings Shares was Lit. 1,000 per share, while for 2001, following the resolution of the extraordinary shareholders' meeting held on May 3, 2001 regarding the re-denomination of Telecom Italia share capital into Euro, the calculations take into account the new par value per share of €0.55. Net income (loss) per Savings Share was €0.1890, €0.2737, €0.2412, €0.2844 and €(0.2748) in each of 1997, 1998, 1999, 2000 (historical and pro forma) and 2001, respectively, and net income (loss) per Savings Share ADS was €1.8902, €2.7372, €2.4119, €2.8443 and €(2.7481) in each of 1997, 1998, 1999, 2000 (historical) and 2000 (pro forma) and 2001, respectively.

(6) Approved at the Annual Meeting of Shareholders held on May 7, 2002. Pursuant to Borsa Italiana rules, dividends are payable from the fourth business day after the third Friday of each month, and in any case, at least four days after the Annual Meeting of Shareholders approving the dividends. Telecom Italia's dividend coupons for the year ended December 31, 2001 were clipped on May 20, 2002, while Telecom Italia's dividends for the year ended December 31, 2001 were payable from May 23, 2002. Dividends for the year ended December 31, 2001 were paid by utilizing reserves.

(7) In accordance with U.S. GAAP, the Net income per Share has been calculated using the two class method since the Company has both Shares and Savings Shares outstanding. Under this method, set forth in Statement of Financial Accounting Standards No. 128, "Earnings per Share", Basic earnings per share is computed by dividing income available to shareholders by the weighted average number of shares outstanding, and diluted earnings per share is increased to include any potential common shares and is adjusted for any changes to income that would result from the assumed conversion of those potential common shares. For the purpose of these calculations, the weighted average number of Shares and Savings Shares was 6,351,231,924 for the year ended December 31, 1997, 7,421,251,726 for the year ended December 31, 1998, 7,421,660,518 for the year ended December 31, 1999, 7,398,247,829 for the year ended December 31, 2000 and 7,314,353,578 for the year ended December 31, 2001. The calculations take into account the requirement that holders of Savings Shares are entitled to an additional dividend equal to 2% of the par value of Savings Shares above dividends paid on the Shares. Prior to 2001 the par value of the Savings Shares was of Lit. 1,000 per share, while for 2001, following the resolution of the extraordinary shareholders' meeting held on May 3, 2001 regarding the redenomination of Telecom Italia share capital into Euro, the calculations take into account the new par value per share of €0.55. In addition, in accordance with U.S. GAAP, net income per Savings Share—Basic was €0.1057, €0.2129, €0.2101, €0.4834 and €(0.5443) in 1997, 1998, 1999, 2000 (historical) and 2000 (pro forma) and 2001, respectively, and net income per Savings Share ADS—Basic, was €1.0572, €2.1288, €2.1015, €4.8340 and €(5.4431) in 1997, 1998, 1999, 2000 (historical) and 2000 (pro forma) and 2001, respectively.

(8) As a consequence of the introduction of the new Italian Accounting Principle for Income Taxes, beginning in 1999, deferred tax assets and liabilities are offset. Due to this change as of December 31, 1998 the amount of current assets was reduced by €114 million, while total assets and liabilities were reduced by the same amount of €379 million.

(9) Stockholders' equity under U.S. GAAP is calculated after elimination of minority interest. See Note 26 of Notes to Consolidated Financial Statements included elsewhere herein.

(10) Gross operating profit is equal to operating revenues plus operating grants and reimbursements for personnel costs and costs of external services rendered less operating expenses other than provision for bad debts, write-downs of fixed and intangible assets, provision for risks, other provisions and operating charges and depreciation and amortization. Gross operating profit

was €11,044 million, €11,821 million, €12,226 million, €13,118 million, €12,217 million and €13,619 million in each of 1997, 1998, 1999, 2000 (historical), 2000 (pro forma) and 2001, respectively.

(11) Data include multiple lines for ISDN and exclude internal lines.

(12) Data exclude internal lines.

(13) Data refer to TACS and GSM services lines, including holders of Prepaid Cards.

(14) Ratio is based on employees of Telecom Italia only.

Dividends

Telecom Italia has normally paid annual cash dividends on its outstanding Shares and Savings Shares, although the determination of Telecom Italia's future dividend policy, and the amounts thereof, will depend upon a number of factors, including but not limited to the Company's earnings, financial condition and cash requirements, prospects and such other factors as may be deemed relevant at the time.

The dividends per share and per savings share declared by Telecom Italia with respect to each of the last five fiscal years and the aggregate dividend paid in such years are shown below. Actual dividends paid are rounded to the nearest whole cent.

	Dividends on Shares			Dividends on Savings Shares		
Year ended December 31,	**Euros per Share**	**U.S. dollars per Share(2)**	**(millions of euros)**	**Euros per share**	**U.S. dollars per share(2)**	**(millions of euros)**
1997(1)..	0.0981	0.11	515.67	0.1085	0.12	234.93
1998(1)..	0.1446	0.15	759.94	0.1549	0.17	335.61
1999(1)..	0.3099(3)	0.29	1,638.10	0.3218(3)	0.30	688.58
2000(1)..	0.3125	0.27	1,643.93	0.3238	0.28	664.84
2001	0.3125(4)	0.28	1,644.19	0.3237(4)	0.29	662.33

(1) Dividends for 1997, 1998, 1999 and 2000 were paid in lire. The lire amounts were translated into euros at the irrevocably fixed rate of exchange of Lit.1,936.27 = €1.

(2) Euro amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on the respective payment dates. See "—Rates of Exchange".

(3) The per share amount paid with respect to the fiscal year ended December 31, 1999 includes the distribution to all shareholders of the dividends payable on 26,046,820 Savings Shares held in treasury on the date the dividend was paid. A total of approximately €3.12 million was also distributed from the statutory reserve in order to round up such per share amounts.

(4) Approved at the Annual Meeting of Shareholders held on May 7, 2002. Pursuant to Borsa Italiana rules, dividends on the Shares and the Savings Shares are payable from the fourth business day after the third Friday of each month, and in any case, at least four business days after the Annual Meeting of Shareholders approving the dividends. Telecom Italia's dividend coupons for the year ended December 31, 2001 were clipped on May 20, 2002 and were payable from May 23, 2002. Dividends for the year ended December 31, 2001 were paid also utilizing reserves.

Payment of annual dividends is subject to approval by the holders of ordinary shares at the annual general shareholders' meeting, which must be convened within six months after the end of the financial year to which it relates. In addition, Article 21 of the Company's Bylaws gives the Board of Directors the power to approve the distribution of "interim dividends". Pursuant to Italian law, the distribution may be approved after the final approval of the preceding year's financial statements, and the interim dividends may not exceed the lower of (i) the difference between profits from the preceding fiscal year and amounts required to be attributed to legal and statutory reserves and (ii) available reserves. Once paid in compliance with applicable laws, shareholders cannot be required to repay interim dividends to the Company if the shareholders collected such dividends in good faith. Dividends are usually payable within 30 days of the general shareholders' meeting at which they are approved. Dividends not collected within five years from the date they become payable will be forfeited in favor of the Company.

According to the Italian Civil Code, before dividends may be paid with respect to any year, an amount equal to 5% of the net income of the Company for such year must be set aside to the legal reserve until the legal reserve, including amounts set aside during prior years, is at least equal to one-fifth of the par value of the Company's issued share capital. This legal reserve is not available for payment of dividends. Such restriction on the payment of dividends applies, on a non-consolidated basis, to each Italian subsidiary of the Group. The Company may also pay dividends out of available retained earnings from prior years.

Dividends in respect of Shares and Saving Shares held with Monte Titoli S.p.A ("Monte Titoli") are automatically credited to the accounts of the beneficial owners with the relevant participant of Monte Titoli, without the need for presentation by such beneficial owners of any documentation. See "Item 10. Additional Information—Description of Bylaws and Capital Stock".

Arrangements between Euroclear or Clearstream and Monte Titoli permit the shareholders to collect the dividends through Euroclear or Clearstream. Holders of American Depositary Receipts ("ADRs") will be entitled to receive payments in respect of dividends on the underlying Shares and Savings Shares, as the case may be, in accordance with the relevant Deposit Agreement. If profits are not fully distributed, additional reserves are created. The shareholders can adopt a resolution, at an extraordinary meeting, to convert such reserves into additional share capital. In such case, the shares resulting from the increase in share capital are allocated to the shareholders in proportion to their ownership before the increase without further contribution or payment from the shareholder.

Dividends payable on the Company's Shares and Savings Shares may be subject to deduction of Italian withholding tax. See "Item 10. Additional Information—Taxation". Italian regulations do not contain any specific restrictions on the payment of dividends to non-residents of Italy. See "Item 10. Additional Information—Exchange Controls and Other Limitations Affecting Security Holders".

Pursuant to Italian law, in connection with the payment of dividends, participants of Monte Titoli are required to supply to the Italian tax authorities certain information concerning the identity of non-resident shareholders holding Shares or Savings Shares and resident shareholders holding Shares or Saving Shares in registered form provided that such resident shareholders have not exercised the option to receive dividends with the deduction of the withholding tax and to subsequently include such dividends in the annual income statement. Shareholders are required to provide their Italian tax identification number, if any, or alternatively, in the case of legal entities, their name, country of establishment and address, or in the case of individuals, their name, address and place and date of birth, or in the case of partnerships, the information required for legal entities and the information required for individuals with respect to one of their representatives.

In the case of Ordinary Share ADSs and Savings Share ADSs owned by non-residents of Italy, Telecom Italia understands that the provision of information concerning the Depositary, in its capacity as holder of record of the Shares and Savings Shares, as the case may be, will satisfy these requirements. However, Telecom Italia will be required to provide information concerning non-resident beneficial owners of Ordinary Share ADSs and Savings Share ADSs, to the extent such owners wish to benefit from reduced withholding tax rates on dividends under an income tax convention, and claims for such benefits therefore must be accompanied by the required information. See "Item 10. Additional Information—Taxation".

Item 4. INFORMATION ON THE COMPANY

BUSINESS

A glossary of selected telecommunications terms used in the following description of Telecom Italia's business and elsewhere in this Annual Report is to be found at the end of Item 4 of this Annual Report.

The legal and commercial name of the Company is Telecom Italia S.p.A. The Company is incorporated as a joint stock company under the laws of Italy. The duration of the Company extends until December 31, 2050.

On July 18, 1997, Old Telecom Italia was merged with and into STET—Società Finanziaria Telefonica—per Azioni ("STET"), its parent holding company, with STET as the surviving corporation (the "Merger"). As of the effective date of the Merger, STET changed its name to Telecom Italia. In November 1997, the Ministry of the Treasury of the Republic of Italy (the "Treasury") completed the privatization of Telecom Italia selling substantially all of its stake in Telecom Italia through a global offering, and a private sale to a stable group of shareholders. On May 21, 1999 Olivetti S.p.A. ("Olivetti"), through a tender offer, obtained control of Telecom Italia when approximately 52.12% of Telecom Italia Shares were tendered to Olivetti. Through a series of transactions which started in July 2001, Olimpia acquired a 28.7% stake in Olivetti which resulted in the replacement of the then Board of Directors, including Roberto Colaninno, who led the takeover of Telecom Italia by Olivetti. Please see "—Significant Developments During 2001—The Pirelli-Olimpia Transaction".

On November 7, 2001, the extraordinary meeting of the shareholders of Telecom Italia amended article 2 of Telecom Italia's bylaws and moved the registered offices of Telecom Italia to Piazza degli Affari 2, 20123 Milan, Italy from Via Bertola 34, 10128, Turin, Italy; the corporate headquarters and the principal executive offices of Telecom Italia are located at Corso d'Italia 41, 00198 Rome, Italy, the telephone number is +39 06 3688-1.

Introduction

At the end of 2001, Telecom Italia was one of the world's largest fixed telecommunications operators, with approximately 27.4 million subscriber fixed-lines installed (including ISDN equivalent lines). Through its subsidiary TIM, Telecom Italia was also the largest mobile telecommunications operator in Italy and one of the largest in the world, with approximately 50.7 million mobile lines (which includes 31.9 million proportionate lines). Telecom Italia also had 5.3 million mobile lines (1.9 million proportionate lines) through companies indirectly owned through Stet International Netherlands N.V. ("SIN"), now Telecom Italia International N.V. ("Telecom Italia International"). In Italy TIM is the sole provider of analog mobile telecommunications services, one of four operators with the right to provide GSM digital mobile telecommunications services and, one of four operators with the right to provide DCS 1800 digital mobile telecommunications services. TIM is one of five entities which have acquired a UMTS license to provide third generation mobile services in Italy.

Telecom Italia also provides leased lines, data communications services and satellite telecommunications services. Through SEAT, Telecom Italia is a leading provider of Internet and directory publishing services. Other activities of Telecom Italia include the provision of IT software and services.

Telecom Italia's international portfolio of subsidiaries and investments includes fixed and mobile telecommunications companies which operate mainly in various countries in Europe and in Latin America.

Significant Developments during 2001

The Pirelli-Olimpia Transaction

The information contained herein on the Pirelli-Olimpia transaction has been taken from publicly available information filed by the parties involved therein with regulatory authorities. So far as Telecom Italia is aware, no facts have been omitted herein which would render the information misleading. No further or other responsibility in respect of such information is accepted by Telecom Italia.

On July 30, 2001, Pirelli S.p.A. (hereinafter "Pirelli") and Edizione Holding S.p.A. (hereinafter "Edizione") signed an agreement with Bell for the acquisition, through a company to be named, of Olivetti stock package owned by Bell, representing about 23.3 percent of Olivetti's share capital.

The agreement called for the acquisition of 1,552,662,120 ordinary shares and 68,409,125 warrants 2001-2002 on ordinary shares of Olivetti (hereinafter the "Olivetti Investment"), at a per unit price, respectively, equal to €4.175 and €1.0875, for a total price of €6,557 million, with a value date at August 31, 2001. The value date was to indicate that the price for the Olivetti Investment would be reduced if the payment was made before August 31, 2001 and increased if made after that date on the basis of the following formula: interest = total price x (1-month Euribor + 0.75%) x the number of days of early or delayed payment / 360.

The purchase transaction was subject to receipt of the necessary authorizations and in particular from the EU Commission. This authorization was received on September 20, 2001.

On August 3, 2001, Pirelli (80 percent) and Edizione Finance International S.p.A. (20 percent – a wholly-owned company of Edizione), set up Olimpia, the company designated for the acquisition of the aforementioned Olivetti Investment.

On August 9, 2001, Kallithea S.p.A. (a subsidiary of Pirelli S.p.A.) sold 147,337,880 Olivetti ordinary shares (equal to about 2.02% of Olivetti's share capital) to Olimpia for a price per share of €4.193, for a total of approximately €618 million. Pirelli Finance Luxembourg S.A. (a subsidiary of Pirelli S.p.A.) and Edizione sold a total of 265,302,250 Olivetti ordinary shares (equal to about 3.64% of Olivetti's share capital) to Olimpia at a total price of approximately €576 million.

On September 19, 2001, an agreement was signed among the majority shareholders of Bell, Pirelli, Edizione and Olimpia which called for a commitment by the majority shareholders of Bell to ensure that the latter, at the same time payment was made by Olimpia for the purchase of the Olivetti Investment, subscribed to bonds issued by Olimpia itself, with the following features: 6-year bonds for an amount of approximately €1,033 million, repayable at maturity, unless the bonds are redeemed in advance by the bondholder, convertible into 263,500,000 Olivetti shares in a ratio of one share for every bond with a face value of €3.92, bearing an annual fixed rate of interest of 1.5%, payable in cash at maturity or at the date of early redemption.

The agreement also called for the transfer of the Olivetti Investment in two tranches, the first for 552,000,000 Olivetti shares to be carried out on September 27, 2001 and the second for the remaining shares and warrants by October 12, 2001.

In execution of the above agreement, on September 27, 2001, 552,000,000 Olivetti shares were transferred from Bell to Olimpia (for an equivalent amount of €2,315 million), while on October 5, 2001, the remaining 1,000,662,120 Olivetti shares and 68,409,125 warrants were transferred from Bell to Olimpia (for an equivalent amount of €4,199 million and €74 million, respectively). On the same date, October 5, 2001, Bell subscribed to the Olimpia Bonds.

Under the agreements on July 30, 2001, Pirelli and Edizione agreed to purchase a further 54 million Olivetti shares, held originally by Banca di Roma, for a price of €225 million, corresponding to a price per share of €4.175. Based on these understandings, on October 31, 2001, with the value date and delivery of the stock on November 2, 2001, Olimpia purchased these shares. This resulted in a holding of approximately 27.7% of the share capital of Olivetti.

On November 20, 2001, in order to hedge the risk on the value of the Olivetti shares to be delivered to the holders of the Olimpia Bonds, Olimpia entered into a forward purchase agreement with UniCredit Banca Mobiliare S.p.A. and Caboto IntesaBci S.p.A. (ex-Caboto Holding Sim S.p.A.), for 263,500,000 Olivetti shares at a price equal to the average purchase price of approximately €1.37 per Olivetti share plus a premium equal to approximately 32% of the average purchase price. Settlement can be made through the physical delivery of the shares against payment of the agreed price or payment of the differentials compared to the market price.

On November 23, 2001, after the capital increase voted by the Board of Directors of Olivetti on October 13, 2001, Olimpia, by exercising its option rights subscribed to 504,825,563 Olivetti shares (for a price of approximately €505 million) and 504,825,562 Olivetti 1.5% 2001-2010 convertible bonds with a premium at redemption (for a price of approximately €505 million).

As of today, after these transactions, Olimpia holds 2,524,127,813 Olivetti shares (equal to approximately 28.7% of the share capital of Olivetti), 504,825,562 Olivetti 1.5% 2001-2010 convertible bonds with a premium at redemption and 68,409,125 Olivetti 2001-2002 warrants on ordinary shares .

At December 31, 2001, the average book value per Olivetti share, recorded by Olimpia as financial assets, is equal to €3.14. By taking into account the convertible bonds, the book value of the Olivetti shares would fall to €2.78 per Olivetti share.

As of today, the share capital of Olimpia is fully paid and is equal to €1,562,596,150, consisting of 1,562,596,150 shares of par value €1 each.

This share capital is held by Pirelli (60%), Edizione Finance International S.A. (20%), IntesaBci S.p.A. (10% - hereinafter "IntesaBci") and UniCredito Italiano S.p.A. (10% - hereinafter "UniCredito").

There are shareholders' agreements among Olimpia's shareholders.

In particular, shareholders' agreements have been entered into between Pirelli and Edizione on August 7, 2001, as amended on September 14, 2001 and February 13, 2002 (hereinafter the "Agreements"). Shareholders agreements were entered into also between Pirelli, IntesaBci and UniCredito on September 14, 2001 - amended on September 26, 2001 and October 24, 2001 - (hereinafter "Agreements with the Banks").

The Agreements and the Agreements with the Banks cover a three-year period and can be renewed at each expiration date. The renewal period is three years for the Agreements and two years for the Agreements with the Banks.

The Agreements and the Agreements with the Banks deal with the nomination of the Board of Directors of Olimpia, Olivetti, Telecom Italia, TIM and SEAT. They identify the key issues on which the board resolutions of Olimpia, Olivetti, Telecom Italia, TIM and SEAT have to decide in accordance with the Agreements and the Agreements with the Banks. The Agreements and the Agreements with the Banks also discuss the rules for the composition and resolution of dissent among the contracting parties on key issues (the so-called deadlock situations). The Agreements and the Agreements with the Banks also govern the *inter partes* consequences of any change in the structure of control of Pirelli (Agreements with the Banks) and of Edizione or of Pirelli (Agreements); and attribute to contracting parties the right to purchase or sell (puts and calls) Olimpia shares in the event of withdrawal from the agreements themselves. See "Item 6.— Directors, Senior Management and Employees — Directors".

CONSOB in its resolution dated October 30, 2001, which dealt with the matter of the authorization for the publication of the Olivetti prospectus for the offer of options on Olivetti ordinary shares and Olivetti 2001-2010 bonds, asked that the above prospectus indicate, based on CONSOB's evaluation, that de facto control of Olivetti is held by Olimpia and Olimpia is subject to the sole control of Pirelli. CONSOB explained the reasons why this supplementary information was requested in the communication published in the *CONSOB Informa* Newsletter dated November 5, 2001.

Pirelli did not agree with the reasons expressed by CONSOB and on December 6, 2001 filed a request to review the matter so that the questions surrounding the issue could be reexamined and the comments expressed about Olimpia's control over Olivetti could be revised. On January 8, 2002, under ruling No. RM/2001124, CONSOB gave its decision not agreeing with the request to review the matter of qualifying the holdings between Pirelli and Olimpia and between Olimpia and Olivetti.

Since the rulings were adverse, Olivetti, Pirelli and Olimpia filed an appeal with the TAR of Lazio to obtain their cancellation. The TAR of Lazio, in a ruling released on February 25, 2002, ruled favorably on the appeal, canceling the contested CONSOB rulings.

New Strategy and Business Plan

On February 14, 2002, Telecom Italia announced its 2002-2004 Plan, which includes the disposal of certain group assets. The 2002-2004 Plan is intended to rationalize the Group's structure and portfolio with the intention of divesting non-strategic holdings of Telecom Italia valued at approximately €5 billion.

The 2002-2004 Plan provides that Telecom Italia's activities will be highly focused on its core businesses, with the objective of further enhancing its strong market position in Europe. Italian domestic fixed and mobile telecommunications will be further strengthened, as well as international mobile telecommunications; no further acquisitions are planned in the area of international fixed telecommunications. The SEAT directories and Internet activities associated with fixed and mobile telecommunications are included among Telecom Italia's core businesses. Telecom Italia will increasingly operate as a supplier of integrated services, particularly as regards core business activities:

- in fixed telecommunications, the objective will be to offer business customers a broader span of services, via optical fiber-based broad band access; with mass market customers, the emphasis will be on DSL technology, using the existing telephone links;
- in mobile telecommunications, the aims are to increase revenues per customer through the provision of value added services, to bolster its leadership position in Latin America through the provision of pan-Latin American GSM services, and to strengthen European infrastructures and activities; and
- in directories and Internet, the aims are to increase market share and traffic in the access market, and to develop synergies with fixed and mobile telecommunications.

The Group will seek to meet its goals by:

- capitalizing on leadership in core businesses (wireline and wireless) in Italy; in particular, it will seek to (i) develop high potential segments, namely broadband access and services, data and Internet; and (ii) serve top business customers with a commercially integrated approach;
- portfolio restructuring - it will seek to divest non-strategic investments in Europe;
- rationalizing international operations- it will seek to prioritize its current wireless footprint and stabilize its wireline network by not making any new wireline acquisitions; and
- maintaining operational efficiency through capital expenditure and cost control.

Reorganization

In 2001 the corporate structure of the Group was reorganized.

The reorganization entailed the introduction of new top-management, the introduction of top management committees and institutionalized meetings (Business Management Meetings, Investments Committee and International Steering Committee).

As part of the reorganization, the Domestic Wireline, Internet and Media, and Information Technology Business Units underwent significant changes. Please see below "—Overview of the Group's Major Business Areas" and "—Business Units". In early 2002 the Group further reorganized certain of its business units. See "—Overview of the Group's Major Business Areas".

In 2001 a process was begun to the streamline the corporate structure and to reduce the number of companies in the Group from over the 700 existing at the end of 2001.

Sale of Stake in Satellite Consortia

In accordance with the 2002-2004 Plan, on December 19, 2001, Telecom Italia sold its interests in former satellite consortia converted into joint-stock companies Eutelsat, Intelsat, Inmarsat and New Skies Satellite, corresponding to 20.5%, 2.8%, 2.1% and 3.9%, respectively, of the share capital of those companies, to the Lehman Brothers Merchant Banking Partners II L.P. fund ("LBMBPII") and other investors including BCI and Interbanca.

According to the terms of the agreement, the transaction was effected through the establishment of a new company, Mirror International GmbH ("Mirror"), to which Telecom Italia transferred its entire minority holdings in Intelsat, Inmarsat and New Skies Satellite. Telecom Italia subsequently sold its stake in Eutelsat and transferred 100% of MI to a second newly established company, Mirror International Holding S.a.r.l. ("MIH"). The last step of the transaction was the sale of 70% of MIH to LBMBPII.

The portfolio Telecom Italia transferred to MIH was valued for the purposes of this transaction at approximately €550 million. Telecom Italia received €450 million in cash andrecorded a capital gain, after tax, exceeding €100 million. Telecom Italia retains a 30% stake in MIH and has the right to appoint a member of the board in Eutelsat and in MIH.

Under U.S. GAAP, MIH was deemed to be a non-qualifying special purpose entity, therefore requiring the accounts of Mirror to be consolidated with the Group. Under U.S. GAAP, the gain was reversed, the cash received from the debt financing is reflected in consolidated Group debt and the partial sale of the investment is reflected as a minority interest.

Real Estate Assets

An important element of Telecom Italia's restructuring plan is to realize the value of its extensive real estate portfolio. The 2002-2004 Plan implements the rationalization of the real estate assets portfolio.

In May 2001, IM.SER (60% owned by Beni Stabili and 40% by Telecom Italia) contributed its real estate trading portfolio to Telemaco Immobiliare S.p.A. ("Telemaco Immobiliare"), a newly formed company. Following such contribution, IM.SER sold the shares of Telemaco Immobiliare to its shareholders. The shareholders of Telemaco Immobiliare are Beni Stabili with a 60% stake and Telecom Italia with a 40% stake.

In connection with further initiatives to realize value from real estate transactions, the Group expects to conclude the sale of its 40% interest in Telemaco Immobiliare for an estimated gross proceeds of approximately €200 million. For purposes of U.S. GAAP, Telecom Italia's continuingownership interest in IM.SER requires that the assets transferred continue to be accounted for at historical cost. Additionally, the gain recognized under Italian GAAP was reversed and the receipt of cash from the partial sale and special dividend paid by IM.SER are considered secured borrowings, with the debt reflected in the U.S. GAAP balance sheet.

The €1.5 Billion Share Buy-Back Program

On November 7, 2001, the ordinary shareholders' meeting of Telecom Italia granted Telecom Italia's Board of Directors authorization for the buyback of Shares or Savings Shares, or both, up to a maximum amount of €1.5 billion, provided however that the total number of shares acquired shall not exceed 10% of registered capital.

The share buyback may be undertaken on one or more occasions within a period of 18 months, starting from the November 7 shareholders' meeting, and will be undertaken in accordance with conditions agreed with the Italian Stock Exchange in order to guarantee equal shareholders' treatment, pursuant to article 132 of the Draghi Law. The purchase price of each share must be neither 15% higher nor 15% lower than the average of the reference prices recorded by the Italian Stock Exchange in the three trading days preceding each individual transaction. The disposal of shares purchased pursuant to the share buy-back program is not subject to any time limit. Disposal of the shares may take place in one or more transactions and the shares may be disposed of by sale or exchange, including public offers and offers to shareholders, employees, directors and certain agents of Telecom Italia. The shares purchased pursuant to the share buy-back may also be disposed of within the framework of any stock option or share incentive plans. In the case of a sale, the sale price may not be less than the lowest purchase price; the shares may also be disposed of by coupling them with bonds or warrants. The sale price limit will not be applicable to disposal of shares in respect of employees, directors or certain agents of Telecom Italia, within the framework of any share incentive plans or stock option plans.

As of June 15, 2002 2,981,200 Shares and 10,350,000 Savings Shares were purchased.

Recent Developments

Acquisition of Webegg

On June 27, 2002 the Board of Directors of Telecom Italia and Olivetti approved the acquisition by IT Telecom S.p.A. (100% owned by Telecom Italia) of Olivetti's 50% stake in Webegg S.p.A ("**Webegg**"). The price to be paid by Telecom Italia is €57.5 million and was agreed on the basis of independent evaluations carried out by KPMG Corporate Finance for Telecom Italia and by UBM for Olivetti.

This transaction will permit the integration of Webegg's specific strategic expertise with current Telecom Italia Group Information Technology unit resources, and will enable the setup of skills centres able to offer services to the Telecom Italia Group and to the marketplace.

Following this operation, Webegg will be owned by IT Telecom (69.8%) and Finsiel (30.2%).

Sale of 9Telecom

On June 21, 2002 the Telecom Italia Group and the Louis Dreyfus Communication Networks Group ("LDCOM"), reached an agreement pursuant to which Telecom Italia will dispose of its interest in the 9Telecom Group to LDCOM and, at the same time, acquire a 7% stake in LDCOM. This disposal reflects the objectives of the 2002-2004 Plan by focusing Group resources on high value creation businesses offering attractive prospects for growth.

Under the terms of the agreement, Telecom Italia is to pull out of 9Telecom operations. Over the last three years Telecom Italia's stake in thecompany has generated net losses of €1,182 million. The deal enables the Telecom Italia Group to end the structural losses of its French subsidiary, and will allow 9Telecom to grow as part of a consolidated French market conglomerate. The deal will result in a net charge on the Telecom Italia 2002 financial statements equal to €282 million, roughly corresponding to 9Telecom's forecast losses for the current year.

The effectiveness of the agreement is subject to French regulatory authority approval.

Sale of Interest in Mobilkom and gradual disposal of interest in Telekom Austria

At the beginning of June 2002, the Group reached an agreement with Telekom Austria for the sale of TIM's 25% stake in Mobilkom, through the acquisition by Telekom Austria from TIM International N.V. ("TIM International") of 100% of Autel Beiteiligungs GmbH, which owns the participation in Mobilkom. In the same period, the Group also reached an agreement with Telekom Austria's main shareholder Österreichische Industrieholding AG ("ÖIAG"), for a gradual and coordinated disposal of Telecom Italia's interest in Telekom Austria starting from the second half of 2002.

TIM International's disposal of its stake in Mobilkom is expected to generate proceeds of approximately €716 million out of which €690 million represents the price of the stake and €26 million represents the dividend for the 2001 financial year. The capital gain for TIM, on a consolidated basis, will correspond to approximately €163 million.

The disposal does not require clearance by the relevant antitrust authorities and is expected to close by the end of June 2002. As a consequence of such disposal, the Mobilkom shareholders' agreement will be terminated.

In conjunction with the Mobilkom transaction, the Group has also reached an agreement with ÖIAG regarding, among others, an amendment to the shareholders' agreement relating to Telekom Austria, in which the Group, through Telecom Italia, has approximately a 29.8% stake.

The agreement will permit Telecom Italia International to undertake a gradual, coordinated disposal of its interest in Telekom Austria, and allow ÖIAG to take further steps in its privatization of the Austrian telephone company. Although Telecom Italia and ÖIAG will continue to review strategic alternatives for the sale of their stakes in Telekom Austria, the amended agreement will give them the right to dispose of shares in the public market in the following way:

- in the second half of 2002 Telecom Italia International will have the right to dispose of up to 75 million shares (approximately half of Telecom Italia International's holding in Telekom Austria) in a public market transaction;
- in 2003 ÖIAG will have the right to place 25 million Telekom Austria shares in either public market or private transactions. Telecom Italia International will then, together with ÖIAG, have the right to sell any of the unsold shares of the 75 million shares previously authorized; and
- for any shares sold thereafter in a public market transaction, Telecom Italia and ÖIAG will have the right to sell an equal number of shares.

In order to amend the shareholders' agreement, Telecom Italia will have to forfeit some of its special rights (granted at the time of the acquisition of its stake in Telekom Austria). Following the sale of the first 50 million shares, and in any event no later than April 30, 2003, the remaining special rights and the terms of the two representatives of Telecom Italia on the Supervisory Board will expire. The representatives will be replaced by two independent representatives of the shareholders.

SEAT Put Option

In connection with the merger of SEAT and Tin.it the Company agreed to grant Huit II a put option (the "SEAT Put Option") on 710,777,200 SEAT ordinary shares at a strike price of €4.20 per share. The SEAT Put Option permitted the option to be exercisable upon the recording, pursuant to Italian law, of the deed of merger of the SEAT Tin.it merger in the company register which occurred in November 2000.

Huit II transferred its rights under the SEAT Put Option and the ownership of the underlying SEAT shares to Chase Equity Limited ("CEL") a company of the J.P. Morgan Chase & Co. group.

On December 4, 2000 the Company and CEL renegotiated the SEAT Put Option by extending its duration until December 6, 2005 with the possibility of an early exercise in April and May of 2003, 2004 and 2005. The time extension made it possible for the Company to defer the financial impact of the SEAT Put Option.

At the same time, SIN (now Telecom Italia International) indirectly purchased from CEL, a call option (the "SEAT Call Option" and, together with the SEAT Put Option, the "Options") on 660,777,200 SEAT ordinary shares. The Options had the same strike price, duration and exercise dates. The total consideration paid by SIN for the SEAT Call Option was €747 million. The benefit of the SEAT Call Option was transferred from SIN to the Company through an option agreement.

On February 25, 2002, the Company and the J.P. Morgan Chase & Co. group renegotiated the Options. The strike price of the option was reduced from €4.20 to €3.40 per share. In consideration for the reduced strike price, the Company agreed to pay the J.P. Morgan Chase & Co. group approximately €569 million on the original expiration date of the Options. The Company may elect to make the payment of such consideration earlier, in which case the consideration will be discounted to its present value as of the time of payment. As renegotiated, the SEAT Put Option is not exercisable before its expiration in December 2005; while the SEAT Call Option can be exercised starting from December 2004, for up to 355,000,000 Seat ordinary shares in predetermined installments.

Telecom Italia will record the SEAT shares to be purchased pursuant to the Options as a long-term investment.

The valuation of the futures purchase commitment of SEAT shares pursuant to the Options led to a provision, at the end of 2001, of approximately €569 million in the reserves for risks and charges (other reserves) to cover the estimated nonrecoverability of the original prices of the Option. This provision corresponds to the consideration payable for renegotiation of the strike price and for the J.P. Morgan Chase & Co. group to forego the right to exercise the Put Option prior to its maturity in 2005.

For purposes of U.S. GAAP, the put and call agreement is considered in substance to be the acquisition financing of a minority interest. All amounts due under the arrangement are considered the original purchase price and allocation. The obligation is considered to be long-term debt on the U.S. GAAP balance sheet. The recognition of this additional ownership interest also results in a proportionally lower amount of minority interest outstanding as the Italian GAAP financial statements consolidate a lower ownership percentage. The inclusion of the minority interest acquisition for purposes of U.S. GAAP resulted in additional goodwill.

Project Tiglio

On May 24, 2002 the Telecom Italia Group and the Olivetti Group reached an agreement with Pirelli & C. Real Estate S.p.A., Pirelli S.p.A., MSMC Italy Holding B.V. and Popoy Holding B.V. with regard to the so called "Tiglio Project", aimed at integrating real-estate assets and activities of the companies involved with real-estate services and consequently maximizing their value.

According to the terms of the agreement, the Telecom Italia Group will transfer property, land and staff in charge of real estate asset-management activities to two newly founded companies; at the moment it is expected that at a later date a closed-end real-estate fund will receive the above mentioned assets.

In particular, Telecom Italia Group's contribution will be approximately €1,350 million with gross capital gains of approximately €170 million and net cash proceeds at the end of the project of approximately €650 million to be received in several stages.

The implementation of the project is subject to obtaining the necessary financing and the transfer of 40% of IM.SER real-estate to the Telecom Italia Group, to be realized through a spin-off of the company.

Sale of Interest in Auna

On January 15, 2002, Telecom Italia, Endesa, Unión Fenosa and Banco Santander Central Hispano signed an agreement for the sale of Telecom Italia's interest in Auna Operadores de Telecomunicaciones, S.A. ("Auna") for a price of €2 billion in cash. The effectiveness of the agreement is subject to applicable regulatory approvals. The purchasers have granted Telecom Italia a right of first refusal for two years to acquire any shares currently held by the Telecom Italia group which the purchasers may seek to sell during this two-year period. The costs associated with the right of first refusal together with financial advisory fees and other expenses are approximately €150 million, which will result in net proceeds for the Telecom Italia group of approximately €1.85 billion. Furthermore, in connection with the foregoing Telecom Italia has obtained a pre-emptive right on Amena shares for the same period of time.

Auna is a holding company for various telecommunications and other related assets, including Retevision I, a fixed-line telecommunications operator and Retevision Movil, a mobile telecommunications operator.

Sale of Stake in Bouygues

In February, 2002, Telecom Italia reached an agreement with Bouygues S.A. to sell TIM International's stake (19.61%) in BDT, the company that controls 55% of the French mobile company Bouygues Télécom for a consideration of approximately €750 million. The transaction was completed on March 28, 2002 and TIM recorded a consolidated net capital gain of approximately €484 million; while the Group recorded a consolidated net capital gain of approximately €266 million.

Sale of Interest in Stream

In February 2002, Telecom Italia reached an agreement with News Corporation and Vivendi Universal/Canal+ for the sale of its 50% stake in Stream S.p.A., a multimedia services platform, for a total consideration of U.S.$42 million. The agreement, which is subject to regulatory approvals by Italian authorities, provides for the sale of Telecom Italia's 50% stake in Stream to News Corporation(which holds the remaining 50% of Stream) and the successive sale by News Corporation of 100% of Stream to the Vivendi Universal/Canal+. Telecom Italia has agreed to forfeit approximately U.S.$80 million of account receivables from Stream. The economic impact of the sale of Stream was already reflected in previously announced write-downs. The sale was expected to become effective on April 30, 2002 or at a later date if any of the conditions precedent for closing would not previously occur. Please see "—Business—Multimedia Services".

On May 13, 2002 the Competition Authority authorized the acquisition of Stream by Canal+/Telepiù, subject to certain conditions aimed at easing entry by new competitors in the pay-TV market, the development of alternative means of transmission, as well as guaranteeing the protection of consumers. On May 15, 2002 Vivendi Universal and Canal+ announced that, due to the conditions imposed by the Antitrust Authority, they would abandon their plan to acquire Stream.

On June 8, 2002 News Corporation announced the signing of an agreement with respect to the acquisition of Telepiù by a group of investors headed by News Corporation. This agreement is subject to a number of conditions, including the agreement of Telecom Italia. As of the date of this report the sale of Stream is in discussions.

Sale of Interest in Lottomatica

On January 18, 2002, Finsiel accepted the tender offer launched by Tyche S.p.A. (De Agostini Group) and tendered its 18.3% stake in the share capital of Lottomatica. The transfer took place on February 5, 2002 resulting in proceeds equal to €212 million.

Group Results for the First Quarter Ended March 31, 2002

For a discussion of first quarter results for 2002 see "Item 5. Operating and Financial Review and Prospects—Recent Developments – Group Results for the First Quarter Ended March 31, 2002 compared to March 31, 2001 (pro forma)".

Overview of the Group's Major Business Areas

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services. Outside Italy, the Group's telecommunications business is operated by its subsidiaries and affiliated companies, generally, in Europe and Latin America. Some of these companies are held directly by Telecom Italia while others are owned through the subsidiaries TMI-Tele Media International Italia, Telecom Italia International N.V. ("Telecom Italia International", formerly known as STET International Netherlands N.V.) and TIM International.

The Company owns 100% of Telecom Italia International, the primary vehicle through which the Group holds its international wireline investments and TIM owns 100% of TIM International, the primary vehicle for international wireless investments.

In 2001 Telecom Italia organized its businesses by business unit. These business units (the "Business Units") include:

Domestic Wireline. This Business Unit includes Telecom Italia Domestic Wireline services (TIDW) which relates to the Italian domestic fixed line voice and data businesses on the fixed network; it also includes national businesses, such as Atesia, related to call centers, telemarketing and market researches and international activities relating to developing networks such as the European, Mediterranean and Latin American fiber optic rings as well as TMI.

Mobile Services. This Business Unit includes national and international mobile telecommunications businesses which are managed by TIM. Previously TIM largely managed domestic mobile communications with international mobile communications included as part of "International Telecommunications Services". International mobile operations are now consolidated with, and managed by TIM, through TIM International.

Internet and Media. This Business Unit includes the SEAT Group which was consolidated with the Group in results of operations for the first time in 2001. SEAT manages the Group's internet and media business which arose from the merger of Tin.it and SEAT. This Business Unit includes a multimedia network, whose main business areas include advertising, publishing, information marketing, business information, call center services, the Internet and television.

International Operations. The International Operations Business Unit manages and develops international wireline businesses and certain integrated companies providing fixed and mobile telecommunication services. This Business Unit was reorganized in the first half of 2002.

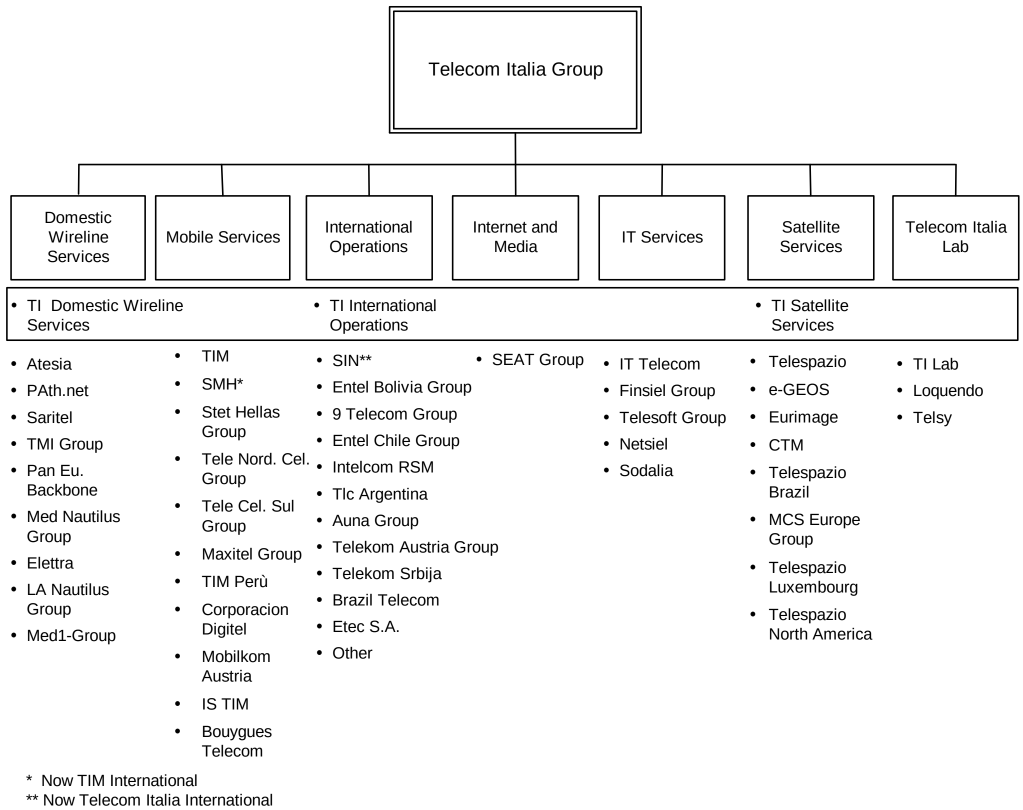
Information Technology. This Business Unit is responsible for the information technology activities of the Group and covers a broad range of information services. This Business Unit was split into two groups at the beginning of 2002:

- the Information Technology Group, which is now an operational activity. The businesses within this unit primarily provide IT services to other Business Units in the Group; and
- the Information Technology Market, which is a Business Unit – these companies (primarily the Finsiel Group) provide IT services to unrelated third parties, including banks, government agencies and other businesses.

Satellite Services. The Satellite Services Business Unit is responsible for developing satellite communication systems for voice and data transmission as well as for radio and television broadcasting and earth-observation.

TILAB. The TILAB Business Unit, combines the technological knowledge acquired by CSELT and the venture capital management experience of the Company. The TILAB Business Unit identifies and manages new initiatives, and creates business opportunities for companies of the Group as well as for the external market. TILAB is now part of the Information Technology Group Business Unit.

The following is a chart of Telecom Italia' s business unitsas of December 31, 2001:



In the first months of 2002 Telecom Italia reorganized its structure (the "2002 Reorganization"). Please see below "—The Organizational Structure".

The table below sets forth certain key data for each Business Unit:

		Domestic Wireline	Mobile Services	Internet and Media	International Operations	IT Services	Satellite Services	TILAB	Sub-total	Other activities and eliminations	Consolidated total
		(millions of Euro, except number of employees)									
Operating revenues	2001	17,291	10,250	1,957	1,879	2,033	648	134	34,192	(3,374)	30,818
	2000 (pro forma) (1)	17,514	9,418	263	505	2,138	340	123	30,301	(3,132)	27,169
	2000	17,514	9,418	263	2,292	2,138	340	123	32,088	(3,177)	28,911
	1999	18,449	8,651	228	394	2,240	316	119	30,397	(3,293)	27,104
Gross operating profit	2001	7,788	4,760	444	347	332	159	(14)	13,816	(197)	13,619
	2000 (pro forma) (1)	7,421	4,447	(35)	(3)	329	50	(9)	12,200	17	12,217
	2000	7,421	4,447	(35)	898	329	50	(9)	13,101	17	13,118
	1999	7,918	3,887	(31)	(9)	352	46	(25)	12,138	88	12,226
Operating income............	2001	4,379	3,136	31	(268)	162	60	(34)	7,466	(792)	6,674
	2000 (pro forma) (1)	3,915	2,988	(73)	(134)	134	(52)	(34)	6,744	(303)	6,441
	2000	3,915	2,988	(73)	230	134	(52)	(34)	7,108	(303)	6,805
	1999	4,045	2,708	(65)	(122)	120	(11)	(47)	6,628	(195)	6,433
Capital expenditures (2)...	2001	2,835	3,182	378	1,290	130	29	22	7,866	298	8,164
	2000 (pro forma) (1)	2,746	5,105	34	984	126	31	33	9,059	7,425	16,484
	2000	2,746	5,105	34	1,508	126	31	33	9,583	7,425	17,008
	1999	2,846	1,835	20	125	158	35	19	5,038	416	5,454
Number of employees at year-end..........................	2001	58,406	16,721	9,264	7,307	11,288	1,196	1,422	105,604	4,352	109,956
	2000 (pro forma) (1)	62,782	15,257	7,515	2,572	12,005	1,206	1,287	102,624	4,547	107,171
	2000	62,782	15,257	7,515	10,070	12,005	1,206	1,287	110,122	4,547	114,669
	1999(3)	69,575	12,363	336	2,403	12,126	1,299	1,302	99,404	23,258	122,662

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(2) Include goodwill of €1,174 million in 2001, €9,109 million in 2000 (pro forma), and €567 million in 1999.

(3) As of December 31, 1999, Other activities and eliminations includes the employees of Sirti and Italtel groups totaling to 12,704 and 5,153, respectively.

The following table sets forth, for the periods indicated, certain selected statistical data for the Italian fixed-line, mobile and internet businesses.

	Year ended December 31,		
	1999	2000	2001
Subscription and Customers:			
Subscriber fixed-lines at period-end (thousands)(1)	26,502	27,153	27,353
Subscriber fixed-line growth(%)	2.0	2.5	0.7
Subscriber fixed-lines per full-time equivalent employee at period-end(2)	354	409	448
ISDN equivalent lines at period-end (thousands)(3)	3,049	4,584	5,403
TIM lines at period-end (thousands)	18,527	21,601	23,946
TIM lines growth per annum(%)	29.6	16.6	10.9
Average revenue per mobile line per month(€)(4)	34.9	30.5	29.1
Cellular penetration at period-end (TIM lines per 100 inhabitants)(%)	32.5	37.5	41.6
Cellular market penetration at period-end (lines for the entire market per 100 inhabitants)(%)	53.1	73.3	89.0
Traffic:			
Average minutes of use per fixed-line subscriber during period(5)	4,298	4,722	4,739
Of which:			
Local traffic during period (in average minutes)(6)	2,767	3,203	3,069
Long-distance traffic during period (domestic and international) (in average minutes)	1,531	1,519	1,670
Growth in international incoming andoutgoing traffic in minutes(%)(7)	9.8	5.4	12.1
Total mobile outgoing traffic per month (millions of minutes)	1,219	1,569	1,795
Internet and Media:			
Directories customers (thousands)	714	736	759
of which SEAT Pagine Gialle	621	647	670
of which Thomson (TDL Infomedia Ltd.)	93	89	89
Page Views Virgilio (millions)	505	2,218	3,945
Active Users (at year-end, thousands)	1,104	1,656	1,804

(1) Data include multiple lines for ISDN and exclude internal lines.

(2) Ratio is based on employees of Telecom Italia only.

(3) Data excludes internal lines.

(4) Including Prepaid Customers' revenues and excluding equipment sales, including non-TIM customer traffic.

(5) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks) and excludes traffic for special services.

(6) Not including district traffic and traffic for special services, including internet dial-up traffic.

(7) Data include retail from wireline and wholesale international traffic. The reduced growth between 1999 and 2000 is due to increased competition and the decrease of "international bouncing" by the Italian competitors of Telecom Italia. International bouncing takes place when a national call is diverted through a foreign operator and is therefore included in international traffic. Growth between 2000 and 2001 is mainly due to wholesale traffic (incoming and outgoing).

Strategy

General

The Group's strategy is focused on its core businesses and will continue to focus on:

- defining customer segments for each Business Unit;
- providing superior value by customizing services and offers tailored to the identified customer segments;

- matching its customer focus by providing services utilizing its core businesses efficiently to bundle services together (e.g., wireline providing access and SEAT providing content and services); and

- a business model which allows Telecom Italia to capture the most value in a competitive market place.

In addition the Group intends to continue to operate as a global player in wireline, wireless and Internet but with greater focus on areas where it generally controls operations. Telecom Italia's international focus will be on Latin America and Europe.

Wireline

The Group's wireline strategy will be driven by defense of market share of voice, traffic, data/internet growth and aggressive cost cutting. In particular, Telecom Italia intends to:

- exploit its leading position in providing network access to fixed-line subscribers by providing value-added propositions (such as flat pricing schemes, bundling of services and increases in bandwidth with the latter through "Alice", the brand of ADSL for the mass market using several formulas and competitive prices) and leverage opportunities to retain its client base by enhancing customer loyalty (through billing, CRM and customer contact). Special plans are also directed to win back former customers;

- exploit growth opportunities by developing innovative pricing schemes, integrated data/services offerings, offers targeted to content and service providers, and by pursuing opportunities in the wholesale market (increasing revenues through sales to alternative operators and ISPs);

- run efficient operations and continue its cost-cutting program (personnel, real estate, general and administrative); and

- maintain competitive services and focus investment on enhancing network evolution and innovation (optical transport, Voice Over/IP).

Wireless

The Group's strategy will be driven by client loyalty and innovative services offered and will focus on core aspects of domestic business and international expansion. In particular, TIM intends to:

- focus on the most profitable market segments, the quality of its services, the consolidation of its leading position with corporate clients and the stabilization of its churn rate as new competitors offer similar services;

- provide innovative services to develop voice and non-voice revenues;

- improve core business profitability through rationalization of costs and reallocation of resources; and

- maximize value creation from international activities, focusing on South America and the Mediterranean Basin.

Internet and Other Information Services

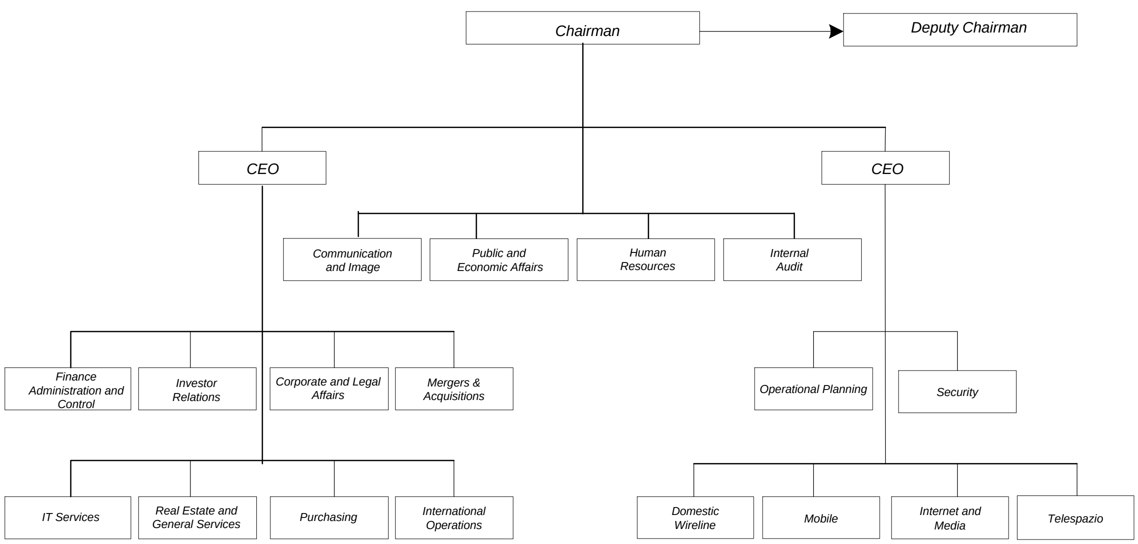
Telecom Italia intends to leverage its technological and market leadership to reach the largest possible audience and create a highly attractive, flexible and innovative service, to stay ahead of the competition.

In particular, Telecom Italia intends to:

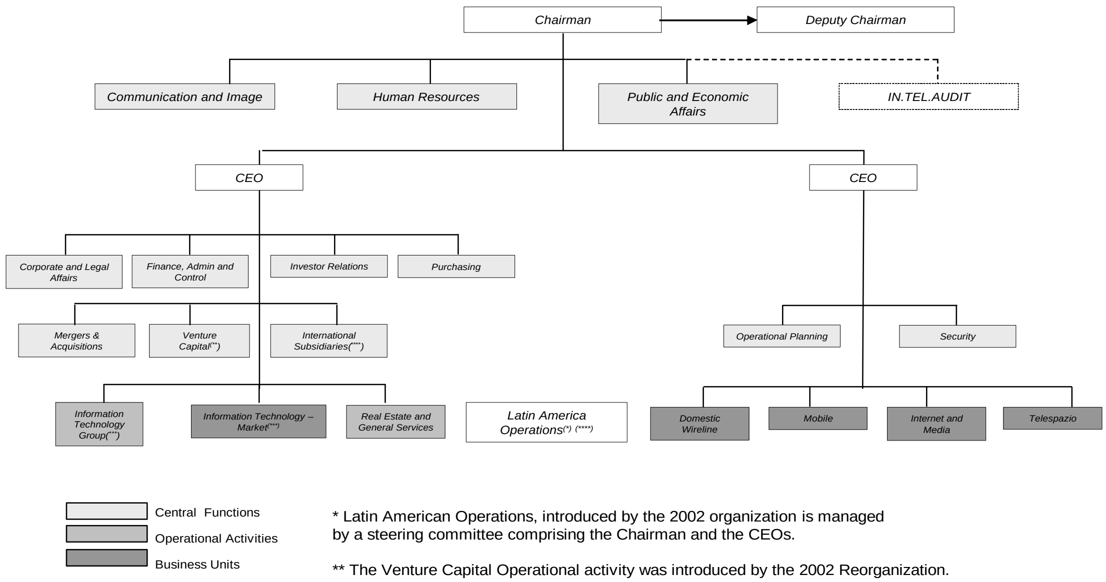
- leverage on Telecom Italia Group networks (e.g., fixed, mobile, satellite, narrowband, broadband);
- develop a multidevice portal accessible by In ternet, mobile devices and TV;
- maintain leadership on portal technological and service innovation;
- leverage on market leadership to attract partners/providers; and
- continue to expand internationally.

The Organizational Structure

The Group' s organizational structure was revised when new management was installed following the Olimpia transaction in September 2001 and was subsequently revised again during 2002. The following chart highlights the organizational structure of the Group at December 31, 2001.



The following diagram highlights the organizational structure of the Group as it was changed as part of the 2002 Reorganization. As of June 10, 2002, the new structure is the following:



* Latin American Operations, introduced by the 2002 organization is managed by a steering committee comprising the Chairman and the CEOs.

** The Venture Capital Operational activity was introduced by the 2002 Reorganization.

*** Prior to the 2002 Reorganization, the activities of the Information Technology Group Operational Activity and of the Information Technology – Market Business Unit were part of the Information Technology Business Unit.

**** Prior to the 2002 Reorganization, the activities of the international subsidiaries Business Unit and of the Latin American Operations were part of the International Operations Business Unit.

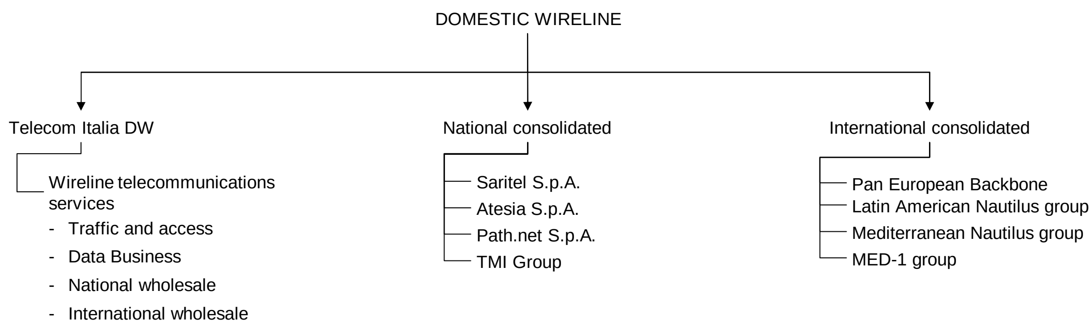
Telecom Italia's current structure is composed of:

- *Central Functions*, which are responsible for the Group's operations;
- *Operational Activities*, which are responsible for the synergies of Intra-Group activities and for the supply of common services;
- *Business Units*, which are responsible for the business development, managing the operations for the external markets; and
- *Latin America Operations*, which is responsible, within the Group's strategies and within the framework of the Business Units, for all of the Group's activities in Latin America.

Business Units

Domestic Wireline

The Domestic Wireline Business Unit accounted for gross operating revenues of €17,291 million in 2001, €17,514 million in 2000 and €18,449 million in 1999. At the end of 2001, Telecom Italia Domestic Wireline implemented a new organizational structure and became part of the Domestic Wireline Business Unit focused on customer segments. As of December 31, 2001 the structure was as follows:



Except for Saritel being moved to the Information Technology Group Business Unit, the structure of the Domestic Wireline Business Unit did not change significantly as a result of the 2002 Reorganization. Domestic Wireline operates on a national level as the consolidated market leader in wireline telephone and data service and call centers, for consumers and other operators. On an international level, Domestic Wireline develops fiber optic networks for wholesale customers, mainly in Europe and Latin America.

Subscribers. The table below sets forth, for the periods indicated, certain subscriber data of Domestic Wireline.

	As of December 31,				
	1997	**1998**	**1999**	**2000**	**2001**
Subscriber fixed-lines at period-end (thousands)(1)	25,698	25,986	26,502	27,153	27,353
Subscriber fixed-line growth (%)(2)	1.7	1.1	2.0	2.5	0.7
Subscriber fixed-lines per full-time equivalent employee at period-end(3)	317	332	354	409	448
ISDN equivalent lines at period-end (thousands)(4)	897	1,735	3,049	4,584	5,403

(1) Data include multiple lines for ISDN and exclude internal lines.

(2) For each of the years ended December 31, the percentage growth figure represents growth per annum over the prior year end.

(3) Ratios are based on employees of the Company.

(4) Excluding internal lines. Included also in subscriber fixed-lines.

At December 31, 2001, Domestic Wireline had approximately 27.4 million fixed subscriber lines, including approximately 21.7 million residential lines (including multiple lines for ISDN), approximately 5.4 million business lines (including multiple lines for ISDN), and approximately 300,000 public telephones lines (including ISDN equivalent lines). Italy has 47.9 subscriber lines per 100 inhabitants.

At December 31, 2001, Domestic Wireline had approximately 5.4 million ISDN equivalent lines with approximately 4.5 million equivalent basic rate ISDN lines and approximately 0.9 million equivalent primary rate ISDN lines. Telecom Italia introduced ISDN services commercially in 1994. Basic rate ISDN subscribers receive two telecommunications lines and primary rate ISDN subscribers receive up to 30 lines. The number of subscribers is expected to continue increasing as ISDN equipment and applications become less costly and more widely used and as a result of the recent adoption by many European countries, including Italy, of the Euro-ISDN standard.

At December 31, 2001, Domestic Wireline had contracts for approximately 390,000 broadband points of access (115,000 at the end of 2000) with approximately 143,000 wholesale points of access and 247,000 points of access for the retail market. ADSL wholesale points of access are marketed to operators providing internet access; offers are marketed to residential, small business and corporate customers.

At December 31, 2001, 80% (unchanged compared to 2000) of the public telephones in service were equipped with phone card readers. The density of public telephones in Italy is among the highest in the world, with one public telephone per square kilometer and approximately 5 public telephones for every 1000 inhabitants. During 2001, ISDN technology was introduced to more than 25% of public telephones in order to support the launch of innovative services (70,000 basic ISDN equivalent lines in public telephony architecture; unlike residential and business ISDN lines, each ISDN public telephone line is linked to only one phone).

Domestic Traffic

The table below sets forth, for the periods indicated, certain traffic data for Domestic Wireline.

	Year ended December 31,				
	1997	1998	1999	2000	2001
Average minutes of use per fixed-line subscriber during period(1)	4,270	4,259	4,298	4,722	4,739
of which:					
Local traffic during period (in average minutes)(2)	2,607	2,628	2,767	3,203	3,069
Long-distance traffic during period (domestic and international) (in average minutes)	1,663	1,631	1,531	1,519	1,670

(1) Data includes total fixed outgoing traffic; excludes traffic for special services.

(2) Data does not include district traffic and traffic for special services, including internet dial-up traffic.

Domestic Fees and Tariffs. Telecom Italia introduced per second billing on November 1, 1999, with an initial fixed charge (the "call setup"). The price per call set up is €0.0619 for local calls, €0.0787 for long-distance calls (fixed to mobile and fixed to fixed) and €0.3098 for international calls. The price per second varies according to the time of day and day of the week and, for long-distance calls only, the price also varies according to distance. Since December 1997, Telecom Italia has introduced several tariff packages for residential and business clients which provide for discounts on national and international traffic tariffs and additional rental charges.

Tariff packages offered during 2000 included targeted discount and customized programs for residential and business customers:

- The "160/89" program was launched setting a maximum and a minimum price per minute for long-distance calls in Region 3. See "—Regulation—Tariff and Pricing Policy—Tariff Rebalancing".

- "Teleconomy Voice" (introduced in June 2000), which consists of three flat-fee programs, "24" (all national calls to other fixed lines at €1.49 cent per minute plus a call set up and calls to customer's favorite ISP at €0.92 cent per minute plus a call set up), "24 Aziende" and "No Stop", in which either local and long-distance calls have a single price and which allows customers, for €55 per month, to make an unlimited number of national calls to other fixed lines. At year end 2001, approximately 4,080,000 residential and business customers had subscribed to Teleconomy Voice (of which 3,240,000 are residential, an increase of 97% compared to the end of 2000).

- "Teleconomy ADSL", is bundled with "Teleconomy", and provides high-speed Internet connection for a flat fee.

- Specific tariff packages targeted for business and top business customers (Business Voice, Business Call and Business Net tariff packages) include discounts on a wider range of telecommunications services such as: specific international area codes, specific international telephone numbers, on-net calls and Call Centers.

- "Neteconomy ADSL", designed for small and medium-sized companies, combining high-speed Internet connections for groups of LAN users, always-on connection and flat fees.

During 2001 numerous new commercial plans were offered for residential and business customers, including:

Residential telephone services

- BBB/Teleconomy ADSL – Broadband subscription bundled with the Teleconomy plan.

- Sirio 187 – First telephone in the world able to handle the Short Message Service ("SMS").

Business telephone services

- Teleconomy24 aziende – Subscription with approximately 840,000 customers at year-end.

- Teleconomy ADSL – Broadband subscription bundled with the Teleconomy offer.

- ADSL Smart – Broadband subscription for small and medium-size companies.

Further incentives are planned for families and, in particular, one hour of free local calls for every two-month period and free subscription to certain new services. In March 2002, Telecom Italia launched its new ADSL rate package. For the wholesale market, a package has been marketed with a capacity of up to 640 Kbit/s, directed at other operators and Internet Service Providers, or ISPs, with discounts of up to 45% on previous prices, improved quality and standardization of the levels of service, and reduction of the time taken to activate connections. For retail customers, in April 2002 Telecom Italia began marketing two different rate plans directed at families and small and medium-size companies. One plan is based on "consumption" and the other on a "flat" rate, the latter having unlimited access to Internet traffic.

Tariff Rebalancing

Telecom Italia commenced rebalancing its tariffs in 1991 and made various adjustments until 1997. Since December 1998, the National Regulatory Agency has been responsible for tariff regulation. On July 28, 1999, the National Regulatory Agency introduced a price cap mechanism designed to promote productivity and efficiency for the incumbent operator in markets with a low level of competition. The price cap applies until December 31, 2002 to a whole basket of public voice telephone services composed of activation fees, basic charges, long-distance and international tariffs.

The table below sets forth, for the periods indicated, initial connection fees, bimonthly subscription fees and the average cost of a three-minute local call and a three-minute peak rate call for the four different domestic long-distance regions (exclusive of value-added tax) and the percentage change since 1997.

	Year ended December 31,					Percentage change since
	1997(1)	1998(1)	1999(1)	2000(1)	2001	1997(2)
			(€)			(%)
Connection fee	103.29	103.29	103.29	103.29	103.29	0.0
Bimonthly subscription fee: (3)						
Residential subscribers	15.80	16.84	18.59	19.32	21.38	35.3
Business Subscribers	26.24	26.24	27.27	27.27	29.23	11.4
Basic ISDN connection fee	103.29	103.29	103.29	103.29	103.29	0.0
Basic ISDN bimonthly subscription fee:						
Residential subscribers	33.05	33.05	33.05	33.05	33.05	0.0
Business Subscribers	51.65	51.65	51.65	51.65	51.65	0.0
Three minute local call:						
Standard	0.0930	0.0930	0.0992	0.0992	0.0992	6.7
Higher(4)	0.0930	0.0930	0.0992	0.0992	0.0992	6.7
Three-minute call in the same District at higher rate(5)(6)			0.1312	0.1312	0.0992	
Three minute domestic long-distance call at higher rate(7):						
Region 1	0.2231	0.2231	0.2231	0.2231	0.2205	-1.2
Region 2	0.3610	0.3610	0.3610	0.3610	0.3522	-2.4
Region 3	0.5903	0.5903	0.4772	0.4065	0.3522	-40.3
Region 4(8)	0.5903	0.5903	0.4772	0.4065	0.3522	-40.3

(1) The fees and costs for 1997, 1998, 1999 and 2000 were in Lire. The lire amounts have been converted to euros at the irrevocably fixed exchange rate of Lit. 1,936.27 = €1.

(2) Data are not adjusted for inflation.

(3) In February 2001, the residential and business subscription fees increased to €20.45 and €27.89, respectively.

(4) In March 1997, the "higher" and "standard" rates were unified as standard. For the year 1999, the introduction of "per second billing" resulted in an increase in the cost of a three-minute call, while leaving unchanged the overall spending of the customers.

(5) Long-distance calls within the same area code. This tariff was introduced in November 1999.

(6) In February 2001, district rates for three-minute calls decreased by 24.4%.

(7) In February 2001, the week-end flat tariff (€0.1431 for three-minutes call) was introduced.

(8) As of December 1, 1997, Region 4 charge (applied to calls over 60 Km) was combined with the former Region 3 charge (applied to calls between 30 and 60 km), with the result that current Region 3 tariffs apply to all long-distance calls over 30 km.

International Traffic

The table below sets forth, for the periods indicated, information with respect to incoming and outgoing traffic, including direct dial and operator assisted calls and mobile traffic.

	Year ended December 31,				
	1997	1998	1999	2000	2001
Total outgoing traffic (millions of minutes)	2,209	2,339	2,390	2,706	3,015
Growth in outgoing traffic (%)(1)	8.93	5.89	2.18	13.2	11.4
Total incoming traffic (millions of minutes)	2,619	2,950	3,419	3,415	3,845
Growth in incoming traffic (%)(1)	11.49	12.64	15.90	-0.1	12.6

(1) For each of the years ended December 31, the percentage growth figures represent growth per annum over the prior year's end.

With respect to outgoing traffic, Telecom Italia's international traffic ranks seventh worldwide by number of minutes. Growth in the volume of international traffic from 1997 to 2001 has resulted mainly from macroeconomic factors such as growth in foreign demand and import/export activities, immigrants and new subscribers. The decline in gross operating revenues from 2000 to 2001 has resulted mainly from the impact of continuing tariff reductions and increasing competition. International traffic is most concentrated in communications with Germany, France, Switzerland, United Kingdom, United States and Spain, which together accounted for approximately 50% of total minutes of outgoing international traffic at the end of December 2001.

Regarding incoming traffic, the growth from 1998 to 1999 is mainly due to the increase of traffic directed to mobile networks (an increase of 115%) that is a result of increasing usage of mobile telephony in the European Union. The growth from 2000 to 2001 is mainly due to traffic from fixed and mobile competitors.

International Tariffs. International calls utilize the same per second billing as domestic calls, with the price per minute depending upon the country called. See "—Domestic Traffic—Domestic Fees and Tariffs".

The table below sets forth, for the periods indicated, the average cost of a three-minute international call at standard rates (exclusive of value-added tax) for selected countries for outgoing traffic and the percentage change since 1997.

	As of December 31,					Percentage change since
	1997(1)	**1998(1)**	**1999(1)(2)**	**2000**	**2001**	**1997(3)**
			(€)			**(%)**
Germany, France	1.43	1.43	1.03	0.88	0.88	-38.4%
United Kingdom	1.15	1.15	1.03	0.88	0.88	-23.8%
Spain	1.43	1.43	1.03	0.88	0.88	-38.4%
Russia	2.09	2.09	2.09	1.65	1.65	-20.8%
Canada and United States	1.42	1.42	1.03	0.88	0.88	-38.0%
Australia	3.29	3.29	2.64	2.43	2.43	-26.3%
Japan	3.29	3.29	2.64	2.43	2.43	-26.3%
Brazil	4.29	4.29	3.29	3.05	3.05	-28.9%
Chile	5.45	5.45	5.45	4.91	4.91	-10.0%

(1) All amounts for 1997, 1998 and 1999 were converted to euros at the fixed exchange rate of Lit. 1,936.27 = €1.

(2) Rates became effective on November 1, 1999.

(3) Data are not adjusted for inflation.

Tariff Rebalancing. As part of its overall tariff rebalancing process, Telecom Italia has gradually been reducing tariffs for international calls to reflect their underlying cost. Average tariffs for calls to countries in the EU have fallen approximately 38.0% in nominal terms and 66.0% in real terms during the period 1988 through 2001 and average tariffs for calls to other countries in the Organization for Economic Cooperation and Development ("OECD") fell approximately 50.0% in nominal terms and 76.0% in real terms during that period.

Since March 1996, Telecom Italia has also sought to reduce its international tariffs, in particular to North and South America, Japan and the United Kingdom, to align them more closely to those of other European operators and address competitive pressures. Further tariff adjustments were made in 1997, in August 1999 and in August 2000, Telecom Italia reduced the tariffs by 13%, unifying and reducing charges for all western European countries. Further prices policies were adopted in 2001 to compete with other operators reducing revenues despite volume growth.

Settlement Arrangements. Telecom Italia derives revenues from foreign telecommunications operators for incoming calls which use Telecom Italia's network. Telecom Italia has bilateral settlement arrangements with other international telecommunications operators under the general auspices of the ITU. Because incoming and outgoing international traffic are relatively equal, Telecom Italia's net payments on international accounting rates are negligible. This has the effect of limiting Telecom Italia's exposure to changes in currency exchange rates. The exposure to changes in currency exchange rates has also been reduced due to the adoption of the euro.

Leased Lines

In 2000 and 2001, gross operating revenues from leased lines remained unchanged amounting to approximately €1,500 million, per year. Leased line gross operating revenues also include revenues from the leasing of lines to business customers and other providers of telecommunication services in Italy.

The leased line service involves making a permanent connection for telecommunications services between two geographically separate points that can be used to handle high-volume voice, data or video transmissions, and is an alternative to the public switched telecommunications networks. Last year, Telecom Italia experienced growth in revenues from digital lines leased to other telecommunications operators and a decrease in revenue from leased lines to business customers due to the new offers in broadband access and tariff policy. As of December 31, 2001, there were approximately 342,400 (in points of entry of data network) lines leased to business customers (including direct leased lines for data and voice telephony). In 2001, there were approximately 152,500 digital leased lines. During the last year, new offers towards IP protocol and Xdsl technology have been pushing the leased lines market in two different directions: a decrease in demand for low speed lines (up to 64 kbit/s) offset by an increase of Broadband Accesses demand, and a growing demand for high speed lines. In addition, as of December 31, 2001, there were approximately 30,300 digital leased lines related to backbone networks and approximately 39,300 digital leased lines for interconnection between the Telecom Italia network and the other domestic telecommunications operators (approximately 28,000 connections from Other Local Operators' network to Telecom Italia's network and approximately 11,300 connections from Telecom Italia's network to Other Local Operators network "reverse").

Telecom Italia has been subject, since 1995, to competition from the resale of leased line capacity for data transmission, certain voice services (other than fixed public voice telephony services) and other value-added services. The provision of such services, including voice services to closed user groups, is subject to specific rules. Pursuant to the Telecommunications Regulations, the right to supply leased lines was liberalized effective October 7, 1997, although their use for the transmission of fixed public voice telephony services was liberalized only beginning January 1, 1998. See "—Regulation—The Telecommunications Regulations and Implementing Regulations".

Telecom Italia commenced rebalancing its domestic leased line tariffs in 1991. Since 1996, tariffs for domestic leased lines, both digital and analog, have been reduced by an average of 15%.

Interconnection with Other Operators

Under Italian telecommunications regulations, Telecom Italia is required to provide interconnection to its switched telephone network for calls to and from competing domestic operators at rates that must be approved by the National Regulatory Agency. See "—Regulation—The Telecommunications Regulations and Implementing Regulations—Special Status of Operators Having Significantl Market Power—EU Telecommunications Law—Interconnection—Local Loop unbundling". On March 4, 2002 the National Regulatory Agency approved, subject to certain technical and economical amendments, the interconnection rate for 2001 submitted by Telecom Italia in September 2001. Telecom Italia's catalogue, revised on April 3, 2002, quotes interconnection rates at a lower rate than the catalogue of November 2000 (in particular, a reduction of 7.6% for local service, and, of 17.4% for single transit in peak time and a reduction of 2.9% for local service and of 12.2% for single transit in off-peak time).

Telecom Italia offers a comprehensive range of network access services that give other telecommunications companies access to its fixed-telephony network, including:

- *Terminating services.* Incoming calls from other telecommunications operators' networks to Telecom Italia's fixed telephone network.

- *Originating services.* Through carrier pre-selection and carrier selected, operators have access to calls originating on Telecom Italia's network. Telecom Italia also offers callers on its network interconnection with toll-free numbers and pagers or virtual private networks. At the end of 2001, Telecom Italia started offering wholesale interconnection with Internet dial-up numbers.

- *Transit services*. Telecom Italia routes incoming and outgoing international calls between other telecommunications operators' networks, including calls between other Italian mobile telecommunications operators, through its network.

- *Main distribution frame access*. Competing telecommunications operators may request a connection through Telecom Italia's network to their customers. Telecom Italia has been offering this service since 1998.

Data Services

Data services consist primarily of data transmission and network services for business customers as well as on-line services for business and residential customers. Revenues from data services are included primarily in fixed subscription and connection fees.

Telecom Italia provides a broad range of data transmission services, integrating voice, data and video elements. These data services are based upon a wide spectrum of technological platforms ranging from traditional technologies, such as digital leased lines and the X.25 protocol technology (used in Business Packet services), to advanced transmission technologies based on SDH and xDSL.

The year 2001 was characterized by a strong increase in the broadband market. More than 390,000 broadband points of access have been sold to the retail and the wholesale market (115,000 at the end of 2000). The integration of business data services with Internet applications (Ring and Full Business Company offers), based upon the successful pay-per-use model, facilitated such increase in the broadband market. Broadband offerings have successfully penetrated the residential market through Teleconomy ADSL (140,000 accesses sold at the end of 2001), a service bundled with voice services, launched in November 2000. During the first quarter of 2002 Telecom Italia launched a new brand: "Alice", ADSL for mass market, available at competitive prices and with several formulas. Broadband penetration and web services are among the most important strategic goals for the 2002-2004 Plan.

In February 2001 the National Regulatory Authority introduced new rules for the offering of broadband services and fixed the wholesale tariffs to be applied to other operators. This enabled Telecom Italia to restart the commercial offering of its Ring and Full Business Company offers.

During 2001, the commercial range of data packages was expanded by products such as:

- Hyperway: a private national virtual network based on an IP protocol and a virtual LAN network for metropolitan areas, in which all services and applications are available (voice, data and video)

- NetVantage: E-business solutions distributed through Internet Data Centers ("IDC") to handle virtual communities' processes on-line

- Full Business Government: E-business solutions distributed through the IDC for the local public administration

- Full Business Banking: E-business solutions distributed through the IDC for the financial sector

- Web-Kit: E-business solutions distributed through the IDC for ADSL connectivity.

Fixed Network

Since 1988, Telecom Italia has installed high levels of fiberoptics, intelligent nodes, digital switching, satellite connections and high-speed data transmission technology. The technologically advanced nature of its fixed network permits Telecom Italia to offer a variety of advanced services such as toll-free numbers, call waiting and call forwarding, VPNs, premium charges and charge splitting.

Domestic Network

Fixed Network. Telecom Italia's domestic fixed network includes 66 transit switches and 628 main local switches. The long-distance fixed network includes 3.7 million circuits, while the distribution fixed network includes 104 million kilometers of pairs over copper cable.

In 2001, Telecom Italia set up interconnections with the networks of 12 additional operators, in addition to the 33 recorded in 2000. During the year, the following contracts were also signed or renewed:

- 12 new interconnection agreements (adding to the 65 interconnection agreements previously agreed, including agreements with IPSE 2000 and H3G the new mobile operators that won the auction for UMTS licenses; and

- 15 additional "reverse" agreements, teminating calls on the network of another operator, for a total of 60, since 1998.

In addition, Telecom Italia entered into the following additional agreements in 2001:

- 16 agreements to supply high-speed access services using ADSL technology;

- 18 carrier preselection contracts, 3 district carrier selection agreements, 13 number portability agreements and 19 housing framework agreements for interconnection and local loop unbundling; and

- 19 contracts for the local loop unbundling service on the local network.

Digitalization and ISDN. At December 31, 2001, approximately 20% of Telecom Italia's domestic telecommunications lines were connected to digital telecommunications exchanges. The digitalization of the long-distance fixed network was completed in 1994, and in most major cities, the level of digitalization of the local fixed network is close to 100%. Since the end of 1999, ISDN services have been accessible to substantially all of Italy. Telecom Italia has one of the largest ISDN networks in Europe. ISDN allows subscribers to use their existing access lines for a number of purposes, including high-speed data transmission, video-conferencing, high-speed fax and faster Internet access. Telecom Italia expects to continue to make investments in its fixed network to permit the expansion of ISDN and IN services.

SDH and ATM. Telecom Italia introduced SDH advanced transmission technology into operation in the long-distance fixed network in 1996 and introduced such technology into operation for its local fixed network during 1997. These transmission systems are operating on fiberoptics at 2.5 Gbit/s and 155 Mbit/s. Work on the development of the Arianna network which, by use of the latest generation of SDH technologies and the new optical DWDM technology (Dense Wavelength Division Multiplexing) constitutes the basis for a new transport network with a high transmission capacity capable of covering the entire Italian territory, continued during 2001. The network will be used to transport flows with a high requirement for quality and availability, both in terms of incremental requirements and migration away from the current transit network. Arianna is based on a structure with SDH rings; since 2000, in order to reduce the number of fibers, DWDM systems have been used to multiply by a factor of 12 the available optical fiber band and the current transmission capacity, thus increasing the transport capacity of the connections. The network will be operated by the same system that is currently used for regional networks. The DWDM systems provide the natural link between current transport networks and the future optical OTN networks (Optical Transport Networks), multiplexing and exchange entirely within the optical domain, without any need for optical-electric conversion.

The evolution of the transport network towards the optical network will make it possible to increase the operational capacity of all types of traffic, from phone calls to Internet traffic. The Pegaso Project will be replaced by "Ulisse" a new system for domestic wholesale services.

ATM switching technology, introduced in 1996, allows the transfer of information combining data, video and other services over public and private networks both domestically and internationally. Telecom Italia ATM (Atmosfera) and Frame Relay (Business frame) networks are overall networks that work together as a multiservice network, using SDH transmission systems as physical layer. The ATM network, currently based on 79 Point of Presence ("POP"), allows for the provision of ATM native services with access rates ranking from 2Mbit/s up to 155 Mbit/s. It also acts as a backbone for both the Frame Relay Access network, currently based on 140 POP and used to supply frame relay services (with access rates ranking from 64 kbit's upto 2 Mbit/s), and for the DSL network, currently based on more than 1,500 POP and used for the provisioning of ADSL and SDSL ATM and IP Services. The ATM/Frame Relay networks permits access to IP Customers with access rate ranking from 64 kbit/s to 155 Mbit/s.

Fiberoptic Cables. At December 31, 2001, Telecom Italia had installed approximately 3.2 million kilometers of optical fiber for access and transfers, of which approximately 0.96 million kilometers were installed on long-distance fixed-lines. Fiberoptic cables significantly increase the capacity of the network and permit Telecom Italia to provide new advanced services based on the simultaneous transmission of several kinds of signal, such as voice, data and video. To enable it to offer such services, Telecom Italia is planning to introduce fiberoptics in its local access network.

In 2001, a project, which started in the second half of 2000, consisting of the creation of an optic-fiber ring between Milan and Palermo (T-Bone), will involve the installation of more than 6,000 kilometers of cable with 96 optic fibers on two backbones and the laying of two submarine links under the Strait of Messina.

Flexible Data Network. Telecom Italia also operates a flexible network equipped with a centralized system that makes it possible to establish dedicated data links from a work station. At December 31, 2001, 660,000 "direct digital line" access points and 166,500 "direct analog line" access points had been installed.

Value Added Services

SARITEL is the Internet factory of the Group. SARITEL, 100% owned by Telecom Italia, develops internet products and provides Value Added Services "on-the-net", a strategic element of the integrated market offer of the Group. SARITEL is one of the leading national players in the outsourcing and management of Internet Operations and advanced voice services on fixed and mobile networks. SARITEL provides a wide range of products and services: Internet Hosting Services for security, performance and operative continuity in Internet and global outsourcing of systems and applications; Internet to companies relating to customer usage; Internet Managed Services for the management of portals and platforms dedicated to e-commerce, security systems, digital certificates, electronic signatures, packaging and the distribution of specialized contents and Interactive Voice Services - the development and management of voice systems on the Internet and on intelligent networks. In its state-of-the-art Internet Data Centers (in Pomezia and Milan) SARITEL hosts thousands of servers for Telecom Italia, TIM and Tin.it as well as for Internet outsourcing from un-affiliated third parties with a high level of security; in particular, SARITEL manages the range of the most important application services of Telecom Italia among which are Full Business Company and Full Business Management. SARITEL recorded operating revenues of €186 million in 2001.

International Network

Since the Telecom Merger, Telecom Italia has rationalized its international fixed network and enhanced international transmission capacity.

Telecom Italia owns capacity in a number of international cable links, and its international network includes fiberoptic cables to many countries. During 2001, major digital submarine links were installed in the Atlantic area. In order to satisfy the demand for new services (such as Internet and multimedia applications) as well as to serve the areas with the greatest strategic importance such as North and South America, the Trans Atlantic Backbone has been developed through the acquisition of high-capacity wavelengths on submarine systems. Other acquisitions have been made in order to increase capacity:

- in South America and North Atlantic, with the upgrades of the Atlantis 2 system and the Colombus III submarine systems; and
- in the West and South African regions, with the SAT 3/WASC submarine system.

Moreover, Telecom Italia has developed a new strategy and is building a number of proprietary networks in Europe, Latin America and in the Mediterranean area. These multiservice backbones are optical-fiber rings that use the DWDM (Dense Wavelength Division Multiplexing) technology for transmission, while, for access and delivery, the POPs (Point of Presence) use multiservice platforms (voice, data and IP). These platforms complete the switching functions for voice and routing for data with packet/cell switching IP/ATM technology.

The European fiberoptic network (Pan European Backbone) is laid in the main industrialized European countries: Italy, France, U.K., Holland, Belgium, Germany, Switzerland, Austria with a total length of 9,100 km. An extension of the Pan European Backbone to Madrid and Barcelona in Spain has been planned for year 2002.

The Mediterranean Nautilus (MN) owned by Mediterranean Nautilus Ltd., a company controlled by Telecom Italia, is building a new submarine optical ring with a total length of 7,000 km and will link the main markets of the Southern Mediterranean area: Italy, Greece, Turkey, Israel and Egypt. In 2001, the cities currently linked are Catania, Chania-Creta, Haifa and Tel Aviv.

In Latin America, Telecom Italia has launched the Latin American Nautilus. The Latin American Nautilus is a new high-capacity backbone in the region, integrated with the transatlantic and European networks. The backbone is an optical-fiber ring network both on earth and under sea, 30,000 km long including the Miami-NYC link. The ring, having optical automatic traffic protection and a bandwidth greater than 320 Gbits, will link the most important cities of South America to Central and North America. In 2001, the initial configuration of the ring was completed.

In 2001, Telecom Italia further rationalized its international fixed network and enhanced international transmission capacity. At December 31, 2001 there were nine exchanges utilized for voice services and 406,000 international circuit links, including about 3,000 via satellite and 403,000 via cable. The digitalization of the international network exceeded 98% in December 2001.

In the aggregate, Telecom Italia has access to more than 390,000 kilometers of submarine cable. At the same time, Telecom Italia operates a number of satellite earth stations to handle international traffic.

Network Quality and Productivity. Telecom Italia's investment in its domestic service network has enabled it to continue to reduce the average time required for the installation of new lines and to repair over 88% of faults on main lines by the second day after the claim. The effectiveness rate of the local fixed network has steadily increased from 98.2% in 1993 to 99.7% in 2001. Similarly, the effectiveness rate of the long-distance fixed network increased from 95.4% in 1993 to 99.4% in 2001. The effectiveness rate of the fixed network is defined as the ratio of successful calls to the total number of call attempts, not including failures caused by the calling party's behavior, in a specified time period. A successful call is a call attempt to a valid number, properly dialled, where the called party's busy tone, ringing tone, or answer signal, is recognized on the access line of the calling user.

To reduce costs and improve efficiency, Telecom Italia undertook in 2001, an extensive program to reengineer its network operation and maintenance organization, which will permit the more effective use of human resources.

In 1999, 2000 and 2001, operating systems were, in turn, developed with the aim of ensuring the offering of new services, optimizing operational activities and pursuing objectives of total quality. Procedures were developed for systems dedicated to supervising traffic for verifying levels, the immediate management of measurements and constant monitoring of the quality of the service provided; in systems that operate the flexible network for data transmission, features were activated which reduce activation and connection time, permit the timely recognition of customers who have experienced malfunctions in services and augment the availability of the connections themselves; finally, operating systems have been equipped with new features for marketing new services.

Broadband Network/ADSL. Telecom Italia's broadband network, SOCRATE, is capable of supporting advanced telecommunications services and multimedia applications and, to this end, Telecom Italia has installed significant levels of fiber-optic cables in its fixed network. As of December 31, 2001, the broadband network program extended to 58 cities, passing approximately 525 households, and approximately 1.1 million had been equipped with the necessary transmission equipment and the wiring backbone to receive advanced telecommunications services, cable television broadcast services and multimedia. The HFC infrastructure is based on mature technology using the fiber and coaxial cable network and is able to broadcast to customers a large number of video channels, both analog and digital.

In1998, Telecom Italia began introducing ADSL systems over copper pairs to deliver interactive services (e.g., fast-Internet). ADSL allows Telecom Italia to fulfill, in the short-term, market driven needs to provide services like fast-Internet, multimedia, video conferencing and teleworking either for business or residential customers. Furthermore, ADSL together with the HFC infrastructure and the introduction of satellite services allows Telecom Italia to focus the commercialization of its broadband network on a market basis and to tailor investments to the growth of the market over the next few years.

Experiments are being performed with "in-house" cabling for apartments, which facilitates the supply of high-speed services by integrating existing telecommunications links (telephone and TV) and by also allowing the use of ISDN access and ADSL technology. In addition, the technical specifications of the "new network termination" have been established which, by replacing the three-hole socket, will also make it possible to exploit new telecommunications and multimedia services.

With reference to access services using ADSL technology, in 1999, the technical and commercial trials with fast Internet access for residential and SOHO (small office home office) customers, begun in Rome and Milan at the end of 1998, were concluded. In 2001, commercial services with access to ADSL technology for business customers and Internet Service Providers were extended to 700 cities in addition to the 25 cities to which such services were extended in 2000. The commercial services for business customers include the use of ADSL technology in urban areas to supply access to IP and ATM services of Telecom Italia's data networks. The services for ISPs supply ATM access based on ADSL technology to the public, leaving the commercial interface with the final customer to the Service Provider. At the end of 2001, the "local exchange areas" covered by ADSL technology numbered 1,372, covering 707 local areas; in 2002, 1,300 local areas and approximately 2,000 local exchange areas are expected to be served.

Mobile Services

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

As of December 31, 2001, the business unit was organized as follows:

* Starting from May, 2002 all Latin American subsidiaries of TIM International are coordinated by Latin American Operations. Please see "Item 4 - Description of the Company-Business-The Organizational Structure".

** In June 2002 the Group has agreed to sell its 25% stake in Mobilkom Austria. Please see "Item 4. Description of the Company-Business-Recent Developments".

*** On March 28, 2002 the Group sold its interest in Bouygues Decaux Telecom S.A., which controlled Bouygues Telecom S.A..

Other than the inclusion of the activities of Latin American companies in Latin America Operations, the Business Unit did not change in connection with the 2002 Reorganization.

Among the large mobile telecommunications operators in Europe at the end of 2001 TIM has the largest number of lines in its domestic market (source: *Mobile Communication* magazine) and has been the fastest growing area of the Group's business for the past several years. Line growth was 30% in 1999, 17% in 2000 and 11% in 2001. Gross operating revenues from TIM totaled €7,450 million, €7,929 million and €8,357 million in 1999, 2000 and 2001, respectively.

Holdings of International Operations

As a result of a corporate reorganization completed at the end of 2000, TIM acquired 100% of STET Mobile Holding ("SMH"), the international holding company of the Group holding substantially all of the Group's wireless investments outside of Italy. On December 28, 2001, SMH merged with TIM International the holder of stakes in Digitel and IS TIM. TIM International is managed by TIM and the international results have been fully consolidated with TIM's results since January 1, 2001. In January 2001, TIM Brasil, a wholly owned subsidiary of TIM International, was incorporated in order to act as a sub holding company for TIM Celular Centro Sul, TIM Sao Paulo and TIM Rio Norte. In November 2001, TIM International's stake in Bitel (the majority shareholder of Tele Nordeste Celular and Tele Celular Sul) was contributed to TIM Brasil. TIM Brasil currently owns 100% of Bitel's share capital. Corporacion Digitel and the Maxitel Group, whose controlling stake was acquired at the end of 2000 have been fully consolidated with Telecom Italia's results since January 1, 2001.

At December 31, 2001, the overall number of TIM lines calculated on a proportionate basis, in Italy and internationally was approximately 31.9 million. There are approximately an additional 1.9 million equity mobile lines calculated on a proportionate basis that are part of the Telecom Italia group.

The following tables list the countries in which TIM (through TIM International) currently has operations, the ownership interest in each operator and the number of lines for each operator. Beginning in May 2002 TIM International will remain the owner of the Latin America companies that will be coordinated by Latin America Operations. The mobile operations in Austria, France and Spain have been sold during the first half of 2002.

Controlled Operations

Country	Operator	Percentage interest of TIM International	Total Wireless lines per operator at December 31, 2001
			(millions)
Europe			
Greece	Stet Hellas	63.95(2)	2.1
Latin America(1)			
Brazil	Maxitel	96.67	1.2
	Tele Nordeste Celular	19.38	1.8
	Tele Celular Sul	19.37	1.6
Perú	TIM Perú	100.00(3)	0.2
Venezuela	Digitel	56.56	0.7

Affiliated Companies

Country	Operator	Percentage interest of TIM International	Total Wireless lines per operator at December 31, 2001
			(millions)
Europe			
Austria	Mobilkom Austria	25.00(4)	2.8
Czech Republic	Radiomobil	4.35	2.8
France	Bouygues Decaux Telecom	19.61(5)	6.4(6)
Spain	Auna/Amena	3.81(7)	5.2(8)
Turkey	IS TIM	49.00	0.5(9)

(1) Pursuant to the 2002 Reorganization the activities of the Latin American companies are now part of Latin America Operations.

(2) In July 2001, STET Hellas acquired a UMTS license for €145 million and a DCS 1800 license for €26 million. The acquisition of the licenses was partly financed by a share capital increase of €87 million. The capital increase, concluded in

October 2001, was entirely subscribed for. As a consequence of TIM's participation in the capital increase the stake owned by TIM International in STET Hellas increased from 59.29% to 63.95%.

(3) Operations started January 25, 2001.

(4) In 2002, the Group reached an agreement for the sale of its holding in Mobilkom Austria for €716 million.

(5) In 2002, the Group sold its stake in Bouygues Decaux Telecom for approximately €750 million.

(6) The amount refers to Bouygues Telecom lines (the wireless company of Bouygues Decaux Telecom).

(7) In 2002, the Group reached an agreement for the sale of its holding in Auna for €2 billion in cash. The agreement is subject to applicable regulatory and corporate approvals. Under the agreement, the purchasers have granted Telecom Italia a right of first refusal for two years to acquire any shares currently held by the Group which the purchasers may seek to sell during this two year period. The costs associated with the right of first refusal together with financial advisory fees and other expenses are approximately €150 million, which will result in net proceeds for the Telecom Italia group of approximately €1.85 billion.

(8) The amount refers to Retevision Movil (brand name Amena) lines (the wireless company of Auna).

(9) Operations started March 21, 2001.

Services—Italy. TIM offers both digital and analog mobile services. The GSM digital service, which commenced operations in April 1995, uses digital technology and is the standard throughout Europe. GSM generally provides higher quality transmission than analog service and may be used by customers to make and receive mobile calls throughout Europe and certain other countries. As of May 17, 2002, roaming agreements have been reached with 269 operators in 162 countries, allowing customers to make and receive calls abroad. See "—Tariffs" below. The analog service is based on the TACS 900 standard and began operation in 1990. See "—Cellular Network".

The table below sets forth, for the periods indicated, geographic and population coverage data for TIM's TACS and GSM services.

	Year ended December 31,			
	1998	1999	2000	2001
	(%)			
TIM Italian geographic coverage				
TACS	81	83	83	83
GSM	83	89	92	94
TIM Italian population coverage				
TACS	98	98	98	98
GSM	98	99	100	100

Customers and Lines. The penetration of mobile telecommunications service in Italy is above the Western European average at approximately 89 lines per 100 inhabitants and growth rates have been substantially higher than the European average. This compares to a penetration rate of 53 and 73 lines per 100 inhabitants at the end of 1999 and 2000, respectively. The increase is due to innovative services and an increase in customers with multiple lines and operators. TIM's customer base consists of TACS subscribers, customers holding TACS prepaid services, ("TACS Prepaid Customers"), GSM subscribers and customers holding GSM TIM Cards ("GSM Prepaid Customers", and together with TACS Prepaid Customers, "Prepaid Customers"). In 2001, TIM added 31.4% of the net additional GSM customers, with 3.1 million net additions compared to 2.5 million for Omnitel and the remaining 4.2 million attributable to the third and fourth operator. At December 31, 2001, the number of lines for TIM's TACS and GSM mobile service was approximately 23.9 million (of which 22.2 million were GSM lines, consisting of 2.5 million GSM subscribers and 19.7 million GSM Prepaid Customers). As of March 31, 2002, TIM's customer base had increased to 24.1 million lines.

The table below sets forth, for the periods indicated, selected customer data for TIM' s domestic business.

	Year ended December 31,				
	1997	1998	1999	2000	2001
	(number of customers in thousands)				
Lines at period end(1)	9,278	14,299	18,527	21,601	23,946
TACS subscribers	3,211	1,563	832	495	304
TACS prepaid lines	183	2,001	2,344	1,950	1,430
GSM subscribers(2)	2,056	2,453	2,442	2,485	2,538
GSM TIM Card	3,828	8,282	12,909	16,671	19,674
			(in %)		
Customer growth	62.8	54.1	29.6	16.6	10.9
Churn(3)	18.0	16.8	12.7	15.7	15.6
TIM penetration(4)	16.3	25.1	32.5	37.5	41.6
Cellular market penetration(5)	20.6	35.9	53.1	73.3	89.0
			(€)(6)		
Average revenue per line per month(7)	49.5	40.0	34.9	30.5	29.1

(1) Includes lines of TACS and GSM services, including Prepaid Customers.

(2) Commenced GSM services in April 1995.

(3) In 1997 and 1998 net of internal migration between TACS and GSM networks; since 1999 data refers to total lines. The churn rate for any given period represents the number of TIM customers whose service was discontinued during that period due to a payment default or who voluntarily gave up a mobile telephony service during that period, expressed as a percentage of the average number of customers during that period.

(4) TIM customers per 100 inhabitants.

(5) Customers per 100 inhabitants for the entire market.

(6) The data for the years ended December 31, 1997, 1998, 1999 and 2000 was in lire and was translated into euros at the irrevocably-fixed rate of exchange of Lit. 1,936.27 = €1.

(7) Including Prepaid Card revenues and excluding equipment sales and, since 1999, including non-TIM customers traffic revenues.

The significant growth in TIM' s mobile lines since October 1996, has resulted almost entirely from the marketing success of the GSM TIM Card, a prepaid card which permits the customer to make outgoing calls up to the limit on the card for the 12 months following issuance of the card or the last recharge of the card and receive an unlimited number of calls for the 13 months following issuance of the card or the last recharge of the card. If a GSM TIM Card is not recharged within this 12-month period, the customer will not be able to make outgoing calls but for one additional month such customer will be able to receive incoming calls. The GSM TIM Card can be recharged at any time to permit additional outgoing calls. The GSM TIM Card offers several advantages, including elimination of bad debt charges and lower administration costs, as no statements are sent to customers. The TACS prepaid service, which was introduced in December 1997, functions the same way as the GSM TIM Card and has successfully reduced the decline in usage of the TACS network. Approximately 88% of TIM' slines at December 31, 2001 are prepaid.

UMTS License. The Italian government awarded five UMTS licenses in Italy in November 2000. TIM, together with Omnitel S.p.A., WIND S.p.A., Andala S.p.A. and IPSE S.p.A., were awarded licenses to provide the third-generation mobile services. TIM has committed to pay €2,417 million for its license, with approximately €117 million and €2,066 million having been paid in November 2001 and December 2000, respectively. The remaining €234 million will be payable in 2002 and 2003. The licenses are valid for 15 years starting January 1, 2002. In 2001, TIM started an experimental UMTS service in its service centre in Padoa, and a gradual roll-out of the UMTS network has begun. Transition toward the third generation will be gradual. A massive launch of the service will be in 2004.

Traffic. The table below sets forth, for the periods indicated, selected traffic data for TIM' s business.

	Year ended December 31,				
	1997	1998	1999	2000	2001
	(millions of minutes)				
Total outgoing traffic per month	542.8	838.7	1,218.6	1,568.8	1,794.9
Total incoming and outgoing traffic per month	1,016.8(1)	1,472.6(2)	1,989.3(3)	2,479.1(4)	2,815.3(5)
	(% of total)				
Of which:					
TACS(6)	56.3	33.3	19.5	10.3	5.4
GSM(6)	43.7	66.7	80.5	89.7	94.6

(1) Includes domestic mobile incoming and outgoing domestic traffic (96.9% of total mobile traffic in 1997 compared to 97.3% in 1996), international traffic (2.1% in 1997 compared to 1.6% in 1996) and roaming traffic (1% in 1997 compared to 1.1% in 1996). These data include fixed outgoing traffic to the mobile network.

(2) Includes domestic mobile incoming and outgoing domestic traffic (96.2% of total mobile traffic in 1998 compared to 96.9% in 1997), international traffic (2.3% in 1998 compared to 2.1% in 1997) and roaming traffic (1.5% in 1998 compared to 1.0% in 1997). These data include fixed outgoing traffic to the mobile network.

(3) Includes domestic mobile incoming and outgoing domestic traffic (93.9% of total mobile traffic in 1999 compared to 96.2% in 1998), international traffic (3.2% in 1999 compared to 2.3% in 1998) and roaming traffic (2.9% in 1999 compared to 1.5% in 1998). These data include fixed outgoing traffic to the mobile network.

(4) Includes domestic mobile incoming and outgoing domestic traffic (90.4% of total mobile traffic in 2000 compared to 93.9% in 1999), international traffic (2.9% in 2000 compared to 3.2% in 1999) and roaming traffic (6.7% in 2000 compared to 2.9% in 1999). These data include fixed outgoing traffic to the mobile network.

(5) Includes domestic mobile incoming and outgoing domestic traffic (92.8% of total mobile traffic in 2001 compared to 90.4% in 2000), international traffic (2.7% in 2001 compared to 2.9% in 2000) and roaming traffic (4.5% in 2001 compared to 6.7% in 2000). These data include fixed outgoing traffic to the mobile network.

(6) Includes traffic from Prepaid Customers.

Tariffs. TIM' s mobile customers (other than Prepaid Customers) are charged a onetime connection fee, a monthly basic charge and traffic fees for calls, as well as a monthly government tax. Prepaid Customers are charged an initial connection fee of €26 for the GSM TIM Card and TACS prepaid service and are required to pay a fee ranging from €5 to €1 to the dealer for each recharge, according to the cost of each recharge. No other connection or subscription fees or taxes are payable by Prepaid Customers. Mobile customers (including Prepaid Customers) must purchase their own mobile telephone handsets. TIM does not subsidize the cost of mobile telephone handsets to its customers and does not intend to do so in the foreseeable future. In 2001, approximately 85.5% of revenues from TIM mobile services (net of access charge) were derived from traffic charges, 5.5% from sales and rental of equipment and 9.0% were miscellaneous revenues (subscription and connection fees).

TIM offers its customers a variety of different pricing packages which are tailored to address different usage patterns. Such packages include offerings to TIM' s GSM customers of "free minutes packages" which are available in various options. Since June 1, 1997, GSM customers are charged on the basis of a per-seconds-based billing system paying for the actual duration of the call plus a call setup charge of €0.1 (which is not charged when free minutes are being used). At the end of 1997 TIM also introduced local tariffs. Since July 1, 1998 TIM has also used a per-seconds-based billing system for its TACs customers. From time to time, TIM offers promotional packages intended to attract additional customers.

During 1998, TIM introduced various promotional packages offering GSM and TACS customers various incentives, including free connection as well as a certain number of months without subscription fees.

In May 1999, TIM introduced a new offer: TIM Menù, a dedicated TACS and GSM pre-paid card. The customer can choose a rate suited to his or her own needs, combining the various items on a menu. The objective is to simplify the service offer and at the same time make them more flexible. In July 1999, TIM extended TIM Menù to TACS and GSM subscribers (with two tracks, family and business). In November 1999, TIM continued to offer innovative services, with an offering called AutoRicarica. The AutoRicarica formula has proven to be particularly innovative for the market: according to this formula, TIM gives a bonus of €3.7 (VAT included) for each 100 minutes of calls received.

TIM also offers certain discount packages, which include TopTim, a discount plan for professionals that rewards both length of subscription and volume of traffic, and TimClub, a 15% discount on the three most frequently called wireless numbers (which is only available after the free bonus minutes have been used).

During 2001, in the consumer segment, TIM introduced a number of new packages including:

- **"LoSai di TIM"**, a free service which allows GSM customers to know who has called while the telephone was switched off or out of range;
- **FreeSMS Package**, an automatic charging mechanism based on the number of SMS sent; and
- **GPRS,** all TIM lines are equipped to handle General Packet Radio Service ("GPRS") traffic.

Value Added Services. TIM is building its brand as a platform for content providers by entering into partnerships and developing business synergies. TIM introduced WAP in May 2000 and entered into over 200 partnerships and commercial agreements with primary content and service providers, such as SEAT-Tin.it, Yahoo!Europe, Sonera Zed, Caltanet, Kataweb, Sit.com and Excite. TIM also entered into agreements with leading Italian banks and financial institutions for the development of on-line trading and mobile banking. In August 2000, TIM launched GPRS in the areas of Rome and Milan and GPRS national coverage was completed in December 2000. The GPRS service was offered to corporate customers in the first quarter of 2001 and was extended to consumer segments starting May 21, 2001. This offer represents the breakthrough in the evolution of second (GSM) to third (UMTS) generation mobiles.

The introduction of GPRS also paved the way for the launch of other initiatives. All the GSM lines are able to handle GPRS traffic, which is becoming a fundamental service for the professional market. TIM has been the first provider to market GPRS in Italy, consolidating its technological leadership in the domestic market.

TIM also introduced M-Services, which represents a combination of multimedia services on its GSM and GPRS networks. M-Services allows customers to use their mobile phones to send photographs and images accompanied by written or musical messages and to access a WAP page simply by pressing a button (*WAP Push*). TIM has been the first in Europe to introduce the PhotoMessage service, a major step towards multimedia message services. In June 2002 these services are available with the new MMS (Mobile Multimedia Services) and in the future with UMTS.

Billing. TIM's customers (other than Prepaid Customers) are billed in a staggered bimonthly billing cycle. TIM endeavors to minimize bad debts by implementing a credit check on each customer at the time of sign-up and by requiring certain customers to post a security deposit. In addition, if payment is not received, the customer is notified and his or her ability to place outgoing calls is interrupted. If no payment is received, all service is terminated.

Marketing and Distribution. TIM believes that its active marketing programs, extensive customer service and distribution network (primarily a nationwide network of independent dealers) and responsiveness to customer needs provide it with a significant competitive advantage. At December 31, 2001, there were 1,669 dealers, with 5,166 sales points (including 42 Telecom Italia outlets marketing TIM products and 24 shops directly owned by TIM), an increase of 329 over 2000. 5,797 TIM employees (about 60% of its total workforce) were involved in marketing and customer service activities at December 31, 2001.

TIM connects approximately 98.8% of its customers through its independent dealer network and approximately 1.2% through TIM shops and Telecom Italia outlets. TIM compensates independent dealers with sign-up commissions and air-time commissions, to maintain their loyalty and to reward them for producing high-volume subscribers and related traffic. In a further effort to promote dealer loyalty, TIM has offered a share purchase program to independent dealers.

Cellular Network. TIM's TACS network consists of 2,743 radio base stations and 69,211 radio channels TIM has reduced the level of investment in its TACS network as the number of TACS customers has decreased, TIM's GSM network consists of 10,572 radio base stations and 585,968 radio channels (an increase of 7.2% over 2000). Telecom Italia believes that as a result of TIM's enhancement of the GSM service and increased coverage, TIM's network is in line with the best European GSM networks. See "Item 5. Operating and Financial Review and Prospects—Liquidity and Capital Resources—Capital Expenditures".

Services—International. TIM is consolidating its role as a global player. TIM International's presence is concentrated in the Mediterranean Basin and in Latin America. In December 2001 TIM had 26.7 million lines attributable to customers abroad, corresponding to 7.9 million proportionate lines. 79.8% of TIM's international lines are European mobile lines while 20.2% are Latin American mobile lines. See "? Companies Controlled by TIM International". Included in the international figures are customers of the Austrian, French and Spanish affiliated companies which have been sold in 2002. See "— Holdings of International Operations — Affiliated Companies."

"In-Europe", TIM's pan-European tariff, was introduced in 2001. This offer combines the preferential roaming agreements among TIM, its foreign subsidiaries and other European partners, allowing TIM customers to roam in 30 countries using the same tariff. In 2001, as part of its international roaming service, TIM offered its customers the possibility of making calls from abroad with a simplified rate plan. New schedules have been offered allowing subscribers to use the same rates twenty-four hours a day and prepaid customers to charge the cost directly to their remaining credit rather than to a credit card. See "? Companies Controlled by TIM International".

TIM is focusing its efforts on becoming a technological and marketing partner for its affiliates. Examples of the synergies among TIM and affiliated companies are represented by the commercial launches of TIM Perú (Perú) and IS TIM (Turkey) both in 2001. TIM's strategy for international development focuses on consolidation in countries where new markets may develop rapidly and where there is greater growth potential. Targeted countries include Turkey, Perú and Venezuela where TIM's affiliates have been awarded licences and services have recently been started. These markets currently have low penetration rates and dense populations made up of young consumers who are more oriented toward value added services ("VAS"). See "? Companies Controlled by TIM International".

Companies Controlled by TIM International

Greece

The Group's first international investment in Western Europe was the establishment of STET Hellas. STET Hellas was awarded one of two GSM licenses granted in Greece, in the 900 Mhz frequency band, and commenced commercial services in June 1993.

In July 2001, the company was awarded a UMTS license at the price of €145 million and a DCS 1800 license for €26 million. The acquisition of the new licenses was partly financed by a capital increase of €87 million. This increase, which was completed in October 2001 was entirely subscribed to and led to an increase in TIM International's ownership from 59.29% to 63.95%. At December 2001, STET Hellas had approximately 2.1 million lines. In 2001, operating revenues were €523 million against €526 million in 2000, operating income was €89 million against €76 million in 2000 (an increase of 17.1% compared to 2000) and net income was €34 million against €27 million in 2000.

STET Hellas was listed on NASDAQ and on the Amsterdam Stock Exchange in June 1998 through an initial public offering of American Depositary Shares on NASDAQ and of Dutch Depositary Receipts on the Amsterdam Stock Exchange. After completion of the initial public offering, the Group's stake through TIM International was reduced from 74.8% to 58.1%. In February 2001, a stake of 1.14% was acquired by TIM International.

Brazil

On February 13, 2001 TIM's subsidiaries TIM Sao Paolo, TIM Celular Centro Sul and TIM Rio Norte acquired PCS licenses in Brazil, in the regions of São Paolo, in the southern states and on March 13, 2001 in the Rio de

Janeiro area. TIM has thus extended its cellular network to cover the entire country, becoming the first nationwide cellular operator in Brazil. See "International Telecommunications Services".

In 2001, TIM Brasil, a wholly owned subsidiary of TIM International, was incorporated in order to act as a sub holding company for TIM Celular Centro Sul, TIM Sao Paulo and TIM Rio Norte. TIM International's stake in Bitel (the majority shareholder of Tele Nordeste Celular and Tele Celular Sul) was contributed to TIM Brasil. The Maxitel Group results of operations, have been fully consolidated with Telecom Italia since January 1, 2001.

Maxitel. In November 2000, TIM, through Bitel Participacoes, acquired from UGB Participaçoes S.A. and Vicunha S.A., respectively, 19.43% and 18.53% of the ordinary and preferred shares of Maxitel, the Brazilian mobile telephony operator licensee in the states of Minas Gerais, Sergipe and Bahia in which it already held a 58.7% interest (43.15% of ordinary share capital). The transaction involved a total investment of approximately US$240 million.

In February 2002, TIM International, through its wholly owned subsidiary TIM Brasil S.A., acquired from the minority shareholders UGB Participacoes S.A. and Vicunha S.A. the remaining 10% of Maxitel ordinary shares for the equivalent of €27 million by exercising a call option.

Maxitel reported operating revenues of Brazilian reais 582 million (€ 277 million), an increase of 20.2% compared to 2000, as a result of an increase in traffic and sales of handsets. The operating result showed a loss of Brazilian reais 44 million (€21 million), primarily due to higher amortization and depreciation charges. The net result, which showed a loss of Brazilian reais 488 million (€232million) compared to a loss of Brazilian reais 641 million in 2000, was also affected by the charge to net income for accumulated deferred taxes recorded in prior years in receivables which are no longer recoverable on the basis of the new corporate business plan.

Tele Nordeste Celular Participacoes. A controlling interest in Tele Nordeste Celular, a supplier of mobile telephone services in the regions of Alagoas, Cearà, Paraiba, Pernambuco, Piaui and Rio Grande do Norte, was acquired in 1998. At the end of 2001, in a market characterized by a level of penetration of 10.3%, Tele Nordeste had more than 1.8 million lines (an increase of 16% compared to 2000), corresponding to a market share of approximately 65%.

In 2001, Tele Nordeste reported operating revenues of Brazilian reais 876 million (€416 million), a decrease of 1.6% compared to the end of 2000; operating income of Brazilian reais 215 million (€102 million), an increase of 8% compared to 2000; and consolidated net income of Brazilian reais 46 million (€22 million), an increase of 84% compared to 2000.

Tele Celular Sul Participacoes. A controlling interest in Tele Celular Sul Participacoes, a mobile telephone operator in the states of Paranà, Santa Caterina and in the city of Pelotas, was acquired in 1998. In 2001, Tele Celular Sul had 1.6 million lines (an increase of 13% compared to 2000) representing an overall market share of 65.4%. The prepaid service reached 62% of the customer base of 1.6 million of lines.

Tele Celular Sul reported operating revenues of Brazilian reais 889 million (€423 million), an increase of 18.5% compared to 2000; operating income of Brazilian reais 185 million (€88 million), an increase of 48% compared to 2000; and consolidated net income of Brazilian reais 50 million (€24 million), 257% higher than in 2000.

Perú

In March, 2000 TIM Perù was awarded the third mobile PCS license in the country at a cost of U.S.$180 million. The license has a duration of 20 years, is renewable, and provides for the supply of mobile telecommunications service on the 1900 MHZ frequency band. The license permits TIM Perú to request licenses for supplementary services, including basic and long-distance telephone services. The licences were obtained in March 2001 and October 2001. In 2001, TIM Perù had a loss of €82 million due to its start-up phase. TIM Perú commenced providing service in January 25, 2001.

In 2001, TIM Perú installed more than 330 radio stations, launched business packages with new rate plans and entered into 70 international roaming agreements.

The Group has elected to use GSM technology for its mobile services in Perú consistent with the development of a Latin American platform and GSM roaming worldwide.

In 2001, TIM Perú reported operating revenues of 105 million nuevo soles (€34 million) and an operating loss of 238 million nuevo soles (€76 million) against an operating loss of 62 million nuevo soles in 2000.

Venezuela

In December 2000 TIM acquired a 56.6% stake in Digitel S.A., a Venezuelan mobile operator. The amount paid for this acquisition was approximately US$363 million (of which approximately US$107 million was in the form of a capital increase and the balance was in the form of a share purchase). Digitel S.A. was awarded a 900 MHZ 20-year renewable GSM license in January 1998 and is operating in the Venezuelan Central Region, which, including Caracas and other major cities, is the most important economic region of Venezuela, with 60% of the national GDP.

In 2001, Digitel S.A. improved its distribution channels by converting its outlets into retail stores and by further developing its network with 429 radio stations in operation. Moreover, Digitel launched promotional packages for prepaid customers and promoted advertising campaigns for its proprietary brand names. Following advertising campaigns, Digitel' s market share increased by more than 10%.

In 2001, Digitel S.A. reported operating revenues of 173 billion bolivares (€255 million), an increase of 203.4% against operating revenues of 57 billion bolivares (€ 90 million) in 2000; and an operating loss of 21 billion bolivares (€32 million), a decrease of 47.5% against an operating loss of 40 billion bolivares in 2000.

Investments held by TIM International

Austria

TIM International holds a 25% (plus one share) stake in Mobilkom Austria through its wholly-owned Austrian subsidiary Autel GmbH; the remaining 75% is indirectly held by Telekom Austria. The Group has a 29.78% stake in Telekom Austria. See "—International Operations—Investments–Europe—Austria".

In 2002, the Group reached an agreement for the sale of its stake in Mobilkom Austria to Telekom Austria. TIM International' s disposal of its stake in Mobilkom is expected to generate proceeds of approximately €716 million out of which €690 represents the sale price of TIM International' s stake and €26 million represents the dividend for the 2001 financial year. The capital gain for TIM, on a consolidated basis, will correspond to approximately €163 million.

Furthermore, in 2002 Telecom Italia has also reached an agreement with ÖIAG, the main shareholder of Telekom Austria and of Mobilkom Austria, allowing Telecom Italia' s gradual divestiture of its 29.8% stake in Telekom Austria. See above "—Significant Developments during 2001."

TIM International' s interest in Mobilkom Austria was acquired in July 1997. TIM is providing Mobilkom Austria with senior management and support. In May 2000, partly as a result of the entry of the fourth operator, the penetration rate reached 74.5%, corresponding to more than 6 million lines, which high penetration slowed overall growth rates. In 2001, Mobilkom Austria retained its leadership position with 2.8 million lines (an increase of 1.6% compared to the end of 2000) and a market share of 43%.

In November 2000, Mobilkom Austria was awarded one of the six UMTS licenses auctioned by the Austrian government; the cost of the license was €172 million. During 2001, Mobilkom Austria reported operating revenues of €1,408 million; the operating result was €278 million; and net income was €299 million.

Czech Republic

The Group holds a 7.16% interest in a company which owns a 60.76% interest in Radiomobil, a mobile telecommunications operator, which in March 1996 won a GSM license in the Czech Republic. As of December 31, 2001, the penetration rate in the Czech Republic had reached 67% and Radiomobil had approximately 2.8 million customers. Radiomobil had operating revenues of €633 million and net income of €33 million in 2001. In March 2001, following TIM International' sdecision not to subscribe to a share capital increase in C-Mobil B.V. that had been finalized in order to exercise the option rights to subscribe to a reserved capital increase of Radiomobil S.A., the Group' s stake in GMobil was diluted from 12% to 7.16%.

France

In October 1996, the Group entered the French telecommunications market through an alliance with the Bouygues Group, which operates the DCS 1800 wireless telephone service, a paging network and private wireless telephone networks in France through Bouygues Telecom, the third mobile operator in France. In 2001 the company reported operating revenues of €2,681 million, an increase of 31.6% compared to 2000 on account of its increased penetration. This was accompanied by a reduction in industrial and commercial costs, with significant repercussions on the operating result, which showed an operating income of €53 million compared to an operating loss of €195 million in 2000.

In February, 2002, Telecom Italia reached an agreement with Bouygues S.A. to sell TIM International' s stake (19.61%) in BDT, the company that controls 55% of the French mobile company Bouygues Télécom for a consideration of approximately €750 million. The transaction was completed on March 28, 2002 and TIM registered a consolidated net capital gain of €484 million, while the Group registered a consolidated net capital gain of €266 million.

Turkey

In line with its expansion strategy in the Mediterranean Basin, in April 2000, the Group was awarded a mobile GSM 1800 license in Turkey. The GSM service was launched on March 21, 2001, through IS TIM and under the brand name Aria. At the end of 2001, there were over 540,000 clients.

The bid involved the issue of two new licenses to private operators through an auction, and the award of one license reserved for the fixed network operator. A special consortium was created to compete, 49% of which was owned by Telecom Italia and 51% by Is Bank (the leading private bank in Turkey) in compliance with the restrictions imposed by local laws about foreign investment.

The consortium was awarded the license at a price of U.S.$2,525 million; the second license was awarded to the fixed operator at the same time. The third license was not awarded because the bids were not raised.

In September 2000, the Telecom Italia Group and Is Bank, a leading Turkish financial institution, formed IS TIM, which launched its mobile telecommunications services in March 2001. According to the agreements with Is Bank, TIM will be responsible for the technical and commercial operation of IS TIM. In December, 2000, 49% of IS TIM was transferred to TIM International B.V. (now TIM International N.V.).

The Group believes there is high growth potential in the Turkish market, which, through 1999, had mobile phone penetration of only 11%, considerably lower than the European average (40%), and that of emerging countries (20%).

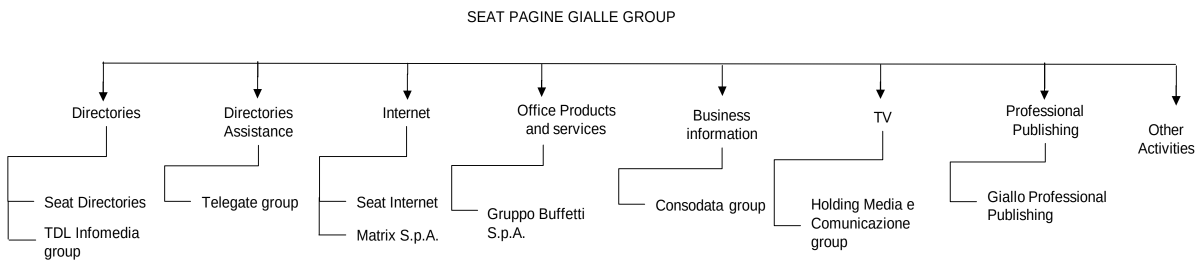
In 2001, IS TIM introduced a simple, innovative rate plan, extended its network penetration to cover important tourist resorts and developed nationwide points of sale. In 2001, IS TIM recorded operating revenues of 58,753 billions of Turkish lire (€46 million) and an operating loss of 484,897 billion of Turkish lire (€382 million) due to its start-up phase.

Ukraine

TIM International, through U-Mobile, held a 49% interest in Astelit, a Ukranian company, which won a DEC national license in the 1800 MHZ frequency band in June 1998. In 2000, due to the worsening of the economic and competitive conditions in Ukraine, TIM decided to divest its interest in Astelit. In November 2000, this interest was sold.

Internet and Media

The Internet and Media Business Unit consists of the SEAT group. As of December 31, 2001 the Business Unit was organized as follows:



The Internet and Media Business Unit did not change in connection with the 2002 Reorganization.

General

The Group operates in the Internet and publishing services sector through SEAT. Telecom Italia acquired control of SEAT (60.17% of ordinary share capital as of December 31, 2000) in 2000 pursuant to the SEAT/TIN.IT transaction.

Business

SEAT's business activities are organized in seven business segments:

- directories,
- directories assistance,
- Internet,
- office products and services,
- business information,
- television,
- professional publishing, and
- others activities.

In directories, SEAT is the principal seller in Italy of advertising in the Yellow Pages (*Pagine Gialle*) and the White Pages (*Elenchi Telefonici*) and the principal publisher of the Yellow Pages and the White Pages in Italy. In addition, SEAT offers a variety of other directory products and services in Italy. During 2000, SEAT significantly increased its presence in the European directories market, through acquisitions in France, Germany and the United Kingdom. Through the combination of SEAT and Tin.it in 2000 and a number of key acquisitions in 2000 and 2001 (Telegate, Consodata, Netcreations, Cecchi Gori Communications), SEAT has evolved into a leading multiplatform directory and business information provider, targeting small and medium-sized enterprises. Capitalizing on its strength in customer relationships, SEAT also provides a variety of services, including internet, office products and business information. Through Gruppo Buffetti, SEAT is also a leading distributor of office products and business solutions in Italy.

Directories and Directory Assistance

SEAT' s principal revenue generating activity is the sale of advertising in the telephone directory products that it publishes. SEAT' s principal publishing products are businessto-business Yellow Page directories (*Pagine Gialle Lavoro*), business-to-consumer Yellow Page directories (*Pagine Gialle Casa*) and the White Pages (*Elenchi Telefonici*).

SEAT also publishes business-to-business Yellow Page directories with regional coverage (*Pagine Gialle Professional*) and national subscriber-only business-to-business directories, segmented by industry (*Annuario* SEAT PG), provides an operator-assisted talking Yellow Pages directory service accessible 24 hours a day, 365 days a year (*Pronto Pagine Gialle*) and publishes city maps and information about local public services (*Tutto Città*) to be inserted into certain editions of the Yellow Pages.

SEAT also provides on-line directory Yellow Pages service (*Pagine Gialle On-Line*) and White Pages service (*Pagine Bianche On-Line*).

SEAT also participates in the European telephone directory advertising and services market through shareholdings in:

- TDL Infomedia, which is the second largest directories publisher in the United Kingdom, through Thomson Local Directories;
- EURÉDIT, a French company, which publishes and distributes Europages;
- Telegate, the second largest operator of directory assistance services and vocal portal services in Germany, with operations in Italy, Spain and the United States became part of the directories assistance business unit.

Internet

SEAT offers a full range of Internet services, consisting of:

- Internet access services;
- portal services;
- on-line advertising services; and
- web services.

Internet Access Services. Through Tin.it, SEAT provides Internet access services to residential, SOHO and SME Internet users. The small office/home office, or SOHO, market consists of businesses that use telephone lines to connect to the Internet, as opposed to dedicated lines, and is made up of small businesses, generally with one or two employees, and businesses conducted out of the home. The small- and medium-sized enterprise, or SME, market consists of businesses having between 3 and 50 employees.

Tin.it offers two principal access subscription plans:

- free access (Virgilio Club Net); and
- premium access (dial-up, ISDN and ADSL access).

At December 31, 2001, Tin.it's subscriber base amounted to approximately 5.0 million registered users and 1.8 million active users (defined as users who connect to the Internet at least once every 45 days).

Million users	2001	2000
Registered users	5.0	4.0
Active users	1.8	1.6

Portal Services. SEAT provides portal services through Matrix, which operates the *Virgilio* portal.

Virgilio is a leading Italian portal, with approximately 1.4 billion web page views in the first quarter of 2002 and approximately 3.9 billion web page views for 2001, that caters to the Italian speaking community on the Internet. Management believes that *Virgilio*, which has been on-line since July 1996, is one of the most complete Italian portals. It contains a search engine and a websites index, and it centralizes services in various interest areas such as stock quotes, weather forecasts, TV guides, games, chats advertisements and shopping. In order to simplify the use of information, *Virgilio* offers personalized, interactive services that correspond to the requirements of individual customers.

During 2001, *Virgilio* concentrated primarily on developing new content and services for its site, including *Virgilio Soldi* (a section entirely dedicated to personal finance), a broadband section with links to video streaming features, enhanced its community section through the acquisition of Xoom.it (a newsgroup and chat line operator), and implemented its integration with other Business Segments including Television Services (news programs of La7 are provided through video streaming technology), as well as links to *Pagine Gialle* and *Pagine Bianche*.

On-line Advertising Services. Matrix's division *Active Advertising* is a leading on-line advertising agency in Italy and has arrangements with approximately 70 Italian websites to provide advertising services.

Web Services. SEAT provides web services through Tin.It and Matrix's division Matrix Communication.

Tin.It provides different packages, which enable SME and SOHO customers to establish a presence on the Internet or provide e-commerce services. In particular, Tin.It's *Easy* and *Village* packages provide SME and SOHO customers with solutions to build an Internet site, to advertise the site with a pre-assembled banner advertising campaign and to establish and manage e-commerce capabilities on the Internet.

Matrix Communication provides a wide range of web services, including communication consultancy, website construction and maintenance, housing and hosting services and technical assistance.

Matrix has formed Kmatrix, a joint venture involving strategic consulting and the development of e-commerce services, with KPMG Consulting S.p.A., and plans to spin-off Matrix Communications into Kmatrix.

Office Products and Business Information. Through SEAT's control of Gruppo Buffetti S.p.A. ("Buffetti"), SEAT is a leading distributor of office products and business solutions in Italy. Through certain controlled companies (Consodata and Databank) it also offers direct marketing and database services.

Television Services. SEAT provides televisions services through Holding Media e Comunicazione S.p.A. (formerly Cecchi Gori Communication) which holds the broadcasting licenses for La7 and MTV Italia (formerly the TeleMonteCarlo TV network).

In September 2001, following a decline in advertising revenues and in accordance with an evaluation by SEAT of the costs of competing against other generic-content television channels, SEAT decided to change the editorial content of La7 from generic-content to content-specific. La7 is providing news information on a 24-hour basis, and is currently interacting with the Internet Services business segment in order to provide on-line news information through the use of video-streaming technology. La7 started broadcasting under the new format on March 18, 2002.

MTV Italia is a television channel providing music programs on a 24-hour basis. The brand MTV is a well known brand in the music industry and in the television network business. MTV Italia started broadcasting its programs on May 1, 2001.

Professional Publishing. Through Giallo Professional Publishing, SEAT has interests in companies publishing specialized information in the hotel, restaurant and entertainment industry, in electronics, information technology and audiovisual communication and in ceramics, architecture and urban design sectors.

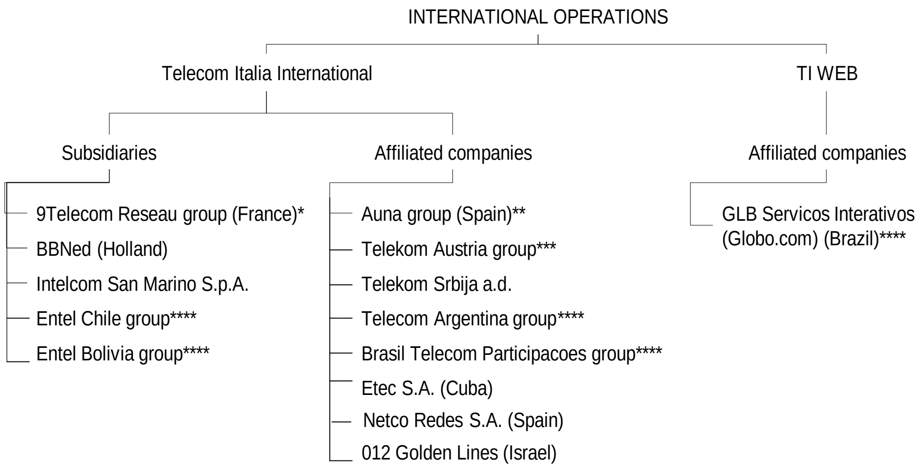
Other Business and Assets. Through other subsidiaries SEAT also engages in the following businesses:

- 49% Interest in ESRI Italia. The principal business of ESRI Italia is the distribution and customization throughout Italy of territorial and environmental software applications and information systems that utilize Geographic Information System, or GSI, technology; and
- VIASAT S.p.A. VIASAT S.p.A. was formed in 1998 as a 50%-50% joint venture between Telespazio, Telecom Italia's wholly-owned satellite telecommunications subsidiary, and Magneti Marelli S.p.A. VIASAT is a provider in Italy of satellite automotive telecommunications services in Italy.

International Operations

International Operations include the Group' s fixed and integrated fixed-mobile telecommunications (outside Italy) which are mainly concentrated in Europe and Latin America. International Operations coordinated the international activities, which are, for the most part, controlled by Telecom Italia International.

As of December 31, 2001 the International Operations Business Unit was organized as follows:



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* Pursuant to an agreement dated June 21, 2002 Telecom Italia agreed to sell its stake in 9Telecom. See "? Recent Developments ? Sale of 9Telecom"."

** Pursuant to an agreement dated January 15, 2002, Telecom Italia has agreed to sell its stake in Auna for €2 billion. See "? Recent Developments".

*** In 2002, the Group has reached an agreement with Telecom Austria' s main shareholder which will allow Telecom Italia to gradually divest its stake in Telecom Austria. See "–Recent Developments".

****Pursuant to the 2002 Reorganization the activities of these companies are now part of the Latin America Operations.

Pursuant to the 2002 Reorganization, the International Operations Business Unit became a Central Function and was renamed International Subsidiaries. International Subsidiaries reports to the CEO in order to strengthen the relationship with other Central Functions and, in particular, with Mergers & Acquisitions with whom International Subsidiaries will evaluate opportunities to reorganize or restructure participations.

International Subsidiaries manages all the subsidiaries previously managed by the International Operations Business Unit with the exception of the Latin American subsidiaries. All Latin American subsidiaries (whether controlled by Telecom Italia International or by TIM International) are currently managed by Latin America Operations which reports directly to the steering committee for International Subsidiaries. The steering committee for the International Subsidiaries includes the Chairman of the Board of Directors and the Chief Executive Officers of Telecom Italia.

Significant International Developments During 2001

France. In 2001 in France, Jet Multimedia (a company of the 9Telecom Reseau group) acquired Victoire Multimedia from the LVMH Group for €33.5 million.

Spain. In Spain the Group reached an agreement in 2001 with Endesa, Union Fenosa and Santander Central Hispano for the disposal of its investment in Auna while retaining a right of first refusal for two years for dispositions of such interest. The agreement is subject to regulatory approvals.

Chile. In Chile, further investments were made in the Entel Chile group, bringing the stake of Telecom Italia to 54.76% of the Entel Chile group.

Mediterranean Area. A 30% stake in the Mediterranean Nautilus S.A. was sold by Telecom Italia International to F.T.T. Investment, a company belonging to the Israeli Fishman group reducing the stake directly held by the Company to 7.4%.

International Operations accounted for gross operating revenues of €1,879 million in 2001, €505 million in 2000 pro forma (giving pro forma effect to the consolidation of the Nortel Inversora Group on an equity basis at year end 2000) and €394 million in 1999.

In 2001, the revenues and the gross operating profit from International operations increased following a larger contribution by 9Telecom and the inclusion in the scope of consolidation of the Entel Chile and Jet Multimedia groups. In 2001 there was also a significant increase in the operating loss which is mainly attributable to higher amortization of goodwill, and the increase in provisions for adjustments relating to the Entel Chile and 9Telecom groups.

International Investments

The Group's international strategy has the following objectives :

- to consolidate the Group's international presence in Latin America;
- to develop its international investments in high-growth market segments, such as wireless, data and Internet through the creation of a common GSM platform and the launch of services that provide synergies to the group;
- to strengthen its role of strategic partner in the current operations by increasing the transfer of the Group's technological expertise and marketing know-how; and
- to divest investments in the existing international portfolio where the Group does not have control, in non-core businesses or by divesting minority participations in non-strategic geographical markets. Divestitures will be carried out in a time frame which enables the Group to maximize proceeds.

Regional Investments

In late December, 2000, Telecom Italia completed the corporate reorganization of its international holdings. As a result of the reorganization, Telecom Italia now owns 100% of Telecom Italia International, the primary vehicle through which the Telecom Italia group holds its international wireline investments (and certain integrated mobile/fixed-line investments).

In the following discussion the Group's main international holdings are shown by geographical area (principally Europe and Latin America). The discussion is further subdivided between holdings controlled by the Group and consolidated in the financial statements of Telecom Italia or accounted for pursuant to the equity method.

European Companies Controlled by Telecom Italia International

France

9 Télécom Reseau S.A. ("9Télécom"), a 97.52% controlled subsidiary is a French wireline telephone carrier which offers indirect access to voice, data and Internet services for the residential, professional and small- and medium-size business segments.

Through Jet Multimedia, 9Télécom supplies value added services for business customers and in the development of online applications using the Internet, Audiotel and Minitel platforms.

In 2000, 9Télécom together with Pinault-Printemps-Redoute ("PPR"), a French industrial group which is a leader in the distribution sector, particularly in the media and "new media" sector, acquired the free ISP Mageos S.A. In 2001, Mageos S.A. had a customer base of approximately 5,800. In May 2001, Europe Explorer and Mageos S.A. merged to form Mageos-Explorer. Mageos-Explorer was transferred to 9Télécom in 2001. Mageos-Explorer focuses on the internet, and internet access operations.

In 2001, 9Télécom acquired 652,307 new customers (reaching 672,432 active customers compared to 360,000 at the end of 2000). In addition, it acquired about 80,759 new Internet customers (for a total of 113,692 or an increase of 153% compared to the end of 2000).

In 2001, 9Télécom recorded operating revenues of €277 million, against €96 million in 2000. The gross operating profit, which showed a loss of €129 million in 2001 compared to a gross operating loss of €151 million in 2000 and an operating loss of €296 million in 2001 compared to a loss of €175 million in 2000, was due to the start-up phase of most of 9 Télécom's activities.

Republic of San Marino

The Group owns a majority stake (70%) in Intelcom San Marino, a telecommunications operator, which owns the monopoly for international voice telephony services in the Republic of San Marino and offers value added services, data transmission and Internet services. Intelcom San Marino owns a 51% interest in the company Telefonia Mobile Sanmarinese, the second operator in the Republic of San Marino, which launched its services in December 1999. Intelcom San Marino also holds minority stakes in companies which provide satellite services, business television and data transmission as well as interactive multimedia services. In 2001, Intelcom San Marino entered into agreements with new customers that manufacture prepaid cards, the most important sector of activity of Intelcom San Marino. As of December 31, 2001, Intelcom San Marino had 4,600 Internet customers and 98,000 mobile customers, revenues were equal to €41 million, a decrease of 28.1% compared with 2000, and operating income was €1 million, a decrease of 50% compared with 2000. Such decreases are primarily due to an overall decrease of tariff levels in the highly competitive market of prepaid card services.

The Netherlands

BBNed was a company established in July 2000 and is 96.17% owned. BBNed is an alternative carrier in the Netherlands, providing broadband local access to ISPs and business clients. BBNed successfully rolled out its commercial operations based on co-locations acquired from the incumbent operator, connected to its own backbone.

As of December 31, 2001 BBNed had 462,000 ADSL lines. In 2001 BBNed had a gross operating loss and an operating loss of €16 million and €18million, respectively.

Latin America Companies Controlled by Telecom Italia International

Pursuant to the 2002 Reorganization the activities of the Latin American companies are now part of Latin America Operations.

Chile

Telecom Italia International acquired an additional stake in Entel Chile while increasing its ownership to 54.76%. The overall cost of the acquisition was US$905 million. Entel Chile is the largest long-distance and international telecommunications operator in Chile and the second largest national telecommunications operator. Through its mobile and two PCS licenses, Entel Chile is the second largest wireless telecommunications operator with nationwide coverage.

In 2001 Entel Chile consolidated its position as an integrated provider of telecommunications services; Entel PCS (a subsidiary of Entel Chile and the owner of one of the largest GSM network in Latin America) achieved a leadership position in the mobile phone market. In 2001 Entel Chile acquired for US$12.1 million three WLL licenses to provide fast Internet-access services and fixed telephone services in Chile and abroad.

In 2001, Entel Chile, through Entel Telefonia Personal, reached 1.9 million customers (an increase of 52% compared to 2000). Internet traffic increased by 40% in 2001. As an integrated telecommunications operator, it also provides additional services, including business packages of telephony, data transmission, Internet access and local telephone services in the Santiago Metropolitan Region. Based on its development plans, Entel has invested heavily to build out its mobile subsidiary Entel PCS as well as its United States-based long-distance carrier, Americatel.

Entel Chile group had consolidated operating revenues of approximately €1,251 million (an increase of 35.8% compared with 2000, due to increases of 24% in mobile and 13% in long-distance traffic) and consolidated net income of €47 million in 2001. Entel Chile has been fully consolidated with Telecom Italia since the first quarter of 2001.

Bolivia

In November 1995, Telecom Italia International acquired a 50% stake in Entel Bolivia, the Bolivian national long-distance and international telephony operator, for approximately U.S.$ 610 million through a capital increase. Entel Bolivia also owns a license to provide mobile and CATV services. Local regulations established that until November 2001, when liberalization of the market began, long-distance telecommunication services would be provided by Entel Bolivia under a monopoly system. In 2001 complete deregulation of the telecommunication market took place, carrier selection was introduced and local access, previously in the exclusive hands of cooperatives, was liberalized. In 2001, GSM technology was introduced in Bolivia; Entel Bolivia consolidated its leadership position in the business and corporate client segments. In 2001, Entel Bolivia reached 368,000 mobile customers and 53,000 connections through direct lines, representing increases of 41% and 32%, respectively, compared to 2000. Internet clients amounted to approximately 12,000 as at the end of 2000. Due to the start up of operations by the competition in its relevant markets, Entel Bolivia experienced a decrease in revenues and in its profitability. Operating revenues were approximately €220 million, a decrease of 0.2% compared with 2000, gross operating profit was €91 million (a decrease of 1.6% compared with 2000) and operating income was €15 million in 2001 (a decrease of 35.5% compared with 2000).

Investments—Europe

Austria

In December 1998 Telecom Italia International acquired a 25% (plus one share) stake in Telekom Austria, the incumbent fixed telecommunications operator in Austria. The initial public offering and listing on the New York Stock Exchange of Telekom Austria was completed on November 21, 2000. As a result of the IPO, Telecom Italia increased its stake in Telekom Austria by 4.78% without any cash payment pursuant to the terms of an earlier shareholders' agreement. As of June 10, 2002 the Group's shareholding in Telekom Austria is 29.78%. Telecom Italia provides Telekom Austria with senior management and support.

In June 2002, Telecom Italia reached an agreement with ÖIAG regarding an agreement with Telekom Austria which allows Telecom Italia to gradually dispose of its investment in Telekom Austria including selling up to half its stake in the second half of 2002. See "—Recent Developments".

In 2001, due to continuing competitive pressures, Telekom Austria continued to lose market share in terms of wireline traffic, which declined from 71% in 2000 to 54.6% in 2001. In response Telekom Austria restructured its human resources and cut back approximately 2,700 employees (19% of its fixed-lines workforce) and introduced a more customer-oriented organizational model, continued its international expansion in the mobile segment and launched a new portal for the development of new services and applications.

At the end of 2001, Telekom Austria's had a 51.9% market share in terms of traffic (a decline of 16% compared to 2000) and a 93.9% market share in terms of the number of lines, equal to approximately €3,166,000 (95.1% in 2000). Internet customers numbered 656,221 (with a residential market share of 39%). Telekom Austria remained the leading provider for the residential segment.

In 2001, the Telekom Austria Group reported operating revenues of €3,943 million, an increase of 1.2% against €3.897 million in 2000 and an operating income of €326 million against an operating loss of €5 million in 2000.

Spain

The Group' s investments in Spain date back to 1997 and include six companies: Netco Redes, Retevisión, Euskaltel, Madritel, CTC—Cable i Televisio de Cataluña (which operates under the brand name Menta) and Retevisión Movil, that operates under the commercial brand of Amena. In each of the above mentioned companies, the Group is in partnership with Endesa (Empresa Nacional de Electricidad SA) and Union Electrica Fenosa, the major Spanish electric companies.

On January 15, 2002, the Group reached an agreement for the sale of its holding in Auna for €2 billion in cash. Please see above "—Recent Developments—Sale of Interest in Auna".

As of December 31, 2001, Telekom Italia' s stake in Auna was 26.89% (of which 22.77% was held through SIN, 3.81% was held through TIM International and 0.31% held through Multimedia Cable).

Auna holds the main telecommunications operations of the group in Spain:

- Retevision I: 100% (wireline communication company);
- Retevision Movil (Amena): 97.9% (wireless telecommunication company);
- Cable i Televisio de Catalunya (Menta): 100% (cable television company);
- Madritel: 100% (cable television company);
- Supercable Andalucia: 96.36% (cable television company);
- Supercable Almeria: 100% (cable television company);
- Supercable Sevilla: 98.17% (cable television company);
- EresMas Interactiva: 99.72% (internet company);
- Quiero TV: 49% (television company);
- Hispasat: 18.57% (satellite communication company);
- Aragon del Cable: 100% (cable television company); and
- Cable Telca: 100% (cable television company).

Retevision I ended 2001 with more than 1,291,099 customers, corresponding to 1,236,818 indirect access lines and 4,281 direct access lines, confirming its position as the second largest fixed telecommunications operator in Spain. Strong competition led to a reduction in rates and lower margins.

EresMas Interactiva is the new name of Retevision Interactiva, and operates in the Internet sector for residential customers. As of the end of 2001, it had 1,225,000 customers, confirming its position as the second largest operator in the Spanish market of Internet Service Providers and portals, with 4,557 million pages visited during the year.

Retevisión Movil, which operates under the brand name Amena, owns the third mobile telecommunication license in Spain. At December 31, 2001 Amena had more than 5.2 million lines (an increase of 40.5% compared to the end of 2000), and a market share of 18% of the total market. During 2001 it increased its market share adding 11% net new additions during the period. The additional market share was attributable to the innovative nature of its offering, launching the first WAP service in Spain.

In March 2001, Retevision Movil was also awarded a UMTS license for a total cost of €133 million. On April 1, 2001, after long debate, the Spanish government decided to postpone the first available date for launching UMTS services from August 1, 2001 to June 1, 2002. Such postponement was caused by the delays in the development of the required technologies for the mass market. Due to the postponement, installment payments by the owners of UMTS licenses have been postponed.

In 2001, Auna strengthened its position as Spain's second largest integrated telephone operator; Eresmas reached a 40% market share in the Internet portals and ISPs segments. Auna continued to invest in the mobile market for the development of GPRS and UMTS networks with expenditures of about €27 million in 2001.

Euskatel and Netco Redes operate in the Spanish market but are not part of Auna. Euskaltel provides telecommunication services and CATV in the Basque Region. At the end of 2001 Euskaltel had reached 392,000 customers through carrier selection and, through a cooperation agreement with Retevision Movil, it became an integrated fixed-line mobile operator. In 2001 Euskaltel had total operating revenues of €140 million, an operating loss of €26 million and a net loss of €38 million.

In August 1997, SIN acquired a 30% stake in Netco Redes SA for approximately €166 million. In 2001, Netco Redes had operating revenues of €21 million and a net result of €6 million in line with those of the prior year. Netco Redes SA owns the right to use the fiber-optic network of the Spanish electric companies, which represents the most extensive Spanish telecommunications network after Telefonica's. At the beginning of 2000, pursuant to a decision on the part of the Spanish Antitrust Authorities, Netco Redes lost its exclusive right to use the networks.

Serbia

Telecom Italia owns a 29% stake in Telekom Srbija, the Serbian national fixed-line telecommunications and second largest mobile operator.

At December 31, 2001, Telekom Srbija had 2,264,000 subscribers to the fixed-line network (compared to 2,220,000 at the end of 2000) and 821,000 mobile lines (compared to 433,000 at the end of 2000).

No official evaluation of the extent of the damage resulting from the hostilities in 1999 has as yet been forthcoming; the lifting of the state secret imposed on this subject, which should have expired on June 26, 2000 has been postponed indefinitely.

In 2001, Telekom Srbija, according to the draft financial statements of Telecom Srbija, reported operating revenues of Serbian dinars 26,152 million (€438 million based on an exchange rate of 59.7 Serbian dinars to the euro), compared to Serbian dinars 21,819 million in 2000. Gross operating profit was Serbian dinars 9,592 million (€161 million), compared to Serbian dinars 9,240 million in 2000. Telekom Srbija reported a profit for the year of Serbian dinars, 1,499 million (€25 million), compared to a loss in 2000 of Serbian dinars 2,970 million. See "Item 8. Financial Information—Legal Proceedings".

Investments—Latin America

Pursuant to the 2002 Reorganization the activities of the Latin American companies are now part of Latin America Operations.

Argentina

The current interest of the Group in Nortel is the result of an initial share of 32.5% acquired in 1990 for approximately U.S.$33 million and an additional share of 17.5% acquired in August 1999 for approximately U.S.$265 million. Nortel currently owns 54.74% of Telecom Argentina, which until October 1999 operated the telecommunications network in the northern part of Argentina (including Buenos Aires) among others, fixed-line and mobile telecommunications operations, international services, data transmission services, value-added services and directories publishing. Since October 1999, the Argentinean market has been progressively liberalized, and as a consequence Telecom Argentina has expanded its operations to the entire national territory. In June 1999, Telecom Argentina also expanded its mobile telecommunications services, by acquiring new licenses in the PCS technology, for a total amount of U.S.$327 million. At the end of 2001, Telecom Argentina had accumulated 3.6 million fixed-line network subscribers corresponding to a market share of 45%. Its subsidiary Telecom Personal, a subsidiary of Telecom Argentina and a leading company in the wireless segment, accumulated more than 2 million mobile customers (66% with prepaid cards), with a market share of 18%. In the Internet sector, there were approximately 247, 000 subscribers, with a market share of 18%. In 2001, Telecom Internet achieved a market leadership position in ADSL access packages.

On April 22, 2002 and April 24, 2002, Telecom Internet and Telecom Argentina held meetings of their shareholders and approved the merger of Telecom Internet into Telecom Argentina. Therefore, the reorganization formalities that will result in a dissolution without liquidation of Telecom Internet, with retroactive effect since December 1, 2001, has started.

Argentina's economy is in its fourth straight year of recession. In January 2002, the Argentine government removed the peg of the Argentine peso to the U.S. dollar, resulting in a significant devaluation of the peso against the U.S. dollar and against the other major currencies. The Argentine government has also defaulted on the payment of its debt obligations. Whether companies doing business in Argentina will default on their obligations depends upon their own financial condition, and, in the case of U.S. dollar obligations, continued access to the foreign exchange markets. The default by the Argentine government and its decision to devaluate the currency have resulted in considerable uncertainty about the government's political stability, its management of the economy and the current exchange rate regime. Economic activity slowed sharply in the last weeks of 2001, and real GDP declined 4.5% for the year. Argentina's economic outlook is poor for 2002 with real GDP expected to decrease another 9.0% to 12.0%. Argentina is also likely to experience increased inflation as a consequence of the currency devaluation.

In February 2002, Telecom Argentina hired Morgan Stanley as financial advisor in order to explore the possibility of restructuring and consequently reducing its debt. In April 2002 Telecom Argentina declared that it was not going to be able to meet its obligations on the US$3.2 billion debt; the moratorium on Telecom Argentina's payment of its debts is mainly attributable to the devaluation of the Argentine Peso. In 2001, Telecom Argentina implemented a cost and investment optimization process focused on cost cutting in order to improve cashflow. The implementation of this strategy is expected to continue in future years.

In 2001, the Telecom Argentina group recorded consolidated operating revenues of Argentine pesos 3,188 million (€3,558 million), a decrease of 5.2% compared to 2000. The decrease can largely be attributed to the crisis the country is currently undergoing. The operating income was Argentine pesos 570 million (€636 million); the net result attributable to Telecom Argentina was a loss of Argentine pesos 2,079 million (€1,364 million) due to the strong impact of the local currency devaluation.

Brazil

Brasil Telecom Participacoes ("BTP") group, the former Tele Centro Sul Participacoes group in which SIN owns a 7.28% stake through Solpart in which Telecom Italia International has a 38% stake, operates in the wireline telephone sector, providing local and long distance telephony services. At the end of 2001, BTP held 65.47% of the total share capital of Brasil Telecom (97.97% of ordinary shares and 39.34% of preferred shares).

Investments were made during the year to strengthen the transmission and switching structures and completing the digitalization of the exchanges. At the end of 2001, there were 8.6 million lines in service (of which about 1.2 million were newly installed). In addition, during the year, the technological platform to support the broadband Internet services became available.

In 2001, BTP formed BrTurbo a company focused on Internet access (narrow band and broadband) and value-added services.

BTP's consolidated financial statements showed operating revenues of Brazilian reais 6,464 million (€3,074 million) an increase of 36.6% compared to 2000; operating income was Brazilian reais 1,201 million (€571 million).

Telecom Italia and Globo Organizaçoes have agreed to undertake a joint strategic Internet initiative in Brazil. To formalize this strategic partnership signed on June 2, 2000, Telecom Italia acquired 30% of the voting and total capital of Globo.com for U.S.$810 million. Globo.com is the exclusive Internet portal of Globo Organizaçoes, the market-leader in television, magazine, newspaper and radio operations in Brazil. Telecom Italia has its own members in the Globo.com' s Board of Directors and supports the operations of the company, with focus on its technological aspects. Telecom Italia and Globo Organizacoes are exploring further joint initiatives in the Internet field. As of December 31, 2001, Telecom Italia held, through TI Web, a wholly-owned subsidiary, 28.57% of the total share capital of Globo.com.

Cuba

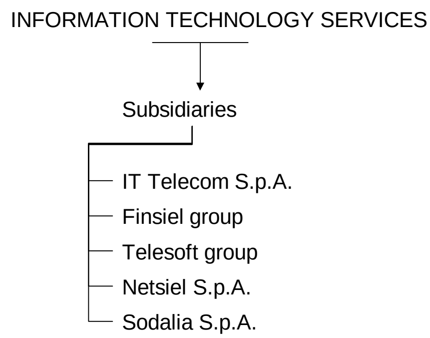
Telecom Italia International has a 29.29% interest in Empresa Nacional deTelecomunicaciones de Cuba S.A. ("ETEC S.A."), the operator for national and international wire telecommunications services in Cuba. In order to realize the objectives of its license, ETEC S.A. has increased the number of lines from 470,000 in 2000 to 555,000 in 2001 and the digitalization rate from 53% in 2000 to 69% in 2001. The data network was also improved in 2001 with net ATM/Frame Relay technology. In 2001, ETEC S.A. improved its Internet activities by doubling the number of customers (from approximately 3,000 in 2000 to 5,000 in 2001) and launched an horizontal portal focused on Cuban history, culture and tourism.

In 2001, ETEC S.A. had operating revenues of U.S.$281 million (€314 million) compared with U.S. $293 million in 2000. Operating income was U.S.$137 million (€153 million) compared with U.S.$169 million in 2000.

Information Technology Services

The Information Technology Services (IT Services Business Unit) is responsible for the information technology activities of the Group and covers the entire range of information services, while pursuing objectives to reposition its activities on higher value-added products.

The Business Unit, established as part of a plan to integrate various companies, such as Finsiel, Netsiel, Telesoft, Sodalia and the former information technology function of Telecom Italia, as of December 31, 2001 was organized as follows:



To reflect the new strategic guidelines, the Business Unit' s structure was alteredpursuant to the 2002 Reorganization and is now subdivided into two organizational structures:

- The Information Technology Group Operational Activity includes IT Telecom S.p.A., a wholly owned subsidiary of the Company, Netsiel, a company held as of December 31, 2001 by the Company (68,65%) and Finsiel (31,35%), Telesoft S.p.A., a company held by the Company (60%) and Finsiel (40%) and its subsidiaries, Sodalia S.p.A., which is 100% owned by the Company and Netikos S.p.A. a company held by IT Telecom (25%) and Finsiel (75%). ITG is oriented towards increasing efficiency and quality of service activities directed at all the Business Units of the Telecom Italia Group. The companies Saritel and TILAB – both 100% owned by the Company – will also report to ITG.

- The Information Technology Market Business Unit, includes the Finsiel Group. ITM will continue to pursue activities mainly geared towards central and local administrations moving towards decentralization and e-government, as well as banks and businesses.

Finsiel is held 77.92% by the Company, 14.38% by the Bank of Italy and 7.70% by other shareholders.

The Finsiel Group provides services in the field of information technology and related activities, including the design, management and maintenance of software and information products and services for local and central government entities, as well as for banks, manufacturers and service companies. In addition, the Finsiel Group provides management consulting and services related to company automation. Finsiel is the leading firm in the Italian systems integration and information technology consulting market (excluding hardware support), and one of the largest European companies of its type. Finsiel is the principal supplier of systems integration and information technology consulting to the Italian government and local government authorities, typically under long term exclusive arrangements.

The Finsiel Group has a leading role in the Italian marketplace and acts as an ICT outsourcer and systems integrator for national and local governments, banks and private sector organizations. During 2000, Finsiel increasingly focused on Internet and e-commerce solutions, with new offerings of customized web-based solutions for the group' s corporate, bank and governmental clients.

The Finsiel Group strengthened its traditional role as partner of the Public Administration, supporting the process of improving its structures and services and playing an advisory role in the key areas of administrative decentralization, taxation and healthcare systems.

SOGEI, (100% owned by Finsiel) the main operations partner of the Ministry of Finance, has provided the "Online Revenue Service" project, which processed more than 45 million tax returns. The introduction of more advanced technologies in the fundamental processes of the Ministry makes it possible not only to reduce delays and malfunctions of the Administration, but also to improve and broaden the range of services available to taxpayers. In addition, other projects are being developed to support the reform of the Ministry, including the creation of four independent agencies and the extension of on-line services to other subjects.

In the travel and transportation sector, Finsiel is the second largest national operator with a 10-year outsourcing contract with the Italian Railways, focusing also on large Enterprise Resources and Planning ("ERP") systems (finance, administration, logistics) as well as e-business systems and solutions for the railways supply chain and online ticketing systems.

Services also cover e-business for industries and the services sector, where Finsiel has developed a full range of strategic outsourcing services, from facilities management to ERP packages, consulting services for business process re-engineering and e-commerce packages.

On December 31, 2000, Telecom Italia contributed the "Information Systems Operation" business segment which operates the information infrastructures of Telecom Italia itself and related services to Netsiel. After this transaction, Netsiel (formerly a wholly owned subsidiary of Finsiel) is 68.65% owned by Telecom Italia and 31.35% owned by Finsiel. Beginning in 2001, through its outsourcing contract from Telecom Italia, Netsiel will concentrate on the operation of the information services of the Group.

Telesoft is the main engineering center for the Telecom Italia Group and has an in-depth knowledge of the telecommunications market and operators business practices and processes. It also has a comprehensive knowledge of the methods and procedures which support the daily operation of the telecommunications infrastructure ("OSS" or "Operation Support System") and the particular type of OSS which overviews such operations as billing, sales management, customer-service management and customer databases ("BSS" or "Business Support System").

Sodalia, established in 1992 by Telecom Italia and Bell Atlantic, is a software developer providing advanced software for the management of telecommunication services and networks.

In June 2002, Telecom Italia contributed its shares in Telesoft, Netsiel, Sodalia and Saritel to IT Telecom. Finsiel is also planning to give its shares in Telesoft, Netsiel and Netikos to IT Telecom within the end of June 2002. After these transactions, these companies would become wholly owned subsidiaries of IT Telecom.

Satellite Services

The Satellite Services Business Unit (consisting of the Telespazio group and Telecom Italia's Satellite Telecommunications business segment) is responsible for developing satellite communication systems for phone and data, radio and television broadcasting and earth-observation.

SATELLITE SERVICES

- National subsidiaries
  - Telespazio S.p.A.
  - e-GEOS S.p.A.
  - Eurimage S.p.A.
  - CTM S.C.p.A.
- International subsidiaries
  - Telespazio Brasil S.A.
  - MCS Europe group
  - Telespazio Luxembourg S.A.
  - Telespazio North America Inc.

Telespazio (a wholly owned subsidiary of Telecom Italia) designs, develops and manages satellite telecommunications systems for a variety of commercial uses and manages such systems for the Group, including the public network utilized by Telecom Italia.

Telespazio's principal activities include: (i) telecommunications—marketing turnkey systems (ground stations, VSAT systems, overlay networks) and services for satellite-based voice, video and data links between fixed and mobile points; (ii) space systems and services—providing systems and services for the in-orbit control of satellite data acquisition and processing as well as consultancy and engineering services for the design, implementation and operation of new satellite systems for customers such as Intelsat; (iii) television—providing distribution and other ancillary services for Italian and foreign TV broadcasters; (iv) earth observation and environmental information—offering systems and services for the acquisition and processing of environmental data from all major remote sensing satellites; and (v) mobile communications—providing localization, data and messaging services through satellite systems. Telespazio holds a license to offer European Mobile Systems services in Italy.

Telespazio is a significant participant in a number of ventures relating to global space systems. Telespazio is developing the Cosmo/Skymed Global System, the first earth observation system based on a constellation of satellites which will provide high-resolution remote sensing data in any condition of light (day, night, clouded sky). In close cooperation with the European Space Agency, Telespazio is participating in the Galileo program, the most important European satellite based navigation and radio localization system designed for land and air navigation purposes. At the end of 2001, through its EVOLVE-E multimedia platform, Telespazio has started the distribution of high value added satellite-based wideband solutions such as high-speed distribution of multimedia contents for professional applications and territorial marketing to business customers.

Telespazio's customers include the principal national and international space organizations and agencies, Ministries and local governments, publicly owned and private companies operating in the areas of telecommunications, television, transport, Internet access, research, university education and medicine.

Telespazio was developing, together with the U.S. companies Liberty Media, Lockheed Martin Global Telecommunications and TRW, a global technology, manufacturing and service company, the Astrolink Broadband Communication System project. The project, which was intended to support high-speed Internet access and broadband interactive multimedia services was abandoned in 2001. Astrolink International LLC, the company in charge of the Astrolink Broadband Communication System project, was not able to obtain the required funding to complete the broadband satellite constellation. As a result the contracts related to the project were terminated in the fourth quarter of 2001.

TILAB

TILAB was established in March 2001 to combine Telecom Italia' s venture capital and innovation Business Unit, the CSELT research laboratories in Turin, the Future Centrein Venice and the Consumer Lab in Rome. The Technology Observatory in San Francisco collaborates, on an exclusive basis, with TILab. Telecom Italia Lab was formed to enhance Telecom Italia' s competitive position promoting and managing innovation and by identifying and developing business opportunities. Telecom Italia Lab' s strongest assets are its rich and consolidated R&D activities, its ability to promote corporate venture capital activities in emerging technology and to identify internal research areas through the development of new ideas.

As of December 31, 2001 TILAB had the following structure:

TILAB

- TILAB S.p.A.
- Loquendo S.p.A.
- Telsy S.p.A.

Pursuant to the 2002 Reorganization, the venture capital activities of TILAB became part of a separate venture capital central function and TILAB became part of the Information Technology Group.

The Group spent €331 million, €269 million and €138 million on research and development in 1999, 2000 and 2001, respectively. The Group also receives grants from research and development national and international programs.

The purposes of the Group' s research and development activities is mainly the development of innovative services and applications, to meet the increasing demand from the market. Some R&D activities are also devoted to support the manufacturing sector outside the group in an increasingly competitive market.

Development of innovative services is pursued through both the introduction in the network infrastructure of new platforms and systems that enable the provision of a wide range of services, and the use of state-of-the-art information and communications technologies for the development of highly innovative applications, tested on selected customers' sites. Such activities are mainly carried out by TILAB, the corporate research center of the Group. TILAB performs both strategic research and research specifically requested by Group Companies.

The following operations and developments occurred in 2001:

- the beginning of a cooperation with Pirelli Lab;
- the refinement and multi-lingual extension of techniques for voice synthesis and recognition;
- the development of an experimental fiber optic automatic routing network, which would implement the new Internet;
- the definition of analytical models for dimensioning the radio resources of a GSM/GPRS cell shared by voice and data services, and for characterizing data traffic;
- creation of a platform to locate mobile land-based terminals based on in-house technology;
- the creation of the AMICO platform, which can create and manage Instant Messaging (or chatting) services. The platform, which has been adopted by TIM, is particularly innovative because it integrates mobile access; and

- the development of the JoeXpress platform, in the field of the development of MPEG, a service which will become operational in June, and Movida. In the same field, the Easy Video Platform proposal was designed to supply audiovisual services on mobile systems.

Other Operations

Real Estate and General Services

The Real Estate and General Services segment provides asset and property management services and leverages the value of the real estate properties of the Group, carries out the project design and work on properties and provides project and facility management. The segment comprises the internal structures of Telecom Italia (Telecom Italia's Real Estate and General Services business segment), as well as the consolidated companies Emsa Telimm and Immsi and the affiliates IM.SER and Telemaco Immobiliare. The two latter companies became operational from December 1, 2000 and from May 1, 2001, respectively, following the real-estate spin-off transactions carried out by Telecom Italia, at the end of 2000. See below "—Description of Property".

Multimedia Services

Stream, a wholly owned subsidiary of Telecom Italia, was formed in 1993 with the objective of establishing and promoting a wide range of multimedia services and applications for the Italian and other international markets. See "—International Network—Broadband Network/ADSL".

At the end of 1996, Stream launched a commercial offering of digital video broadcasting services via cable, acting as a service provider on the Telecom Italia broadband cable network. During 1998, Stream launched a commercial offering of digital video broadcasting services via satellite.

On May 29, 1999, Telecom Italia, News Corporation, Gruppo Cecchi Gori and SDS (an Italian company that sells broadcast rights for the exploitation of Italian football games) signed an agreement to develop the second digital TV platform, pursuant to a memorandum of understanding signed by the parties on April 27, 1999. Following such agreement, on June 7, 1999 Telecom Italia sold 65% of Stream's shares to News Corporation, Cecchi Gori Group and SDS for a total of €67 million. On May 16, 1999, SDS and Stream signed an agreement for the cable broadcast by Stream of sports events for the 1999-2000, 2000-2001 and 2001-2002 seasons. Stream has an option to renew the agreement for an additional three-year term. Stream will pay SDS an annual fee of €124 million.

On April 18, 2000, Telecom Italia and News Corp agreed to acquire the stakes owned by Cecchi Gori and SDS in Stream. Through the above mentioned transaction Telecom Italia and News Corp increased their respective stakes in Stream to 50%. The total cost to Telecom Italia and News Corp was approximately €196 million.

In 2000, Stream acquired broadcasting rights, for new television channels and programs and for Italian and European soccer championships. Interactive and Internet applications were developed and in December 2000 an e-mail service via the television set was launched.

Stream's main activities in 2001 were:

- enhancing its offer packages by including the Calcio channel and three new theme-oriented channels (MT Channel, Stream Verde and Fox News);

- the acquisition of the broadcasting rights for all the football matches of the UEFA Champions League for seasons 2001-2002 and 2002-2003, and the rights of Bologna Calcio starting from the season 2001-2002; and

- creation of the "single decoder" a machine which allows the customer to purchase the subscription to both Stream and Stream's main competitor, Telepiu' without installing two separate decoders.

At the end of 2001, Stream had 799,000 customers, compared to 670,000 at the end of 2000. Operating revenues were €250 million (an increase of 70.1% compared to 2000). The expenses incurred for the acquisition of content, sales assistance and extension of the technical infrastructures led to a deterioration in the results for 2001. In 2001, Stream' soperating loss was €475 million (an increase of 38.1% compared to 2000).

As previously announced during the year 2001, Telecom Italia decided to exit Stream.

For this purpose, on February 2002, Telecom Italia reached an agreement with News Corporation and Vivendi Universal/Canal+ for the sale of its 50% stake in Stream for a total consideration of U.S.$42 million. The agreement, provides inter alia that: (i) Telecom Italia will sell its 50% stake in Stream to News Corporation, (ii) News Corporation will sell the 100% of Stream to the Vivendi Universal group and (iii) Telecom Italia will write off Stream' s credit exposure towards Telecom Italia for a total of U.S.$80 million. The sale was expected to become effective on 30 April 2002 or later if any condition precedent for closing would not previously occur.

On May 13, 2002 the Competition Authority authorized the acquisition of Stream by Canal+/Telepiù, subject to certain conditions aimed at easing entry by new competitors in the pay-Tv market, the development of alternative means of transmission, as well as guaranteeing the protection of consumers. On May 15, 2002 Vivendi Universal and Canal+ announced that, due to the conditions imposed by the Antitrust Authority, they would abandon their plan to acquire Stream.

On June 8, 2002 News Corporation announced it had signed an agreement with respect to the acquisition of Telepiù by a group of investors headed by News Corporation. This agreement is subject to a number of conditions, including Telecom Italia' s agreement.

Competition

Domestic Fixed-line and International Telecommunications Services

Pursuant to the Telecommunications Regulations, fixed-line public voice telephony services and the operation of the fixed-line network for the provision of such services was liberalized effective January 1, 1998. Until January 1, 1998, Telecom Italia was the sole provider of fixed-line public voice telephony services, which consist of local, long-distance and international telecommunications services, in Italy. In addition to fixed-line public voice telephony services, over the last five years there has been increasing liberalization of all other business areas in which the Group operates. The operation of telecommunications infrastructure for the provision of all telecommunications services other than fixed-line public voice telephony services was opened to competition by the Telecommunications Regulations and the Maccanico Law during 1997. As a result of the complete liberalization of the market for telecommunications services, the Group has faced increasingly significant competition since 1998 in the Italian domestic market, including competition from foreign telecommunications operators, particularly with respect to medium-sized and large business customers.

Since 2000, TIM has faced competition for providing mobile telecommunication services not only from Omnitel, the second mobile operator which commenced operations in 1995, but also from WIND, which commenced operations in March 1999, and from BLU S.p.A., which obtained the license as fourth national operator on August 4, 1999, and began commercial operations with a DCS 1800 service from May 2000. Management believes that the increase in competition in the mobile market, together with the maturation of the market, has caused TIM to grow more slowly in 2000/2001 than in prior years and expects that this will continue in the future. With penetration in the Italian market at 90.3% on March 31, 2002, the overall market is not expected to grow as rapidly as in prior years. TIM' s overall lines growth was only 11%, and 17% in 2001 and 2000, respectively, (compared to 30% in 1999) and its overall market share declined to 47% in 2001 from 61% in 1999.

In April 2002, the number of licenses for the provision of both fixed voice telephony service and building public telecommunications networks granted by the Ministry of Communications and the National Regulatory Agency were approximately 235. See "—Regulation".

Telecom Italia is now facing increasing competition in international and domestic telecommunications services from, among others, Infostrada (controlled by ENEL), Albacom (a joint venture among British Telecommunications, Banca Nazionale del Lavoro, ENI and Mediaset) and Wind (a joint venture between Deutsche Telekom, ENEL, and France Telecom which merged with Infostrada in 2001), TISCALI (national competitor: 90% Renato Soru, 10 KIWI Venture Capital), and Tele2 (Italian branch of the Sociètè Europenne de Communications S.A.). International telecommunications services and long-distance domestic services as well as mobile telecommunications services are the areas of its business which are attracting substantial competition, which will be based mainly on rates.

Since the beginning of 2001 there has been increased competitive pressure with respect to local calls.

Although increased competition (including the need to adjust tariffs in response to competition) has affected the Group's operations, management believes that it will be able to increase traffic and revenue from domestic telecommunications services as a result of (i) the introduction and continued growth of new telecommunications services (in particular, non-voice services), capitalizing on Telecom Italia's advanced fixed network, (ii) growth in traffic due to increased Internet and data usage, (iii) increased interconnect traffic as a result of the growth of other mobile telecommunications operators and alternative telecommunications operators in Italy, (iv) continued growth of the Group's mobile telecommunications businesses, (v) continued focus on customer service quality and marketing initiatives, and (vi) growth of the Italian economy. Telecom Italia expects a significant change in its revenues mix for domestic fixed telecommunications due to regulatory and competitive reasons, and the new business opportunities driven by data and Internet services and broadband access. On voice services, Telecom Italia will seek to implement a strategy based on greater efficiency for its internal structure and competitive offerings in its services portfolio aimed to reduce market share losses.

The legal framework for regulation in the telecommunications sector in Italy has been completely transformed in recent years, particularly as a consequence of the adoption of the Maccanico Law (effective August 1, 1997), the Presidential Decree No 318/97 (the "Telecommunications Act") (effective September 22, 1997) and a series of Orders issued by the National Regulatory Agency (see "—Regulation") which are important to Telecom Italia as it faces increasing competition. To date the regulatory environment has been characterized by an intensive implementation process in order to complete liberalization. The trend continued in 2001 as additional steps were taken regarding tariff rebalancing, interconnection charges and the further signing of contracts to permit the unbundling of the local loop. See "—Regulation".

Although management has taken steps to prepare for increased competition, as management expected it has lost fixed-line telephony services market share, in particular, with respect to domestic fixed long-distance traffic (including fixed to mobile traffic) and outgoing fixed-line international traffic. In 2001, revenues from fixed-line telecommunications services were primarily affected by increased competition due to the development of carrier selection operators. Any decline in market share is expected to be offset in part by increased interconnection revenues as new competitors utilize Telecom Italia's domestic fixed-line network. Telecom Italia expects to maintain its subscriber lines volume for 2002, because the unbundling of the local loop is not expected to have a significant impact before the end of 2002.

With respect to domestic fixed traffic as a result of increasing competition and to limit market share losses, in particular for long-distance traffic, Telecom Italia introduced a number of innovative tariff packages, such as Teleconomy No Stop and Teleconomy 24. Its overall strategy is to focus on pricing, customer service and loyalty, and new offers to achieve customer retention in order to stop or slow further losses in market share.

In the domestic wireline telecommunications services market, Telecom Italia is also continuing to pursue the new opportunities offered by Internet and data services that have offset, in part, the continuing decline in voice revenues. Telecom Italia believes it is in the best position to capture the potential benefits to be derived from E-value. Telecom Italia intends to develop broadband networks in order to offer customers more bandwidth and convergent services.

Mobile Telecommunications Services

The Italian Mobile Market. The mobile telephone market continued to grow in Italy in 2001, but at a slower pace (21% in 2001 compared to 40% in 2000). By December 31, 2001, the number of cellular phone lines reached 51.3 million, corresponding to a penetration rate of around 89% of the population.

The demand growth curve has, however, reached its inflexion point and the remaining potential market, though it is still of a considerable size, will be smaller than the one already acquired. In addition, the increasing saturation means that new customers to be acquired are likely to result in lower revenues per customer as has been the case in recent years.

Competition for mobile telecommunication services grew stronger in 2001. WIND, which introduced its services in March 1999, obtained a market share of 15.6%, and the fourth Italian operator, which began commercial operations in May 2000, reached a market share of 3.7% at December 31, 2001.

The Regulatory Framework

In a scenario of increasing liberalization, the decisions taken by the National Regulatory Agency have greater impact. The most significant measures taken by the National Regulatory Agency were the designation of TIM and Omnitel as providers with considerable market strength in terms of cellular service, interconnection, the definition of new pricing scheduled for fixed-to-mobile communications, and the introduction of mobile number portability.

TIM's role in the New Economy. The opportunities offered by new technologies will accelerate the Information and Communication Technology (ICT) convergence process, linking the two currently fastest growing businesses: mobile communications and the Internet. TIM's strategic choice with respect to this convergence is the open model. TIM will not focus on Internet content but, rather, it will create alliances with the best content producers in order to provide its customers with the most innovative and the widest range of opportunities, while guaranteeing customers transaction security through TIM's authentication center. This is the context in which the strategic partnership with SEAT and agreement with YAHOO Europe in May 2000 will operate.

Traditional Business and Value Added Services. The development of new advanced services will necessarily lead to changes in TIM's revenue structure. Value Added Services will undoubtedly account for a rising proportion of revenues compared to those generated by voice traffic. TIM's growth will be increasingly dependent on its ability to develop data traffic and innovative services.

Technological development in the WAP, SIM Toolkit, and UNI.TIM platforms will generate new business models based on the capability of offering information and advertising through mobile phones and of executing an increasing number of complete commercial and banking transactions.

This means the mobile economy will play a fundamental role in the new economy as a whole, and it is one of the segments with the highest potential growth rates and profitability.

TIM will seek out commercial synergies with web-oriented companies in the market, which will increasingly demand mobile services (information and media, on-line banking and trading, geographic positioning information system). A further objective will be the consummation of partnerships with prime content and service providers to develop m-commerce.

REGULATION

Overview

The legal framework for the regulation of the telecommunications sector in Italy has been extensively revised in recent years. This revision includes the liberalization of substantially all telecommunications services including the provision of fixed-line public voice telephony services and the operation of networks to support the provision of such services, which were opened to competition as of January 1, 1998. Most importantly, the legal framework for regulation of the telecommunications sector in Italy has been completely transformed through the formation of the National Regulatory Agency in accordance with the Maccanico Law, which implemented the Framework Law, and the adoption of the Telecommunications Regulations by the Italian Government pursuant to Law No. 650 of December 23, 1996 ("Law 650") and Law No. 189 of July 1, 1997 ("Law 189") to implement a number of EU directives in the telecommunications sector. Effective August 1, 1997, the former Ministry of Posts and Telecommunications changed its name to the Ministry of Communications pursuant to the Maccanico Law. The Telecommunications Regulations (Presidential Decree no. 318 of September 19, 1997) became effective on October 7, 1997, and have been implemented by specific regulations. The Framework Law in general aimed at:

- ensuring the improvement of competition and efficiency in the telecommunications sector;
- establishing adequate quality standards;
- ensuring access to telecommunications services in a homogeneous manner throughout Italy;
- defining a clear and transparent tariff system based on the "price cap" method which, pursuant to the Maccanico Law, would apply to Telecom Italia's fixed public voice telephony services for up to two years starting on August 1, 1997. The National Regulatory Agency with Order 171/99 applied the price cap to Telecom Italia fixed public voice telephony from August 1, 1999 to December 31, 2002; and
- protecting consumers' and users' interests.

The Telecommunications Regulations completed the liberalization of the provision of all telecommunications services and the operation of all telecommunications networks in Italy, effective from October 7, 1997, except for the provision of fixed public voice telephony services and the operation of telecommunications networks to support provision of such services, which were liberalized as of January 1, 1998. Restrictions on other operators providing telecommunications services, other than fixed-line public voice telephony services and the operation of telecommunications networks, had been lifted by several previous measures, including the National Telecommunications Plan referred to in a Ministerial Decree of April 6, 1990 (the "NT Plan"), Law Decree No. 55 of February 11, 1997 (satellite communications) and Law Decree No. 103 of March 17, 1995 ("Decree 103")and its implementing decrees and regulations (data communications, voice telecommunications for closed user groups and Value Added Services).

The Telecommunications Regulations contain provisions concerning:

- the granting of general authorizations or individual licenses to provide telecommunications services;
- universal service obligations and the mechanism for funding the net cost of such obligations;
- access deficit contributions;
- special obligations imposed on operators having significant market power, including the determination of interconnection charges using principles of cost orientation;
- numbering, carrier selection and number portability;

- right of way; and
- the essential requirements that must be complied with in the provision of services and when interconnecting between public telecommunications networks.

The National Regulatory Agency has established and will continue to establish detailed regulations governing the telecommunications sector and will monitor their application, while the Ministry of Communications will retain the responsibility for defining telecommunications policy in Italy. See "—The Telecommunications Regulations and Implementing Regulations".

The activities of Telecom Italia and TIM were subject to the terms and conditions of their public operating concessions (the "Public Concessions") which were the basis under which telecommunication services were provided by Telecom Italia and TIM prior to adoption of the Telecommunications Regulations. The Public Concessions were expected to be made consistent with the new regulatory framework by January 1, 1999, as required by the Telecommunications Regulations but the National Regulatory Agency started the procedures to achieve such amendments only at the end of December 1999. See "—Public Concessions".

Since January 2001 Telecom Italia has been operating pursuant to a license (Order 820/00/cons). See "—The Telecommunications Regulations and Implementing Regulations—Authorizations and Licensing".

Other significant telecommunications measures include Ministry of Communications decrees, Presidential decrees and other regulations as well as orders of the National Regulatory Agency issued since its formation.

The National Regulatory Agency and the Maccanico Law

The National Regulatory Agency consists of a President that has been appointed by the Italian Government through a Presidential decree, a Committee for Infrastructures and Networks, a Committee for Products and Services and the Council. Each of the Committees' members is selected by the Italian Parliament (four by the Senate and four by the Chamber of Deputies) and appointed through a Presidential decree. Each of the Committees and the Council is responsible for establishing regulations for their specific areas.

The Committee for Infrastructures and Networks is responsible for, among other things, allocating radio frequencies relating to telecommunications services; defining objective and transparent criteria for establishing tariffs for interconnection and network access; regulating relationships among telecommunications companies; settling disputes regarding interconnection; and defining the scope of the universal service obligation and the operators subject to it, together with criteria for calculating and sharing its costs.

The Committee for Products and Services is responsible for, among other things, regulating product quality and conformity with EU directives governing the relationship between companies controlling fixed or mobile telecommunications networks and telecommunications service providers.

The Council is responsible for adopting regulations establishing criteria for issuing licenses for the telecommunications sector and for TV and radio activities (including cable and satellite broadcasting).

The Framework Law provides that the National Regulatory Agency shall cooperate with the Italian Government and the Parliament, advising and assisting them in several areas:

- preparation of regulations in the telecommunications field;
- preparation of drafts for renewal of and amendments to concessions, authorizations, and program contracts (*contratti di programma*), which are usually multi-year agreements between the relevant Ministry and the concession holders concerning quality of service and tariffs;
- supervision of the procedures and requirements for adopting general authorizations and issuing individual licenses, with reference to matters such as network access and interconnection conditions;

- establishment of the criteria to be followed by operators in determining tariffs;
- monitoring operators to ensure their compliance with such tariff criteria;
- issuance of directives aimed at ensuring accounting separation between different activities carried out by the same operator;
- monitoring of the performance of services to ensure compliance with contracts and qualitative levels of service;
- issuance of directives regarding quality of services;
- examination of complaints filed by users and customers in relation to quality of services and the level of tariffs;
- control of steps taken by operators to ensure equal treatment of their customers and verifying periodically the quality of the service provided; and
- control of operators' compliance with the general principles issued by the Italian Government and the National Regulatory Agency in relation to public services.

The National Regulatory Agency has been operational since June 1998.

The National Regulatory Agency has investigative powers, as well as the authority to impose sanctions on operators who do not comply with their directives and resolutions. In addition, the National Regulatory Agency is entitled to propose to the Ministry of Communications the revocation and/or suspension of general authorizations and individual licenses in the event of repeated violations by the holder. The Maccanico Law also permits the National Regulatory Agency to limit access to networks for security reasons.

The Telecommunications Regulations and Implementing Regulations

The provisions contained in the Telecommunications Regulations, most likely to affect the provision of telecommunications services by Telecom Italia and its competitors relate to:

- authorizations and licensing;
- universal service obligations;
- obligations imposed on operators having significant market power, in particular with respect to interconnection agreements and accounting policies;
- numbering (carrier selection, preselection, and number portability);
- rights of way;
- alignment of Public Concession to the new regulatory framework;
- assignment of UMTS licenses; and
- introduction of new broadband services (ADSL and XDSL).

Authorizations and Licensing

Pursuant to law No. 66/01 of 2001, the Ministry of Communications has the power to grant individual authorizations and licenses.

The Telecommunications Regulations distinguish between a regime of general authorizations, under which operators meeting pre-established conditions determined by the Ministry of Communications may provide telecommunications services or operate telecommunications networks within the scope of such authorizations without individual licenses for the provision of telecommunications services and the operation of telecommunications networks. Operators are required to obtain individual licenses from the Ministry of Communications to provide telecommunications services or operate telecommunications networks not covered by a general authorization. An individual license is required for:

- provision of fixed public voice telephony services;
- mobile and personal communications services;
- creation and operation of public telecommunications networks;
- when specific obligations are to be imposed or limited resources such as frequency bandwidths have to be allocated.

The number of individual licenses can be restricted only to the extent required to ensure the efficient use of radio frequencies or until sufficient additional numbers are made available. The procedures for granting such licenses must be based on objective, non-discriminatory criteria. Mobile and personal communications licenses will be required to permit the provision of services using different technologies and cannot include unjustified technical restrictions.

The Ministry of Communications Decree of November 25, 1997, concerning the issue of individual licenses and general authorizations in the telecommunications sector, pursuant to the Telecommunications Regulations ("License Decree") imposes specific obligations on operators in accordance with the scope of their individual licenses. Moreover, on dominant operators, and thus on Telecom Italia, additional obligations are imposed such as:

- non-discriminatory and cost-oriented interconnection offering;
- publication of a standard list of interconnection tariffs;
- offering of special accesses to the network (*i.e.*, access at network termination points other than the standard ones);
- accounting separation between the interconnection offering and other activities carried out by the operator;
- carrier selection and number portability (see also "—Special Status of Operators Having Significant Market Power" and "—Numbering"); and
- carrier selection should be considered both as "easy access" and "equal access".

The Ministry of Communications issued, on February 5, 1998, a decree regarding fees to be paid by authorized and licensed operators, specifying the fees the latter will have to pay to refund the relevant administrative costs incurred by the National Regulatory Agency and the fees for the assignment of frequencies and numbering resources.

Telecom Italia (but not TIM) has been operating under a license regime since January 2001.

Universal Service Obligations

Under the Telecommunications Regulations, the universal service obligations include the provision of fixed-line public voice telephony service, publication of telephone directories and provision of subscriber information services, public payphones, free emergency call services and special services for disabled or disadvantaged people. To date Telecom Italia is the only operator subject to the universal service obligations, although similar obligations could be imposed on other operators. In such an event such other operators will be required to provide all or part of the services included in the universal service obligations on all or part of the national territory, under reasonable and non-discriminatory conditions. The net costs for the provision of the universal service is calculated on a long-run forward-looking incremental cost basis. The telecommunications operators providing fixed-line public voice telephony service or mobile and personal communications services are required, under certain circumstances, to contribute to such costs.

In compliance with Ministry Communication Decree of March 10, 1998, Telecom Italia submits yearly (within March 31 of each year) the evaluation of the net cost of the universal service to the National Regulatory Agency. The National Regulatory Agency determines if the net cost represents an unfair burden on Telecom Italia and, in that case, appoints an independent Advisor to audit the cost evaluation. Before July 1 of each year, the National Regulatory Agency determines the final evaluation of the net cost, taking into account any indirect benefits, and informs the Ministry of Communications of the amounts due from each operator called to contribute.

By July 15 of each year, the Ministry of Communications publishes the amount due by the operators obliged to finance universal service, which has to be paid within August 15th . Telecom Italia, as the operator required to provide the universal service, receives payment from the Ministry of Communications on September 15 of the same year.

In accordance with the Telecommunication Regulations, Telecom Italia submitted the net cost of providing universal service for the first time for the year 1998. The National Regulatory Agency concluded that for 1998 the costs of such service were not an unfair burden for Telecom Italia. By March 31, 2000 Telecom Italia filed the net costs for 1999. The National Regulatory Agency appointed an independent Advisor to audit such net costs. With Order 8/00/CIR of August 1, 2000, the National Regulatory Agency recognized a net cost for the provision of the universal service in the year 1999 of €62.4 million. The operators obliged to contribute to finance such net cost were: (a) Telecom Italia (57.1%); (b) TIM (28.1%); (c) Omnitel (13.8%), and (d) Infostrada (1%).

With Order 8/00/CIR Telecom Italia was requested to provide an assessment on the net cost foreseen for the year 2001 together with information regarding areas and customers estimated as not profitable, in order to allow the National Regulatory Agency to launch a public consultation aimed at determining the guidelines for the provision of the universal service on a competitive basis. On January 31, 2001, pursuant to the same Order, Telecom Italia filed its evaluation for the year 2001. On July 12, 2001, the National Regulatory Agency opened a public consultation in order to assess the possibility of using a bidding procedure for the assignment to operators, other than Telecom Italia, of all or part of the obligations relating to the universal service. The outcome of the consultation was published on January 17, 2002. The National Regulatory Agency is still evaluating whether to establish a bidding procedure for the offer of the universal service.

On March 31, 2001, Telecom Italia filed the evaluation of the net cost for the year 2000. With resolution No. 23/01/CIR of November 21, 2001, the National Regulatory Agency recognized a net cost of € 58.9 million, of which Telecom Italia shall contribute 48.3%. Other Operators obliged to contribute to finance such net cost are: TIM (31.4%); Omnitel (18.9%), and Infostrada (1.4%).

In compliance with the timetable of the National Regulatory Agency for 2002, on April 30, 2002, Telecom Italia submitted its evaluation of the net cost for the year 2001 for providing universal service. The National Regulatory Agency is in the process of appointing the independent Advisor to conduct the audits of the 2001 cost.

Regarding the net cost of 1999 and 2000, reimbursements have not yet been paid to Telecom Italia by the other operators, because such operators have instituted a claim in front of the Administrative Court. On January 27, 2002 the Administrative Court issued a decision in favour of the Other Local Operators only for procedural reasons. Consequently, the procedure for the evaluation of the net cost for 1999 shall be re-opened.

In December 2001, the National Regulatory Agency published rules designed to grant to low income and to disabled customers certain reductions of the monthly rental fee for voice telephony services.

Special Status of Operators Having Significant Market Power

Under the Telecommunications Regulations, telecommunications operators operating fixed-line or mobile networks, or offering fixed public voice telephony services, leased lines or international circuits, are subject to special obligations with respect to interconnection and accounting policies if they have significant market power. An operator is presumed to have significant market power if its share of the relevant market is greater than 25%, although the National Regulatory Agency may determine that an operator having a market share greater than 25% does not have significant market power, in view of the operator's ability to influence market conditions and its access to financial resources, or that an operator with a market share lower than 25% does have such power. In April 1998, Telecom Italia was identified as an operator having significant market power in the markets of fixed telecommunications networks, fixed-line public voice telephony services, leased lines and interconnection services. Telecom Italia is the sole operator identified as having significant market power for the above-mentioned markets. In April 1998, TIM was identified as having significant market power in the market of mobile telecommunications services. See "—EU Telecommunications Law—The 1999 Review".

With order 197/99 the National Regulatory Agency in September 1999 also determined that TIM and Omnitel had significant market power for mobile telecommunications services and for domestic interconnections. The National Regulatory Agency reviews and evaluates significant market power operators every year. In 2001, the National Regulatory Agency started a market analysis to identify the operators with significant market power in the year 2000. The outcome of the analysis is pending.

On April 8, 2002 law No. 59/02 which regulates the economic conditions to be applied by the operators having significant market power to the Internet service providers was enacted. The law provides that the ISPs must have access to the same economic conditions applied to the operators with individual license. Moreover the law 59/02 identifies the new relevant market "Internet Access" and assigns to the National Regulatory Agency the duty to identify the operators having significant market power in that market. The National Regulatory Agency held a public consultation on this issue which concluded on May 29, 2002. According to the deadline established by law 59/02, the National Regulatory Agency should have identified the Operators by June 12, 2002. To date the decision is still pending.

Considering that competitors of Telecom Italia are unlikely to have significant market power in the fixed-line sector in the near future, Telecom Italia expects that for some period of time it will have to compete with providers not subject to these requirements.

Interconnection. Telecommunications operators providing fixed-line public voice telephony services, mobile telecommunications services or leased line systems and having significant market power are required to negotiate and enter into interconnection agreements at the request of other operators wishing to provide telecommunications services, to apply non- discriminatory terms and to communicate copies of their interconnection agreements to the National Regulatory Agency. Public fixed network operators and leased line service providers having significant market power are required to publish a Reference Interconnection Offer (RIO). As required by EU Directive 96/19, Telecom Italia published its RIO on July 1, 1997. Such list was subject to approval by the National Regulatory Agency. The Ministry of Communications Decree of April 23, 1998, published on June 10, 1998, pertaining to the interconnection agreements ("Interconnection Agreements Decree") also provides specific implementing rules to be applied to interconnection agreements to be executed by telecommunications operators having a significant market power and providing fixed public voice telephony services, mobile telecommunications services or leased lines systems. Such rules deal with, among other things, nondiscriminatory and transparent practices, economic offering conditions (based on actual costs, including a reasonable return on investments), accounting separation and the content of the RIO to be published by the above mentioned operators, except those operating mobile networks. The economic conditions included in the RIO must range between the minimum and maximum thresholds fixed by the Recommendation of the European Commission C(98)50, with interconnection tariffs exceeding the maximum thresholds to be duly justified by the concerned operators.

On July 15, 1999, Telecom Italia submitted a new costbased RIO. Prices proposed were consistent with the thresholds fixed by the Recommendation of European Commission 98/511/CE (Best Practice 1999). With Order 1/00/CIR of February 2000 the National Regulatory Agency established some modifications to be introduced in

Telecom Italia's RIO 1999, including the retroactive effect from January 1, 1999 for interconnectionprices. In the same Order the National Regulatory Agency fixed terms and a deadline for publication of the Reference Interconnection Offer 2000. As a result, on April 3, 2000, Telecom Italia published the RIO 2000, which has been evaluated by National Regulatory Agency Order 10/00/CIR. Consequently, Telecom Italia published a new RIO for the year 2000, consistent with the new order, which increases interconnection services (*i.e.,* access to non-geographical numbers for dial-up Internet) and defines service level agreements.

On September 7, 2001 Telecom Italia published the RIO 2001 concerning interconnection and unbundling of the local loop services. The RIO 2001 was approved, with certain technical and economic amendments, by the National Regulatory Agency on March 4, 2002. On April 18, 2002 Telecom Italia published the RIO 2002 for Interconnection and Unbundling 2002, which is currently under evaluation by the National Regulatory Agency. There is no deadline for the outcome.

With regard to interconnection services:

- in Resolution No. 18/01/CIR of August 7, 2001, the National Regulatory Agency established the technical and economic conditions for billing services with the risk of non-payment for access by Telecom Italia subscribers to non-geographical numbers belonging to other operators and the rates for the partial circuits for the interconnection of dedicated lines;

- in Resolution 13/01/CIR Telecom Italia was authorized not to insert the economic conditions for the routing of international traffic of other operators towards the United States, Canada, Switzerland, Norway or the member states of the European Community; and

- with regard to direct calls to Internet, Resolution No. 25/01/CIR establishes that Telecom Italia should introduce the new flat-rate interconnection rate known as "FRIACO" (the licensed operators pay a fixed charge instead of an amount based on the minutes of interconnection). On March 12, 2002, the National Regulatory Agency issued Resolution No. 5/02/CIR, approving Telecom Italia's flat interconnection rate, but reducing the prices proposed by the Company.

On April 30, 2002 Telecom Italia published the Reference Offer on FRIACO.

According to Law 59 of April 8, 2002, Internet Service Providers also have the right to be granted the same economic conditions applicable to the other licensed operators according to the RIO. The National Regulatory Agency has to define a specific regulation.

On May 15, 2002 the National Regulatory Agency approved a resolution on non discrimination criteria in interconnection and wholesale market between Telecom Italia and the other licensed operators: Telecom Italia shall provide the same conditions to the other licensed operators as applied to its retail units: obligations of accounting separation, administrative separation between network and retail units, network cap in the RIO and price squeeze tests for retail offers.

Local Loop Unbundling. With Order 2/00/CIR issued on March 16, 2000 the National Regulatory Agency published the general guidelines regarding the services that must be offered by Telecom Italia on an unbundled basis: twisted copper pairs; fiberoptics; access extension (lines between switches), and digital transmission channels (*i.e.,* digital circuits between the local office of Telecom Italia and the operator's point of presence) and the related economic pricing criteria, based on fully distributed historical costs. The Order allows other operators to have direct access to end users by leasing the network components from Telecom Italia.

Telecom Italia appealed this Order to the *Tribunale Amministativo Regionale del Lazio* (TAR Lazio), in particular with respect to the inclusion of fiberoptics in the mandatory offer and the costing criteria. The decision is still pending. On May 12, 2000, Telecom Italia put forward a Reference Offer for Local Loop Unbundling, for approval by the National Regulatory Agency. The National Regulatory Agency finally issued on January 2001 Order 14/00/CIR setting the rates for the unbundled services (€11.46 /month for a single POTS/ISDN BRA copper pair, €12.43 /month for ADSL conditioned copper pair and €22.20 /month for 2 HDSL conditioned copper pairs).

During 2001, in line with the suggestions made by the National Regulatory Agency, special areas were made available in exchanges to accommodate other operators with the aim of unbundling local loops. At December 31, 2001 Telecom Italia handed over equipped technological areas to operators in 748 exchanges. In addition, following Resolution No. 24/01/CIR, on December 12, 2001, Telecom Italia presented its rate plan to the National Regulatory Agency for shared access and sub loop (shared access to the local network and access to line boxes).

On April 18, 2002 Telecom Italia published the Reference Offer of Local Loop Unbundling for 2002, with price reductions for copper pair. On March 2002 around 17,400 unbundled lines were in place, 27 licensed operators requested co-location, 1,043 local switches for co-location were requested by licensed operators and 919 sites were ready for co-location.

Accounting Policies. Operators having significant market power are required to have an accounting system showing their costs in a transparent manner. Upon request, such operators must provide the National Regulatory Agency with a description of their cost accounting system to verify compliance with the provisions of the Telecommunications Regulations. Moreover, operators of fixed public networks and mobile networks and providers of fixed public voice telephony services, mobile telecommunications services and leased line services with significant market power must keep a separate accounting system distinguishing between the activities related to the building and operation of public telecommunications networks, the activities related to the provision of telecommunication services, the interconnection offering and the universal service provision.

The regulatory accounting reports, including the access-deficit evaluation and the related methodology for the year ended December 31, 1998, have been audited and approved by the independent Advisor appointed by the National Regulatory Agency. In accordance with the Telecommunication Regulations, on September 4, 2000 Telecom Italia submitted the Regulatory Accounting Reports for the year ended December 31, 1999 to the National Regulatory Agency. To date, the National Regulatory Agency has not appointed an independent Advisor to conduct the audits of these accounts.

The regulatory accounting reports, including the access-deficit evaluation and the related methodology for the year ended December 31, 1998, have been audited and approved by the independent Advisor appointed by the National Regulatory Agency. In accordance with the telecommunication regulations, on September 4, 2000 Telecom Italia submitted the Regulatory Accounting Reports for the year ended December 31, 1999 to the National Regulatory Agency.

On September 14, 2001 the Regulatory Accounting Reports for the year ended December 31, 2000 were also submitted to the National Regulatory Agency. Due to a delay in the appointment of the independent advisor, both the 1999 and the 2000 reports have not been audited. The audit of the 1999 Report started in March 2002 and is still in progress. On June 17, 2002, the National Regulatory Agency issued Order 152/02 CONS which requires Telecom Italia to provide more detailed accounting reports on a current cost basis (fully allocated costs); the cost basis previously adopted was the historical one.

During year 2001 the National Regulatory Agency issued an order which raised the allowed return on capital employed - WACC (weighted average cost of capital) for regulatory purposes from 12.5% to 13.5% before taxes.

Numbering

In accordance with the Telecommunications Regulations and with Order 3/99/CIR, 4/99/CIR, 4/00/CIR, 7/00/CIR, 9/00/CIR, 12/01/CIR, 19/01/CIR, and 7/02/CIR, the National Regulatory Agency issued regulations related to Number Portability and Carrier Preselection as described below.

Number Portability ("NP")

Since February 2000, following the National Regulatory Agency Order 4/99/CIR and 7/00/CIR, which is consistent with EU Directive 98/61/CE, Service Provider Portability (SPP) in fixed networks was introduced, including non-geographic numbers (Premium Rates, Freephone Numbers, Splitting Charges).

Service Provider Portability allows an end user to retain his number independent of the organization providing service, in the case of geographic numbers at a specific location (same Local Area) and in the case of other than geographic numbers at any location. Implementation of SPP is related to negotiations and technical implementation timing among operators. Telecom Italia has upgraded its network and operational systems to be in a position to offer NP consistent with the requirements of the regulations. NP for non-geographic numbers started in May 2000. NP for geographic numbers is planned to consistently develop with unbundling of the local loop.

The roles regarding number portability for mobile services was established during 2001 and commenced in April 2002. The impact of this service on fixed networks (fixed/mobile calls) will only take effect from April 2003.

On March 28, 2002, the National Regulatory Agency issued Order 7/02/CIR: by November 30, 2002 the National Regulatory Agency will determine the price of Mobile Number Portability ("per number costs") which shall be equal to the one-off price that the operator receiving the customer/recipient must pay to the operator giving the customer/donor the price. Mobile Number Portability will apply starting January 1, 2003. In the same order the National Regulatory Agency has anticipated that "per cost number" will not be higher than the price applied to fixed-line services as established by Order 10/00/CIR (approximately €10).

Carrier Preselection. Carrier selection (call by call) has been operational since the end of 1998 for long-distance (national and international) and fixed mobile calls. Carrier selection for local calls has been available since January 2000.

Since February 2000, in accordance with Order 3/99/CIR and 4/00/CIR, which introduced new obligations for the provision of Carrier Preselection (*i.e.*, timing, minimum daily number of user activations), customers can make inter-district, international calls and calls to mobile networks using a pre-selected carrier as an alternative to Telecom Italia, without dialing the identifying code required. Since July 2000 customers have also been able to make local calls (within the same district) with a pre-selected operator.

Numbering Plan. In July 1999, the National Regulatory Agency adopted a new numbering plan (Order 1/CIR/99) which provided for the reorganization of numbering per services (first digit) by September 2001 and introduced some new codes for new services.

Order 6/00/CIR of June 2000 defined the new numbering plan, with specific non geographical numbers for dial up internet access. Order 11/00/CIR solved critical issues on scarcity of numbers (extension to 11 digits of numbering plans).

Rights of Way

The Telecommunications Regulations prohibit public authorities from discriminating in the granting of rights of way for the installation of public telecommunications infrastructures. The National Regulatory Agency and the local public authorities can promote the sharing of such structures and rights of way. If the access to such rights of way cannot be granted to a new operator, the National Regulatory Agency and the local public authorities can allow the access to existing infrastructure. The parties involved agree on the commercial terms of the sharing of the existing infrastructure.

Public Concessions

As a result of the Telecom Merger which took place in August 1994, Old Telecom Italia succeeded to the concessions and associated agreements for telecommunications services for public use of the companies previously providing these services (formerly SIP, Italcable, Telespazio, Iritel and Sirm).

The Telecommunications Regulations provided that by January 1, 1999, the Public Concessions had to be modified to make them consistent with the new regulatory framework, on the initiative of the National Regulatory Agency, with the aim of bringing into line the dispositions contained in the Telecommunications Regulations. With the expiry of this limit, all special or exclusive rights held by Telecom Italia under the former monopoly system, and not compatible with the introduction of competition, were to be considered abolished.

The National Regulatory Agency opened an inquiry on December 15, 1999 into bringing the Public Concessions into line after a significant delay, modifying the content of the Public Concessions with the aim of eliminating the special and exclusive rights and obligations which were in conflict with the Telecommunications Regulations, such as approval by the Ministry of Communications of the long-term and technical plans of Telecom Italia, the installation and operating of public telephone facilities in specific areas of the country, and the development of services in small centers.

At the end of its inquiry the National Regulatory Agency issued three individual licences and a general authorization to Telecom Italia - formally notified on January 19, 2001:

- An individual licence for the installation and provision of public telecommunications networks, and for the provision to the public of voice telephone services (modification of the concessions and associated agreements formerly granted to SIP, Iritel and Italcable).
- An individual licence for the installation and operation of a network of coastal stations with the aim of providing mobile maritime services via Inmarsat satellite (modification of the concession and associated agreement formerly granted to Iritel).
- An individual licence for the plant and operation of radio-electric boarder stations, and the supply of mobile maritime services and mobile services via satellite through Inmarsat terminals (modification of the concession and associated agreement formerly granted to Sirm).
- Authorization for the supply of satellite network and communications services (modification of the concession and associated includes a list of agreement formerly belonging to Telespazio).

Each individual licence includes a list of specific charges, drawn up on the basis of the indications given by the ministerial Decree of November 25, 1997, containing "Provisions for the issue of individual licences in the telecommunications sector".

The licences and authorizations issued to Telecom Italia have the same expiry date as the Public Concessions (2012, according to Article 14 of Law No. 359/92, containing "Urgent measures for the rehabilitation of public finances").

Pursuant to Law No. 448 of December 23, 1998, a new fee was instituted from January 1, 1999 to take the place of the license fee payable under the previous regulatory regime. The amount of the operating fee is based on a sliding scale (2.5% for 2001, 2.0% for 2002 and 1.5% for 2003). The Ministerial Decree of March 21, 2000 established that the fee should only be applied to revenues from installation activities and the supplier of public telecommunications networks, local telephone service and mobile and personal service.

Under its Public Concession, Old Telecom Italia had the right to provide all mobile public telecommunications services, regardless of the technologies used. These rights were transferred to TIM as a consequence of the TIM Demerger. The duration of TIM's GSM concession is 15 years, commencing on February 1, 1995.

The Telecommunications Regulations provided that by January 1, 1999, the existing GSM concessions (Omnitel also was granted a GSM concession) were to be modified to make them consistent with the new regulatory framework. In March 2001 the GSM concessions were transformed into individual licenses with Order 127/01 CONS. On December 13, 2001, the Cabinet of Ministers met and approved the Ministry of Communications proposal to introduce a regulatory scheme increasing the duration of individual licenses in the telecommunications sector from fifteen to twenty years. The extension applies to all issued licenses and, taking into consideration the continuous growth in mobile radio services and subsequent increase in competiveness, guarantees all operators a longer operating time horizon.

On the basis of this scheme, which has already been approved by the Communications Guarantee Authority but has not yet been formally implemented, TIM's licenses (TACS, GSM, UMTS and voice telephony) will be extended to twenty years, to the extent they have not been superseded by relevant domestic and EU regulations.

Licensed Operators

In April 2002, the number of licenses for the provision of both fixed voice telephony service and building public telecommunications networks and for mobile and satellite services granted by the Ministry of Communications and the National Regulatory Agency was more than 235.

In the segment of mobile telecommunications services, one license was granted to the third national mobile operator (DCS-1800, GSM) Wind, which started on March 1, 1999, and another license (only for DCS-1800) was granted to the fourth national operator BLU, which started on May 16, 2000. Wind is the sole Italian telecommunications operator that was granted both a mobile and a fixed license at the time it started its operations. Fixed licenses have also been awarded to TIM (February 2001) and Omnitel. Mobile telecommunications services based on the DSC-1800 technology are also provided by the two GSM operators, TIM and Omnitel.

UMTS

The Italian government awarded five UMTS licenses in Italy in December 2000. TIM, together with Omnitel S.p.A., WIND S.p.A., Andala S.p.A. and IPSE S.p.A., were awarded licenses to provide the third generation mobile services. TIM has committed to pay €2.4 billion for its license, with approximately €2 billion having been paid in December 2000 and €117 million having been paid in November 2001. The remaining €234 million will be payable during 2002 and 2003. The licenses are valid for 15 years starting January 1, 2002.

XDSL/ATM Broadband

In December 1999, Telecom Italia received temporary authorization from the National Regulatory Agency for the wholesale offering of ADSL/ATM access service to Other Licensed Operators and Internet Service Providers. In February 2000, Telecom Italia started the "always on" retail offering for fast internet access. The ADSL 640 wholesale offer has been partially modified by the National Regulatory Agency with order 217/00/CONS issued in April 2000. In February 2001, the National Regulatory Agency approved the Permanent Virtual Circuit (ADSL up to 2 Mbit/s and HDSL up to 155 Mbit/s technologies) offer as presented by Telecom Italia and authorized Telecom Italia to offer XDSL retail services branded as RING and FULL BUSINESS COMPANY from April 2001. By June 2001, ADSL 640 and XDSL wholesale services will be available in 163 districts (out of 231 total districts).

Tariff and Pricing Policy

Overview

Telecom Italia operates in both domestic and international markets. Its pricing policy is established in accordance with existing regulations for Regulated Services, and in accordance with market and competitive factors.

Fixed Network. Management believes that it is essential for Telecom Italia to continue rebalancing its tariff structure and to have the flexibility to price its telecommunications services selectively in order to counter increased competition.

With Order 171/99 the National Regulatory Agency described the rules to be applied by Telecom Italia in setting the tariffs for the services offered. The Agency distinguishes two kinds of tariffs. The first requires prior approval by the Agency and applies to:

- services under a price-cap obligation (RPI-X): the "X" is differentiated according to different levels of competition in the provision of the various telecommunications services (such as installation, connection charge, local voice calls, long-distance voice calls, international voice calls);

- services under cost-orientation and accounting separation obligations: Interconnection, Special Access and Leased Lines, due to the significant market power of Telecom Italia in the provision of these services; and

- services to be kept "affordable", on the basis of the regulation concerning the universal service obligation.

The second category of tariffs requires only a prior communication to the Agency itself and applies to so-called value added services for which a high level of competition exists.

Mobile Network. GSM prices are established autonomously by each of the GSM Operators, taking into account, among other factors, structure and levels of prices/tariffs for interchangeable services (analog mobile services and basic telephony services) and the policies of the main European operators, subject only to the obligation to give the Ministry of Communications or the National Regulatory Agency, as applicable, 30 days' notice of changes in prices. Since June 1998, subscribers' TACS traffic fees were liberalized, so that TIM can modify all TACS prices according to its own strategy (but such fees may not be set lower than those for GSM).

Regulation of Tariffs and Pricing

Until the adoption of the Framework Law, the criteria applicable to setting tariffs for exclusive services provided by Telecom Italia under its Public Concessions were established in accordance with the Tariffs Restructuring Plan (the "Plan"). The Plan was prepared by the Ministry of Communications in accordance with Law 58 and approved by the Interministerial Committee on Pricing ("CIP") in December 1992. Tariffs established under the Plan adopted an informal price cap scheme. The Plan governed tariffs with respect to domestic and international fixed public voice telephony, mobile telecommunications, paging and direct links (cable and satellite). The tariff structure for fixed public voice telephony services had three main components: a connection charge (initial connection or transfer), a subscription charge and call charges (local, national and international). Call charges were fixed on the basis of their duration as well as distance, time of call and international areas and on the impulse's value. Discounts related to the number of impulses and to the users' category (residential or business) were provided for under the Plan. In April 1996, the Interministerial Committee for Economic Planning ("CIPE") published specific guidelines for the regulation of public telecommunications services, with particular reference to the price cap method and the quality standards required to be applied to such services.

On July 28, 1999, the National Regulatory Agency issued Order 171/99 and introduced the price cap mechanism to promote productivity and efficiency for the incumbent operator over the succeeding three years. The price cap mechanism relates to:

- rental and connection charges;
- local charges;
- trunk charges; and
- international charges.

The Order stated that, on a yearly basis, the reduction of overall customer expenditure had to be less than or equal to RPI + 4.5%. In the same Order, the National Regulatory Agency introduced specific subcaps on rental fees (RPI + 1%), local calls (RPI + 0%) and overall expenditure of residential customer (RPI-2.5%).

Following the EU Commission infringement procedure against Italy concerning the rebalancing of voice telephony tariffs (subscription fees, and charges for local, inter-district and international calls), on December 11, 2000, the National Regulatory Agency issued Order 847/00/CONS revising the price cap formulas in effect for rental and installation fees, and charges for local, national and international calls. For the period from January 2001 through December 2002, the price caps in effect are as follows:

General price cap (installation fees; monthly rentals, local, national and international call charges)	RPI	-4.5%
Sub-price cap on overall expenditures of residential users	RPI	-2.5%
Sub-price cap on installation fees and monthly rentals	RPI	+6%
Sub-price cap on local call charges	RPI	+0%

The change compared to the previous price cap formulas is in an increase from RPI + 1% to RPI + 6% in the sub-price cap on installation fees and monthly rental charges.

The general effect of the new price cap formulas for 2001 provided for an increase of up to 8.5% in Telecom Italia's access service charges (*i.e.*, subscription fee) and a reduction of 9.8% in Telecom Italia's traffic charges.

With Orders No. 375/01/CONS and 376/01/CONS of September 26, 2001, the National Regulatory Agency approved the prices of international calls from public telephones and though an operator and created a new list classifying foreign countries according to the various rate zones. In Resolution No. 271/01/CONS of July 4, the Regulator also approved the new price for the "12" directory information service (which is part of the universal service and therefore at a regulated price), of €0.43 + VAT.

Tariffs set on the foregoing basis are proposed directly by the operator to the National Regulatory Agency and, to the extent the National Regulatory Agency does not object within 30 days (reduced from 90 days), the tariffs will be considered to have been approved.

Prices for all other services provided by Telecom Italia may be established without the approval of the National Regulatory Agency. Management believes that the ability to price each service (other than universal services) selectively is important to Telecom Italia's competitive position.

Pricing Policy and Telecom Italia's Tariffs

Tariff Rebalancing. Telecom Italia commenced rebalancing in 1991 with further adjustments approved by the Ministry of Communications in 1993, 1994, 1996, 1997 and 1998, and by the National Regulatory Agency in 1999, 2000 and 2001. The adjustments have progressively rebalanced Telecom Italia's tariffs to align them more closely to underlying costs, taking into account demand for its services, particularly with respect to international calls, and inflation. As a consequence, subscription fees have been raised, while the relationship between tariffs for local and domestic long-distance calls has gradually been narrowed to a current ratio of approximately 1:2.7 for reduced rate calls and 1:3.6 for standard rate calls.

These tariff adjustments caused subscribers' costs to remain unchanged in 1995, and decrease by 2.6%, 3.4%, 1.6%, 3.8%, 4.5% and 4.5% in 1996, 1997 , 1998, 1999, 2000 and 2001, respectively, compared to inflation rates as set forth in the table below.

	Year ended December 31,						
	1995	1996	1997	1998	1999	2000	2001
				(%)			
Inflation Rate	5.4	4.0	1.9	2.0	1.7	2.5	2.7

Rebalancing has been accompanied by a simplified tariff structure which has reduced the number of tariff schemes, and clarification of the price of the services being offered to customers. For example, in the case of domestic fixed public voice telephony services, district (*settore*) tariffs were reduced to the same level as local tariffs effective October 1, 1996 and, in December 1997, the number of zones based on distance was reduced from four to three and those based on time have been reduced from four to two. In December 1997, the local tariff based on duration of calls was extended to all urban networks and the smaller local areas have been enlarged. In March 1998, residential rental fees increased by 6.5%. On January 5, 1999, the National Regulatory Agency published Order 85/98 on tariff rebalancing. Order 85/98 stated that the rebalancing process was to be accomplished in three steps by July 1999. The first step introduced the following tariff changes:

- from January 6, 1999, long-distance national calls (peak time, maximum distance) were reduced by 6% and international calls were reduced by 10% (for calls to the U.K., Germany, Canada, U.S.A., Australia, Japan, Brazil); and

- from March 1, 1999, bimonthly subscription fees were increased both for residential (+ 3%) and business customers (+ 4%).

On June 25, 1999, the National Regulatory Agency published another Order (101/99). This Order stated the following tariff changes:

- from August 1, 1999, long-distance national calls (maximum distance) were reduced by 5% and international calls were reduced by 5.5% (mainly for calls to EU countries);

- from November 1, 1999, charges for calls between local areas within the same "destination code area" were decreased by 58%; and

- from November 1, 1999, bimonthly subscription fees were increased for residential customers by 7.1%.

On July 28, 1999, the National Regulatory Agency issued Order 171/99, introducing the price cap mechanism, which was applied for the first time in 2000. Its effects have been:

From August 1, 2000:

- increase in monthly rentals and installation fees (+ 2.8%)

- decrease in international calls prices (- 13.2%) due to both a reduction of prices and a modification in the number of international tariff zones (reduced from 12 to 7);

From December 28, 2000:

- decrease in long-distance national calls prices (- 10.0%)

From February 1, 2001:

- increase in monthly rentals and installation fees (+ 4.1%)

- decrease in district calls prices (- 23.4%) and long-distance prices (- 7.9%)

Telecom Italia also made the following changes:

From July 1, 2001:

- increase in monthly rentals and installation fees (+ 4.4%)

- decrease in long-distance prices (- 10.6%)

Following the EU Commission infringement procedure against Italy concerning the rebalancing of voice telephony tariffs (subscription fees, and charges for local, inter-district and international calls), on December 11, 2000, the National Regulatory Agency issued Order 847/00/CONS revising the price cap formulas in effect for rental and installation fees, and charges for local, national and international calls. For the period from January 2001 through December 2002 the level of monthly rental sub cap was established at RPI+6% by the National Regulatory Agency's Regulation 847/00/CONS.

With Order 469/01/CONS of December 19, 2001 the National Regulatory Agency established for 2002 the same level of monthly rental sub cap as that of 2001 (RPI+6%). On May 20, 2002 Telecom Italia notified the

National Regulatory Agency of the final tariff changes relating to rebalancing, to be applied from July 1, 2002. Monthly rental for residential customers will increase from € 11.36 to € 12.14.

Additional tariff rebalancing has been in effect since February 1, 2002. Residential basic subscriber charges were increased by 6.3% (from €10.69 to €11.36 a month, net of VAT) while the weekend rate (€0.02582 per minute plus the unit charge when the call is answered and VAT) was extended from 6.30 p.m. to 8 a.m. on weekdays and from midnight until midnight on Saturday, Sunday and public holidays for all local and long-distance calls.

On January 12, 1999, the National Regulatory Agency stated that Telecom Italia is responsible for fixing fixed-to-mobile call tariffs. As a consequence, Telecom Italia was required to renegotiate its interconnection agreements with the three mobile operators and present a proposal for fixed-to-mobile call tariffs. In an Order issued on March 17, 1999, the National Regulatory Agency set fixed-to-mobile call tariffs based on a proposal from Telecom Italia resulting from the renegotiation of its interconnection agreements with the three mobile operators (TIM, Omnitel and Wind). Such new fixed-to-mobile call tariffs were introduced on April 18, 1999. It is estimated that fixed-to-mobile tariffs were reduced, on average, by approximately 12%.

On December 6, 1999, the National Regulatory Agency published Order No. 338/99, on fixed-to-mobile call prices: with this Order new and lower prices became effective on February 17, 2000 in accordance with Telecom Italia's proposal, which takes into account the reduction of termination charges and Telecom Italia retention. In 2001, the National Regulatory Agency concluded the proceedings on interconnection between fixed and mobile networks, begun in 2000, stating that TIM had observed the termination tariff for calls originating from the fixed network indicated in Order 338/99.

In 2001, the National Regulatory Agency published Order No. 485/01 CONS entitled "Guidelines for the regulatory accounting of operators with Significant Market Power" and Order 486/01 CONS that opens a public consultation on introduction of calculation methods for the maximum termination prices (price cap), as applied by operators with Significant Market Power.

The new charging regime provides for tariff levels which vary according to the type of originating calls from Telecom Italia's fixed network (from Residential users, from Business customers, from public Payphones) and according to the called mobile network (BLU, Omnitel, TIM, WIND) and are independent from the type of subscription of the mobile customers (Family, Business).

The overall reduction of customers expenditure has been approximately 29%.

For international traffic, the current rate structure continues to be optimized to correspond more closely with the type and volume of traffic and the evolution of competition in various geographic areas. Volume discounts and discounts based on the calling destination have been offered to business customers under the most recently implemented tariff structure.

For ISDN and telecommunications services provided through INs, tariffs will evolve in line with those for traditional telecommunications traffic, but are expected to involve specific tariff packages to stimulate growth.

Billing

As part of its efforts to increase transparency pursuant to Order 85/98 of the National Regulatory Agency, Telecom Italia introduced per second billing, which, since November 1, 1999, has been provided for each service and for all customers on a permanent basis. Telecom Italia offers itemized billing services free of charge. Resolution No. 78/02/CONS confirmed itemized billing free of charge.

EU Telecommunications Law

Italy is a member of the EU and, as such, is required to implement the directives issued by the EU. Although directives must be incorporated into domestic legislation to be fully effective, a directive or certain provisions of a directive may take effect automatically in a Member State on the prescribed deadline if it is sufficiently clear and specific, even if it is not formally adopted by such Member State by the prescribed deadline. If a directive is not formally implemented by the prescribed deadline, the only remedy available for an interested party is to seek damages against the Member State. Italy is also the addressee of various EU resolutions, recommendations and communications which are not legally binding, although politically important.

EU Directive on Competition in the Markets for Telecommunications Services and Networks

In June 1990, the European Commission adopted a Directive on Competition in the Markets for Telecommunications Services ("EU Directive 90/388"), which opened to competition telecommunications services other than fixed public voice telephony services. In particular, EU Directive 90/388 required the liberalization of circuit and packet switched data transmission, in accordance with regulations promulgated by each National Regulatory Agency. EU Directive 90/388 was formally implemented in Italy by Decree 103/1995.

On March 13, 1996, the European Commission adopted EU Directive 96/19, modifying EU Directive 90/388, which required the introduction of full competition in the telecommunications market, both for services and networks. In particular, EU Directive 96/19 called for liberalization of fixed public voice telephony services and the operation of networks to support such services by January 1, 1998. Pursuant to the Telecommunications Regulations implementing this EU directive and Law 650, the operation of telecommunications networks (other than for providing fixed public voice telephony services) was liberalized on effectiveness of the Telecommunications Regulations, and the offering of the infrastructure for the provision of fixed public voice telephony services has been liberalized since January 1, 1998. Under EU Directive 96/19, Telecom Italia published its standard interconnection offer.

In March 2001, the European Commission published in the Official Journal a notice concerning a draft directive on competition in the markets for electronic communications services, consolidating existing directives on competition in telecommunications market. The draft Directive makes reference to "electronic communications services" and "electronic communications networks" in order to take account of the convergence phenomenon which shapes the information technology, media and telecommunications industry, by bringing together under one single definition all electronic communications services and/or networks involved in the transmission of electromagnetic signals (*i.e.*, fixed, wireless, cable TV, satellite networks). Among other provisions, the draft Directive provides that member States must remove exclusive and special rights in the provision of all electronic communications networks and in the use of radio frequencies. Also, dominant providers of electronic communications services must operate their public electronic communications networks and cable TV networks under separate legal entities. The adoption of the Directive is expected by July 2002.

Satellite Directive

The European Commission also adopted EU Directive 94/46 (the "Satellite Directive") modifying EU Directive 90/388 and the EU Directive 88/301 relating to telecommunications terminal equipment (the "Telecommunications Terminal Equipment Directive"). The Satellite Directive provides for the removal of all special and exclusive rights to import, market, connect, install and maintain satellite telecommunications terminal equipment. Moreover, it removes all special and exclusive rights for the provision of satellite network services, including the establishment and operation of satellite earth station networks, and the offer of space segment capacity and satellite communications services and services that make use of space segment capacity except telex service and voice telephony services. The Satellite Directive was implemented in Italy by Law Decree No. 55 of February 11, 1997.

With Decision No 1215/2000/EC of May 16, 2000 the European Parliament and the European Council extended the application of Decision No 710/97/EC on a coordinated authorization approach in the field of satellite personal communications services in the EU until December 31, 2003. This approach implies that member States coordinate on authorization procedures with a view to authorizing the same satellite personal-communications services throughout the Community.

On June 27, 2001, the European Commission adopted a Communication on the application of the general principles of free movement of goods and services concerning the use of satellite dishes. The Communication states that private individuals should be free to use satellite dishes without undue technical, administrative, urban planning or tax obstacles. The right to do so flows from the free movement of goods and services, which are both fundamental Internal Market freedoms.

CATV

On October 18, 1995, the European Commission adopted EU Directive 95/51, amending EU Directive 90/388, allowing CATV operators to provide to third parties the use of their cable networks to provide all telecommunications services which had been liberalized (*i.e.*, all telecommunications services except for fixed public voice telephony services, which were liberalized as of January 1, 1998). This directive has been implemented in Italy by Law 650 and the Telecommunications Regulations.

On December 9, 1997, the Commission adopted a communication and a proposal for a Directive concerning the review, under competition rules, of joint provision of telecommunications and CATV by a single operator and the abolition of restrictions on the provision of CATV capacity over telecommunications networks. The Directive was adopted on June 23, 1999.

Mobile Telecommunications Directive

On January 16, 1996, the European Commission adopted EU Directive 96/2, liberalizing mobile telecommunications services within the EU (the "Mobile Telecommunications Directive"). The most important elements of the Mobile Telecommunications Directive implemented by Law 189 are the following:

- Mobile telecommunications operators are authorized to construct their own infrastructure for the mobile network or to utilize infrastructure owned by third parties.
- Direct interconnection among mobile networks is to be guaranteed.
- The number of licenses for mobile telecommunications systems may be limited only on the basis of essential requirements and in case adequate frequencies are not available.
- The conditions for granting licenses for access to frequencies and for interconnection to the fixed public telephony network shall be regulated with transparency, proportionality and non-discrimination.
- Licenses to provide mobile telecommunications services using the advanced DCS 1800 digital technology were required to be issued by January 1, 1998.

On December 14, 1998, the European Parliament and the EU Council adopted decision 128/99/EC with the aim at facilitating the coordinated introduction of a third generation mobile and wireless communication system (UMTS) in the Community, on the basis of internal market principles and in accordance with commercial demand.

Commission's Communication Concerning the Introduction of Third Generation Mobile Communications in the EU.

In March 2001, the Commission published a Communication concerning the introduction of third generation Mobile Communications in the European Union. The Communication confirms the confidence the Commission has in the Third generation market perspectives, while recalling the underlying policy objectives in terms of building the Information Society, capitalizing on the success of Second generation, securing jobs, and preserving and expanding the lead the EU has on mobile communications in terms of technology development, competitiveness and service deployment. The Commission intends to begin a dialogue with the member States, operators and manufacturers in order to explore the concrete means to facilitate deployment of Third generation, and, among others, the conditions to permit network infrastructure sharing, which the Commission considers positively. On June 12, 2002, The Commission produced an analysis of the situation of 3G today, adopting a Communication entitled "Towards a full roll out of third generation mobile communication". The Communication provides an overview of the 3G sector, focusing on the technological aspects, the new regulatory framework, the secondary trading of spectrum and on the obstacles to the roll out of 3G networks, such as environmental and local planning issues and health concerns.

Electromagnetic fields

In July 1999, the Council adopted a recommendation on the limitation of exposure of the general public to electromagnetic fields. The recommendation is based on a set of basic restrictions and reference levels as developed by the International Commission on non-ionizing radiation protection (ICNIRP) in the Guidelines for limiting exposure to time-varying electric, magnetic and electromagnetic fields. In accordance with the provisions contained in Recommendation 1999/519/CE, the Commission in April 2002 drew up the first Implementation report confirming the reference levels of exposure limits set by the 1999 Recommendation.

Terminal Equipment

The Telecommunications Terminal Equipment Directive provides for the complete liberalization of the market for terminal equipment, *i.e.*, equipment directly or indirectly connected to the termination of a public telecommunications network used to send, process or receive information. This directive has been implemented in Italy through a series of decrees. Italy has also implemented an EU directive harmonizing procedures for reciprocal authorization of terminal equipment on the basis of common European requirements (EU Directive 91/263).

On February 12, 1998, the European Parliament and the Council adopted the EU Directive relating to telecommunications terminal equipment and satellite earth station equipment, including the mutual recognition of their conformity (98/13/EC). The purpose of this Directive is to merge previous Directives about terminals into a single consolidated text.

On March 9, 1999, the European Parliament adopted EU Directive 99/5, a directive on radio equipment and telecommunications terminal equipment and the mutual recognition of their conformity. This directive establishes a regulatory framework for the placing on the market, free movement, and putting into service, of radio equipment and telecommunications terminal equipment in the EU. The Commission adopted on April 4, 2000 Decision 2000/299/EC establishing the initial classification of radio equipment and telecommunications terminal equipment and associated identifiers.

The ONP Directives

The EU directive relating to open network provision ("ONP" (Council Directive 90/387/EC) (the "ONP Framework Directive") sets out a body of principles for access to public telecommunications networks and services. The principles set out in this directive are intended to harmonize technical interfaces, usage conditions and rate principles throughout the EU and to insure objectivity, transparency and non-discrimination in access to services provided in accordance with ONP segments. The implementation of the general principles set forth in the ONP Directive has been deferred to other directives, such as the EU directive relating to leased lines (Directive 92/44/EC) (the "Leased Line Directive").

The Leased Line Directive, adopted following the ONP Directive, requires Member States to ensure provision of a minimum set of leased lines and to publish certain information concerning the characteristics of the service (*e.g.*, period of supply, duration of the contract and quality standards). It also establishes that, in order to ensure transparency, the relevant tariffs should be on a flat-rate basis, consisting of an initial connection charge and a periodic rental fee. According to this directive, leased line tariffs must be cost oriented. On October 6, 1997, the European Parliament and the Council adopted an EU Directive amending the ONP Framework Directive and Leased Line Directive for the purpose of adaptation to a competitive environment in telecommunications (Directive 97/51/EC). This Directive establishes that the ONP obligations, in the new competitive environment, apply only to organizations with significant market power (25% of relevant market).

On December 13, 1995, the European Parliament and the Council adopted the EU directive relating to ONP voice telephony (the "ONP Voice Telephony Directive") (Directive 95/62/EC), applying ONP regulation to voice telephony services. This directive provides rules for publication of information, quality of services, subscription contracts, tariffs, accounting principles and access and use conditions.

On February 26, 1998, the European Parliament and the Council adopted the EU Directive on the application of ONP to voice telephony and on universal service for telecommunications in a competitive environment (Directive 98/10/EC). This Directive replaces the ONP Voice Telephony Directive, ensures the availability throughout the European Community of good quality fixed public telephony services and defines the set of services to which all users should have access in the context of universal service, in the light of specific national conditions, at an affordable price.

Licenses. On April 10, 1997, the European Parliament and the Council adopted the EU directive relating to general authorizations and individual licenses, establishing a common framework for general authorizations and individual licenses and defining the conditions attached to such authorizations andlicenses (Directive 97/13/EC).

Interconnection. On June 30, 1997, the European Parliament and the Council adopted the EU directive relating to interconnection, establishing a common framework for interconnection obligations and interconnection tariff principles (Directive 97/33/EC). This Directive, that applies to organizations providing publicly available telecommunication services/networks, requires Member States to remove restrictions which prevent commercial negotiation about interconnection in accordance with EU Law. In particular all organizations providing public networks and/or publicly available telecom services:

- have the right and the obligation to negotiate interconnection;
- must publish terms and conditions for interconnection, including points of interconnection and interface specifications (reference interconnection offer);
- must offer interconnection services applying ONP principles of non-discrimination and transparency; and
- must introduce accounting separation for interconnection.

In late 1997, the Commission adopted Part 1 of a "Recommendation on Interconnection in a Liberalized Market", which was officially approved on January 8, 1998. The purpose of this Recommendation was to make available to the national regulatory authorities in the Member States information concerning best practice for interconnection pricing and accounting separation, based on experiences from liberalized telecommunications markets around the world. In particular, Part I of this Recommendation concerned the pricingof call termination on networks operated by operators with significant market power. The Commission recommended maximum interconnection charges to be applied by such operators starting January 1, 1998. Part 2 of the Recommendation, which was officially adopted on April 8, 1998, aimed at ensuring transparency in the methods used for calculating interconnection charges. This Recommendation concerned the implementation of accounting separation and cost accounting systems by operators identified by their national regulatory authorities as having significant market power in accordance with Directive 97/33. The purpose of accounting separation, promoting the principles of transparency and cost orientation is to provide an analysis of information derived from the accounting records which reflect the performance of the different segments of the business as if they had been operated as separate businesses. The Commission adopted an amended Recommendation in March 2000. It has reviewed the best current practice charges for 2000 and sees no need to change them for 2001. On February 22, 2002 the Commission adopted a recommendation introducing further amendments to Recommendation 98/195/EC (previously amended by Recommendation 2000/263/EC), phasing out the Commission's benchmarking exercise for call termination charges on fixed networks operated by organizations with significant market power. However, the points in the Recommendation concerning costs have not been amended.

Numbering. On September 24, 1998, the European Parliament and the Council adopted Directive 98/61 which amended Directive 97/33 with regard to operator number portability and carrier preselection. The new Directive required number portability and carrier preselection to be provided by January 1, 2000.

Recommendation on local loop unbundling

In May 2000, the Commission adopted a recommendation to instruct national regulatory agencies on the following local access issues:

- full unbundling: requires unbundled access to the copper pair;
- line sharing: it is required that the high frequency portion of the telephone subscriber line, be made available according to 98/10 directive; and
- bitstream access: requires the provision of DSL services by incumbents.

The 1999 Review

It was intended that the 1998 regulatory package be reviewed by January 1, 2000. The Commission started a number of studies on the following subjects: (i) remaining barriers in the EU-wide telecommunications market; (ii) assessment of the interconnection situation in the EU; (iii) fixed-mobile convergence/integration; (iv) consumer demand; (v) quality of telecommunication services and consumer protection; (vi) need for a European regulator; and (vii) universal service obligations.

As a result of the above-mentioned studies, the Commission has proposed the following five Directives:

- a common regulatory framework for electronic communications networks and services ("Framework Directive");
- the authorization of electronic communications networks and services ("Authorization Directive");
- access to, and interconnection of, electronic communications networks and associated facilities ("Access Directive");
- universal service and users' rights relating to electronic communications networks and services ("Universal Service Directive"); and
- the processing of personal data and the protection of privacy in the electronic communications sector ("Personal Data Directive").

The Framework, Authorization, Access and Universal service Directives were adopted in March 2002 and published in the Official Journal on April 24, 2002.

Draft Directive on a Common Regulatory Framework. In an important change described by the Commission as "rolling back regulation", the directive redefines the concept of Significant Market Power ("SMP") and the threshold for imposing obligations on certain operators. The directive amends the current definition of SMP based on a 25% or more share of the relevant market.

In the directive, the notion of SMP is based on the concept of dominant position, calculated in a manner consistent with competition law practice. The SMP implies the application of rules in accordance with the conditions imposed by the other Working Documents.

Draft Guidelines on Market Analysis. In March 2001 the Commission published Draft Guidelines on market analysis and the calculation of significant market power. The Commission has called for public comments and an exchange of views among the interested authorities and different market operators. The Guidelines set out the principles for use by national regulatory authorities in the analysis of effective competition, when determining whether an operator has significant market power. Operators having significant market power may be subject to obligations under other Directives in the regulatory package. The adoption of a definitive version of the Guidelines is expected by the end of June 2002.

On June 17, 2002, the Commission issued the draft of the Recommendation on the list of markets to which the new framework will be applied and a working document, for opening the public consultation on the Recommendation in accordance with Art. 15(1) of the Framework Directive.

Directive on Authorizations. The Authorizations Directive provides for electronic communications services and networks to be provided under general authorization. Licenses would no longer be required and specific rights of use would be granted, separately from authorizations, for the assignment of radio frequencies and numbers.

A notification will require only the following elements:

- a declaration of the intention to start operation;
- the coordinates of the undertaking; and/or
- a short description of the service provided.

Upon notification an undertaking could start to operate a network and provide services, provided that it had the right to use radio frequency and numbers if needed. No information should be required prior to, or as a condition for, market access. Nonetheless, Member States could require some justified information (listed in the proposal) from undertakings.

Directive on Access and Interconnection. The Access Directive represents a significant departure from the current Interconnection Directive 97/33/EC which sets out common obligations to be followed by SMP operators in all Member States.

Under the directive, national regulatory agencies will have flexibility to select which access and interconnection obligations to impose on operators notified as having SMP in relevant markets. A maximum list of obligations is contained in the directive.

The proposed operators with rights and obligations to interconnect are essentially the same as those defined in the current ONP Interconnection Directive.

National regulatory agencies will carry out an analysis of the competitiveness of a designated list of relevant product and service markets and identify which operators (if any) have SMP on any of the particular markets.

A national regulatory agency will be able to impose price controls, including obligations for cost orientation of prices and obligations concerning cost accounting systems, for the provision of specific types of interconnection and/or access services.

National regulatory agencies will also be able to impose obligations for transparency, non-discrimination, and accounting separation on SMP operators in relation to interconnection and/or network access. These obligations are carried over from the current regulatory framework.

Directive on Universal Service. The Universal Service Directive replaces the existing directive on voice telephony and universal services. The directive also contains rules on number portability, carrier selection and carrier pre-selection which are currently in the Interconnection Directive. The directive also covers the provision of leased lines and other mandatory services as well as a number of issues concerning users' rights, such as contracts, tariff transparency and information and quality of service.

In general, the existing requirements for the provision of universal service, voice telephony facilities and leased lines will remain in place, at least for the time being. The principal changes are described below.

In an important section on retail price regulation (up to now only covered in national law), it is proposed that, when an operator has SMP in the provision of access to, and use of, public telephone services, the national regulatory agency must:

- determine appropriate mechanisms for retail price control, such as price caps or specific price floors and ceilings;

- ensure that the SMP operator sets prices at normal commercial levels;

- notify to the Commission the names of organizations subject to retail price control; and

- retail price control mechanisms should not be applied where effective competition exists.

The directive also provides for the extension of the requirement for number portability to mobile operators.

As a mandatory service, Member States will be required to ensure that all schools have access to the Internet at transparent and cost-oriented tariffs, with National Regulatory Agencys ensuring conditions for competitive provision of access.

The processing of personal data and the protection of privacy is currently regulated by the general Data Protection Directive (95/46/EC) with specific issues in the telecommunications sector addressed by the Data Protection and Telecommunications Directive (97/66/EC).

The main changes would be the extension of scope and technological neutrality. The principle of technological neutrality implies that "consumers and users should get the same level of protection regardless of the technology used. "Telecommunications services and networks" would be replaced by "electronic communications services and networks" in line with the proposed common Framework Directive.

The scope of the future directive would then include networks used for radio and television broadcasting and cable TV networks, irrespective of the type of information conveyed (these were excluded from Directive 97/66/EC) but would exclude content of broadcasting transmissions.

In February 2000, the European Commission launched the second phase of the investigation under the competition rules into the telecommunications sector, sending out formal information requests concerning the conditions and pricing of national and international mobile roaming. In December 2000, the Commission published the Working Document on the preliminary findings of this phase of the sector inquiry. In July 2000, the Commission sent a request for information to the incumbent telecommunications operators to find out whether, and under what conditions, they allow their competitors access to the local loop. The purpose of the enquiry is to detect any abuses of a dominant position. These new requests for information mark the third stage of the sectoral enquiry on the telecommunications industry. The collection of the information is still ongoing. A public hearing has been called for July 8, 2002. In July 2001, the Commission queried nine mobile operators in the UK, Germany and the Netherlands, to ascertain whether there is evidence of collective fixing of roaming prices. DG Competition is still examining the Vodafone Eurocall flat roaming plan and the GSM Association standard international roaming agreements. The Commission should end the examination of these cases by the end of 2002.

Leased Lines Pricing

In the context of the growing debate on prices for leased lines in the EU, the Commission adopted, on November 24, 1999 a Recommendation on Leased Lines Interconnection prices in a liberalized telecommunications market.

The Recommendation focuses on the pricing of short distance interconnect leased lines (*i.e.*, local ends or leased lines part circuits) supplied by one operator, normally the incumbent, to another operator so that the latter can provide a complete end-to-end leased line to a customer. The Commission expects significant competition soon in the long-distance leased line market in Europe. Conversely, the Commission considers that competition with incumbent operators in the provision of short distance local leased lines will remain weak. The Commission therefore claims that the setting of price ceilings for short distance leased lines will stimulate the competitive provision of end-to-end leased lines to users by new entrants.

Pricing of services for the interconnection of leased lines have to be provided in the RIO of public fixed network operators designated by the national regulatory authority as having significant market power in accordance with Directive 97/33/EC.

The Recommendation takes the form of a set of recommended price ceilings based on the prices in the three lowest cost Member States. Where charges are above the price ceilings, National Regulatory Agency should use their rights under article 7(2) of the Interconnection Directive (97/33/EC) to request full justification of the charges, and, if appropriate, require these charges to be lowered.

Local Loop unbundling

In responses to the conclusions of the special European Council in Lisbon in March 2000 and to the commitments made in the Commission's Communication on the results of the public consultation on the 1999 Review, the Commission decided to proceed with a separate legal measure on Local Loop Unbundling distinct from the proposal for a Directive on Interconnection and Access.

In December 2000, the European Parliament and the European Council adopted Regulation No. 2887 ("Regulation 2887") on local loop unbundling.

Regulation 2887 is very concise and consists of only five articles; the decision to use a regulation on LLU instead of a Directive was made because regulations do not require time for transposition and are immediate in effect once adopted. Regulation 2887 covers unbundled access to the access to the local loops and related facilities of fixed public telephone network operators that have been designated by the national regulatory authority as having significant market power in the provision of fixed public telephone networks. Notified operators shall publish from December 31, 2000 and keep updated, a reference offer for unbundled access to their local loops and related facilities. They will meet reasonable requests from beneficiaries for unbundled access to their local loops and related facilities under transparent, fair and non-discriminatory conditions, and charge prices for such services set on the basis of cost-orientation.

When the National Regulatory Agency determine that the local access market is sufficiently competitive, it shall relieve the notified operators of the obligation for cost-oriented prices.

Together with the LLU Regulation, the Commission adopted a complementary Communication, which aims at clarifying the application of Community competition rules to the provision of services in the local access network. The Communication also supplements the previous Commission Notice on the application of the competition rules to access agreements in the telecommunications sector.

Radio spectrum policy

In July 2000, the Commission presented a proposal for a decision of the European Parliament and of the Council on a regulatory framework for radio spectrum policy in the European Community, which is intended to ensure the harmonized availability and efficient use of radio spectrum, where required to implement Community policies in areas such as communications, transport, broadcasting and research and development. The proposal draws upon the experience gained with Community decisions in the areas of satellite Personal Communications Services and UMTS. The decision was adopted on March 7, 2002 and published in the Official Journal on April 24, 2002. The decision seeks to complement, rather than to replace, the spectrum management activities of ITU/WRC and CEPT and of the member States by providing for a Radio Spectrum Committee which the Commission will consult periodically on relevant matters, thus contributing to the formulation, preparation and implementation of the Community radio spectrum policy.

Moreover, the Commission has announced its intention to adopt a Decision to establish a Radio Spectrum Policy Group (RSPG), whose main function would be to advise the EU the Commission on the requirements and on the co-ordination of policy approaches and harmonised conditions related to radio spectrum. The decision is expected to be adopted in Summer 2002.

Voice over Internet

On December 22, 2000 the Commission published in the Official Journal a Communication on the status of voice services over the Internet. This updates a similar notice issued in January 1998 and follows a public consultation held in 2000.

The Commission considers that Internet telephony in general continues to fall outside the definition of voice telephony, except where Internet telephony meets each of the conditions established in the Directive as set out in the 1998 notice. This means, that Member States should normally continue to allow Internet access/service providers to offer voice on Internet under data transmission general authorizations, and that no mandatory requirement for an individual licence is required. Conversely, voice communication services fulfilling the four conditions enshrined in the Directive and therefore appearing as substitutes for voice telephony services provided by traditional means should be regarded as voice telephony and be submitted to the relevant regulatory regime, in consideration of the principle of technological neutrality.

VAT and Electronic commerce

The Commission tabled in June 2000 proposals for a regulation to amend Reg. 218/92 on VAT and electronic commerce and for a Directive to amend the VI VAT Directive. The Commission' s proposal aims to ensure that certain electronically delivered services are taxed at the place of consumption. The proposals also clarify that VAT would apply to television and radio broadcasting services that are supplied on a subscription or pay-per-view basis. On May 7, 2002 the Council adopted the Commission's proposal for the Directive. According to the new rules, EU suppliers will no longer have to levy VAT when they sell certain electronic services to non-EU Member States. Non-EU suppliers selling into the EU to private consumers would have to charge VAT and register for VAT purposes in one of the Member States. The new rules will need to be implemented by July 1, 2003.

Concerning the regulation, the Council reached a political agreement on the proposal in February 2002 but the Parliament needs to be consulted on the draft Regulation. Moreover, in November 2000 the Commission proposed a proposal for a Directive on the harmonization of the rules relating to VAT invoicing. The Directive 2001/115/EC was adopted and published on the Official Journal on December 20, 2001. The directive amends the existing provision on VAT invoices contained in the VI VAT directive to take account of electronic commerce. It contains provisions which aim at harmonising the statements that must be included on invoices for VAT purposes, allowing invoices to be transmitted and stored electronically, and enabling competent authorities of a Member State to access electronic invoices that are stored in other Member States.

Data protection

In July 2000, the Commission published a Draft proposal for a Directive for data protection on the Electronic Communications sector. It aims at replacing directive 97/66 of 1997 on the processing of personal data and the protection of privacy in the telecommunications sector by updating and adapting it to market and technological development. The adoption of the Directive is expected by the end of June 2002.

Internet Domain Name

In April 2000 the Commission published a Communication on the organization and management of the Internet—International and European policy issues 1998-2000. The EP adopted a resolution in March 2001.

Moreover, a Communication on the follow-up of the Working paper on the creation of .EU. Internet top level domain was published by the Commission in July 2000.

On April 22, 2002 the European parliament and the Council adopted a Regulation on the implementation of the .eu Top Level Domain, which sets out the framework to allow companies, organizations and individuals to register a .eu domain name address provided that they are established or reside in the EU. The regulation also provides for a register which will be the entity responsible for the organization, administration and management of the .eu top level domain.

Public procurement

On May 12, 1999, the EU Commission adopted a Communication including a list of services regarded as excluded from the scope of Council Directive 93/38/EEC coordinating the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors (under Article 8of this Directive, the Commission may exempt services from the application of the public procurement rules where it believes competition has developed sufficiently).

The Commission has thus reached the conclusion that public contracts relating to most telecommunications services in most Member States should be considered excluded from the scope of the Utilities Directive.

Proposal for directive on waste electrical and electronic equipment

The proposed Directive is designed to tackle the fast growing waste stream of electrical and electronic equipment and complements EU measures on landfill and incineration of waste. The proposal affects all electrical and electronic equipment used by consumers and electrical and electronic equipment intended for professional use, which are likely to end up in the municipal waste stream and which are currently not treated before going to incinerators or landfills. The Directive would apply without prejudice to other Community legislation on safety and health requirements as well as to requirements set out in specific Community waste management legislation (e.g. Directive 91/157/EEC on batteries and accumulators containing certain dangerous substances). On April 10, 2002 the European parliament voted the proposed Directive in second reading.

Competition Law

Telecom Italia is also subject to Law No. 287 of October 10, 1990 ("Law 287"), the Italian competition law of general application, to the substantive rules of the Maccanico Law and to the competition rules of the EU Law 287 forbids:

- agreements (including resolutions and concerted practices) aimed at fixing prices, limiting production or access to markets and technological developments, sharing of markets, applying different conditions for the same services to the detriment of competitors, and subjecting contracts to the acceptance of conditions that, according to their nature and common practice, are not linked to the object of the contract;

- abuses of dominant position (including practices aimed at fixing prices, limiting production or access to markets and technological developments, applying different contractual conditions for the same services to the detriment of competitors, as well as subjecting contracts to the acceptance of conditions that, according to their nature and common practice, are not linked to the object of the contract); and

- concentrations of enterprises (*i.e.*, mergers, acquisitions of controlling interests and concentrative joint ventures) which would result in the creation or strengthening of a dominant position. All concentrations in relation to which the combined overall turnover, in Italy, of the companies involved is higher than €377 million or the turnover of the company being acquired is, in Italy, higher than €37 million, must receive a prior authorization from the Antitrust Authority. These thresholds are adjusted every year to take account of inflation. Failure to file prior notification of a concentration to the Antitrust Authority will result in a fine from 1% to 10% of the turnover of the parties involved in the concentration, or higher in the case of fines for violation of a prohibition of a concentration.

Law 287 is administered by the Antitrust Authority which, either on its initiative or following a complaint submitted by any interested party (the "Interested Party"), has the power to investigate and ascertain compliance with Law 287. When the Antitrust Authority finds *prima facie* evidence that Law 287 has been violated, the parties involved (including the Interested Party) are notified of the opening of a formal investigation. The party under investigation (the "Investigated Party") and the Interested Parties shall then have the right to be heard and to file written arguments with the Antitrust Authority. Pending the investigation, the Antitrust Authority may also require the parties involved and third parties to disclose information or to submit documents that it considers useful for the investigation. In addition, the Antitrust Authority may appoint experts and carry out direct inspections at the Investigated Party's premises in order to examine and seize relevant documents.

If at the conclusion of the investigation the Antitrust Authority determines that Law 287 has been violated, it orders the Investigated Party to cure the relevant violation and, in the case of serious violations, imposes fines up to 10% of the turnover relating to the relevant activities. Any failure to comply is sanctioned with an additional fine up to 10% of the turnover of the Investigated Party.

With respect to competition matters, the decisions of the Antitrust Authority are considered administrative acts and may be appealed before the TAR of Lazio, based in Rome, for violation of law, abuse of power and lack of jurisdiction. The TAR may either reject the appeal or declare the Antitrust Authority's decision null and void. The TAR, upon request of the complainant, may also suspend the enforcement of the decision of the Antitrust Authority. The TAR's judgments may be further appealed before the State Council, whose decision is final.

The Antitrust Authority has no powers other than those indicated above. It may not issue provisional injunctions or impose liquidated damages for abuses of dominant positions. For these remedies, Law 287 confers special jurisdiction on the Court of Appeal that has jurisdiction over the relevant case.

In addition to Law 287, the Maccanico Law confers upon the National Regulatory Agency the power to enforce provisions aimed at ensuring pluralism in the communications sectors, including radio and television broadcasting activities.

Moreover, the competition rules of the EU ("EU Competition Law") also have a direct effect in Italy. The main principles of EU Competition Law are contained in Articles 85 and 86 of the Treaty of Rome. (Following the adoption of the treaty of Amsterdam on October 2, 1997, articles 85 and 86 became respectively articles 81 and 82). Article 81 prohibits agreements or concerted practices between undertakings that may affect trade between Member States and has the object or effect of restricting competition within the EU. Article 82 prohibits any abuse of a dominant position within a substantial part of the EU that may affect trade between Member States. These rules are primarily enforced by the European Commission, which cooperates with the national competition authorities, and through the national courts. The Antitrust Authority has the power to apply Article 85(1) and Article 86, following its own procedures and imposing, if necessary, the fines provided for under Law 287. In September 1991, general guidelines were published by the European Commission on the application of EU Competition Law in the telecommunications sector. In August 1998, the European Commission published a notice updating the 1991 guidelines. These guidelines outline the EU's approach to common competition issues.

On December 11, 1996, the Commission adopted a Communication on the application of the competition rules to access agreements in the telecommunications sector. The purpose of this notice is:

- to set out access principles stemming from EU law in order to create more market certainty;
- to define and clarify the relationship between competition law and sector specific regulation; and
- to explain how competition rules will be applied in a consistent way across the converging sectors. On October 3, 1997, the EU adopted a further communication on the definition of the relevant market for the purpose of EU competition law. The aim of this notice is to provide guidance as to how the Commission applies the concept of relevant product and geographic market in its ongoing enforcement of EU competition law.

In April 1999, the Commission adopted a White Paper on modernization of the rules implementing Articles 81 and 82 of the EC Treaty, which examined various options for reforming the system and proposed the adoption of fundamentally different enforcement system called a direct applicable exception system. Such system is based on the direct applicability of the exception rule of Article 81.3, implying that the Commission and national competition authorities and courts would apply Art. 81.3 in all proceedings in which they are called upon to apply Art. 81.1, which is already directly applicable.

In September 2000, the Commission presented a Proposal for a Council regulation on the implementation of the rules on competition which provides for the abolition of the Commission exclusivity in the application of art. 81.3; a system of legal exception and evaluation ex post of the agreements; an effective decentralization of the enforcement of EU competition rules; and the strengthening of Commission' s investigation powers. Further to the debate at the European parliament in December 2001, the final adoption of the Regulation is expected by the end of 2002.

Under Regulation 17/62 ("Regulation implementing Articles 81 and 82 of the Treaty"), the EU Commission may initiate general inquiries into those sectors of the economy where it believes competition might be restricted or distorted. The aim of this provision is to allow the Commission to investigate suspicious pricing structures or other practices indicating a possible anti-competitive situation across a whole industry. No indications are required that specific companies have infringed the EC Treaty.

Once the Commission has decided to start such an inquiry it has the powers to request and obtain all necessary information from governments and competent Member State authorities as well as from companies. In October 1999, the Commission launched the first phase of sectoral inquiries into telecommunications, regarding the conditions for providing and pricing of leased lines. In September 2000, the Commission published a Working document on the initial findings of the leased lines sector inquiry.

In February 2000, the European Commission launched the second phase of the investigation on competition rules into the telecommunications sector, sending out formal information requests concerning the conditions and pricing of national and international mobile roaming. In December 2000, the Commission published the Working Document on the preliminary findings of this phase of the sector inquiry. In July 2000, the Commission sent a request for information to the incumbent telecommunications operators to find out whether, and under what conditions, they allow their competitors access to the local loop. In July 2001, the Commission sent a questionnaire to new entrants asking to identify the remaining difficulties in obtaining local loop access. The purpose of the enquiry is to detect any abuses of a dominant position. These new requests for information mark the third stage of the sectoral enquiry on the telecommunications industry. The evaluation of the information collected is still ongoing.

On December 11, 2001 the European Commission issued a Green paper on the Review of Council Regulation (EEC) No 4064/89, concerning mergers with community dimensions. The Commission seeks to launch a wide ranging debate on the functioning of the EU merger control regime based on the experience gained during the last 10 years.

The Commission finds it is the appropriate time to review the Regulation, to ensure effective, efficient, fair and transparent control of concentrations at the most appropriate level.

GLOSSARY OF SELECTED TELECOMMUNICATIONS TERMS

The following explanations are not intended as technical definitions, but to assist the general reader to understand certain terms as used in this Annual Report.

Access charge: Amount paid per minute charged by the national operators for the use of their network by operators of other networks. Also, known as an "interconnection charge".

ADSL (Asymmetric Digital Subscriber Line): A copper based access technology that allows a telephony channel and a digital channel (from 1.5-8 Mbit/s) to be carried from the network to the customer (downstream) and a telephony channel and a low bit rate digital channel (16-64 Kbit/s) to be carried from the customer to the network (upstream). It is generally utilized in conjunction with an ATM transport network

Analog: A transmission or switching which is not digital, *e.g.*, the representation of voice, video or other modulated electrical audio signals which are not in digital form.

Analog network: A network using analog technology with circuit switching, capable of connecting one user with all the others, but with limited transmission capacity.

ATM (Asynchronous Transfer Mode): A broadband switching technology that permits the use of one network for different kinds of information (*e.g.*, voice, data and video).

Backbone: A primary shared communication path that serves multiple networks and may facilitate communications between different protocols.

Broadband services: Services characterized by a transmission speed of 2 Mbit/s or more. According to international standards, these services are divided into two categories: (i) Interactive services, including videotelephone/videoconferencing (both point-to-point and multipoint); videomonitoring; interconnection of local networks; file transfer; CAD; highspeed fax; e-mail for moving images or mixed documents; broadband videotex; Video on demand; retrieval of sound programs or fixed and moving images; and (ii) Broadcast services, such as sound programs, television programs (including high-definition TV and pay TV) and selective document acquisition.

Broadcast: Simultaneous transmission of information to all nodes and terminal equipment of a network.

BSS (Business Support System): The system used by network operators to manage business operations such as billing, sales management, customer-service management and customer databases. A type of Operations Support System OSS.

Business Packet: The Italian packet-switching data network.

Carrier: Traditionally, the carrier is the company that makes the physical lines available.

CATV (Cable television): Cable or fiber-based distribution of TV programs.

Cellular: A technique used in mobile radio technology to use the same spectrum several times in one network. Low power radio transmitters are used to cover a "cell" (*i.e.*, a limited area) so that the frequencies in use can be reused without interference for other parts of the network.

Channel: The portion of a communications system that connects a source to one or more destinations. Also called circuit, line, link or path.

Closed User Group: A group of telecommunications users that share a longstanding economic interest. This definition has arisen in a regulatory context; it permits the partial liberalization of some telecommunications services.

Coaxial cable: A type of electrical cable in which a central conductor covered by an insulator is then surrounded with a cylindrical conducting sheath whose axis coincides with that of the central conductor, hence the term "coaxial".

Corporate Network: A network, which could be a virtual private network, provided by a corporation for its own use and possibly for that of other corporations. The network's features are tailor-made to address the specific need of the client. It is separate from the network provided by the national telecommunications carrier, but it may be connected to the latter for the use of selected facilities.

Data Network Access Point: Unit of measurement used in data network business.

DCS 1800 (Digital Communication System): A derivative of the GSM cellular mobile telephone standard. "1800" refers to the frequency used of 1800 MHz. DCS 1800 is the European PCN standard.

Digital: A mode of representing a physical variable such as speech using digits 0 and 1 only which vary in relation to the variable being represented. The digits are transmitted in binary form as a series of pulses. Digital networks are rapidly replacing the older analog ones. They allow for higher capacity and higher flexibility through the use of computer-related technology for the transmission and manipulation of telephone calls. Digital systems offer lower noise interference and can incorporate encryption as a protection for external interference.

District traffic: Long-distance telephone calls within the same area code.

ESPRIT (European Strategic Programme for Research and Development in Information Technologies): A program financed by the EU to sponsor research and development in information technology.

Exchange: See Switch.

Frame Relay: A data transmission service using fast protocols based on direct use of transmission lines.

Gateway: A connection between the LANs and WANs of one or more suppliers. Can also mean the access nodes to international networks of various kinds.

GPS (Global Positioning System): A constellation of satellites, orbiting the Earth two times a day, that is able to pinpoint precisely where a certain object is on Earth.

GSM (Global System for Mobile Communications): A standard for mobile cellular telephony used in Europe, Asia, South Africa and Australia, based on digital transmission and cellular network architecture with roaming.

GSM TIM Card: A prepaid, rechargeable card which permits the TIM mobile customer to make outgoing calls up to the limit of the card and receive an unlimited number of calls.

HFC (Hybrid Fiber Coaxial): Connection system that uses mixed technology, combining optical fibers with coaxial cable.

Infomobility: A group of systems and services made available to all worldwide customers using wireless phones in vehicles in order to satisfy the safety and information requirements of private business users.

IN (Intelligent Network): Network architecture that centralizes processing of calls and billing information for calls.

INTELSAT (International Telecommunications Satellite Organization): An international organization formed in 1964 to provide satellite communications among countries.

Interactive: The user can change some aspect of the program received.

Internet: The world's best-known data network. Initially used by the U.S. Department of Defense, the Internet now provides an interface for networks based on different technologies (LANs, WANs, data networks, etc.), but which use the TCP/IP protocol platform.

ISDN (Integrated Services Digital Network): A system in which several services (*e.g.*, speech and data) may be simultaneously transmitted end to end in digital form.

ITU (International Telecommunication Union): The worldwide policy, spectrum regulation and standardization body in telecommunications operating under the auspices of the United Nations.

LAN (Local Area Network): A private network that covers a local geographic area and provides public telecommunications services as well as interconnection between personal computers.

Modem: Modulator/Demodulator. A device that modulates digital data to allow their transmission on analog channels, generally consisting of telephone lines.

Multimedia: A service involving two or more communications media (*e.g.*, voice, video, text, etc.) and hybrid products created through their interaction.

Network: An interconnected collection of elements. In a telephone network, these consist of switches connected to each other and to customer equipment. The transmission equipment may be based on fibre optic or metallic cable or point to point radio connections.

Nodes: Topological network junction, commonly a switching center or station.

ONP (Open Network Provision): Principles and conditions laid down by the EU for access to and usage of public telecommunications networks and services. A network architecture that permits telecommunications services to be offered on facilities of public operators and for equipment to be connected to such networks.

Optical fiber: A transmission medium which permits extremely high capacities. It consists of a thin strand of glass that provides a pathway along which waves of light can travel for telecommunications purposes.

OSS (Operations Support System): Methods and procedures (mechanized or not) which directly support the daily operation of the telecommunications infrastructure.

Outsourcing: Hiring outsiders to perform various telecommunications services, which may include planning, construction, hosting of a network or specific equipment belonging to a company, and, ultimately, the management of entire telecommunications systems. Value-added applications may also be provided in various sectors.

PABX: Private Automatic Branch Exchange. Telephone switchboard for private use, but linked to the national telephone network.

Packet-Switched Services: Data services based on parceling or breaking the data stream into packets and switching the individual packets. Information transmitted (whether voice or data) is segmented into cells of a standardized length, which are then transmitted independently of one another, allowing maximization of available capacity and usage of a single transmission path for multiple communications. The cells are then reassembled upon reaching their destination.

Pay-Per-View: A system by which the viewer pays to see a single program (such as a sporting event, film or concert) at the moment at which it is transmitted or broadcast.

Pay TV: Paid-for TV channels. To receive Pay TV or Pay-Per-View programs, a decoder must be connected to the television set, connected to a conditional access system.

PCN (Personal Communications Network): PCN is a cellular telephony network designed to have the high capacity required to support a mass market service.

PDH (Plesiochronous Digital Hierarchy): Standard for digital transmission.

Penetration: The measurement of the take-up of services. As of any date, the penetration is calculated by dividing the number of subscribers by the population to which the service is available and multiplying the quotient by 100 on such a date.

Platform: The total input, including hardware, software, operating equipment and procedures, for producing (production platform) or managing (management platform) a particular service (service platform).

POTS (Plain Old Telephone Service): The basic telephony service supplying standard, single-line telephones, fixed-line services and access to public voice telephony network.

PSTN (Public Switched Telephone Network): The public telephone network delivering the basic telephone service and, in certain circumstances, more advanced services.

Roaming: A function that enables wireless subscribers to use the service on networks of operators other than the one with which they signed their initial contract.

Satellite services: Satellites are used, among other things, for links with countries that cannot be reached by cable or to provide an alternative to cable and to form closed user networks.

SDH Standard (Synchronous Digital Hierarchy): The European standard for high-speed digital transmission.

Service Provider: The party that provides end users and content providers with a range of services, including a proprietary, exclusive or third-party service center.

SOHO: refers to the small office/home office market which consists of businesses that use telephone lines to connect to the Internet, as opposed to dedicated lines, and is made up of small businesses, generally with one or two employees, and businesses conducted out of the home.

SOCRATE: Telecom Italia' s broadcasting/broadband network platform.

SME: refers to the small- and medium-size enterprise market which consists of businesses having between 3 and 50 employees.

Switch: These are used to set up and route telephone calls either to the number called or to the next switch among the path. They may also record information for billing and control purposes.

Switched Transit Traffic: Consists of calls placed between two other countries that are routed through the Italian fixed network.

Synchronous: Type of data transmission in which there is permanent synchronization between the transmitter and the receiver.

TACS (Total Access Communication System): An analog cellular network using the 900 MHz band based on a European standard also used in the UK, Ireland, Austria and Spain. Features include handover and available add-on services include answering, call notification, call transfer, differentiation of business and private calls, authorization code for outgoing international calls and itemized billing.

UMTS: (Universal Mobile Telecommunication System): third generation mobile communication system.

Universal service: The obligation to supply basic service to all users throughout the national territory at reasonable prices.

Value Added Services (VAS): Value Added Services provide a higher level of functionality than the basic transmission services offered by a telecommunications network for the transfer of information among its terminals, which include wired or wireless switched-circuit analog voice communications; direct "unrestricted" digital point-to-point service at 9, 600 bit/s; packet switching (virtual call); direct broadband analog transmission of TV signals, and supplementary services, such as closed user groups; call waiting; collect calls; call forwarding, and identification of number called. Value Added Services performed by the network, the terminals or the specialized centers include message handling services (MHS) (which can be used, among other things, for commercial documents in predetermined formats); electronic directories listing users, network addresses and terminals; e-mail; fax; teletex; videotex and videotelephone.

Value Added Services could include also value added voice telephony services such as Freephone or Premium Rate Services.

VAN (Value-added Network): A type of public network that leases basic transmission facilities from a common carrier, adds features that enhance the service and provides the improved communications capability to end users. Automatic alternate routing network management and error correction are examples of the value added.

Videotex: A service pursuant to an ITU standard, permitting remote access to database by telephone.

VPN (Virtual Private Network): A network designed for a business or government agency, using the infrastructures of a carrier and providing customized services, which operates in such a manner as to appear dedicated to the user thereof.

VSAT: Very Small Aperture Terminal. A satellite telecommunications system that uses small parabolic antennas operating on the satellite as transceivers to connect closed user groups with one another.

WAN (Wide Area Network): A private network that covers a wide geographic area using public telecommunications services.

WAP (Wireless Application Protocol): A Technology which allows access to Internet using mobile radio sets, even without the use of a computer.

X.25 Protocol: A protocol for packet-switched data transfer.

DESCRIPTION OF PROPERTY

As of December 31, 2001, the Group owned approximately 7,400 buildings located throughout Italy. Specialized buildings for telecommunications services account for the majority of properties both in number and book value. They house mainly exchange equipment and transmission equipment, and are used as part of the Group' s continuing telecommunications operations. General purpose properties consist chiefly of offices, depots and computer centers. Telecom Italia has its registered office in Milan and owns some of the buildings in which its headquarters in Rome are located. TIM has its registered office in Turin and its headquarters in Rome. The Finsiel Group has its headquarters in Rome in a building which it rents from a third party.

The principal categories of the Group' s equipment are exchanges and transmission equipment, cable networks, base stations for cellular networks and equipment for radio communications, all of which are located throughout Italy. The Group also has numerous computer installations which are primarily located at the headquarters of the Group' s significant subsidiaries.

At December 31, 2001, telecommunications installations, including local and domestic long-distance networks and radio transmission equipment, represented approximately 76% of the fixed assets of the Group, land and buildings represented 13%, plant under construction, advances to suppliers and stock for fixed assets represented 7%, and furniture, office equipment and other equipment, technical installations and machinery comprised the remaining 4%.

As of December 31, 2001, the total amount of liens, mortgages and pledges on real property owned by the Group was €723 million. Such liens, mortgages and pledges do not represent major encumbrances on fixed assets and on the material plans to expand or construct new facilities.

An important element of Telecom Italia' s restructuring plan was to realize value on its extensive real estate portfolio. In November 2000, Telecom Italia established a partnership with Beni Stabili, a leading Italian real estate operator, and Lehman Brothers to manage a significant portion of Telecom Italia' s real estate portfolio.

Telecom Italia contributed a going concern including an important portion of its real estate portfolio to IM.SER and subsequently sold 45% of this company to Beni Stabili and 15% to Lehman Brothers.

The real estate portfolio originally held by IM.SER consisted of 581 properties, totaling 3.7 million square meters and was composed of two parts, the "Real Estate Investment Portfolio" and the "Real Estate Trading Portfolio":

- "Real Estate Investment Portfolio", consisting of 386 properties totaling approximately 2.4 million square meters, located throughout Italy. All the properties, including buildings that contain telecommunications equipment, were leased to Telecom Italia at the end of 2000 under long-term lease contracts (21 plus 6 years) at market rates; and

- "Real Estate Trading Portfolio", consisting of 195 properties totaling approximately 1.3 million square meters, located throughout Italy. Of these properties, the majority have been leased at market rates to Telecom Italia under contracts allowing for early termination in favor of Telecom Italia.

In May 2001, IM.SER contributed its Real Estate Trading Portfolio to Telemaco Immobiliare, a newly formed company. Following such contribution, IM.SER sold the shares of Telemaco Immobiliare to its shareholders. The shareholders of Telemaco Immobiliare are Beni Stabili with a 45% stake, Telecom Italia with a 40% stake and Lehman Brothers with a 15% stake.

On May 16, 2001 Beni Stabili exercised an option to buy the Lehman Brothers' stake in IM.SER, resulting in Beni Stabili holding a 60% stake in IM.SER and Telecom Italia a 40% stake.

As of December 31, 2001, the "Real Estate Investment Portfolio" owned by IM.SER consisted of 385 properties; on the same date the "Real Estate Trading Portfolio" owned by Telemaco Immobiliare consisted of 163 properties as a result of the disposal of 32 assets occurred during 2001.

On May 24, 2002, the Telecom Italia Group and the Olivetti Group reached an agreement with Pirelli & C. Real Estate S.p.A., Pirelli S.p.A., MSMC Italy Holding B.V. and Popoy Holding B.V. with regard to the so called "Tiglio Project", aimed at integrating real-estate assets and activities of the companies involved with real-estate services and consequently maximizing their value.

According to the terms of the agreement, Telecom Italia Group will transfer property, land and staff in charge of real estate asset-management activities to two newly founded companies; at the moment it is expected that at a later date a closed-end real-estate fund will receive the above mentioned assets.

In particular, Telecom Italia Group's contribution will be approximately €1,350 million with gross capital gains of approximately €170 million, with net cash proceeds at the end of the project of approximately €650 million received in several stages.

The implementation of the project is subject to obtaining the necessary financing and to the transfer of 40% of IM.SER real-estate to the Telecom Italia Group, to be realized through a spin-off of the company.

To the best of the Company's knowledge, there are no material environmental issues that may affect the Company's ability to utilize its assets.

Item 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Annual Report. Such financial statements have been prepared in accordance with Italian GAAP, which differ in certain material respects from U.S. GAAP. For a discussion of the principal differences between Italian GAAP and U.S. GAAP as they relate to Telecom Italia, see Note 26 of Notes to the Consolidated Financial Statements included elsewhere herein. All of the data included in "Item 5. Operating and Financial Review and Prospects" for 2000 is based on the pro forma 2000 numbers which accounts for the Nortel Inversora group on the equity method.

Background

Market Developments

The Italian market for telecommunications services. In 2001, the Italian telecommunications market grew by 11%, with revenues of more than €409 billion (source: Gartner Group). 43.7% of the total market was attributable to fixed line telephone services, 46.3% to wireless telephone services and 10% to the data and web services.

The growth in demand for telecommunications services in recent years has been driven by the spread of mobile telephone services and by the development of Internet and data services. These sectors are expected to continue to expand during the next few years and a portion of the expenditures of households and businesses will continue to be diverted to digital products and services, creating more opportunities to integrate transmission services and applications content on-line. Subscriber growth in domestic mobile telecommunications is expected to grow more slowly than in recent years as penetration reached 89% at the end of 2001 in Italy, the highest in Western Europe.

Although technological innovation continues, major technological change is not expected in the short-to-medium term. However, services demanded by end users may further stimulate consumption and innovation, especially with regard to the range of value-added services, thus bridging the gap between the potential of available technologies and their use.

During 2001 the telecommunications sector experienced a phase of restructuring and consolidation after the strong boost to growth generated by the phenomenon of the Internet and the boom of stock market listings at the beginning of 2000. During this period, the financial markets partially redirected investments and resources away from "alternative" operators towards those that can leverage assets, have specific qualifications and a consolidated financial strength (typically "incumbent" operators).

The Italian market compared to other major European countries, has a high penetration of mobile telephone services, whereas the spread of Internet services and both residential and business broadband services is still relatively low. At the end of 2001, in Italy, the penetration rate of the Internet had reached 23% for households and 44% for small and medium-size businesses (SMB). Households almost exclusively use dial-up technology (98%) to access the Internet and only a small proportion (2%) use ADSL broadband for this purpose. However, experience in other countries, including Germany, suggests that there is opportunity to increase ADSL penetration. There is also opportunity for growth in data transmission, services connected to the web and new generation mobile services (GPRS, UMTS). In 2001, TIM launched the GPRS offer to the corporate and mass market. TIM has already started experimenting its UMTS service in its Service Center in Padua, and a gradual roll-out of the UMTS network has begun. Transition toward the third generation will be gradual; GPRS will be able to satisfy customers' requirements concerning advanced services and it will take time to guarantee full inter-operability between UMTS and GPRS. The larger roll-out should start in 2004.

Competition

The Group faces domestic competition in all of its businesses, including, since January 1, 1998, the provision of fixed line and mobile voice telecommunications services and the operation of networks to support the provision of such services. See "Item 4. Information on the Company—Business—Strategy" and "Item 4. Information on the Company—Business—Competition".

Competitive pressure in the Italian market continued during 2001, as evidenced by the following:

- issue of licenses for fixed networks and voice telephony service, which rose from 130 at the end of 2000, to 168 at the end of 2001;
- further significant price reductions for voice traffic and for the internet access market;
- gradual development of local loop unbundling and shared access; during 2001, 15 operators have started to sell services based on local loop unbundling;
- the introduction of GPRS mobile services.

Competitive pressures during 2000 were evidenced by the following:

- issuance of five UMTS licenses in November 2000 for providing third generation mobile services;
- the launch of local carrier selection phone services by many operators and the start of international, national and long distance (from January 2000) and local (from May 2000) carrier preselection;
- the proliferation of CLEC (Competitive Local Exchange Carriers) operators, funded with a mix of public and private capital, generally contributed by municipal companies operating in the service area, venture capital funds and other private partners. Since these companies operate in limited areas, the close relations established with their clients (mainly small and medium-size private companies, but, in many cases, also selected businesses) constitute a fundamental competitive advantage. Generally the offering includes basic, value added and broadband services;
- the introduction of new data services (ADSL fiber access on fixed networks, GPRS on mobile networks) and innovative rate plans (such as the flat rate for phone services); and
- communication policies, with considerable investments being geared to trademark awareness, the launch of new products and services and specific price campaigns.

As a result of increased competition the Group's market shares have fallen in the following areas:

- Local Voice traffic: 84% in 2001 compared to 93% in 2000 and 100% in 1999,
- Long distance: 73% in 2001 compared to 76% in 2000 and 83% in 1999,
- International traffic: 68% in 2001 compared to 70% in 2000 and 86% in 1999, and
- New mobile subscribers: decrease of 4.7% in 2001 compared to a decrease of 9% in 2000 and a decrease of 18.5% in 1999. Notwithstanding the decrease of new subscribers, mobile traffic increased by 14% in 2001, 25% in 2000 and 35% in 1999, confirming TIM's strategic focus on high value customers.

Although this increased competition (including the need to adjust tariffs in response to competition) has affected the Group's operations, management believes that it has been able partially to offset the impact of market share losses (and lower prices) as a result of (i) the introduction and continued growth of new telecommunications services (in particular, internet-related revenues as well as traffic growth from data transmission services), capitalizing on Telecom Italia's advanced fixed network, (ii) increased interconnect traffic as a result of the growth of other mobile and fixed telecommunications operators in Italy, (iii) continued growth of the Group's mobile telecommunications businesses, and (iv) continued focus on customer service, quality and marketing initiatives, and including the introduction of innovative tariff packages targeted at specific segments of the market. Although prior to 2001 Telecom Italia also benefited generally from growth in the Italian economy, Italy, like many other countries around the world, saw its economy slowing down in 2001 with GDP growth of 1.8% (2.9% in 2000). Management believes that the Group's ability to continue to increase traffic and revenue will be impacted by the rapidly evolving market dynamics in all parts of its business and the continuing increase in competitive pressure. See "Item 4. Information on the Company—Business—Competition".

With respect to domestic fixed line traffic, as a result of increasing competition and to limit market share losses, in particular for long distance traffic, Telecom Italia has introduced a number of innovative tariff packages, such as Teleconomy No Stop and Teleconomy 24, intended to reduce its market share losses. Its overall strategy is to focus on pricing policy, customer service and loyalty, and new offers to achieve customer retention in order to stop or slow further losses in market share. By the end of 2001 the Teleconomy tariff packages had attracted over 4,080,000 subscribers an increase of 2,025,000 subscribers over the end of 2000.

In the domestic fixed line telecommunications services market, Telecom Italia has continued to pursue the new opportunities offered by Internet and data services that have offset, in part, the continuing decline in voice revenues. Telecom Italia believes it is in a strong position to capture the potential benefits to be derived from this market segment and intends to continue developing broadband networks in order to offer customers more bandwidth and convergent services.

The commencement of mobile telecommunications services in March 1999 by the third mobile operator in Italy, Wind, and the commencement by the fourth mobile operator in May, 2000 contributed to the increased competitive environment in the mobile telecommunications segment. This increased competition has caused TIM's total market share since 1999 to decrease by 14.5% although the total market has grown with a penetration rate of 89% at the end of 2001.

Divestitures and Cost Reduction Plan

In September 1999, following Olivetti's takeover of Telecom Italia, the Group implemented a restructuring plan which included the divestiture of certain group assets and a focus on cost reduction. During 2000 Telecom Italia largely completed this plan with the sale of Sirti (installation), Italtel (manufacturing), Teleleasing (leasing services), Meie (insurance), a sale of a significant portion of its real estate portfolio and certain other non-core assets.

These sales generated approximately €4,413 million in cash and were used to reduce the overall level of indebtedness at the end of 2000 which rose significantly as debt was incurred as a result of various acquisition and other investment activities during 2000, including the SEAT acquisition and international investments.

During 2000 the Group agreed to certain employee reductions with its unions, particularly in the fixed line business. As a result, at the end of 2000, total employment in the Group had been reduced in aggregate by 15,491, owing to personnel turnover, including permanent reductions in the fixed line business, and the effect of the changes in the scope of consolidation. In particular, other than the decrease of 6,793 units in Domestic Wireline (primarily attributable to Telecom Italia), the disposal of the Sirti and Italtel groups led to a reduction in the number of employees of 17,857, compensated in part by the addition of 2,894 units in mobile services (of which an increase of 1,229 was related to Maxitel), and the inclusion of the SEAT group (an increase of 7,179 in the Internet and Media Business Unit).

At December 31, 2001 the Group employed 109,956 persons, an increase of 2,785 employees compared to 107,171 at December 31, 2000 pro forma. The increase of 2,785 units is mainly due to the changes in thescope of consolidation (relating to the increases of 1,749 units in Internet and media and 1,464 units in Mobile Services as well as the inclusion of the Entel Chile group which led to an increase of 4,681 units) and a reduction of 5,460 units at Telecom Italia due to personnel turnover. The main component of the turnover relates to the termination of employment at the Telecom Italia level, partly as a result of employee cutbacks under Law No. 223/1991 following agreements with the labor unions in March and July 2000 and September 2001.

Following Olympia's acquisition of its stake in Olivetti from Bell S.A. and new management and a new Board of Directors taking control, the Group implemented a further restructuring plan. See "Item 4. Information on the Company—Business—Significant Developments during 2001—The Pirelli-Olimpia Transaction" and "—Reorganization". This plan also included further divestitures of assets, particularly non-strategic international assets. During 2001 and the first months of 2002 the Group sold certain satellite assets, its interests in Lottomatica (a 18.3% stake) and in Bouygues Decaux Telecom (a 19.61% stake); these disposals resulted in total net proceeds of €1,414 million.

The Group also expects to realize net proceeds of €1,850 million from the agreed sale of its stake in Auna during 2002.

Regulatory Environment

The regulatory environment in which the Group operates has been reshaped by the adoption and implementation of new laws and regulations at both the Italian and EU levels, including the Framework Law, the Maccanico Law, the Telecommunications Regulations and the Orders issued by the National Regulatory Agency.

The year 2001 continued to be characterized by an intensive implementation process in order to complete deregulation which the Group now considers to be complete. See "Item 4. Information on the Company—Business—Competition" and "Item 4. Information on the Company—Business—Regulation".

In January 2001 Telecom Italia's old Concession was converted to an Individual License for Voice Telephony (Network Installation and Voice Telephony Service). New services were included in the Reference Offer, as Flat Rate Access to Internet, Shared Access and Sub-loop Unbundling. Tariff rebalancing has been reinforced (with final tariff changes under tariff rebalancing planned for July 2002) and the price cap on retail prices will expire on December 2002. Carrier Preselection implementation and provisioning regulation took place, and local loop unbundling regulation was reinforced.

In December 2000 and January 2001, the National Regulatory Agency issued orders which established the prices and terms on which Telecom Italia is required to offer certain services on an unbundled basis (such as physical access to copper pairs and fiber optics, bitstream access, transmission links from MDF sites to switches and access to certain other network components) to other telecommunications operators to enable those operators to access directly end users by leasing the necessary network components from Telecom Italia.

The trials for local loop unbundling started in October 2000, with a duration of three months, and the first contracts with other licensed operators were signed in February 2001. At the end of 2001 3,200 lines were in local loop unbundling; at the end of April, the number was 21,000.

Tariff Rebalancing

Telecom Italia has progressively rebalanced its tariffs to align them more closely to underlying costs, including tariff adjustments made in each of 1997, 1998, 1999, 2000 and 2001. Further tariff adjustments were approved by the National Regulatory Agency and implemented effective February 1, 2002. In general, the tariff rebalancing pursued by Telecom Italia has involved a gradual increase in subscription fees for residential and business customers, along with a decrease in tariffs for domestic long distance and international calls. From February 2002, Telecom Italia offers to residential customers a certain volume of local calls minutes at zero price.

The overall effect on customers' total telephone bills of the tariff adjustments implemented during 2000 and 2001 are estimated as follows:

- €251 million per year (a decrease of 2.84%) in 2000; and
- €165 million per year (a decrease of 1.97%) in 2001.

These estimates are not cumulative and are based on certain average consumption patterns (called "consumption baskets" in regulatory terms - assuming the same volume of traffic for the prior year) and do not necessarily represent the overall effects of the tariff changes on the Group's accounts. The data above compares average levels of the customers' annual spending.

Following the EU Commission infringement procedure against the Republic of Italy concerning tariff rebalancing, on December 11, 2000, the National Regulatory Agency revised the price cap formulas in effect for rental and installation fees, and charges for local, national and international calls through December 2002. The change compared to the previous price cap formulas was an increase from RPI + 1% to RPI + 6% in the sub-price cap on installation fees and monthly rental charges. The same increase for access fees (RPI + 6%) was established by the National Regulatory Agency for the year 2002.

The general effect of the new price cap formulas for 2001 provided for an increase of up to 8.5% in Telecom Italia's access service charges (i.e. monthly subscription fee) and a reduction of 11% in Telecom Italia's domestic traffic charges. The changes in tariffs implemented as of February 1, 2002 which increased residential monthly subscription fees by 6.3% and reduced certain call traffic charges is expected to result in lower revenues from residential users of approximately €94 million.

Greater pricing flexibility has been important to Telecom Italia's ability to remain competitive, particularly with respect to international telecommunications services for which there has been the greatest competition, and it remains an essential element of Telecom Italia's strategy to be able to price services selectively in order to respond to competition by lowering prices on selected services.

See "Item 4. Information on the Company—Business—The Organizational Structure—Domestic Traffic—Domestic Fees and Tariffs—Tariff Rebalancing", "—International Traffic—International Tariffs—Tariff Rebalancing" and "—Regulation—Tariff and Pricing Policy—Pricing Policy and Telecom Italia's Tariffs".

Provisions and Write-downs

Results of operations in 2001 were disproportionately impacted (compared to prior years) by high levels of non-recurring expenses, including write-downs in investments and goodwill for subsidiary and affiliated companies. The following table sets out certain of these expenses and their impact on 2001 results, before income taxes. Additional information can be found in Notes 22 and 23 of Notes to the Consolidated Financial Statements included elsewhere herein.

(millions of Euro)	Value adjustments to financial assets	Financial expense	Other income and expense, net	Total
Impact of Argentina	356		50	406
Provisions and write-downs of goodwill and equity investments:				
-International Operations			2,136	2,136
-International operations of Mobile Services			547	547
-Internet and Media			416	416
-Satellite Services and TILAB BU	259		32	291
Impact of Stream			248	248
Provision for put option on Seat Pagine Gialle shares		569		569
Total nonrecurring expenses	**615**	**569**	**3,429**	**4,613**

- The provisions and write-downs of goodwill and equity investments are consistent with the strategic guidelines of the 2002-2004 Industrial Plan. In particular, after careful examination, adjustments were made to investments and goodwill and provisions were recorded for the losses of subsidiaries and affiliated companies in which it was apparent that the reason for the performance of the companies was not solely due to general economic conditions. The most important adjustments refer to:

  - International Operations: GLB Serviços Interativos (Globo.com), 9Telecom group, Entel Bolivia, Solpart Brazil and Telekom Austria.

  - International operations of Mobile Services: Maxitel, Bitel (Tele Celular Sul, Tele Nordeste Celular) and TIM Brasil (TIM Celular Centro Sul, TIM Sao Paulo and TIM Rio Norte).

  - Internet and Media: NetCreations, Matrix, Mondus and costs connected with the restructuring of La7 television programming.

  - Satellite Services and TILAB: this includes the effect of the writedown of Astrolink by Telespazio, on account of the suspension of the relative project.

- The impact of Argentina comprises the value adjustments made with respect to current economic conditions in Argentina which caused significant exchange differences after parity between the Argentine peso and the US dollar was abandoned.

- The impact of Stream includes the provision made under the agreement with Vivendi/Canal Plus for the sale of the investment in this company. For further developments on the sale of Stream, please see "Item 4. Information on the Company—Recent Developments".

- The provision for the commitment of the put option on Seat Pagine Gialle S.p.A. shares is connected to the nonrecoverability of the original price to exercise the option, as described in more detail below.

Such non-recurring expenses, after tax benefits of €1,577 million, had the impact of reducing net income in 2001 by €3,036 million.

Critical Accounting Policies

Telecom Italia's discussion and analysis of its financial condition and results of operations are based upon Telecom Italia's consolidated financial statements, which have been prepared in accordance with Italian GAAP. Reported financial condition and results of operations of Telecom Italia are sensitive to accounting methods, assumptions and estimates that underlie the preparation of financial statements generally. Telecom Italia bases its estimates on historical experience and on various other assumptions that Telecom Italia believes are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing Telecom Italia's financial statements. Telecom Italia believes the following critical accounting policies involve the most significant judgments and estimates used in the preparation of its consolidated financial statements.

Revenue Recognition

Telecom Italia's primary revenue streams consist of fixed line telecommunication services, mobile telecommunication services, the sale of products including primarily telecommunication (both fixed and mobile) equipment and office products, IT software and services, advertising services, publishing, and internet access and related services.

Revenues related to fixed line and mobile telecommunication services, principally network access, long distance, local and wireless airtime usage, are recognized when the services are provided based on the actual minutes of traffic provided and the contracted fee schedule with the customer. Certain revenues derived from telecommunication services, such as installation and activation fees are recognized at the date of installation or activation. Revenues billed in advance are deferred and recognized at the date the related service is provided.

Under U.S. GAAP, we defer recognition of non-refundable connection fees and other initial fees and recognize these over the estimated customer relationship period. We also defer the associated direct expenses over the estimated customer relationship period in an amount equal to or less than the amount of deferred revenues. If the length of the estimated customer relationship period increases or decreases, the amounts of deferred revenue and deferred expense is adjusted over the revised estimated life.

Revenues from the sale of products, including telecommunication equipment and office products, are recognized when title transfers to the customer, which is either at the date the products are shipped or when the products are delivered and accepted by the customer.

IT services and software revenues are recognized at the date the related services are provided.

Revenues from the sale of advertising and publishing are recognized at the date of publication, which corresponds to the time at which the related publications are printed and delivered. Advertising revenue from on-line services is recorded on the date the on-line advertisement is posted to the related web site. Advertising revenue from television is recorded on the date at which the advertisement is shown. Payments received for advertising services to be rendered in future periods are deferred and recognized at the time the advertising is provided.

Revenues from Internet access and related services primarily represent subscription services, which are recognized over the subscription period on a straight-line basis.

Provisions for returns and other adjustments related to sales are provided in the same period the related sales are recorded. The provision is based on an analysis of historical return patterns, which are subject to such factors as product quality, warranty lives and macroeconomic factors.

In connection with recording revenue, estimates and assumptions are required in determining the expected conversion of the revenue streams to cash collected. The reserve estimation process requires that management make assumptions based on historical results, future expectations, the economic and competitive environment and changes in the credit worthiness of the Group's customers, and other relevant factors. If these assumptions prove to be incorrect, Telecom Italia's actual conversion rate of recorded revenue to cash may be lower than expected and we would be required to increase our allowance for doubtful accounts.

Accounting for Long-lived Assets

Property, plant and equipment and purchased intangible assets other than goodwill are recorded at acquisition cost. If such assets are acquired in a business combination, the purchase price is allocated to the estimated fair value of the acquired property, plant and equipment and intangible assets. Property, plant and equipment and intangible assets are depreciated or amortized on a straight-line basis over their estimated useful lives.

Property, plant and equipment are valued at acquisition or construction cost, less accumulated depreciation. Construction costs include directly allocable costs, an appropriate allocation of material and production overhead and interest accruing during the construction related to debt specifically associated with the related construction project.

Accounting for long-lived assets and intangible assets involves the use of estimates for determining the fair value at the acquisition date for assets acquired in a business combination, and the useful lives of the assets over which the costs of acquiring these assets are charged to the income statement. The useful lives of long-lived assets are subject to such variables as technological feasability, and obsolescence, changes in consumer demand and strategic management decisions.

When an impairment in the value of assets occurs, nonscheduled write-downs are made. Telecom Italia assesses the impairment of identifiable intangibles and long-lived assets whenever there is reason to believe that the carrying value may exceed the fair value and where a permanent impairment in value is anticipated. The determination of impairments of long-lived and intangible assets involves the use of estimates, which include but are not limited to the cause, the expected timing and the amount of the impairment. Impairment is based on a broad measure of factors. In evaluating assets for impairment, Telecom Italia typically considers, among other things, technological obsolescence, discontinuance of services, changes in market prices, significant negative industry or economic trends, significant underperformance relative to expected historical or project future operating results and other changes in circumstances that may indicate impairment.

Valuation of Goodwill

Goodwill resulting from business combinations is amortized on a straight-line basis over its estimated useful life.

The determination of goodwill is dependent on the allocation of the purchase price to the tangible and intangible assets acquired and liabilities assumed. Such allocation is often based on judgmental factors and estimates of fair values for assets that may not have a readily determinable market value. In addition, the useful life assigned to goodwill is an estimate based on the judgment of management at the time of acquisition. The estimated useful life is subject to adjustment if facts and circumstances indicate that the assets' economic life has been affected by other variables, including technological, feasability, competitive factors and contractual rights.

Nonscheduled write-downs are provided when an impairment in the value of goodwill occurs. Telecom Italia reviews on a regular basis, the performance of its subsidiaries and acquired businesses. When there is reason to believe that the goodwill arising from the acquisition of a business is impaired and that the impairment is of a permanent nature, Telecom Italia compares the carrying amount of that subsidiary or business to its fair value. The determination of the fair value of a subsidiary involves extensive use of estimates, depending on the method used and significant judgment is involved. Methods commonly used by Telecom Italia for valuations include discounted cash flow methods, comparable market multiples and quoted stock market prices, if available. Factors affecting estimated fair values typically include discount rates, future cash flows, growth rates, weighted average cost of capital, market prices and control premiums. These estimates, including the methodologies used, are important in determining fair value and ultimately the amount of any goodwill impairment.

Starting in 2002, for purposes of U.S. GAAP the Group will implement the requirements of SFAS 142, "*Goodwill and Other Intangible Assets*". The new pronouncement will require the Group to suspend the amortization of goodwill and qualifying intangible assets with indefinite lives. Intangible assets will require a recoverability test based on their fair values. If asset prices and valuations within the segments of the market in which the Group operates are depressed in the future, the impairment indicators of SFAS 142 could be triggered, requiring additional write downs of intangible assets based on their fair values. See also note 26 and 28(n) of Notes to the Consolidated Financial Statements for a discussion of impairments recorded under U.S. GAAP in 2000 and 2001.

Financial Assets

Telecom Italia holds minority interests in companies having operations or technology in areas within its strategic focus, some of which are publicly traded and have highly volatile share prices. Telecom Italia records an investment impairment charge when it believes an investment has experienced a decline in value that is permanent. Determining whether an impairment is permanent involves considerable judgment and relies heavily on an assessment by management regarding the future development of the investee. In measuring impairments, Telecom Italia uses fair value as described above for goodwill impairments.

Future adverse changes in market conditions or poor operating results of underlying investments could result in losses or an inability to recover the carrying value of the investments that may not be reflected in an investment's current carrying value, thereby possibly requiring an impairment charge in the future.

Deferred Taxes

Telecom Italia is required to estimate its income taxes in each of the jurisdictions in which it operates. This process involves the jurisdiction-by-jurisdiction estimation of actual current tax exposure and the assessment of the temporary differences resulting from differing treatment of items, such as accruals and amortization, among others, for tax and financial reporting purposes. These differences result in deferred tax assets and liabilities, which are included within Telecom Italia's consolidated balance sheet. Telecom Italia must assess in the course of its tax planning procedures the ability of the Company and its subsidiaries to obtain the benefit of deferred tax assets based on expected future taxable income and available tax planning strategies. If in management's judgment, the deferred tax assets recorded will not be recovered, a valuation allowance is recorded to reduce the deferred tax asset.

Significant management judgment is required in determining Telecom Italia's provision for income taxes, deferred tax assets, deferred tax liabilities and valuation allowances to reflect the potential inability to fully recover deferred tax assets. In the Group's Italian GAAP financial statements, the Group generally applies a realization period of three to five years for the recognition of both deferred tax assets and liabilities. The analysis is based on the estimates of taxable income in the jurisdictions in which the group operates and the period over which the deferred tax assets and liabilities will be recoverable. If actual results differ from these estimates, or Telecom Italia adjusts these estimates in future periods, Telecom Italia may need to establish an additional valuation allowance which could adversely affect Telecom Italia's financial position and results of operations.

Under U.S. GAAP, the Group assesses the recoverability of tax assets based on the criteria of "more likely than not", that is, a probability of recoverability just over 50%. The probability assessment requires significant judgment regarding the timing of future book and tax reversals, which could be materially different from the actual results.

Accrued Liabilities

Considerable judgment is exercised by Telecom Italia in recording the Company's accrued liabilities and its exposure to contingent liabilities related to pending litigation or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation as well as other contingent liabilities.

Judgment is necessary in assessing the likelihood that a pending claim will succeed or a liability will arise and to quantify the possible range of the final settlement. In case the occurrence of a contingency or potential liability is more likely than not, Telecom Italia accrues an amount for contingent liabilities that represents management's estimate at that date. Because of the inherent uncertainties in the foregoing evaluation process, actual losses may be different from the original estimated amount accrued.

Financing, Acquisition and Lease Transactions

Telecom Italia has entered into several financing, acquisition and lease transactions that have resulted in material off balance sheet accounting treatment. These transactions include entering into a put and call-agreement related to the acquisition of SEAT, the sale and the subsequent lease of certain real estate assets, the sale of a portion of Telecom Italia' s equity interest in certain satellite sector entities, and the sale of trade accounts receivable under a securitization program.

Telecom Italia has acquired several companies using the shares of listed subsidiaries as a form of currency, often times in conjunction with a mix of cash and equity. For purposes of purchase accounting, no economic value is ascribed to these shares, therefore the recorded value of the acquired company does not reflect the value of the underlying shares traded. For purposes of U.S. GAAP, the shares of the subsidiaries used to acquire a target are fair valued as part of the purchase price, generally based on the quoted market price of the shares that day. As there is an economic value ascribed to these shares, the total investment in the acquired company is generally larger, including the associated goodwill, on a U.S. GAAP basis. Starting in 2001, as part of the adoption of SFAS 142, this goodwill will no longer be amortized, but will instead become subject to the fair value impairment tests as previously described.

Under Italian GAAP the put call arrangement associated with the acquisition of SEAT effectively results in a commitment of the Company to acquire a certain number of additional shares of SEAT at an agreed upon price. Neither the increase in the value of the investment in SEAT, nor the related commitment are required to be recorded as an asset and liability, respectively. Under U.S. GAAP these types of arrangements, and others entered into by the Group that involve the use of puts and calls as a means to effect a transaction, are accounted for based on the substance of the underlying contractual rights and benefits, and can serve to increase the acquisition cost, total indebtedness or compensation expense.

The sale and the subsequent lease of certain real estate assets, the sale of a portion of Telecom Italia' s equity interest in certain satellite sector entities, and the sale of accounts receivable under securitization programs have been recorded as sale transactions and gains or losses were recognized for the differences between the fair value of the consideration received and the carrying value of the real estate assets, investments, and receivables sold. The real estate assets sold continue to be used in the ordinary course of operations of the Group and are accounted for as operating leases. Management has substantial flexibility in structuring transactions to effect the recognition of assets, liabilities' gains and losses.

Results of Operations

General

During 2000 Telecom Italia completed the merger of Tin.it, its internet service provider, with SEAT, in a transaction which resulted in the Telecom Italia Group owning approximately 60% of SEAT' s ordinary share capital. Although SEAT was fully consolidated for balance sheet purposes at December 31, 2000, SEAT' s results of operations were not included in the Group' s income statement for purposes of Italian GAAP. As a result, the full impact of the SEAT acquisition is included in results of operations beginning only in 2001. Therefore the results of operations of the Internet and Media Business Unit is not comparable between 2001 and 2000 and 1999 due to the SEAT acquisition. SEAT, as merged with Tin.it makes up Telecom Italia' s Internet and Media Business Unit.

Late 2000 marked the start of the transformation of the Telecom Italia Group announced in conjunction with the take-over by Olivetti. The transformation was shaped by the divestiture of non-core businesses, the focus on the core areas and the reorganization of the controlling structure of the international companies as well as the reorganization into seven autonomous Business Units from the standpoint of management, objectives, strategies and operational leverage.

At the beginning of 2001 the Group reorganized its businesses into business units and began reporting its results by business unit during 2001. The Business Units consist of the following:

Domestic Wireline. This business unit includes Telecom Italia Domestic Wireline (TIDW) which relates to the Italian domestic fixed line voice and data businesses on the fixed network; includes, also, national businesses such as Atesia, related to call center, telemarketing and market researches and international activities relating to developing networks such as the European, Mediterranean and Latin American fiber optic rings as well as TMI.

Mobile Services. This business unit includes national and international mobile telecommunications businesses which are managed by TIM. Beginning in 2001 international mobile operations were consolidated with, and managed by TIM, through TIM International. International mobile operations are concentrated in the Mediterranean Basin and in Latin America.

Internet and Media. This business unit includes the SEAT group which was consolidated with the Telecom Italia Group in results of operations for the first time in 2001. This business segment includes a multimedia network, whose main business areas include advertising, publishing, information marketing, business information, call center services, the Internet and television.

International Operations. The International Operations business unit manages and develops international fixed line and certain integrated companies providing fixed-mobile services.

Information Technology Services. This business unit is responsible for all information technology services within the Group, including IT services provided to the other business units as well as such services offered in the market.

Satellite Services. This business unit (consisting of the Telespazio group and Telecom Italia's "Satellite Telecommunications" business segment) is responsible for developing satellite communication systems for phone and data, radio and television broadcasting and earth observation.

TILAB and Other Operations. Includes research and development activities of the Group as well as certain other activities such as real estate and financing activities.

For a complete description of these Business Units, see "Item 4. Information on the Company— Business — Business Units." For purposes of the following discussion selected financial data of each Business Unit has been provided for 1999, 2000 and 2001.

2002-2004 Industrial Plan

Following Olympia's acquisition of its stake in Olivetti and replacement of the previous Telecom Italia Board of Directors and senior management, the new management team and Board of Directors adopted, in February 2002, a new business and financial plan, intended to strengthen the Group's financial position (the guidelines of the plan were announced in September 2001). The new plan provided for a strong focus on the core business and development of a leadership position in the markets where the Group operated, with a plan for divestiture, principally of international assets, where such leadership position (or a position of control) was not likely to be achieved.

Strengthening of financial position. In November 2001 it was announced that, over a period of 24 months, €5 billion would be raised by Telecom Italia through divestments.

Telecom Italia has completed or entered into the following agreements for divestments:

- Sale of stake in former satellite consortia which generated net proceeds of €450 million;
- Subscription to the public tender offer launched for Lottomatica which generated proceeds of €212 million;
- An agreement reached with Endesa, Union Fenosa and Santander Central Hispano for the sale of Telecom Italia's 26.9% holding in Auna (the vehicle through which the Group held its Spanish assets)

which will result in net proceeds of €1.85 billion. The closing of this transaction is subject to receiving approvals of the Spanish regulatory authorities;

- The sale of TIM International's 19.61% interest in BDT, the company that controls Bouygues Telecom, for a total value equal to approximately €750 million (closed in the first quarter 2002);

- Agreement with News Corporation and Vivendi Universal/Canal Plus to sell 50% of Telecom Italia's interest in Stream for U.S.$42 million (€47 million). Due to changes in the Vivendi and News Corporation agreement with respect to the acquisition of Telepiù, as of the date of this report the sale of Stream is in discussions;

- In connection with further initiatives to realize value from real estate operations, the Group expects to conclude the sale of its 40% interest in Telemaco Immobiliare, the company now holding certain of Telecom Italia's real estate assets, for an estimated total gross proceeds of approximately €200 million;

- An agreement with Pirelli & C. Real Estate S.p.A., Pirelli S.p.A., HSHC Italy Holdings B.V. and Popoy Holding B.V. with regard to the so called "Tiglio Project" with estimated gross capital gains of approximately €170 million;

- An agreement for the sale of TIM's 25% stake in Mobilkom for a total consideration of €716 million (of which €690 million is the price for the stake and €26 million as dividend for the 2001 financial year). The sale is expected to close by the end of June 2002. At the same time the Group reached an agreement with ÖIAG (Österreichische Industrieholding AG, Telekom Austria's main shareholder) for a gradual and coordinated disposal of Telecom Italia's interest in Telekom Austria, starting from the second half of 2002; and

- An agreement for the sale of Telecom Italia's stake in the 9Telecom Group to Louis Dreyfus Communications Group ("LDCOM"). The agreement is subject to approval by the relevant French regulatory authorities. For more details of these transactions, see "Item 4. Information on the Company — Business — Recent Developments".

These transactions have resulted in significant capital gains at the consolidated level. The net proceeds have been and will be largely used to reduce Group indebtedness.

Actions targeted at improving the Group's financial position also included additional Telecom Italia debt financings, in the principal amount of 4 billion euros since September 2001. These contributed to an improvement of the net debt structure, of which the medium to long-term component has risen from 64% as of December 31, 2001 to 80% of the total net debt as of March 31, 2002.

Strategic Growth. The objective is to create value by leveraging infrastructure, already available technologies and distinctive skills, consisting of:

- An integrated pan-European network extending over 120,000 km;
- One of the world's largest GSM networks;
- 8 Internet Data Centers;
- 8,000 Points of Sale in Italy;
- Expertise in network management and development;
- Rapid broadband service activation;
- Innovation skills for the mobile network;
- Information Technology leadership.

The investment plan of approximately €16 billion for the next three years is focused on strengthening competitiveness as the basis for the Group's international growth strategy and leveraging technological innovation. The plan provides for:

- Approximately €7 billion for fixed-line network services, 55% of which is targeted on innovation (xDSL, data services, fiber-optics) and the remaining 45% on maintaining and upgrading existing networks;

- Approximately €7 billion on mobile network services, with 83% earmarked for innovation (GPRS, UMTS, VAS) and the remaining 17% for maintaining and upgrading existing networks;

- Approximately €1 billion on IT and IP services;

- Approximately €700 million on technological innovation, a business that occupies a key place in the Group's development plans, through synergies expected to be obtained from the collaboration between Telecom Italia LABS and Pirelli LABS.

The Group has developed strategies for each of its business units. A summary of these strategies for the principal Business Units is set forth below.

Domestic Wireline. Domestic Wireline will be oriented towards defense of market share on voice, development of broadband services, optimization of capital expenditure and operating expense excellence in customer relationship. The growth in revenues from data services, mainly driven by broadband growth, assumes the following growth rates by 2002: 10%; 2003: 11%; and 2004: 13%:

- For ADSL technology, average growth rates, for mass market and SOHO, exceeding 100% as access numbers increase to 1.5 million (at the end of 2001 users of ADSL numbered over 80,000);

- For fiber-optic technology, average annual growth in excess of 25%, as the fiber network is extended by a further 800,000 km (at the end of 2001 it was 3.2 million km);

- Average annual growth of 45% in revenues generated by broadband services to the business market;

- Average annual growth of 50% in revenues generated by Web services to the business market.

There can be no assurance that these growth rates will actually be achieved.

Mobile Services. The mobile network is expected to benefit from:

- Rapid introduction of new GPRS and UMTS technologies, which by the end of 2004 is expected to account for more than 60% of total lines;

- Strong growth in revenues generated by VAS, reaching an annual compound growth rate in the next three years (2002-2004) of more than 35%. The growth rate in VAS in 2001 was 57%.

There can be no assurance that these growth rates will actually be achieved.

Internet and Media. Some of the main priorities of the industrial operations defined are:

- To refocus business by selecting core activities and optimum management of the balance between cost/revenues in the Internet and Television areas;

- To overhaul the organizational structure, introducing professional families oriented towards strong central control and greater supervision of the business;

- To reinforce leadership as a multiplatform media company, leveraging strong stand-alone businesses, developing an integrated business portfolio and optimizing the synergies/links among the different platforms and business areas;

- To make the most of the "connection" business model, increasing market share in broadband internet access and emphasizing the Group's role as an integrated ISP/portal.

International operations. International operations will be oriented towards:

- Leveraging the European backbone, which will be extended to approximately 20,000 km and connect 13 countries, through the development of Internet protocol broadband services and capitalization on growth in domestic demand for international data transmission, where appropriate through targeted joint ventures and acquisitions;

- Development of the GSM network in South America, by rapidly integrating subsidiary companies in Brazil to create the country's first nationwide carrier; strengthening the Group's position in countries where GSM networks are already provided (Perù, Bolivia, Chile and Venezuela); and a significant focus on innovative service offerings. The Group's objective in the South American market is to reach 12.8 million GSM lines by the end of 2004, compared with the current figure of 2.8 million.

Change in Scope of Consolidation

The results of operations of the Group fully consolidate all Italian and foreign subsidiaries in which Telecom Italia holds, directly or indirectly, greater than 50% of the voting stock or has dominant influence (effective control). The results of operations of the Group for the year 2001 accounted for the associated companies Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group) under the equity method. In 2000 the Nortel Inversora group had been proportionately consolidated on a line-by-line basis, as permitted by Italian Law 127/1991, Article 37. 2000 has been prepared on a pro forma basis to account for the Nortel Inversora group on the equity method. Nortel Inversora was accounted for using the equity method in 1999. Other entities in which Telecom Italia holds, directly or indirectly, between 20% and 50% of the voting rights are accounted for under the equity method. These include a large number of its international investments. The equity in the earnings of such entities (Telecom Italia's proportional share in the profits or losses of these entities) are included in financial expense. See Note 22 of Notes to the Consolidated Financial Statements included elsewhere herein.

For purposes of the discussion which follows, we will only use the pro forma 2000 numbers so that all three years, 2001, 2000 and 1999, will be comparable as it relates to the treatment of the Nortel Inversora group.

The following main changes in the scope of consolidation took place during 2001 and 2000:

- the groups Seat Pagine Gialle, Jet Multimedia, Magéos Explorer and Maxitel and the company Digitel were acquired at the end of 2000 and were consolidated in 2000 only for balance sheet purposes. These groups and company are fully consolidated in 2001, including in the statement of operations;

- the Entel Chile group is included in the scope of consolidation beginning in 2001. Prior to 2001 this group was accounted for on an equity basis;

- the Sirti and Italtel groups, disposed of during the last part of fiscal 2000, were consolidated only in the statement of operations for the period from January 1, 2000 to September 30, 2000, while in 1999 they were consolidated for the entire year.

Recent Developments – Group Results for the First Quarter Ended March 31, 2002 compared to March 31, 2001 (pro forma)

The information in this section should be read in conjunction with Telecom Italia' s consolidated financial statements, and the notes thereto, included elsewhere in this Annual Report.

The summary historical consolidated financial data for the Group as of March 31, 2002, and for the three months ended March 31, 2001, have been derived from unaudited interim consolidated financial statements which, in our opinion, reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of our results of operations for the unaudited interim periods. Results for the three months ended March 31, 2002 are not necessarily indicative of results that may be expected for the entire year.

For purposes of comparison, the statement of operations items are shown in comparison to the three months ended March 31, 2001 data which have been prepared on a pro forma basis to give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

	Three Months Ended March 31,	
	2001(1) (pro forma)	**2002**
	(Unaudited) (millions of Euro)	
Statement of Operations Data:		
Operating revenues	7,129	7,265
Other income	94	73
Total revenues	7,223	7,338
Cost of materials	370	295
Salaries and social security contributions	1,147	1,170
Depreciation and amortization	1,493	1,421
Other external charges	2,708	2,815
Changes in inventories	(154)	(21)
Capitalized internal construction costs	(62)	(73)
Total operating expenses	5,502	5,607
Operating income	1,721	1,731
Financial income	239	171
Financial expense	(849)	(681)
of which writedowns and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies, net	*(298)*	*(34)*
Other income and expense, net	84	543
Income before income taxes and minority interests	1,195	1,764
Income taxes	(622)	(624)
Net income before minority interests	573	1,140
Minority interest	(187)	(419)
Net income	386	721

(1) The 2001 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

	As of December 31, 2001	As of March 31, 2002
		(Unaudited)
	(millions of Euro)	
Balance Sheet Data:		
Total current assets	16,736	16,939
Total fixed assets	21,757	21,323
Total short-term debt	9,114	4,817
Total current liabilities	21,945	17,817
Total long-term debt	16,083	18,834
Total liabilities	43,361	41,437
Total shareholders' equity before minority interest	13,522	14,519

The following table sets forth operating revenues, gross operating profit and operating income by Business Unit.

	Operating Revenues		Gross Operating Profit		Operating Income	
	Three months ended March 31,		Three months ended March 31,		Three months ended March 31,	
	2001(1) (pro forma)	2002	2001(1) (pro forma)	2002	2001(1) (pro forma)	2002
	(Unaudited) (millions of Euro)					
Domestic Wireline(2)	4,215	4,172	1,941	1,943	1,149	1,200
Mobile Services	2,396	2,498	1,177	1,221	816	831
Internet and Media	292	333	23	27	(53)	(69)
International Operations	443	478	97	96	(40)	(22)
IT Market(2)	246	270	33	32	25	25
IT Group(2)	209	196	28	(1)	(4)	(29)
Satellite Services	65	65	5	4	(4)	(5)
Other activities and elimination	(737)	(747)	(17)	(48)	(168)	(200)
Total	7,129	7,265	3,287	3,274	1,721	1,731

(1) The 2001 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(2) In early 2002, the Information Technology Business Unit was split into two distinct units: Information Technology – Market and Information Technology – Group; beginning January 1, 2002 Saritel S.p.A. is consolidated in the Information Technology – Group Business Unit instead of in Domestic Wireline. For purposes of comparison, the 2001 data of the Business Units have been reclassified.

Group Consolidated Results

For the three months ended March 31, 2002, the consolidated net income after minority interests was €721 million compared to €386 million for the first three months of 2001, an 86.8% increase. The significant increase in consolidated net income after minority interest was primarily attributable to the recognition of capital gains from asset disposals (€339 million in the first quarter 2002 compared to €94 million in the first quarter 2001) as well as a significant reduction in net write-downs and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies which declined from €298 million in the first quarter of 2001 to €34 million in the first quarter of 2002. The lower levels in the first quarter 2002 also reflected the high level of adjustments taken in the fourth quarter of 2001.

The gains realized in the first quarter of 2002 related to the following:

- Sale of the 19.61% stake held by the Mobile Services Business Unit in Bouygues Decaux Telecom (BDT), resulting in a net gain of €484 million, which contributed €266 million to the consolidated net income of the Telecom Italia Group; and

- Acceptance of the tender offer for the purchase of Lottomatica stocks by the Information Technology - Market (Finsiel group), resulting in a net gain of €93 million, which contributed €73 million to the consolidated net income of the Group.

Telecom Italia's consolidated operating revenues for the three months ended March 31, 2002 were €7,265 million, an increase of 1.9% compared to the same period in 2001. The increase in operating revenues of €136 million was due to continued revenue growth from Mobile Services and growth in revenues from Internet and Media and Information Technology offsetting a slight fall in revenues generated by Domestic Wireline (which posted an 8.7% increase in traffic minutes), as price cuts scheduled by the National Regulatory Agency came into effect and lowered the average returns on traffic.

As of March 31, 2002, Telecom Italia had 27.3 million domestic subscriber fixed lines, including ISDN equivalent lines (substantially in line with domestic subscriber fixed lines as of December 31, 2001 and March 31, 2001) and TIM in Italy had 24.1 million domestic mobile lines (compared to 23.9 million as of December 31, 2001 and 22.0 million as of March 31, 2001).

Telecom Italia's consolidated gross operating profit (operating revenues plus operating grants and reimbursements for personnel costs and costs of external services rendered (included in other income) less operating expenses other than provision for bad debts, write-downs of fixed and intangible assets, provision for risk, other provisions and operating charges and depreciation and amortization ("Gross Operating Profit")) was flat at €3,274 million for the three months ended March 31, 2002 compared to €3,287 million for the three months ended March 31, 2001.

Gross operating margin (Gross Operating Profit as a percentage of operating revenues) was 45.1% for the three months ended March 31, 2002, compared to 46.1% for the three months ended March 31, 2001. Although the Italian "domestic" gross operating margins were stable – Telecom Italia Domestic Wireline went from 46.5% in 2001 to 46.8% in 2002 and TIM S.p.A. from 53.3% to 53.5% - the international component accounted for a higher percentage of Gross Operating Profit with margins that were lower than average in both wireline and mobile telecommunications. Furthermore, the Internet and Media Business Unit was affected by the consolidation of the TV area (with a negative impact of €13 million). The rationalization of the Information Technology – Group Operational Activity is currently in progress.

Telecom Italia's consolidated operating income (total revenues less total operating expenses, including depreciation and amortization and other charges) was also flat on a quarter on quarter basis at €1,731 million for the three months ended March 31, 2002 compared to €1,721 for the three months ended March 31, 2001. As a percentage of revenues, operating income decreased to 23.8% from 24.1% in the first quarter of 2001. The slight improvement in amount is particularly due to the reduction in amortization and depreciation charges, whereas the percentage margin was affected by the same factors as the gross operating profit.

Financial income and financial expense, net showed a negative balance of €510 million, with an improvement over the same period of the prior year of €100 million mainly as a result of the followings:

- higher financial expense, net, due to the effect of increased average debt exposure during the period and higher expenses connected with the management of exchange and interest rate risk, as compared to the first quarter of 2001;

- the reduction in the net write-downs and equity in losses in unconsolidated subsidiaries, affiliated and other companies which reflects primarily the Group's proportionate share of the results of operations for the Group's equity method investments. This can be ascribed to lower goodwill amortization charges following the write-downs of international investments made in the 2001 financial statements and the higher results of some foreign associated companies. This caption was not affected by the results of the investments in Nortel Inversora (Telecom Argentina) and the Auna group. The investment in Nortel Inversora, which carrying value was written off in the consolidated financial statements for the year ended December 31, 2001, remained unchanged. As regards the Auna group, no change was made to the carrying value in the 2001 consolidated financial statements since an agreement was reached for the sale of the investment.

Consolidated net income before minority interest increased to €1,140 million in the three months ended March 31, 2002 from €573 million in the three months ended March 31, 2001. Consolidated net income after minority interest for the three months ended March 31, 2002 was €721 million, up 86.8% compared with the first quarter of 2001; excluding the gains from the disposals, mentioned above, consolidated net income after minority had been increased by approximately 31%.

Net financial debt of €20,618 million decreased from December 31, 2001 by €1,324 million, mainly as a result of the followings:

- cash flow from operating activities was higher than capital expenditures (goodwill included) and financial investments totaling to €1,227 million (€4,708 million in the first three months of 2001);

- disposals of €1,076 million, which include €962 million for the divestiture of the investments in Bouygues Decaux Telecom (€750 million) and Lottomatica (€212 million).

During the first quarter the Group also further increased the proportion of its total net financial debt with a maturity over one year with a further €2.5 billion offering under its Global MTN program. At March 31,2002, 80% of the Group's debt had a maturity of over one year compared to 64% at December 31, 2001.

The securitization program, begun in June 2001, also continued for trade accounts receivable generated by the services rendered to residential customers of Telecom Italia S.p.A. The securitization of receivables led to an improvement in net financial debt as of March 31, 2002 of about €644 million (€848 million at the end of 2001).

As of March 31, 2002, the Telecom Italia Group had 108,831 employees, a decrease of 1,125 compared to December 31, 2001. The largest change took place in the Domestic Wireline Business Unit (with a decrease of 928 employees), Mobile Services (with an increase of 403 employees) and the Internet and Media Business Unit (with a decrease of 524 employees).

Business Units

The following discussion relates to the Group's principal Business Units as they were reorganized at the beginning of 2002. Changes which occurred are the followings:

- The Business Unit Information Technology Services was divided into two new organizational structures:

  - Information Technology Group (ITG): the companies comprising the ITG Operating Activity (IT Telecom, Telesoft group, Netsiel, Sodalia, Netikos) are oriented towards increasing efficiency and quality within the framework of service activities directed at all the Business Units of the Telecom Italia Group operating on the market.

  - Information Technology Market (ITM): the companies comprising the ITM Business Unit (Finsiel group) will continue to pursue activities geared directly to the external market. This market is made up of central and local administrations moving towards decentralization and e-government, as well as banks and businesses.

- Saritel has been consolidated with the Information Technology Group Business Unit rather than in the Domestic Wireline Business Unit. For the purposes of comparison, the 2001 data for the two business units have been reclassified.

- TILAB which in 2001 was a separate business unit has been included in the Information Technology Group Operational Activity.

Domestic Wireline

Domestic Wireline gross operating revenues for the three months ended March 31, 2002 were €4,172 million, a decrease of 1% compared to €4,215 million for the three months ended March 31, 2001. The decline was primarily attributable to a decrease in traffic revenues of 8.1% mainly due to a reduction in average call prices, despite an increase of 8.7% in terms of minutes. The decline in traffic revenues was offset in part by significant growth in revenues from wholesale services provided to other Italian and international carriers and ISPs (an increase of 13.6%) as well as revenue growth from data and web offerings to business. Although these services contributed to the increase in minutes, as did the discount policies implemented to promote customer retention and loyalty, the average yield on traffic declined as this mix of traffic is less profitable.

The Domestic Wireline Business Unit' s market share of voice services at March 31, 2002 was approximately 71% (a decline of 6% with respect to December 31, 2001, partly offset by the success of its Teleconomy flat rate tariff plan).

Despite the revenue decline, Gross Operating Profit was unchanged at €1,943 million for the first quarter of 2002 compared to €1,941 million for the three months ended March 31, 2001.

The Domestic Wireline Business Unit showed improved Gross Operating Profit despite a 15.5% reduction in average per-minute prices for voice call traffic in the retail and wholesale market for the three months ended March 31, 2002 compared to the same period in 2001. This price reduction was partially offset by:

- Significant increases in wireline traffic volumes measured by minutes (a total increase of 8.7%), with retail fixed-mobile traffic increasing by 4.7% and traffic from other operators (national and international) increasing by 47%; and

- A 2.1% reduction in labor costs, costs of material and other external charges.

The Domestic Wireline Business Unit gross operating margin for the three months ended March 31, 2002 increased to 46.6% from 46.0% for the first three months of 2001. The improvement was due to the cost savings generated by further reductions in personnel, lower general and administrative expenses and network efficiency.

Operating income improved by 4.4% to €1,200 million for the three months ended March 31, 2002 from €1,149 million for the first three months of 2001.

Data transmission and internet services for businesses continued to grow and, at the end of March 2002, there were contracts for 119,000 Broadband accesses using xDSL and fiber optics technologies. Broadband penetration grew from certain mass market and small office and home office offers (more than 245,000 ADSL accesses sold at the end of March 2002) as well as from wholesale offers targeted at ISP and other telecommunication carriers (approximately 154,000 accesses sold at the end of March 2002). As of early May 2002, there were over 518,000 Broadband accesses sold to the mass market and wholesale market.

As of March 31, 2002, the Domestic Wireline Business Unit had 56,903 employees a reduction of 928 compared to December 31, 2001.

Mobile Services (TIM group)

TIM group gross operating revenues were €2,498 million for the three months ended March 31, 2002, a 4.3% increase over gross operating revenues for the same period in 2001 (€2,396 million). This increase was primarily due to continuing growth in the domestic mobile telecommunications sector, especially in traffic volume, as well as improvements in STET Hellas (the Greek mobile operator) and Digitel, the Venezuelan mobile operator. The increase in revenues was offset by negative exchange rate movements which reduced revenues by €48 million; this effect is principally due to Brazilian and Venezuelan group companies.

Consolidated Gross Operating Profit increased by 3.7% to €1,221 million for the three months ended March 31, 2002 from €1,177 million for the three months ended March 31, 2001. The gross operating margin declined slightly from 49.1% for the first three months of 2001 to 48.9% for the first three months of 2002. This slight decline was attributable to the start-up of international companies and, in particular, the Brazilian companies, which will launch services using the GSM technologies, and above all to the rising labor costs due to the average growth in staff levels.

TIM group operating income for the three months ended March 31, 2002 increased by 1.8% to €831 million compared to the first three months of 2001.

As of March 31, 2002, the TIM group had 39.7 million wireless lines, not including Telecom Italia Group wireless lines, an increase of 0.9 million compared to December 31, 2001 (excluded the lines of Bouygues Telecom and Amena).

For TIM, the Mobile Services business unit's parent company, operating revenues for the three months ended March 31, 2002 were €1,972 million, an increase of 1.2% over the three months ended March 31, 2001. Revenues from services increased by 1.5% to €1,934 million. The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 9.6%). For the first three months of 2002, TIM revenues from VAS grew more than 43% to account for approximately 9.6% of traffic revenues (compared to 6.8% of traffic revenues for the first three months of 2001).

TIM Gross Operating Profit for the three months ended March 31, 2002 was €1,056 million, a 1.7% increase compared to the first three months of 2001, while gross operating margin increased to 53.5% from 53.3%.

TIM operating income for the first three months of 2002 was €794 million, a 4.9% decrease compared to the three months ended March 31, 2001.

During the first quarter of 2002, the consolidated net income attributable to TIM was €918 million, with an increase of €519 million compared to the first quarter of 2001. Such increase was mainly due to the extraordinary gain on the sale of the investment in Bouygues Decaux Telecom (€484 million) and the improvement in the financial area (with reference to the contributions made by the associated companies IS TIM and Mobilkom Austria). In particular, the positive contribution of IS TIM (€45 million) included the impact of exchange rate differences and inflation accounting, which, in the future, could be re-absorbed both by the results of operations and the changes in the macroeconomic data for the region.

The Mobile Services Business Unit's employees numbered 17,124 as of March 31, 2002, an increase of 403 compared to December 31, 2001.

Internet and Media

For the three months ended March 31, 2002, consolidated operating revenues of Internet and Media were €333 million compared to €292 million for the three months ended March 31, 2001, an increase of 14%. This increase was due mainly to changes in the scope of consolidation area. On a comparable consolidation basis, consolidated operating revenues grew by 1%.

For the three months ended March 31, 2002, SEAT consolidated Gross Operating Profit was €27 million compared with €23 million for the first quarter of 2001, a 17.4% increase. On a comparable consolidation basis, there was an increase in gross operating profit of more than 90% associated mainly with the improvement in the profitability of the Directories business area and a slightly positive Gross Operating Profit in the Internet business area.

For the three months ended March 31, 2002, operating income was a loss of €69 million compared to a loss of €53 million in 2001, a 30.2% increase. The greater loss was due to higher amortization charges for goodwill attributable to companies acquired after March 31, 2001 together with higher allocations to provisions for doubtful accounts. On a comparable consolidation basis, however, there was an improvement of 10% which was mainly attributable to a reduction in the losses reported by the companies in the Internet and Directory Assistance business areas.

SEAT consolidated net income after minority interests, for the three months ended March 31, 2002, was a loss of €47 million compared to a loss of €56 million for the three months ended March 31, 2001.

As of March 31, 2002, SEAT group had 8,740 employees, with a decrease of 524 compared to the end of 2001 mainly due to the rationalization program implemented in the Internet business area.

International Operations

Gross operating revenues for the first three months of 2002 increased by 7.9% to €478 million from €443 million for the first three months of 2001. The increase in gross operating revenues was mainly due to volumes growth experienced in 9Telecom (plus 81.6%), while Entel Chile (plus 7.8%) also grew despite the adverse impact of local currency devaluation.

Gross Operating Profit was €96 million in the first three months of 2002, compared with €97 million for the first three months of 2001. Gross Operating Profit was impacted by the decrease in the profitability of the International Operations business area of Telecom Italia (on account of lower revenues from service contracts with Telecom Argentina), as well as the start-up costs of BBned and the deterioration in the economic performance of Entel Bolivia.

On a comparable consolidation basis, operating revenues and Gross Operating Profit for the three months ended March 31, 2002 grew by 7.9% and 0.5%, respectively, compared to the same period in 2001.

Operating income improved by 45% to a loss of €22 million in the first quarter 2002 compared with a loss of €40 million in the first quarter 2001. The reduction in losses was due to lower amortization of goodwill after the significant write-downs in the last quarter of 2001.

As of March 31, 2002, the Business Unit International Operations had 7,250 employees, with a decrease of 57 compared to the end of 2001.

Other Group Activities

The Information Technology Group Operating Activity had gross operating revenues of €196 million for the first three months of 2002 compared to €209 million for the first three months of 2001, a 6.2% decrease. The decrease is mainly due to price levels of Netsiel and Telesoft recorded in the first quarter on the services rendered to the Domestic Wireline Business Unit. In addition, TILAB had a reduction in operating grants (approximately €5 million). The Gross Operating Profit was a loss of €1 million compared to income of €28 million in the same period of 2001. The decline was attributable to the reductions in margins of IT Group companies. Operating Income was a loss of €29 million in 2002 compared to a loss of €4 million for the same period of 2001.

The Information Technology Market Business Unit (Finsiel group) had gross operating revenues of €270 million for the first three months of 2002 compared to €246 million for the first three months of 2001, a 9.8% increase mainly attributable to the higher production volumes achieved particularly by Sogei, Tele Sistemi Ferroviari and Insiel only in part offset by a fall in the revenues of Finsiel. The profitability of the group, both in terms of gross operating profit (€32 million in the first quarter of 2002) and operating income (€25 million in the first three months of 2002), settled at the same levels as in the prior year, while, as a percentage of revenues, they were lower, due to the lower margins on the volumes achieved during the first quarter of 2002.

The Satellite Services Business Unit reported operating revenues of €65 million for the first three months of 2002 compared to the same amount for the first three months of 2001. Gross Operating Profit amounted to €4 million.

Results of Operations for the Three Years Ended December 31, 2001

The following table sets forth the Group' s statement ofoperations for the years ended December 31, 1999, 2000 (pro forma) and 2001.

	1999	2000(1) (pro forma)	2001
		(millions of Euro)	
Operating revenues	27,104	27,169	30,818
Other income	516	402	417
Total revenues	27,620	27,571	31,235
Cost of materials	2,477	2,132	1,972
Salaries and social security contributions	4,977	4,745	4,666
Depreciation and amortization	5,339	5,209	6,275
Other external charges	9,586	10,130	12,171
Changes in inventories	(130)	(255)	58
Capitalized internal construction costs	(1,062)	(831)	(581)
Total operating expenses	21,187	21,130	24,561
Operating income	6,433	6,441	6,674
Financial income	555	806	1,076
Financial expense	(1,466)	(2,261)	(5,031)
of which writedowns and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies, net	(565)	(1,011)	(1,665)
Other income and (expense), net	(507)	(184)	(3,452)
Income (loss) before income taxes and minority interests	5,015	4,802	(733)
Income taxes	(2,606)	(1,910)	(925)
Net income (loss) before minority interests	2,409	2,892	(1,658)
Minority interest	(672)	(864)	(410)
Net income (loss)	1,737	2,028	(2,068)

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

Business Unit Financial Data

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services. Since 2001 the Group has organized its business in seven Business Units. For purposes of this Operating and Financial Review and Prospects the Group is providing three years of certain financial data for its Business Units.

The table below sets forth the gross operating revenues, gross operating profit, operating income and other data for the Group' s Business Units, for the last three years:

		Domestic Wireline	Mobile Services	Internet and Media	International Operations	IT Services	Satellite Services	TILAB	Sub-total	Other activities and eliminations	Consolidated total
		(millions of Euro, except number of employees)									
Operating revenues..........	2001	17,291	10,250	1,957	1,879	2,033	648	134	34,192	(3,374)	30,818
	2000 (pro forma) (1)	17,514	9,418	263	505	2,138	340	123	30,301	(3,132)	27,169
	1999	18,449	8,651	228	394	2,240	316	119	30,397	(3,293)	27,104
Gross operating profit......	2001	7,788	4,760	444	347	332	159	(14)	13,816	(197)	13,619
	2000 (pro forma) (1)	7,421	4,447	(35)	(3)	329	50	(9)	12,200	17	12,217
	1999	7,918	3,887	(31)	(9)	352	46	(25)	12,138	88	12,226
Operating income............	2001	4,379	3,136	31	(268)	162	60	(34)	7,466	(792)	6,674
	2000 (pro forma) (1)	3,915	2,988	(73)	(134)	134	(52)	(34)	6,744	(303)	6,441
	1999	4,045	2,708	(65)	(122)	120	(11)	(47)	6,628	(195)	6,433
Capital expenditures (2)...	2001	2,835	3,182	378	1,290	130	29	22	7,866	298	8,164
	2000 (pro forma) (1)	2,746	5,105	34	984	126	31	33	9,059	7,425	16,484
	1999	2,846	1,835	20	125	158	35	19	5,038	416	5,454
Number of employees at year-end..........................	2001	58,406	16,721	9,264	7,307	11,288	1,196	1,422	105,604	4,352	109,956
	2000 (pro forma) (1)	62,782	15,257	7,515	2,572	12,005	1,206	1,287	102,624	4,547	107,171
	1999(3)	69,575	12,363	336	2,403	12,126	1,299	1,302	99,404	23,258	122,662

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(2) Includes goodwill of €1,174 million in 2001, €9,109 million in 2000 (pro forma), and €567 million in 1999.

(3) As of December 31, 1999, other activities and eliminations includes the employees of Sirti and Italtel groups totaling 12,704 and 5,153, respectively, which were sold during 2000.

Year ended December 31, 2001 compared with Year ended December 31, 2000.

Consolidated Operating Revenues

The Group' s consolidated operating revenues grew by 13.4% in 2001 compared to 2000 (plus 2.7% on a comparable consolidation basis).

The increase in consolidated operating revenues of 13.4% over 2000 was primarily due to the following:

- The positive performance of mobile telephone services which offset a reduction in wireline telephone services in Italy, where revenues from traffic, in spite of a significant increase in terms of minutes, evidenced a reduction in the average return on traffic (retail and wholesale) that went from€5.5 cents to €3.9 cents per minute; and

- The contribution made by the new companies included in the scope of consolidation, especially the Entel Chile group (€1,247 million) and the Seat Pagine Gialle group (€1,707 million), that was partly offset by the exclusion of the companies in the manufacturing and installation sector (Sirti and Italtel groups) which were included in the statement of operations only through September 30, 2000.

The table below sets forth, for the periods indicated, gross operating revenues and consolidated operating revenues by Business Unit and the percentage contribution of such Business Unit to the Group' s consolidated operating revenues.

	Year ended December 31,					
	2000(1)(2)(3) (pro forma)			2001(2)		
	Gross Operating Revenues(4)	Consolidated Operating Revenues(5)	% of Consolidated Operating Revenues	Gross Operating Revenues(4)	Consolidated Operating Revenues(5)	% of Consolidated Operating Revenues
	(millions of Euro, except percentages)					
Domestic Wireline	17,514	15,306	56.3%	17,291	15,206	49.3%
Mobile Services	9,418	9,090	33.4%	10,250	9,963	32.3%
Internet and Media	263	179	0.7%	1,957	1,880	6.1%
International Operations	505	471	1.7%	1,879	1,845	6.0%
IT Services	2,138	1,138	4.2%	2,033	1,246	4.1%
Satellite Services	340	263	1.0%	648	589	1.9%
Telecom Italia Lab	123	21	0.1%	134	28	0.1%
Other activities(6)(7)	2,335	701	2.6%	1,053	61	0.2%
Total operating revenues	32,636	27,169	100.0%	35,245	30,818	100.0%

(1) 2000 gross operating revenues and consolidated operating revenues for each major business area and other activities of the Group are reclassified and presented consistent with the presentation of 2001 gross operating revenues and consolidated operating revenues.

(2) Beginning from the consolidated financial statements for the year ended December 31, 2001, Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group), which in 2000 were consolidated proportionally, have been accounted for using the equity method. Prior to 2000 the Nortel Inversora group was accounted for on the equity method.

(3) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(4) Gross operating revenues are total revenues of the various business areas of the Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(5) Consolidated operating revenues are revenues recorded by each business area on a consolidated basis after elimination of intercompany sales.

(6) In December 2000, 80.1% of Italtel' s capitalstock was sold to a group of foreign investors headed by Clayton, Dubilier & Rice and Cisco System. In connection with this sale, Sogerim SA, a wholly-owned subsidiary of Telecom Italia, on behalf of Telecom Italia, retained the 19.9% (19.4% as of December 31, 2001) stake in Italtel not sold by Telecom Italia. Only the economic results for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group.

(7) In December 2000, Telecom Italia disposed of its interest in Sirti. Only the economic result for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group.

The table below sets forth, for the periods indicated, gross operating revenues by geographic area:

Geographic Area	Year ended December 31,			
	2000(1) (pro forma)		2001	
	(millions of Euro, except percentages)			
Italy	23,033	84.8%	24,863	80.7%
Other European countries	1,809	6.7%	1,817	5.9%
North America	174	0.6%	913	3.0%
Central and South America	1,555	5.7%	2,592	8.4%
Australia, Africa and Asia	598	2.2%	633	2.0%

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

Operating Expenses

The table below sets forth, for the periods indicated, total consolidated operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31,			
	2000 (pro forma)		2001	
	(millions of Euro, except percentages)			
Cost of materials	2,132	7.8%	1,972	6.4%
Other external charges	10,130	37.3%	12,171	39.5%
Personnel costs (salaries and social security contributions)	4,745	17.5%	4,666	15.1%
Changes in inventories	(255)	(0.9)%	58	0.2%
Capitalized internal construction costs	(831)	(3.1)%	(581)	(1.9)%
Depreciation and amortization	5,209	19.2%	6,275	20.4%
Total operating expenses	21,130	77.8%	24,561	79.7%

The Group' s operatingexpenses increased by 16.2% in 2001 compared to 2000 mainly due to the changes in the scope of consolidation (principally the Entel Chile group and the SEAT group) and the expansion of mobile telecommunications services, as well as the increase in the amortization of goodwill. The increase in operating expenses, mainly due to the expansion of the Group' s activities, was also reflected in the€1,619 million increase in costs of external services rendered (included in other external charges).

As a percentage of the Group' s operating revenues, such operating expenses represented 77.8% and 79.7% in 2000 and 2001, respectively.

Cost of Materials

Cost of materials decreased by 7.5% in 2001 compared to 2000, principally due to the exclusion of the companies in the manufacturing and installation sector (Sirti and Italtel groups) which were included in the statement of operations only through September 30, 2000 as well as lower costs of sale for products at Telecom Italia since, beginning with the second half of 2000, for some customers, Telecom Italia only plans the telecommunications systems, leaving manufacturers with the costs of supplying the equipment. Such decrease was partly offset by the inclusion in the scope of consolidation of the SEAT group and the Entel Chile group.

Other External Charges

The table below sets forth, for the periods indicated, consolidated other external charges broken down by major components.

	Year ended December 31,	
	2000 (pro forma)	2001
	(millions of Euro)	
Costs of external services rendered	7,933	9,552
Write-downs of fixed assets and intangibles	48	16
Provision for bad debts	394	439
Rent and lease payments	751	1,069
TLC license fee	543	524
Provision for risk	108	189
Other provisions and operating charges	353	382
Other external charges	10,130	12,171

Other external charges increased by €2,041 million in 2001 compared to 2000 or 20.1%. These charges include costs of external services rendered, write-downs of fixed assets and intangibles, provision for bad debts, rent and lease payments, TLC license fee and other provisions and operating charges.

- Costs of external services rendered increased by 20.4% in 2001 compared to 2000 mainly due to the inclusion of the Entel Chile group and the SEAT group in the scope of consolidation, the increase in the costs of operating and developing mobile telecommunications services and the increase in the operations of certain foreign companies.

- Write-downs of fixed assets and intangibles decreased by 66.7% in 2001 compared to 2000.

- Rent and lease payments increased by 42.3% in 2001 compared to 2000, mainly due to higher costs sustained by the Company for rentals on buildings sold to IM.SER (€252 million) as well as to the inclusion of the SEAT group in the scope of consolidation.

- TLC license fee, which is principally payable to the Italian Government and is proportional to revenues, decreased by 3.5% in 2001 compared to 2000 due to a reduction in the revenue base and a reduction in the rate (the aggregate rate for Telecom Italia and TIM declined from 2.7% in 2000 to 2.5% in 2001).

- Other provisions and operating charges, which include losses on disposals and write-offs of fixed assets and intangibles (€29 million) and taxes other than income taxes (€120 million), increased by 8.2% in 2001 compared to 2000.

Personnel Costs

Personnel costs (salaries and social security contributions) decreased by €79 million or 1.7% to €4,666 million in 2001 from €4,745 million in 2000 as personnel costs declined to 15.1% of the Group's operating revenues in 2001 compared to 17.4% in 2000. The decrease was due to the following:

- The exclusion from the scope of consolidation of the Sirti and Italtel groups (€383 million), and

- The decrease in Telecom Italia costs following employee layoffs.

These decreases were only partly offset by the inclusion in the scope of consolidation of the Seat group (€360 million) and the Entel Chile group (€114 million). Employees at December 31, 2001 numbered 109,956 (107,171 as of December 31, 2000). The breakdown is as follows:

	As of December 31,	
	2000 (pro forma)	**2001**
Italy	93,817	90,628
Abroad	13,354	19,328
Total employees	**107,171**	**109,956**

At December 31, 2001 the Group employed 109,956 persons, an increase of 2,785 employees compared to a pro forma 107,171 at December 31, 2000. The increase of 2,785 units is principally due to the changes in the scope of consolidation (in particular increases of 1,749 units in Internet Media and 1,464 units in Mobile Services as well as the inclusion of the Entel Chile group which led to an increase of 4,681 employees) and a reduction of 5,460 units at Telecom Italia owing to personnel turnover.

Telecom Italia is currently in a dispute with the Italian Social Security Authority ("INPS") concerning the calculation of social security charges to be paid by the companies operated in Italy's telecommunications services of the Group. At December 31, 2001, Telecom Italia's potential range of liability for principal contribution was estimated to be between €960 million and €1,284 million (€334 million of which has already been paid). Management does not believe that an adverse resolution of the dispute will have a material adverse effect on the Group's consolidated financial position in view of the fact that the sums due are to be paid over a period of 15 years (for more details see "Item 8. Financial Information ? Legal Proceedings").

Capitalized Internal Construction Costs

Capitalized internal construction costs represent sales of equipment and installations at market prices by Group companies, principally to Telecom Italia and TIM. Capitalized internal construction costs decreased from €831 million in 2000 to €581 million in 2001 (or 30.1% decrease) principally due to lower levels of capital expenditures spent on products purchased from subsidiaries within the Group as well as the disposal of Sirti and Italtel groups.

Gross Operating Profit

The table below sets forth, for the periods indicated, the Group's Gross Operating Profit and gross operating margin (gross operating profit as a percentage of operating revenues).

	Year ended December 31,			
	2000 (pro forma)		2001	
	(millions of Euro, except percentages)			
Gross Operating Profit	12,217	45.0%	13,619	44.2%

Gross Operating Profit increased by 11.5% in 2001 compared to 2000 (an increase of 6.6% on a comparable consolidation basis) but gross operating margin decreased to 44.2% in 2001 from 45.0% in 2000. The overall increase in Gross Operating Profit was primarily attributable to the changes in consolidation to include the SEAT group (€444 million) and the Entel Chile group (€374 million) and improved Gross Operating Profit from mobile telecommunications (€313 million).

Depreciation and Amortization

Depreciation and amortization which is calculated on a straight line basis over the estimated useful lives of the assets, increased by €1,066 million or 20.5% in 2001 to €6,275 million compared to €5,209 million in 2000. Depreciation of fixed assets decreased by €97 million or 2.3% to €4,034 million in 2001 compared to €4,131 million in 2000. The decrease in depreciation of fixed assets was principally attributable to the change in the scope of consolidation and a reduction in the depreciation expense of Telecom Italia (€415 million), owing to a lower amount of depreciable assets following the contribution of real estate assets to IM.SER, and a change in the mix of depreciable assets.

Amortization of intangible assets increased by €1,163 million or 107.9%, from €1,078 million in 2000 to €2,241 million in 2001. Goodwill represented €1,022 million of intangibles in 2001 compared to €168 million in 2000. The increase in amortization of goodwill which represented 73.4% of the total increase in amortization of intangible assets was mainly due to the acquisition of Seat Pagine Gialle (€574 million), the acquisition of Jet Multimedia (€102 million) as well as other companies within the SEAT group (€99 million).

As a result primarily of the transactions which resulted in Telecom Italia acquiring a controlling stake in the SEAT group as well as certain other international investments made at the end of 2000, Telecom Italia recorded a significant increase in goodwill (goodwill as of December 31, 2000 was €10,171 million compared to €1,020 million as of December 31, 1999). At year end 2001 goodwill had declined to €9,141 million due to the amortization described above as well as the extraordinary write-downs of goodwill (€1,303 million) offset by additions (€1,174 million, of which €731 million was attributable to the acquisition of the additional stake in Entel Chile).

Operating Income

The table below sets forth, for the periods indicated, the Group's operating income (total revenues less total operating expenses, including depreciation and amortization and other charges).

	Year ended December 31,	
	2000 (pro forma)	2001
	(millions of Euro)	
Operating income	6,441	6,674

Operating income for the Group increased by 3.6% in 2001 compared to 2000. The increase in operating income is mainly attributable to improvement in Telecom Italia (an increase of €388 million), improved results of TIM group (operating income increased by €148 million) and positive effects from changes in consolidation area, partly offset by the higher goodwill amortization charges (€854 million). As a percentage of operating revenues, operating income decreased in 2001 to 21.7% from 23.7% in 2000 due principally to the higher goodwill amortization.

Financial Income, Financial Expense, and Other Income and Expense, Net

The table below sets forth, for the periods indicated, the components of financial and other income and expense, net.

	Year ended December 31,	
	2000 (pro forma)	2001
	(millions of Euro)	
Financial income	806	1,076
Financial expense	(2,261)	(5,031)
of which writedowns and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies, net	(1,011)	(1,665)
Other income and (expense), net	(184)	(3,452)
Total financial expense, net and other income and expense, net	(1,639)	(7,407)

Total financial expense, net and other income and expense, net increased from a net expense of €1,639 million in 2000 to a net expense of €7,407 million in 2001, a 351.9% increase.

Financial expense (which includes interest expense on financial indebtedness and income or loss from equity investments) increased by 122.5%. The increase is attributable to the following principal factors:

- higher average borrowings outstanding during 2001 principally attributable to financing the acquisition of SEAT as well as other acquisitions made during 2000 and 2001 which resulted in an increase of interest expense of €698 million (€762 million in 2000 and €1,460 million in 2001). See also "—Liquidity and Capital Resources";

- the provision relating to the forward commitment to purchase Seat Pagine Gialle shares for a total of €569 million in connection with the estimate of the non recoverability of the original price to exercise the option;

- higher levels of equity losses of investments in unconsolidated subsidiaries, affiliated and other companies (€1,665 million in 2001 compared to €1,011 million in 2000) which reflects primarily the results of operations for the Group's equity method investments, including amortization of goodwill that arose upon the acquisition of these investments (€316 million in 2001 and €462 million in 2000).

  The higher expenses in 2001 were particularly affected by:

- the losses of IS TIM (Turkey) of €334 million due not only to expenses incurred in conjunction with the start-up phase but also the effects of the currency crisis in Turkey and the application of inflation accounting principles;

- the writedown of Stream (€241 million);

- the losses of the Nortel Inversora group (€238 million), which were related to the economic crisis in Argentina and due mainly to exchange losses on financial payables.

Other income and expense, net increased from a net expense of €184 million in 2000 to a net expense of €3,452 million in 2001.

This significant increase was mainly due to the extraordinary provisions and write-downs of goodwill and equity investments which are described in more detail below.

Other income in 2001 included:

- Gains on the sale of the 70% holding in Mirror International Holding (the company through which the satellite companies were contributed to the Lehman Brothers group) for €170 million and the 30% holding in Mediterranean Nautilus S.A. to the Israeli company F.T.T. Investments for €94 million;

- Income (€32 million) deriving from the partial cancellation, by the Council of State of resolution No. 7533/1999 by the Italian Antitrust Authority under which TIM and Omnitel were levied administrative fines for the alleged violation of antitrust laws relating to the price fixing of fixed-mobile rates;

- Income from the release of reserves by Telecom Italia recorded in prior years for risks which did not materialize (€120 million, mainly relating to the reserve for a contract with Iraq of €62 million and the reserve for corporate restructuring of €50 million).

Other expense in 2001 included:

- €2,984 million for the extraordinary provisions and write-down of goodwill and equity investments, detailed as follows: i) €1,303 million for the write-down of goodwill relating to consolidated companies (9Telecom group, Entel Bolivia, Entel Chile group, Maxitel group, Tele Celular Sul group, Tele Nordeste Celular group, TIM Brasil (TIM Celular Centro Sul, TIM Sao Paulo, TIM Rio Norte), Med-1 group and certain companies in the Seat Pagine Gialle group); ii) €1,078 million for the write-down of goodwill relating to companies accounted for by the equity method (GLB Serviços Interativos, Solpart Participacoes, Telekom Austria and the Nortel Inversora group); and iii) €603 million for other provisions relating to investments. Such write-down were made on a consistent basis according to the new business plans and market trends and resulted in the conclusion that there was a permanent impairment in the value at which these investments were carried by Telecom Italia;

- €248 million relating to the provision for expenses connected with the Vivendi/Canal Plus agreement for the transfer of Telecom Italia's investment in Stream;

- €380 million of expenses for employee cutbacks and layoffs (of which €203 million relates to Telecom Italia);

- €155 million for social security charges under Law 58/1992 to guarantee uniform status under the former Telephone Employees Pension Fund (FPT) which, as required by the 2000 Finance Bill, has become part of the general Employees Pension Fund;

- €77 million of extraordinary contributions to INPS – established by the 2000 Finance Bill for the three years 2000-2002 to meet the higher financial requirements covered by the rules of the fund that was abolished; and

- €85 million resulting from the decision to reposition the broadcasting station La7 as a consequence of the closing of a series of contracts.

In 2000, other income and expense, net was significantly lower due to significant gains on the disposal of investments (€1,146 million) offset by:

- provision made by TIM to reserve for technological risk (€400 million);
- the expenses and the provisions connected to the transactions for the disposal of investment holdings and the real estate portfolio (€180 million);
- restructuring costs (€480 million) principally related to Telecom Italia's costs for the corporate reorganization plan;
- the social security charges (€153 million) pursuant to Law No. 58/92 to guarantee uniform status under the former Telephone Employees Pension Fund (FPT);
- the extraordinary annual contribution to INPS (€77 million) to meet the higher financial requirements covered by the rules of the Telephone Employees Pension Fund (FPT).

Income Taxes

Income taxes were €925 million in 2001 compared to €1,910 million in 2000. The statutory income tax rate for 2001 and 2000 was 40.25% and 41.25%, respectively. The 2001 decrease in income taxes (€985 million) was primarily due to a reduction in the taxable base caused by the extraordinary expenses associated with the extraordinary write-downs of Telecom Italia and TIM regarding the valuation of foreign investments.

Net Income (loss)

Net income (loss) before minority interest decreased from an income of €2,892 million in 2000 to a loss of €1,658 million. The loss in 2001 was principally attributable to the increase in total financial expense, net and other expense, net described above, offset in part by lower income taxes. Net loss after minority interest was €2,068 million in 2001 compared to income of €2,028 million. Minority interest decreased from €864 million in 2000 to €410 million in 2001 mainly due to lower levels of profit at TIM group.

Results of Operations of Business Units for the Year Ended December 31, 2001 compared to the Year Ended December 31, 2000.

Domestic Wireline

The following table sets forth for the periods indicated certain financial and other data for Domestic Wireline.

Domestic Wireline	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	17,514	17,291
Gross Operating Profit	7,421	7,788
Operating income	3,915	4,379
Number of employees at year -end	62,782	58,406

The following table sets forth for the periods indicated certain statistical data for Domestic Wireline.

	Year ended December 31,	
	2000	2001
Subscription and Customers:		
Subscriber fixed lines at period-end (thousands)(1)	27,153	27,353
Subscriber fixed line growth (%)	2.5	0.7
Subscriber fixed lines per full-time equivalent employee at period-end(2)	409	448
ISDN equivalent lines at period-end (thousands)(3)	4,584	5,403
Traffic:		
Average minutes of use per fixed line subscriber during period(4)	4,722	4,739
Of which:		
Local traffic during period (in average minutes)(5)	3,204	3,069
Long distance traffic during period (domestic and international) (in average minutes)	1,519	1,670
Growth in international incoming and outgoing traffic in minutes(6)	5.4	12.1

(1) Data include multiple lines for ISDN and excludes internal lines.
(2) Ratio is based on employees of the Company only.
(3) Data excludes internal lines.
(4) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks); excludes traffic for special services.
(5) Not including district traffic and traffic for special services, including internet dial up traffic.
(6) Data include retail from wireline and wholesale international traffic. Growth between 2000 and 2001 is mainly due to wholesale traffic (incoming and outgoing).

Revenues from Domestic Wireline services in Italy consists of revenues from domestic and international traffic and fees from subscribers (including retention programs, like Teleconomy) and from other operators for interconnection to Telecom Italia network. Gross operating revenues from Domestic Wireline decreased by 1.3% in 2001 compared to 2000. This decrease resulted principally from a decline of 6.9% in revenues from traffic, inspite of an increase in minutes of use of 30.7%. Although usage increased, the reduction in tariffs for long distance and international rates, the discount policies aimed at customer "retention" and the application of new interconnection rates to traffic to and from the mobile network, more than offset the increased usage and the increase in basic subscription charges (an increase of 12% (plus €426 million), mainly due to tariff increases effective August 1, 2000 and February 1, 2001). The net average return on traffic was €3.9 cents per minute in 2001 compared to €5.5 cents per minute in 2000, a 29% decrease which translates into a revenue loss of approximately €655 million. Included in gross operating revenue is other income which includes revenues for data services and data equipment (€1,600 million), other equipments (€660 million), access from other operators (€1,080 million) and other revenues.

The number of fixed line subscribers in Italy rose by 0.7% to approximately 27,353 million at December 31, 2001 representing a telecommunications density (fixed line subscribers to total population of Italy) of approximately 48% at December 31, 2001, compared to approximately 47% at December 31, 2000. The increase is mainly attributable to the increase in ISDN lines (4,584,000 lines at the end of 2000 and 5,403,000 lines at the end of 2001).

The average minutes of use per fixed line subscriber increased 0.3% during 2001 due to the growth of Internet traffic (included in local traffic). Telecom Italia expects internet-related revenues to continue to increase strongly over the short and medium term. The decline in average minutes of use for long distance traffic (domestic and international) was a consequence of the substitution of mobile outgoing traffic for fixed line traffic and the impact of competitors. Telecom Italia' s market share of local traffic (internet traffic excluded) was approximately 84% at year end (down from 93% at December 31, 2000) and its market share of long distance traffic was approximately 73% at year end (down from 76% at December 31, 2000 and down from 83% at December 31, 1999). The slowing of loss of market share in long distance traffic and high level of market share of local traffic reflects initiatives taken during 2000 and 2001. In particular a selective marketing strategy and focus on service has stabilized the fixed line segments market shares. These targeted marketing strategies included introduction of Teleconomy, an innovative bundled voice and internet service offered on a unitary or flat fee basis. The offer, which was launched in the second half of 2000, was subscribed to by 2.1 million customers by the end of 2000 and by 4.1 million customers at December 31, 2001. Management believes that the success of this offer has increased customer retention in the targeted more demanding and higher consumption (in terms of traffic) segment of the retail market. Telecom Italia' s market share of fxed to mobile traffic declined from 78% at year end 2000 to 72% at year end 2001.

Gross operating revenues from international traffic was unchanged at €1,652 million in 2001 compared to €1,642 in 2000 despite a 16.9% increase in total international traffic volume, to 8,685 million minutes in 2001 from 7,432 million minutes in 2000. The volume increase was largely driven by incoming and mobile (incoming and outgoing) traffic growth. The revenue trend is mainly due to the impact of continuing tariff reductions and increasing competition.

Consolidated operating revenues were €15,306 million and €15,206 million in 2000 and 2001, respectively.

Despite the revenue decline, Gross Operating Profit increased from €7,421 million in 2000 to €7,788 million in 2001, a 4.9% increase compared to 2000.

Domestic Wireline improved Gross Operating Profit despite the decrease in revenues during 2001 compared to the same period in 2000, as the decline in average per-minute prices for voice call traffic in the retail and wholesale market (a decline from €5.5 cents to €3.9 cents per minute) was partially offset:

- by a significant increase in wireline traffic volumes (an increase of 30.7%), access fees by subscribers and other operators (an increase of 14%) and data transmission (an increase of 6.1%);

- by major cost reductions (a reduction of €590 million) exceeding 5.8% due to rationalization and ongoing network efficiency gains.

The gross operating margin improved by 2.6%, from 42.4% in 2000 to 45.0% in 2001 as the cost savings made up for the small decline in revenues.

Due in part to the growing success of Telecom Italia' s Teleconomy offering (with new flat rate tariff programs, launched in the first months of this year), which more than 4.4 million customers had subscribed to by April 2002, overall market share for the month of April 2002 was equal to 71% compared to 72% for the month of December 2001.

Operating income increased from €3,915 million in 2000 to €4,379 million in 2001, an 11.8% increase. Operating Margin was 22.4% in 2000 and 25.3% in 2001. This significant improvement was mainly due to a reduction in the amount of amortization.

Mobile Services

The following table sets forth for the periods indicated certain financial and other data for Mobile Services.

Mobile Services	Year ended December 31, 2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	9,418	10,250
Gross Operating Profit	4,447	4,760
Operating income	2,988	3,136
Number of employees at year -end	15,257	16,721

The following table sets forth for the periods indicated, certain statistical data for TIM.

	Year ended December 31, 2000	2001
TIM lines at period-end (thousands)	21,601	23,946
TIM lines growth per annum(%)	16.6	10.9
Average revenue per mobile line per month(€)(1)	30.5	29.1
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	37.5	41.6
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants)(%)	73.3	89.0
Total mobile outgoing traffic per month (millions of minutes)	1,569	1,795

(1) Including Prepaid Customers revenues and excluding equipment sales.

Gross operating revenues from mobile services increased by 8.8% in 2001 compared to 2000. This increase is attributable principally to the strong performance of TIM in Italy, despite increasing competition with increasing levels of revenues attributable to value added services. The increase is also due to the change in scope of consolidation to include international companies now managed by TIM International.

TIM International operating revenues increased by 28.4% from €1,500 million in 2000 to €1,926 million in 2001. This increase was mainly due to the first time consolidation of the start-up subsidiaries (Maxitel and Digitel which, prior to January 1, 2001, weren' t consolidated line by line, and TIM Perù which starting in January 2001). The Maxitel and Digitel operating revenues amounted in 2001 to €277 million and €255 million, respectively. The operating revenues of TIM Perù in 2001 were €34 million. The growth in operating revenues of Tele Celular Sul Participacoes (plus 18.5% in Brazilian reais) was offset by deterioration of the exchange rates, which reduced the consolidated revenues of Tele Nordeste Celular Participacoes (a decline of 1.6% in Brazilian reais).

At the end of December 2001, the TIM group had a total of more than 50.7 million wireless lines, not including Group wireless lines, an increase of 9.7 million with respect to the end of 2000.

Consolidated operating revenues were €9,090 million in 2000 and €9,963 million in 2001.

Gross Operating Profit increased by 7.0% to €4,760 million in 2001 from €4,447 million in 2000. The gross operating margin, however, declined to 46.4% for 2001 against 47.2% in 2000. Such decrease was mainly attributable to the start-up international operations partially offset by containment of operating costs at TIM which grew more slowly than operating revenues.

Operating income increased from €2,988 million in 2000 to €3,136 million in 2001, a 5% increase. The increase in operating income was less than Gross Operating Profit due to higher depreciation.

TIM (parent company) operating revenues in 2001 were €8,357 million, an increase of 5.4% over 2000. Revenues from services increased 7.9%. The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 13.6%). During 2001, TIM confirmed its leadership in the VAS market.

TIM lines increased to 23,946,000 at December 31, 2001, a 10.9% increase compared to December 31, 2000. TIM' s GSM lines base increased by 16.0% in 2001, to 22,213,000 lines at December 31, 2001, while TIM' s TACS lines base decreased by 29.1% in 2001, to 1,733,000 lines at December 31, 2001, in each case compared to December 31, 2000. Approximately 93% of TIM' s lines are now GSM lines. The continuing growth in GSM lines was attributable principally to the continuing growth of the GSM TIM Card (a prepaid rechargeable GSM card) launched in October 1996, which had 19,674,000 lines by December 31, 2001 compared to 16,671,000 lines at December 31, 2000. 98.3% of the 3.1 million new GSM lines activated by TIM during 2001 were prepaid cards.

At December 31, 2001, TIM had a market share in Italy of approximately 46.7% (including TACS and GSM) compared to 51% at December 31, 2000 and 61% at December 31, 1999, and a market share of approximately 44.8% for GSM only compared to 48% in 2000 and 57% in 1999. The market share decrease is due to increased competition from the third mobile operator (Wind) and a fourth operator (Blutel). Their market share grew from 11.7% and 1.9% respectively in 2000 to 15.6% and 3.7%, respectively, in 2001. The overall market grew by 21.4% in 2001 from 42.2 million customers at the end of 2000 to 51.3 million customers at the end of 2001. With an overall penetration rate of 90.3% at March 2002 in Italy, management does not expect further significant subscriber growth to be the principal driver in the growth of TIM' s domestic Italian mobile services business. The aggregate number of customers at December 31, 2000 for TIM' s analog and GSM services represented a penetration rate of 41.6% compared to 37.5% at December 31, 2000.

TIM traffic volumes increased by 13.6% in terms of minutes and mobile traffic revenues increased by 7.6% in 2001 (€7,127 million) compared to 2000 (€6,621 million). The net increase in lines (up 10.9% compared to 2000) was partially offset by the continuing decline in average revenues per customer and a decline in average revenue per minute due to increasing competitive pressures and the effect on prices. Average monthly revenue per mobile line (which includes traffic revenues and subscription fees) decreased from approximately €31 in 2000 to €29 in 2001, as low-usage customers, principally non-business customers and GSM and TACS TIM Cardholders, grew further in 2001, making up almost 93.8% of the customer base. 98.3% of TIM' s net new additions for its GSM service came from Prepaid Customers.

TIM revenues from equipment sales decreased by 24.1% in 2001 (€462 million) compared to 2000 (€609 million). The mobile subscription fees decreased by 6.5% in 2001 (€215 million) compared to 2000 (€230 million) due to the continuing sharp expansion in the prepaid service customer base, where no subscription fees are paid.

TIM revenues from VAS (€532 million in 2001) increased by 56.5% compared to 2000. Due to the continuing introduction of new services and the particular success of SMS, the VAS business grew significantly with revenues from value added services representing 7.5% of traffic revenues and 6.4% of total revenues in 2001, compared to 5.1% and 4.3%, respectively in 2000. These trends are expected to continue in 2002. In 2001 TIM promoted the increase in use of VAS through promotional campaigns. Such promotions entailed offers of free SMS services and the extension of SMS to TACS users.

In 2001, TIM launched its GPRS offer to the corporate and mass market. TIM has begun experimenting with a UMTS service in its Service Center in Padua, and a gradual roll-out of the UMTS network has begun. Transition toward the third generation will be gradual; GPRS will be able to satisfy customers' requirements concerning advanced services and it will take time to guarantee full inter-operability between UMTS and GPRS. The larger roll-out should start in 2004.

The TIM churn rate, inspite of increased competition, remains at the same rate recorded in 2000, approximately 1.3% per month. This rate is expected to rise as a result of increasing competition.

TIM gross Operating Profit reached €4,225 million, a growth of 9.9% compared with the previous year (€3,845 million) as a result of greater operating efficiency. Gross Operating Profit accounted for 50.6% of overall revenues (48.5% during 2000).

TIM operating income (€3,231 million) grew by 12.9% compared with 2000. Operating margin was 38.7% in 2001 and 36.1% in 2000.

Internet and Media

The following table sets forth for the periods indicated certain financial and other data for the Internet and Media business unit. Information for the two periods discussed below are not comparable due to the acquisition of the SEAT Group which is fully consolidated in the statement of operations only beginning January 1, 2001.

Internet and Media	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	263	1,957
Gross Operating Profit	(35)	444
Operating income	(73)	31
Number of employees at year-end	7,515	9,264

SEAT was consolidated with Telecom Italia's results of operations for the first time during 2001.

In 2001, gross operating revenues were €1,957 million, compared with €263 million in 2000. On a comparable consolidation basis, gross operating revenues increased by 2.6% from €1,908 million in 2000 to €1,957 million in 2001. The Directories business Area made the largest contribution to growth; these results were achieved largely due to a strong increase in number of customers of Seat Pagine Gialle (plus 3.6%; 670,000 at the end of 2001), accompanied by a strong performance of new directory products.

Consolidated operating revenues were €179 million in 2000 and €1,880 million in 2001.

Gross operating profit in 2001 amounted to €444 million, compared with a loss of €35 million in 2000. Gross operating profit increased by 23% over 2000 on a comparable consolidation basis. This improvement can be attributed to the general work to rationalize costs and to the improved profitability of the Directories Area.

Operating Income in 2001 was €31 million compared with a loss of €73 million in 2000. On a comparable consolidation basis, operating income was €31 million as opposed to the operating loss of €1 million in 2000.

Total Internet users has grown from 2 million in 1999 to 4 million in 2000 and 5 million in 2001. At the end of March 2002 SEAT had 5.4 million Internet users, of whom 1.9 million remained active after 45 days. Average connection time increased by 40% in 2001 compared to 2000.

International Operations

The following table sets forth for the periods indicated certain financial and other data for International Operations.

International Operations	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	505	1,879
Gross Operating Profit	(3)	347
Operating income	(134)	(268)
Number of employees at year-end	2,572	7,307

International Operations gross operating revenues increased by 272.1% in 2001 compared to 2000 (plus 25.5% on a comparable consolidation basis), benefiting mainly from the first time consolidation of the Entel Chile group and Jet Multimedia group.

The growth in international revenues is principally attributable to the inclusion of the Entel Chile group which had revenues of €1,251 million in 2001, its first year of full consolidation. This represented a 35.8% increase over 2000 when Entel Chile was accounted for on the equity basis. The increase is largely attributable to the contribution of mobile telephone services (plus 37% in 2001 compared to 2000) and fixed long distance traffic in its US affiliate (plus 46% in 2001 compared to 2000).

Consolidated operating revenues were €471 million in 2000 and €1,845 million in 2001.

Gross operating profit was €347 million in 2001 compared with a loss of €3 million in 2000. Growth is due to the additional contribution of Entel Chile and Jet Multimedia groups, as well as volumes growth in 9Telecom.

Operating Income (loss) was a loss of €268 million in 2001 compared with a loss of €134 million in 2000. The higher losses are attributable to new goodwill amortization associated with Entel Chile group and Jet Multimedia group (amounting respectively to €59 million and €101 million).

Other Group Activities

The following tables set forth for the periods indicated certain financial and other data for IT Services, Satellite Services and TILAB.

IT Services	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	2,138	2,033
Gross Operating Profit	329	332
Operating income	134	162
Number of employees at year-end	12,005	11,288

Gross operating revenues from IT Services decreased by 4.9% from €2,138 million in 2000 to €2,033 million in 2001. Operating revenues declined due to the terms of new service contracts signed with the Domestic Wireline Business Unit. Operating revenues from the FINSIEL group increased due to a growth in activities in the travel and transportation and banking sectors as well as expansion in the national and local government market, in activities such as development and system integration services, enterprise resources planning projects, e-business, e-banking and training on-line services. Gross operating revenues from Telesoft increased due to the development of Group activities and international markets where the Group has been operating (mainly due to Latin America activities).

Satellite Services	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	340	648
Gross Operating Profit	50	159
Operating income	(52)	60
Number of employees at year-end	1,206	1,196

Operating revenues from satellite services increased by 90.6% (€648 million) in 2001 compared to 2000 (€340 million). This increase is principally due to the results of Telespazio's space activities, offset by the early termination of the important Astrolink program. In the "Media & Communications" segment of activities, the revenues generated by the Television sector partly offset the fall in volumes of the Telecommunications sector. The growth of gross operating profit (increase of 218% in 2001 compared to 2000) and operating income reflected the conclusion of the Astrolink program, whereas Media & Communications recorded a slight fall due to a declining price trend in telecommunication services. The suspension of the Astrolink project, on the other hand, involved an extraordinary write-down of the related financial investment. Overall, the negative extraordinary effects deriving from Astrolink were partly absorbed by the gains realized on the sale of shares in portfolio.

TILAB	Year ended December 31,	
	2000	2001
	(millions of Euro, except employees)	
Gross operating revenues	123	134
Gross Operating Profit	(9)	(14)
Operating income	(34)	(34)
Number of employees at year-end	1,287	1,422

Gross operating revenues in 2001 (€134 million) increased by 8.9% compared to 2000 (€123 million). This increase is principally due to the development of TIM's demand and to the non-captive activities.

The Gross Operating Profit (Loss) decreased by 55.6%, showing a loss of €14 million (€9 million in 2000). This evidence is essentially due to the increase in other external charges and labor costs, with particular reference to the acquisition, from Telecom Italia, of the Division "Venture Capital & Innovation".

The Operating Income, with €34 million of losses, results unchanged in comparison with 2000.

Year ended December 31, 2000 compared with Year ended December 31, 1999.

Consolidated Operating Revenues

The Group's consolidated operating revenues grew by 0.2% in 2000 compared to 1999. The slight growth in consolidated operating revenues was primarily attributable to a 9.7% increase in mobile services revenues in Italy and abroad, as well as to increases in Internet and Media and International Operations Business Units. These increases offset the decrease in revenues from Domestic Wireline Business Unit which declined by 4.1% as well as the decline in revenues from manufacturing and installation companies which were sold during 2000.

The table below sets forth, for the periods indicated, gross operating and consolidated operating revenues by Business Unit and the percentage contribution of such Business Unit to the Group's consolidated operating revenues.

	Year ended December 31,					
	1999(1) (2)			2000(1) (2) (3) (pro forma)		
	Gross Operating Revenues (4)	Consolidated Operating Revenues(5)	% of Consolidated Operating Revenues	Gross Operating Revenues(4)	Consolidated Operating Revenues(5)	% of Consolidated Operating Revenues
	(millions of Euro, except percentages)					
Domestic Wireline	18,449	15,961	58.9%	17,514	15,306	56.3%
Mobile Services	8,651	8,290	30.6%	9,418	9,090	33.4%
Internet and Media	228	68	0.3%	263	179	0.7%
International Operations	394	365	1.3%	505	471	1.7%
IT Services	2,240	1,099	4.0%	2,138	1,138	4.2%
Satellite Services	316	229	0.8%	340	263	1.0%
Telecom Italia Lab	119	15	0.1%	123	21	0.1%
Other activities (6) (7)	2,921	1,077	4.0%	2,335	701	2.6%
Total operating revenues	33,318	27,104	100.0%	32,636	27,169	100.0%

(1) 1999 and 2000 gross operating revenues and consolidated operating revenues for each major business area and other activities of the Group are reclassified and presented consistent with the presentation of 2001 gross operating revenues and consolidated operating revenues.

(2) Beginning from the consolidated financial statements for the year ended December 31, 2001, Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group), which in 2000 were consolidated proportionally, have been accounted for using the equity method. Prior to 2000 the Nortel Inversora group was accounted for on the equity method.

(3) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(4) Gross operating revenues are total revenues of the various business area of the Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(5) Consolidated operating revenues are revenues recorded by each business area on a consolidated basis after elimination of intercompany sales.

(6) In December 2000, 80.1% of Italtel's capital stock was sold to a group of foreign investors headed by Clayton, Dubilier & Rice and Cisco System. In connection with this sale, Sogerim SA, a wholly-owned subsidiary of Telecom Italia, on behalf of Telecom Italia, retained the 19.9% stake in Italtel not sold by Telecom Italia. Only the economic results for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group. The figures cannot, therefore, be compared to those of 1999, a year in which, following its reorganization, the results of Italtel were proportionally consolidated at 50% for the first ten months of 1999 and at 100% for the last two months.

(7) In December 2000, Telecom Italia disposed of its interest in Sirti. Only the economic result for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group. Therefore, the figures cannot be compared to those of previous years.

The table below sets forth, for the periods indicated, gross operating revenues by geographic area:

Geographic Area	Year ended December 31,			
	1999		2000(1) (pro forma)	
	(millions of Euro, except percentages)			
Italy	23,209	85.6%	23,033	84.8%
Other European countries	1,807	6.7%	1,809	6.7%
North America	195	0.7%	174	0.6%
Central and South America	1,329	4.9%	1,555	5.7%
Australia, Africa and Asia	564	2.1%	598	2.2%

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

Operating Expenses

The table below sets forth, for the periods indicated, total consolidated operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31,			
	1999		2000 (pro forma)	
	(millions of Euro, except percentages)			
Cost of materials	2,477	9.1%	2,132	7.8%
Other external charges	9,586	35.4%	10,130	37.3%
Personnel costs (salaries and social security contributions)	4,977	18.4%	4,745	17.5%
Changes in inventories	(130)	(0.5)%	(255)	(0.9)%
Capitalized internal construction costs	(1,062)	(3.9)%	(831)	(3.1)%
Depreciation and amortization	5,339	19.7%	5,209	19.2%
Total operating expenses	21,187	78.2%	21,130	77.8%

The Group' soperating expenses decreased from €21,187 million in 1999 to €21,130 million in 2000. This decrease was primarily affected by cost containment programs in Telecom Italia, where costs were reduced, as well as the reduction in operating expenses from manufacturing and installation companies, which were sold during 2000, partly offset by the expansion of mobile services.

As a percentage of the Group' s operating revenues, such operating expenses represented 78.2% and 77.8% in 1999 and 2000, respectively.

Cost of Materials

Cost of materials decreased by 13.9% in 2000 compared to 1999, principally due to the lower costs of sale for products at Telecom Italia since, beginning with the second half of 2000, for some customers, Telecom Italia only plans the telecommunications systems, leaving manufacturers with the costs of supplying the equipment.

Other External Charges

The table below sets forth, for the periods indicated, consolidated other external charges broken down by major components.

	Year ended December 31,	
	1999	2000 (pro forma)
	(millions of Euro)	
Costs of external services rendered	7,380	7,933
Write-downs of fixed assets and intangibles	73	48
Provision for bad debts	363	394
Rent and lease payments	704	751
TLC license fee	606	543
Provision for risk	80	108
Other provisions and operating charges	380	353
Other external charges	9,586	10,130

Other external charges increased by €544 million in 2000 compared to 1999. These charges includes costs of external services rendered, write-downs of fixed assets and intangibles, provision for bad debts, rent and lease payments, TLC license fee and other provisions and operating charges.

- Costs of external services rendered increased by 7.5% in 2000 compared to 1999 mainly due to the increase in the costs of operating and developing mobile telecommunications services and the increase in the operations of certain foreign companies.

- Write-downs of fixed assets and intangibles decreased by 34.2% in 2000 compared to 1999. The decrease in the level of write-downs in 2000 is primarily due to the high level taken in 1999 relating to certain public voice telephony installations.

- Rent and lease payments increased by 6.7% in 2000 compared to 1999, mainly due to the expansion of the TIM group' s activities.

- TLC license fee, which are principally payable to the Italian Government and are proportional to revenues, decreased by 10.4% in 2000 compared to 1999 due to a reduction in the revenue base and a reduction in the rate (the aggregate rate for Telecom Italia and TIM declined from 3.0% in 1999 to 2.7% in 2000).

- Other provisions and operating charges, which include losses on disposals and write-offs of fixed assets and intangibles (€52 million) and taxes other than income taxes (€116 million), decreased by 7.1% in 2000 compared to 1999.

Personnel Costs

Personnel costs (salaries and social security contributions) decreased by 4.7% in 2000 compared to 1999, and, as a percentage of the Group' s operating revenues, personnel costs declined to 17.5% in 2000 compared to 18.4% in 1999. Overall personnel costs decreased following the changes in the scope of consolidation (Sirti group and Italtel group: a decrease of €190 million) together with the lower costs of Telecom Italia (a decrease of €96 million) essentially due to the reduction in the average number of employees compared to 1999, as well as resignations following employee reductions under the agreements with the labor unions.

Total employees at Telecom Italia declined to 66,541 employees at December 31, 2000 compared to 76,113 employees at December 31, 1999. Employees at December 31, 2000 numbered 107,171 (122,662 as of December 31, 1999). The breakdown is as follows:

	As of December 31,	
	1999	2000 (pro forma)
Italy	110,245	93,817
Abroad	12,417	13,354
Total employees	**122,662**	**107,171**

Employees of the Group at the end of 2000 compared to the end of 1999 decreased by 15,491 due to personnel turnover and the effect of the changes in the scope of consolidation. In particular, other than the decrease of 6,793 units in Domestic Wireline (primarily attributable to Telecom Italia), the exclusion of the Sirti group and the Italtel group led to a reduction in the number of employees of 17,857, compensated by the addition of 2,894 units in mobile services (of which an increase of 1,229 was related to Maxitel), and the inclusion of the SEAT group (an increase of 7,179 in the Internet and Media Business Unit).

At December 31, 2000, Telecom Italia's potential range of liability for principal contribution relating to its ongoing dispute with INPS was estimated to be between €981 million and €1,291 million (€263 million of which had already been paid).

Capitalized Internal Construction Costs

Capitalized internal construction costs represent sales of equipment and installations at market prices by Group companies, principally to Telecom Italia and TIM. Capitalized internal construction costs decreased by 21.8% in 2000 compared to 1999 principally due to a decrease in capital expenditures spent on products purchased from subsidiaries within the Group also as a result of the disposal of Sirti and Italtel groups.

Gross Operating Profit

The table below sets forth, for the periods indicated, the Group's Gross Operating Profit and gross operating margin (gross operating profit as a percentage of operating revenues).

	Year ended December 31,			
	1999		2000 (pro forma)	
	(millions of Euro, except percentages)			
Gross Operating Profit	12,226	45.1%	12,217	45.0%

Gross Operating Profit and gross operating margin recorded a slight decrease compared to 1999. The overall decrease in Gross Operating Profit of €9 million was primarily attributable to the improved Gross Operating Profit from mobile services more than offset by declines in profitability of Domestic Wireline and IT services Business Units and other Activities.

Depreciation and Amortization

Depreciation and amortization which is calculated on a straight line basis over the estimated useful lives of the assets, decreased by €130 million or 2.4% in 2000 to €5,209 million compared to €5,339 million in 1999. Depreciation of fixed assets decreased by €220 million or 5.1% to €4,131 million in 2000 compared to €4,351 million in 1999. The reduction in depreciation of fixed assets was principally attributable to a decrease in the depreciation charge of Telecom Italia (a decrease of €245 million) owing to a lower amount of depreciable assets, the change in the mix of depreciable assets, lower depreciation on public telephony installations and DECT assets that were written down in the 1999 financial statements and the adjustment of depreciation rates relating to the submarine network. Such decrease was partly offset by higher levels of depreciation at TIM.

Amortization of intangible assets increased by €90 million or 9.1%, from €988 million in 1999 to €1,078 million in 2000. This change was due to higher amortization at TIM (an increase of €53 million compared to 1999), mainly as a result of the amortization of new investments in software. Goodwill represented €168 million of amortization of intangible assets in 2000 compared to €102 million in 1999.

As a result primarily of the transactions which resulted in Telecom Italia acquiring a controlling stake in the SEAT group as well as certain other international investments made at the end of 2000, Telecom Italia recorded a significant increase in goodwill (€1,020 million as of December 31, 1999 and €10,171 million as of December 31, 2000). See Notes 9, 10, 14 and 23 of Notes to the Consolidated Financial Statements included elsewhere herein for a discussion of write downs in goodwill which were taken in 2001 as a result of impairment in the value of certain acquisitions made during 2001 and in the past years.

Operating Income

The table below sets forth, for the periods indicated, the Group's operating income (total revenues less total operating expenses, including depreciation and amortization and other charges).

	Year ended December 31,	
	1999	**2000 (pro forma)**
	(millions of Euro)	
Operating income	6,433	6,441

Operating income for the Group was flat year on year in 2000 compared to 1999. The slight increase in operating income is mainly attributable to the improved results of TIM (operating income increased by €218 million), partly offset by the lower operating income of Telecom Italia (a decrease of €69 million). As a percentage of operating revenues, operating income in 1999 and 2000 remained stable at the level of 23.7%.

Financial Income, Financial Expense, and Other Income and Expense, Net

The table below sets forth, for the periods indicated, the components of financial and other income and expense, net.

	Year ended December 31,	
	1999	**2000 (pro forma)**
	(millions of Euro)	
Financial income	555	806
Financial expense	(1,466)	(2,261)
of which writedowns and equity in losses in unconsolidated subsidiaries, affiliated companies and other companies, net	(565)	(1,011)
Other income and (expense), net	(507)	(184)
Total financial expense, net and other income and expense, net	(1,418)	(1,639)

Total financial expense, net and other income and expense, net increased from a net expense of €1,418 million in 1999 to a net expense of €1,639 million in 2000, a 15.6% increase. Financial expense (which includes interest expense on financial indebtedness and income or loss from equity investments) increased by 54.2%. The increase is attributable to two principal factors:

- higher average borrowings outstanding during 2000 mainly to finance the acquisition of SEAT resulted in an increase in interest expense of €264 million (€498 million in 1999 and €762 million in 2000);
- higher levels of equity losses of investments in unconsolidated subsidiaries, affiliated and other companies (€1,011 million in 2000 compared to €565 million in 1999) which reflects primarily the

results of operations for the Group' s equitymethod investments, including amortization of goodwill that arose upon the acquisition of these investments (€462 million in 2000 and €184 million in 1999). The increase in 2000 is mainly attributable to the acquisition of SEAT (amortization of €218 million) which was treated as an equity investment during 2000. Amortization of goodwill from this investment was included in depreciation and amortization beginning in 2001. In addition, the increase was due to the losses incurred by the Maxitel group (€224 million), Stream (€202 million), Auna (€176 million) and Telekom Austria (€52 million).

Other income and expense, net decreased from a net expense of €507 million in 1999 to a net expense of €184 million in 2000. In 2000 such balance, among other things, includes gains on the disposal of investments, fixed assets and business segments (€1,146 million). These gains offset the following:

- provision made by TIM to reserve for technological risk (€400 million);
- the expenses and the provisions connected to the transactions for the disposal of investment holdings and the real estate portfolio (€180 million);
- restructuring costs (€480 million) principally related to Telecom Italia' s costs for the corporate reorganization plan;
- the social security charges (€153 million) pursuant to Law No. 58/92 to guarantee uniform status under the former Telephone Employees Pension Fund (FPT);
- the extraordinary annual contribution to INPS (€77 million) to meet the higher financial requirements covered by the rules of the Telephone Employees Pension Fund (FPT).

In 1999 gains on the disposal of investments (€26 million) was more than offset by restructuring costs (€256 million), social security charges pursuant to Law No. 58/92 (€188 million) and certain other charges, net (€89 million).

Income Taxes

Income taxes were €1,910 million in 2000 compared to €2,606 million in 1999. The statutory income tax rate for 2000 and 1999 was 41.25%. Tax as a percentage of income before income taxes was 39.8% in 2000 and 52.0% in 1999. This decrease in tax as a percentage of income before income taxes was primarily due to tax benefits on investments utilized by TIM and the taxation of gains from the sale of investments and the contribution of a portion of the real estate portfolio by Telecom Italia to IM.SER, the real estate company in which the Group sold a 60% interest, using the substitute equalization tax. The tax rate was also affected by the release of deferred taxes by Telecom Italia which involved a reduction in the tax expense for the year 2000 by the excess amount of the "reserve for deferred taxes".

Net Income

Net income before minority interest increased by 20.0% in 2000 compared to 1999. The increase was principally attributable to the significantly lower overall tax provision offset in part by an increase in total financial expense, net and other expense, net. Net income after minority interest was €2,028 million in 2000 compared to €1,737 million in 1999 a 16.7% increase. Minority interest increased from €672 million in 1999 to €864 million in 2000 mainly due to higher levels of profit at TIM.

Results of Operations of Business Units for the Year Ended December 31, 2000 compared to the Year Ended December 31, 1999.

Domestic Wireline

The following table sets forth, for the periods indicated, certain financial and other data for Domestic Wireline.

Domestic Wireline	Year ended December 31,	
	1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	18,449	17,514
Gross Operating Profit	7,918	7,421
Operating income	4,045	3,915
Number of employees at year-end	69,575	62,782

The following table sets forth for the periods indicated certain statistical data for Domestic Wireline Business Unit.

	Year ended December 31,	
	1999	2000
Subscription and Customers:		
Subscriber fixed lines at period-end (thousands)(1)	26,502	27,153
Subscriber fixed line growth (%)	2.0	2.5
Subscriber fixed lines per full-time equivalent employee at period-end(2)	354	409
ISDN equivalent lines at period-end (thousands)(3)	3,049	4,584
Traffic:		
Average minutes of use per fixed line subscriber during period(4)	4,298	4,722
Of which:		
Local traffic during period (in average minutes)(5)	2,767	3,204
Long distance traffic during period (domestic and international) (in average minutes)	1,531	1,519
Growth in international incoming and outgoing traffic in minutes(6)	9.8	5.4

(1) Data include multiple lines for ISDN and excludes internal lines.
(2) Ratio is based on employees of the Company only.
(3) Data excludes internal lines.
(4) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks); excludes traffic for special services.
(5) Not including district traffic and traffic for special services, including internet dial up traffic.
(6) Data include retail from wireline and wholesale international traffic. The reduced growth between 1999 and 2000 is due to increased competition and the decrease of "international bouncing" by the Italian competitors of Telecom Italia.

Revenues from Domestic Wireline services consists mainly of revenues from domestic and international traffic and fees from subscribers for connection and services and other operators for interconnection to Telecom Italia's network. Gross operating revenues from Domestic Wireline decreased by 5.1% in 2000 compared to 1999. This decrease resulted principally from a decline of 13.9% in revenues from traffic, in spite of an increase in minutes of use of 27.6%. Although usage increased, the reduction in tariffs for long distance and international rates beginning August 1, 1999, the discount policies aimed at customer "retention" and the application of new interconnection rates to traffic to and from the mobile network, more than offset the increased usage and the increase in basic subscription charges (an increase of 9.9% due to tariff increases effective August 1, 2000). The net average return on traffic was €5.5 cents per minute in 2000 compared to €8 cents per minute in 1999, an over 30% decrease which translates into a revenue loss of approximately €1,500 million. Included in gross operating revenue is other income which includes fees (€6,700 million) related to retail market (subscribers, rental equipment, data services, etc.) and to wholesale market (interconnection of other operators to Telecom Italia' s network), sales revenues (€350 million), and other less important revenues. Sales revenues, down by €165 million (a decrease of over 32%) compared to 1999, mainly arise from sales of telephone and telematic products (special internal systems, facsimile machines, data transmission equipment and accessories). The decrease is attributable to the fact that in the second half of 2000, for some customers, Telecom Italia only plans the telecommunications systems, leaving manufacturers with the responsibility for the direct sale of equipment.

The number of fixed line subscribers in Italy rose by 2.5% to approximately 27.2 million at December 31, 2000 representing a telecommunications density (fixed line subscribers to total population of Italy) of 47% at December 31, 2000, compared to 46.1% at December 31, 1999. The increase is mainly attributable to the increase in ISDN lines (3,049,000 lines at the end of 1999 and 4,584,000 lines at the end of 2000).

The average minutes of use per fixed line subscriber increased 10% during 2000 due to the growth of Internet traffic (included in local traffic). The decline in average minutes of use for long distance traffic (domestic and international) was a consequence of the substitution of mobile outgoing traffic for fixed line traffic and the entry of new competitors which have begun to take market share from Telecom Italia. Telecom Italia' s market share of local traffic was approximately 93% at year end (down from 97% at June 30, 2000) and its market share of long distance traffic was approximately 76% at year end. The year end market share was the same as at June 30, 2000 but down from 83% at year end 1999. The slowing of loss of market share in long distance traffic and high level of market share of local traffic reflects initiatives taken during 2000. In particular a selective marketing strategy and focus on service stabilized the fixed line segments market shares. For example, the introduction of Teleconomy, an innovative bundled voice and internet service offered on a unitary or flat fee basis. The offer, which was launched in the second half of 2000, was subscribed to by 2.1 million customers by the end of 2000, and management believes that the success of this offer increased customer retention in the targeted more demanding and higher consumption (in terms of traffic) segment of the retail market. Telecom Italia' s market share of fixed to mobile traffic declined from 87% at year end 1999 to 78% at year end 2000.

Gross operating revenues from international traffic decreased by 6.9% in 2000 compared to 1999 despite a 11.5% increase in total international traffic volume, to 7,432 million minutes in 2000 from 6,667 million minutes in 1999 including total outgoing, incoming traffic. The volume increase was largely driven by incoming and mobile (incoming and outgoing) traffic growth. The revenue fall is mainly due to the impact of continuing tariff reductions and increasing competition.

Consolidated operating revenues were €15,961 million in 1999 and €15,306 million in 2000.

Gross Operating Profit was €7,918 million in 1999 and €7,421 million in 2000; the decrease of 6.3% is due to the above mentioned decline in gross operating revenues, partially offset by a reduction in operating costs. Gross operating profit accounted for 42.4% of overall revenues (42.9% in 1999).

Operating Income decreased by 3.2% to €3,915 million in 2000 compared to 1999 (€4,045 million) mainly due to a reduction in gross operating revenues which was almost compensated for by savings in other external charges, labor costs and depreciation and amortization.

Mobile Services

The following table sets forth, for the periods indicated, certain financial and other data for Mobile Services.

Mobile Services	Year ended December 31,	
	1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	8,651	9,418
Gross Operating Profit	3,887	4,447
Operating income	2,708	2,988
Number of employees at year-end	12,363	15,257

The following table sets forth for the periods indicated, certain statistical data for TIM.

	Year ended December 31,	
	1999	2000
TIM lines at period-end (thousands)	18,527	21,601
TIM lines growth per annum(%)	29.6	16.6
Average revenue per mobile line per month(€)(1)	34.9	30.5
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	32.5	37.5
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants)(%)	53.1	73.3
Total mobile outgoing traffic per month (millions of minutes)	1,219	1,569

(1) Including Prepaid Customers revenues and excluding equipment sales.

Gross operating revenues from mobile services increased by 8.9% in 2000 compared to 1999. This increase was primarily due to TIM growth, despite increasing competition, with increasing levels of revenues attributable to value added services, with some contribution from international companies. Tele Nordeste Celular Participacoes, had revenues of €529 million in 2000, an increase of 26.2% over 1999 in Brazilian reais. The increase was due to higher traffic revenues attributable to a 27% increase customers. Tele Celular Sul Participacoes, recorded revenues of €446 million, a 4.7% increase over 1999 in Brazilian reais. Revenues from Stet Hellas amounted to approximately €526 million in 2000, representing an increase of 33% in the number of mobile lines, partly offset by a lower average usage per subscriber as the proportion of non-business users continued to grow.

Consolidated operating revenues were €8,290 million in 1999 and €9,090 million in 2000.

Gross operating profit amounted to €4,447 million, up €560 million, or 14.4% as compared to 1999. The ratio to gross operating revenues increased from 44.9% in 1999 to 47.2% in 2000, mainly attributable to the strong performance of TIM.

Operating income was €2,708 million in 1999 and €2,988 million in 2000. The increase was limited to €280 million, mainly due to the increase of intangible assets amortization (plus €84 million, attributable to TIM investments in software coming into service during the year and to the amortization of the goodwill deriving from the acquisition of controlling stakes in newly consolidated companies), an increase in tangible assets depreciation (plus €112 million) and an increase of write-downs on trade receivables to adjust them to their presumed realizable value. Notwithstanding these increases, the ratio to gross operating revenues improved from 31.3% in 1999 to 31.7%.

TIM (parent company) operating revenues in 2000 were €7,929 million, an increase of 6.4% over 1999. Revenues from services increased by 8.5%. The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 24.6%). During 2000, TIM confirmed its leadership in the Value Added Services (VAS) market.

TIM lines increased to 21,601,000 lines at December 31, 2000, a 17% increase compared to December 31, 1999. TIM' s GSM lines base increased by 24.8% in 2000, to 19,156,000 lines at December 31, 2000, while TIM' s TACS lines base decreased by 23.0% in 2000, to 2,445,000 lines at December 31, 2000 in each case compared to December 31, 1999. Approximately 89% of TIM' s lines are now GSM lines. The continuing significant growth in GSM lines was attributable principally to the continuing growth of the GSM TIM Card (a prepaid rechargeable GSM card) launched in October 1996, which had 16,671,000 lines by December 31, 2000 compared to 12,909,000 lines at December 31, 1999. 86.2% of the 3.1 million new lines activated by TIM during 2000 were prepaid cards.

At December 31, 2000, TIM had a market share in Italy of approximately 51% (including TACS and GSM) compared to 61% at December 31, 1999, and a market share of approximately 48% for GSM only compared to 57% in 1999. The market share decrease was due to increased competition and the commencement of services by the third mobile operator (Wind) in March 1999 and a fourth operator (Blutel) in May 2000. The overall market grew by 40% in 2000 from 30.3 million customers at the end of 1999 to 42.2 million customers at the end of 2000. The aggregate number of customers at December 31, 2000 for TIM's analog and GSM services represented a penetration rate of 37.5% compared to 32.5% at December 31, 1999.

TIM traffic volumes increased by 24.6% in terms of minutes and mobile traffic revenues increased by 9.8% in 2000 (€6,261 million) compared to 1999 (€6,028 million). The net increase in lines (up 16.6% compared to 1999) was partially offset by the continuing decline in average revenues per customer and a decline in average revenue per minute due to increasing competitive pressures and the effect on prices. Average monthly revenue per mobile line (which includes traffic revenues and subscription fees) decreased from approximately €34 in 1999 to €31 in 2000, as low-usage customers, principally non-business customers and GSM and TACS TIM Cardholders, grew further in 2000, making up almost 91% of the customer base. 99% of TIM' s net new additions for its GSM service came from Prepaid Customers.

TIM revenues from equipment sales decreased by 13.0% in 2000 (€609 million) compared to 1999 (€701 million). The mobile subscription fees decreased by 11.9% in 2000 (€230 million) compared to 1999 (€261 million) due to the continuing sharp expansion in the prepaid service customer base, where no subscription fees are paid.

TIM revenues from Value Added Services (VAS) (€340 million in 2000) increased by 121.5% compared to 1999. Due to the continuing introduction of new services and the particular success of SMS, the VAS business grew significantly with revenues from value added services representing 5.13% of traffic revenues and 4.29% of total revenues in 2000, compared to 2.55% and 2.06%, respectively in 1999. In 2000 TIM promoted the increase in use of VAS through promotional campaigns. Such promotions entailed offers of free SMS services and the extension of SMS to TACS users.

The TIM churn rate, as a result of increased competition, particularly because of the entrance of the third and fourth mobile operators, rose to 1.3% per month, up from the 1.0% rate recorded in 1999.

TIM gross operating profit reached €3,845 million, a growth of 10.6% compared with the previous year (€3,478 million) as a result of the increase in operating revenues and the actions taken for the containment of operating costs. Gross operating profit accounted for 48.5% of overall revenues (46.7% in 1999).

TIM operating income (€2,862 million) grew by 8.1% compared with 1999. Operating margin was 36.1% in 2000 and 35.5% in 1999.

Internet and Media

During 2000 Telecom Italia completed the merger of Tin.it, its internet service provider, with SEAT, in a transaction which resulted in the Telecom Italia Group acquiring control of SEAT. Although SEAT was fully consolidated for balance sheet purposes at December 31, 2000, SEAT' s results of operations were not included in the Group' s income statement for purposes of Italian GAAP. Therefore, the results of operations for the years ended December 31, 1999 and 2000 are related only to Tin.it.

The following table sets forth, for the periods indicated, certain financial and other data for the Internet and Media business unit.

Internet and Media	Year ended December 31, 1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	228	263
Gross Operating Profit	(31)	(35)
Operating income	(65)	(73)
Number of employees at year-end(1)	336	7,515

(1) Employees at the end of 1999 were related to Tin.it only. The 7,515 employees as of December 31, 2000 were related to the SEAT group resulting after the SEAT/Tin.it merger.

In 2000, gross operating revenues increased by 15.4% from €228 million in 1999 to €263 million in 2000. The growth was due in part to the increase in internet and products services, which was driven primarily from the overall growth of the internet industry and related traffic volumes experienced in Italy. This increase was also impacted by the decrease in advertising royalties in the White Pages in Italy from SEAT. Prior to the SEAT/Tin.it merger, Tin.it received advertising royalties from SEAT and paid SEAT for the production and printing of the White Pages; after the merger the related contracts have been terminated and the revenues and expenses no longer exist.

Gross operating profit in 2000 remained substantially stable with respect to the previous year with a loss of €35 million compared to a loss of €31 million in 1999. Operating income also was flat year on year (a loss of €65 million compared to a loss of €73 million in 2000). Gross operating profit and operating income were largely impacted by other external charges mainly associated with network utilization costs, advertising expenses and the production and printing costs of the White Pages.

Total Internet users grew from 2 million as of December 31, 1999 to 4 million at the end of 2000.

International Operations

The following table sets forth, for the periods indicated, certain financial and other data for International Operations.

International Operations	Year ended December 31, 1999	2000 (pro forma)
	(millions of Euro, except employees)	
Gross operating revenues	394	505
Gross Operating Profit	(9)	(3)
Operating income	(122)	(134)
Number of employees at year-end	2,403	2,572

International Operations gross operating revenues increased in 2000 to €505 million, an increase of 28.2% compared to 1999 (plus 7.9% on a comparable consolidation basis), benefiting mainly from 9Télécom Reseau revenues of €96 million (five times the amount in 1999) and Intelcom San Marino revenues of €57 million (an increase of €23 million or 147% compared to 1999).

Consolidated operating revenues from International Operations was €365 million in 1999 and €471 million in 2000.

Gross operating profit improved by 66.7% in 2000, reducing the loss from €9 million in 1999 to €3 million in 2000. This was due to the higher contribution of Entel Bolivia and Intelcom San Marino. Operating income fell 9.8% in 2000, compared to 1999, due to the start-up activities in 9Telecom group.

Other Group Activities

The following table sets forth, for the periods indicated, certain financial and other data for IT Services, Satellite Services and TILab.

IT Services	Year ended December 31,	
	1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	2,240	2,138
Gross Operating Profit	352	329
Operating income	120	134
Number of employees at year-end	12,126	12,005

Gross operating revenues from IT Services decreased by 4.6% from €2,240 million in 1999 to €2,138 million in 2000. Operating revenues decreased due to the effects generated by service contracts with the Domestic Wireline Business Unit. Such decrease was offset in part by a 2.5% increase in revenues from the FINSIEL group (€1,167 million in 2000 compared to €1,138 million in 1999) and a 6.6% increase in revenues from Telesoft (€450 million in 2000 compared to €422 million in 1999), which develops software applications for telecommunications services mainly for the Domestic Wireline Business Unit. Gross operating revenues from the FINSIEL group increased due to a growth in activities in the telecommunications, travel and transportation and banking sectors as well as expansion in the local government market. The increase was also attributable to new activities such as development and system integration services. Gross operating revenues from Telesoft increased due to the development of Group activities and international markets where the Group was already operating (Spain, Latin America and Greece).

Consolidated operating revenues for IT Services were €1,138 million in 2000 and €1,099 million in 1999.

Satellite Services	Year ended December 31,	
	1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	316	340
Gross Operating Profit	46	50
Operating income	(11)	(52)
Number of employees at year-end	1,299	1,206

Operating revenues from satellite services increased by 7.6% (€340 million) in 2000 compared to 1999 (€316 million). This increase was principally due to the results of the Telespazio group which recorded increased results in its "space systems and services" segment due to the development of the Artemis, Sicral and Astrolink projects.

The "Media & Communications" business unit, though operating in a mature competitive market, achieved results substantially consistent with 1999. Increased revenues from the television sector offset the negative impact of price declines on telecommunications revenues.

"Space systems and services" gross operating profit recorded performance which offset the negative trend in "Media & Communications" sector, while there was a significant increase for the operating loss in 2000 (€52 million) compared to the operating loss in 1999 (€11 million). The negative figure can mainly be attributed to higher provisions related to mobile satellite sector (especially Iridium and Orbcomm projects), and for bad debts regarding a foreign broadcaster.

TILAB	Year ended December 31,	
	1999	2000
	(millions of Euro, except employees)	
Gross operating revenues	119	123
Gross Operating Profit	(25)	(9)
Operating income	(47)	(34)
Number of employees at year-end	1,302	1,287

Gross operating revenues from TILAB (€123 million) increased by 3.4% in 2000 compared to 1999 (€119 million). This increase is principally due to Telecom Italia demand for investments.

The Gross Operating Profit (Loss) improved by 64.0%, with the 1999 loss reduced from €25 million to a loss of €9 million in 2000. This change is essentially due to an increase in revenues and decrease in other external charges and labor costs.

The Operating income improved by 27.7%, with the 1999 loss (€47 million) reduced to a loss of €34 million in 2000. Such improvement of €13 million was due, substantially, to the same reasons which impacted Gross Operating Profit.

Revenues from Manufacturing and Installation – Sold in September 2000

The table below sets forth for the periods indicated, manufacturing gross operating revenues of Italtel (in 1999 Italtel' s results of operations were proportionately consolidated at 50% from January 1, 1999 to October 31, 1999 and fully consolidated at 100% from November 1, 1999 to December 31, 1999; in 2000, Italtel' s results of operations were fully consolidated only for the first nine months) and installation gross operating revenues (in 2000 only the Sirti' s economic results for the first nine months have been consolidated and therefore are not comparable to those of 1999 related the entire year).

Manufacturing and Installation	Year ended December 31,	
	1999	2000
	(millions of Euro)	
Manufacturing gross operating revenues	1,608	631
Installation gross operating revenues	775	602

During December 2000 Telecom Italia disposed of its interests in Italtel and Sirti, although it retained a passive 19.9% interest in Italtel.

Gross operating revenues of Italtel in 2000 are not comparable with those of 1999 (Telecom Italia' s share was €631 million in 2000 compared to €917 million in 1999). Revenues for the first nine months of 2000 were €631 million, due in part to the significant contribution of activities conducted on foreign markets.

Consolidated operating revenues for the manufacturing and installation businesses were €598 million in 2000 and €927 million in 1999.

Liquidity and Capital Resources

Liquidity

The Group' s primary source of liquidity is cash generated from operations, particularly from telecommunications services, and its principal uses of funds are the payment of operating expenses, capital expenditures and investments, the servicing of debt, the payment of dividends to shareholders and the making of strategic investments, such as international acquisitions.

The table below summarizes, for the periods indicated, the Group' s cash flows.

	Year ended December 31,		
	1999	2000 (pro forma)	2001
		(millions of Euro)	
Net cash provided by operating activities	7,983	5,309	9,602
Net cash used in investing activities	(6,139)	(15,113)	(9,779)
Net cash provided by (used in) financing activities	(1,977)	10,412	(363)
Net increase (decrease) in cash and cash equivalents	(133)	608	(540)
Cash and cash equivalents:			
Beginning of year	811	678	1,305
End of year	678	1,286	765

Net Cash Provided by Operating Activities. Net cash provided by operating activities was €9,602 million in 2001, €5,309 million in 2000 and €7,983 in 1999.

The increase in 2001 compared to 2000 was primarily due to higher levels of depreciation and amortization in 2001 compared to 2000 and the significant level of writedowns of intangibles, fixed assets and investments (€4,039 million in 2001 compared to €1,120 million in 2000) as well as the net change in operating assets and liabilities which reduced cash from operating activities by €3,993 million in 2000 compared with a positive contribution of €372 million in 2001. Such effects were only partially offset by lower levels of net income before minority interest

(€2,892 million of income in 2000 compared to a loss of €1,658 million in 2001) and net gains on disposals of fixed and intangible assets and investments.

The decrease in 2000 compared with 1999 was mainly due to net gains on disposals of fixed and intangible assets and investments, as well as to the changes in operating assets and liabilities, principally as a result of the increases in marketable securities and other current assets, only partially offset by the net change in other liabilities and the higher levels of net income, depreciation and amortization and write-downs of fixed and intangible assets and investments.

Net Cash Used in Investing Activities. Net cash used in investing activities was €9,779 million in 2001, €15,113 million in 2000 and €6,139 million in 1999. Investments in fixed assets, which consisted for the most part of telecommunications installations acquired by Telecom Italia and TIM, were €4,254 million in 2001, €3,405 million in 2000 and €3,875 million in 1999. Investments in intangible assets (including goodwill of €1,174 million in 2001, €9,109 million in 2000 and €567 million in 1999) were €3,910 million in 2001, €13,079 million in 2000 and €1,579 million in 1999. The significant decrease in 2001 compared to 2000 mainly reflects the reduced level of acquisitions in 2001 compared to 2000, in particular when compared to the SEAT acquisition in 2000 which resulted in high levels of goodwill. In addition, 2000 included the initial payments on TIM's UMTS license in Italy. The significant increase in 2000 is principally due to the goodwill arising from the acquisition of subsidiaries (€9,109 million), primarily SEAT as well as the acquisition of 50 million ordinary shares of TIM , and the cost of the UMTS license acquired by TIM in Italy (€2,417 million). Investments in other long-term assets were €3,093 million in 2001 compared with €3,000 million in 2000 and €1,300 million in 1999; in 2001 such investments include €1,906 million of investments made by Tim International to the associated company IS TIM; in 2000 such investments include €871 million for a 30% stake of GLB Servicos Interativos (Globo.com), €662 million relating to the Savings Shares bought back by Telecom Italia and €307 million for setting up IS TIM which won the third GSM 1800 license in Turkey.

In 2000 the outflows due to investing activities were partially offset by the net proceeds arising from the disposal of intangible assets, fixed assets and long-term investments (€4,276 million). In 2001 proceeds from such sales were only €1,439 million.

Net Cash Provided by (Used in) Financing Activities. Net cash provided by (used in) financing activities was a net cash use of €363 million in 2001, and net cash provided of €10,412 million in 2000 compared to net cash used in financing activities of €1,977 million in 1999. Net cash used in financing activities in 2001 reflected a significant increase in long term debt (€10,816 million) as the Group replaced short term debt with long term debt to extend the average life of its debt. The proceeds of such long term debt was primarily used to retire indebtedness, including €6,068 million of short term debt and to fund the dividend payout (€3,097 million). The inflow of cash in 2000 was due to the increases in short-term debt (€9,842 million) and in long-term debt (€1,707 million) as well as to capital contributions (€4,174 million, almost entirely related to the conversion of TIM's savings shares), partly offset by repayments of long-term debt and the dividend payments of €3,049 million. The significant increase in short-term debt was primarily incurred to finance the acquisitions of equity investments, including, among others, the SEAT and Globo.com acquisitions. As noted above, SEAT was treated as an equity investment for income statement purposes in 2000. The outflow of cash in 1999 was mainly due to the repayments of long-term debt (€1,296 million) and the dividend payments (€1,693 million), partly offset by an increase in short-term debt (€242 million) and in long-term debt (€767 million).

Capital Resources

On a consolidated basis, at December 31, 2001, Telecom Italia's outstanding long-term debt was €16,083 million and its short-term debt was €9,114 million (including current portion of long-term debt). Interest on such debt totaled €1,460 million in 2001 compared with €762 million in 2000. Telecom Italia expects its average overall financial indebtedness in 2002 to decline from the high levels of 2001, primarily due to repayments from asset sale proceeds. However, as a result of higher average outstandings and the replacement of short term debt with long term debt with higher average interest costs, interest payable on financial debt is expected to increase in 2002 compared to 2001.

The Group's short-term debt due to banks was €5,790 million at December 31, 2001. As of December 31, 2001, the amount of unutilized short-term bank facilities was €10,295 million; €4,561 million was related to Telecom Italia. Approximately 75% of these facilities are denominated in Euro and have varying interest rates.

In addition, at December 31, 2001, the Group had cash and marketable securities in excess of €2,956 million. The Group believes that its bank facilities, together with its portfolio of marketable securities and cash, are sufficient to meet its present working capital needs.

The following table aggregates Telecom Italia's contractual obligations and commitments with definitive payment terms which will require significant cash outlays in the future. The amounts payable are as of December 31, 2001.

	Year ended December 31,						
	2002	2003	2004	2005	2006	After 2006	Total
	(millions of Euros)						
Long-term debt (including current portion)	1,669	2,946	2,371	2,071	5,760	3,035	17,752
Lease commitments	60	71	53	45	41	345	615
SEAT Put Option(1)	—	—	—	2,985	—	—	2,985
Rental obligations to IM.SER(2)	185	185	185	185	185	2,753	3,678
	1,914	3,202	2,509	5,286	5,986	6,133	25,030

(1) Assumes that J.P. Morgan Chase exercises put option on 710,772,200 SEAT ordinary shares at renegotiated option price of €3.40 at maturity in December 2005. Also includes payment of €569 million by Telecom Italia to J.P. Morgan Chase as compensation for revision to put/call arrangements, also due in December 2005. Telecom Italia has the right to exercise its call option in tranches beginning in December 2004 which could reduce the amounts payable in December 2005 if the put option is exercised. See "Item 4. Information on the Company—Business—Recent Developments—SEAT Put Option" and Note 18 to Notes to Consolidated Financial Statements included elsewhere herein.

(2) Aggregate rental payments due under 21 year contracts.

The table above does not include short term debt due to banks of €5,790 million outstanding at December 31, 2001. For a discussion of the Group's proposed capital expenditure commitments over the next three years, see "—2002-2004 Industrial Plan—Strategic Growth". For a discussion of the Group's capital expenditures in 1999, 2000 and 2001 see "—Capital Expenditures".

The Group's long-term debt was €16,083 million at December 31, 2001 and €6,733 million at December 31, 2000. The increase in long term debt from 2000 to 2001 was primarily due to reduction of short term debt and the consequent extension of the average life of the financial indebtedness.

As of December 31, 2001, approximately 77% of the Group's long-term debt was denominated in Euro, while the remainder was primarily denominated in U.S. dollars, Pound Sterling, Brazilian Reais and Chilean Peso. At December 31, 2001, approximately 41% of the long-term debt carried a floating rate.

In the year ended December 31, 2001, the Group incurred new long-term debt of €10,816 million and reduced short term debt by €6,068 million, respectively, compared to an incurrence of €1,707 million and €9,842 million of long-term and short-term debt, respectively, in the year ended December 31, 2000. In 2001 such long term indebtedness was incurred largely to refinance indebtedness coming due and to retire short term indebtedness as the Group extended the average maturity of its total financial indebtedness. Such indebtedness was incurred to finance investments and refinance certain other indebtedness which had come due.

Long-term indebtedness of €1,669 million, €13,048 million and €3,035 million is scheduled to become due for repayment during 2002, in the years 2003-2006 and beyond 2006, respectively.

The Group's short-term debt (including current portion of long term debt) was €9,114 million at December 31, 2001 and €14,745 million at December 31, 2000. The significant decrease in short term debt reflects the policy of

Telecom Italia to reduce its dependence on short term financing and extend the average maturity of its debt. The Group has achieved this through issuances of debt in the capital markets as described below.

In order to reduce its dependence on short-term debt, extend the average life of its financial indebtedness and expand its investor base, Telecom Italia established a US$10 billion global medium term note program (the "Global Note Program") at the end of 2000; on December 18, 2001 the Board of Directors approved the increase of the above mentioned Global Note Program up to US$12 billion. The Global Note Program includes a shelf registration statement filed with the U.S. Securities and Exchange Commission permitting it to sell up to US$10 billion in debt securities (in any currency) which registration statement was declared effective on October 12, 2000. The Global Note Program also includes a Euro-Tranche which permits the Group to offer debt securities outside the United States. Since January, 2001, the Group has issued an aggregate principal amount of €12.5 billion in long term debt in the capital markets under its Global Note Program, the net proceeds of which have been used to repay short term indebtedness. The debt issued consisted of:

- €2.5 billion of 1% exchangeable notes due 2006;
- €3.0 billion of 6.125% fixed rate notes due 2006;
- €1.0 billion of floating rate notes due 2004;
- €2.0 billion of 7% fixed rate notes due 2011;
- €1.5 billion of floating rate notes due 2005;
- €1.25 billion of 5.625% notes due 2007; and
- €1.25 billion of 6.25% notes due 2012.

The Group's debt to equity ratio, calculated as the ratio of long-term debt and short-term debt less cash and cash equivalents, marketable debt securities and financial receivables to total stockholders' equity, was 113.6% and 69.8% as of December 31, 2001 and December 31, 2000, respectively.

Centralized Treasury. Telecom Italia has a centralized treasury that provides financial assistance to the Group including TIM, and generally operates as the Group's principal banker, allocating cash where needed and collecting liquidity of the members of the Group. As a result, Telecom Italia is able to ensure that its subsidiaries have adequate liquidity to satisfy their requirements. Telecom Italia also acts on behalf of its subsidiaries in negotiating bank lines of credit and provides financial consultancy services to its subsidiaries. The central treasury function reduces the need of the members of the Group to utilize banks, enables members of the Group to obtain more favorable terms from banks when needed and enables Telecom Italia to maintain control over cash flows and to assure better utilization of surplus liquidity.

Cash Management. Telecom Italia utilizes short-term credit lines to support expenses and disbursements that occur in the ordinary course of business, using free cash flow generated by its business to fund capital investments and acquisitions and to repay long-term debt.

Lines of Credit. Short-term lines of credit granted to the Group by banks, according to standard money market terms and conditions, consist partly of lines of credit with specified maturities and partly of lines of credit callable upon notice. All of the Company's medium and long-term lines of credit relate to specific loans drawn down to fund the Company's activities.

Capital Expenditures

The table below sets forth, for the periods indicated, the Group' s total investments (including capital expenditures) based on the organization by Business Unit at December 31, 2001.

	Year ended December 31,		
	1999	2000(1)	2001
		(millions of Euro)	
Fixed assets:			
Domestic Wireline:			
Local and long distance networks	890	697	903
Investment in subscribers' equipment	331	334	298
Exchange equipment	528	449	528
Buildings and land	---	20	18
Other fixed assets	327	342	229
	2,076	1,842	1,976
Mobile Services:			
Radio and transmission equipment	573	542	713
Exchange equipment	337	395	519
Buildings and land	29	31	52
Other fixed assets	257	225	246
	1,196	1,193	1,530
Internet and Media	14	17	82
International Operations	73	94	427
IT Services	136	83	87
Satellite Services	29	29	27
TILAB	14	29	13
Other activities(2)	337	118	112
Total fixed assets	3,875	3,405	4,254
Goodwill	567	9,109	1,174
Other intangible assets(3)	1,012	3,970	2,736
Total capital expenditures(4)	5,454	16,484	8,164
Financial investments(5)	1,300	3,000	3,093
Total investments	6,754	19,484	11,257

(1) The 2000 pro forma amounts give effect to the consolidation of the Nortel Inversora group using the equity method instead of the proportional consolidation method.

(2) In 1999 and 2000 figures included also Sirti and Italtel groups disposed of on December 2000. For the year 2000 the data of such groups only related to the first nine months.

(3) Other intangible assets include investments such as software for telecommunications systems and licenses.

(4) Intercompany capital expenditures are adjusted to eliminate intercompany profit.

(5) Financial investments include the Group' s investment in international activities.

The decrease in capital expenditures in 2001 (€8,164 million) compared to 2000 (€16,484 million) was almost entirely due to the reduction in investments in intangible assets and includes:

- €1,174 million of goodwill (of which €731 million is attributable to the acquisition of the controlling interest in Entel Chile) and €2,736 million of other intangible assets (of which €1,080 million arose from the acquisition of new mobile telecommunications licenses in Brazil and Greece); and

- €4,254 million of fixed assets mainly associated with telecommunications systems and equipment, machinery and installations.

The increase in capital expenditures in 2000 (€16,484 million) compared to 1999 (€5,454 million) was almost entirely due to the increase in investments in intangible assets and includes:

- the goodwill of €9,109 million arising from the acquisition of the controlling interest in SEAT, Maxitel, Digitel, Jet Multimedia and the purchase by Telecom Italia of 50 million TIM ordinary shares and the reorganization of the international telecommunications sector; and
- the cost of the UMTS license acquired by TIM in Italy (€2,417 million) and the PCS 1900 license obtained through Tim Perù (€197 million).

Cash flows from operating activities in 2001 (€9,602 million) exceeded capital expenditures in fixed and intangible assets (€8,164 million) but was lower than total investments (€11,257 million).

Cash flows from operating activities in 2000 (€5,309 million) were lower than capital expenditures in fixed and intangible assets (€16,484 million) and total investments (€19,484 million).

Cash flows from operating activities in 1999 (€7,983 million) exceeded capital expenditures in fixed and intangible assets (€5,454 million) and total investments (€6,754 million).

The expected capital expenditures of the Group for year 2002 to 2004 are €16 billion. Of such capital expenditures, approximately €7 billion is expected to be allocated to wireline telecommunications services Italy, approximately €7 billion is expected to be allocated to mobile telecommunication services (including financing the build out of the UMTS network) and the remaining approximately €2 billion is expected to be allocated to the other Business Units. See "—Results of Operations—2002 - 2004 Industrial Plan—Strategic Growth."

Research and Development Activities

The Group spent €331 million, €269 million and €138 million on research and development in 1999, 2000 and 2001, respectively. The Group also receives grants from national and international programs for use in research and development activities.

The purposes of the Group' s research and development activities is mainly the development of innovative services and applications, to meet the increasing demand from the market.

Development of innovative services is pursued through both the introduction in the network infrastructure of new platforms and systems that enable the provision of a wide range of services and the use of state-of-the-art information and communications technologies for the development of highly innovative applications, tested on selected customers' sites.

Such activities are mainly carried out by CSELT (now TILAB), the corporate research center of the Group. TILAB performs both strategic research as well as research specifically requested by Group Companies.

Consolidated Financial Statements as of and for the Years Ended December 31, 2001 and 2000 – Reconciliation of Italian and U.S. GAAP.

During 2000 and 2001 the Group engaged in certain significant transactions which, under U.S. GAAP give rise to material differences in net income, shareholders' equity and indebtedness when compared to Italian GAAP. In the course of 2000 and 2001, the following transactions occurred that have given rise to significant differences:

- The acquisition of SEAT, including the SEAT put/call option financing entered into concurrently herewith;
- the significant number of acquisitions made by SEAT using its ordinary shares as consideration for such acquisitions;
- the sale of certain equity investments in the satellite sector, with the Group recognizing gains on the sale of an entity for which it still has a continuing ownership interest;
- the sale of certain real estate properties to IM.SER, a wholly owned subsidiary of the Group, and the subsequent sale of 60% of IM.SER to third parties;

- the conversion offers of TIM and SEAT in which savings shares were exchanged for ordinary shares; and

- the substantial decrease in asset valuations in the Telecom and Internet sectors in general.

As a result of the foregoing transactions there are additional material differences and reconciling items in 2001 and 2000, to reconcile Italian GAAP net income and stockholders' equity to U.S. GAAP than the reconciling items disclosed in prior years. The following is a discussion of the U.S. GAAP treatment of such transactions and the impact on net income or loss and stockholders' equity under Italian GAAP for 2001 and 2000. For a complete description of the Group's reconciliation and other required U.S. GAAP disclosures see Notes 26, 27 and 28 of the Notes to the Consolidated Financial Statements included elsewhere herein.

Year Ended December 31, 2001

Net Loss

Under Italian GAAP, net loss was €2,068 million in 2001 and under U.S. GAAP the net loss was €4,039 million. There are many differences between Italian and U.S. GAAP that can result in material adjustments for U.S. GAAP purposes, although the net effect will not necessarily result in material differences between Italian and U.S. GAAP net income or loss. In 2001, the €1,971 million increase in net loss from Italian to U.S. GAAP is largely attributable to certain of the transactions described above that resulted in certain material adjustments. A description of such transactions and their impact on 2001 are described below:

- *SEAT acquisition* – In late 2000 and into 2001, SEAT acquired a significant number of companies using SEAT's own shares as consideration. Under Italian GAAP there is no economic value assigned to the use of stock in a transaction, therefore the purchase price of these transactions on an Italian GAAP basis is considerably lower. For purposes of U.S. GAAP, these transactions have also been treated as acquisitions; however, the fair value of the consideration given is used as the basis to assign the purchase price to the fair value of the assets acquired and liabilities assumed. In general, higher levels of intangible assets, including goodwill, exist in these transactions. Since the acquisition of SEAT effective October 1, 2000, for U.S. GAAP purposes SEAT added additional goodwill of €981 million in 2000 and €810 million in 2001 due to the use of its stock as the acquisition currency. In 2001, €184 million of this goodwill was amortized in the statement of operations.

- In 2001, the Group recorded €2,381 million in impairment charges under Italian GAAP. For purposes of U.S. GAAP, an additional €2,641 million in impairment charges were recorded, for a total charge of €5,022 million. For purposes of Italian GAAP the Group used the fair value of the individual entities reviewed, with fair value generally being based on a discounted cash flow model. For purposes of U.S. GAAP, the process of reviewing assets for possible impairments requires the review of assets assuming the "lowest level of cash flows". Therefore, for purposes of U.S. GAAP, the Group was required to review certain assets for impairment at a lower level of analysis than that performed in the Italian GAAP review. Of the total charges under U.S. GAAP for impairment in 2001, €2,338 million was related to SEAT and SEAT subsidiaries. The remaining amount of the impairment charge is related to investments in Austria and Latin America.

- As part of the SEAT acquisition in 2000, Telecom Italia entered into a put/call transaction with Huit II. For purposes of Italian GAAP, there were no amounts recorded in the financial statements, however, it was fully disclosed in the commitments of the Group. For purposes of U.S. GAAP, the arrangement was considered in substance the acquisition of a minority interest, therefore, the value of the put/call was recorded on the balance sheet as additional indebtedness, with the corresponding value considered part of the acquisition price of SEAT. In 2001, the Group re-negotiated certain terms with the option holder, with an agreement to reduce the option put price. However, the Group is still required to pay the difference in the strike price reduction to the holder. For purposes of Italian GAAP, an accrual of €569 million was made to record this portion of the obligation in 2001, with a comparable charge to the statement of operations. For purposes of U.S. GAAP, since the transaction is recorded as debt on the U.S. GAAP balance sheet and accounted for in the SEAT purchase accounting the charge is reversed under U.S. GAAP and reduces the U.S. GAAP loss by €569 million before tax.

- In 2001 Telecom Italia sold certain non-core investments in satellite sector companies, transferring its equity interests to Mirror, a wholly owned company, at fair value. Mirror borrowed €217 million in non-recourse debt to acquire these assets. Subsequent to the transfer, Telecom Italia sold 70% of Mirror to a merchant bank for €233 million. For purposes of Italian GAAP the Company recognized a gain of €170 million, with no additional debt recorded on the balance sheet. For purposes of U.S. GAAP, Mirror was deemed to be a non-qualifying special purpose entity, therefore the accounts of Mirror are required to be consolidated within the Group. The effects of consolidating Mirror into the Group's U.S. GAAP financial statements was to reverse the gain recognized and increase the U.S. GAAP net loss, and to place an additional €450 million in debt on the balance sheet, €217 million as bank debt and €233 million as additional minority interest.

- Certain subsidiaries of the Group have their own publicly traded shares, which they use from time to time to effect acquisitions. Under Italian GAAP the reduction of the Group's ownership interest in a subsidiary is accounted for as an adjustment to stockholders' equity. Under U.S. GAAP, the Group consistently accounts for these types of dilutions as a non-operating gain or loss through the statement of operations. In 2001, €325 million in gains were recorded in the U.S. GAAP results due to these types of transactions.

Partially offsetting the effects of the foregoing was the capitalization of interest expense on construction in progress (including the UMTS licenses and their supporting networks) which reduced the U.S. GAAP loss by €124 million pre-tax.

Stockholders' Equity, net of minority interests

Stockholders' equity under U.S. GAAP at December 31, 2001 was €12,457 million, compared to €13,522 million under Italian GAAP. Although the overall impact on stockholders' equity of the U.S. GAAP adjustments was to reduce stockholders' equity net of minority interest by only €1,065 million, certain adjustments were material and certain line items of the U.S. GAAP condensed consolidated balance sheet were materially impacted.

Total assets as of December 31, 2001 under Italian GAAP were €62,670 million, compared to €72,518 million on the U.S. GAAP balance sheet, an increase in total assets of €9,848 million. The difference can be attributed to three asset classes: i) at the end of 2001, there was a total of €12,752 million goodwill recorded under U.S. GAAP, compared to €9,141 million for Italian GAAP, an increase of €3,611 million. The higher level of goodwill is attributable to the continuing effects of both the SEAT acquisition and the subsequent acquisitions done by SEAT, generally using their stock as the acquisition consideration, as well as the residual amount of goodwill from STET-Old Telecom Italia Merger; ii) net fixed assets on the U.S. GAAP balance sheet are higher due to the inclusion of the real estate transferred to IM.SER in 2000 which under U.S. GAAP have a book value of €2,202 million as of December 31, 2001; iii) other intangibles arising from the purchase accounting under U.S. GAAP for €2,698 million.

With respect to liabilities, the material impact from the U.S. GAAP adjustments relates to long-term debt. Long-term debt increased from €16,083 million to €21,906 million, due to the following items:

- *SEAT Put/Call Option Financing* – pursuant to the various transactions relating to the arrangements between Huit II and the J.P. Morgan Chase Group, in which J.P. Morgan Chase has a put option to Telecom Italia for approximately 710 million SEAT shares at a price of €4.20 per share and Telecom Italia has a call option on approximately 660 million SEAT shares for the same price. U.S. GAAP considers this transaction as the acquisition financing of a minority equity interest. As a result, U.S. GAAP requires Telecom Italia to record additional long-term debt of €2,985 million.

- *Sale of Real Estate to IM.SER* - In 2000 Telecom Italia transferred certain properties to a wholly owned subsidiary, IM.SER, after which Telecom Italia sold 60% of the shares to third party investors. After the sale of the majority stake in IM.SER, it subsequently borrowed € 2,427 million and distributed the cash to the shareholders as an extraordinary dividend. Telecom Italia received, from both the divested equity ownership stake and the special dividend from IM.SER, approximately €2,700 million in cash receipts. Under Italian GAAP the Group recognized a gain on the partial sale of the ownership interest, removed the historical cost of the real estate from the balance sheet and IM.SER' s debt was not recognized. The assets were subsequently leased by Telecom Italia from IM.SER. For purposes of U.S. GAAP, the continuing economic interest of the Group in IM.SER requires that the real estate remain on the consolidated balance sheet, along with the associated debt. The debt on the consolidated U.S. GAAP balance sheet at the end of 2001 for this transaction was €2,520 million.

Year Ended December 31, 2000

Net Income

Under Italian GAAP, net income for 2000 was €2,028 million and under U.S. GAAP net income was €3,522 million. In 2000, the €1,494 million increase in U.S. GAAP net income compared to Italian GAAP net income is largely attributable to the transactions referred to above which resulted in certain material adjustments:

- *SEAT acquisition.* The acquisition of Telecom Italia' s controlling interest in SEAT consisted of both a cash component as well as the contribution of Tin.it shares, in each case in exchange for SEAT shares. Under Italian GAAP the cash component of the acquisition was accounted for under purchase accounting, and the exchange of shares was treated as a pooling of interest. Under U.S. GAAP the entire transaction was treated as a purchase for acquisition accounting purposes, which resulted in higher levels of goodwill being recorded for U.S. GAAP purposes than under Italian GAAP. U.S. GAAP also required Telecom Italia to record gains on the contribution of Tin.it shares to SEAT and on the distribution made by SEAT of SEAT shares to Telecom Italia shareholders in exchange for Tin.it shares. This distribution was treated as a dividend at fair value. The resulting gains under U.S. GAAP of €7,866 million increased U.S. GAAP net income.

- Subsequent to acquiring control of SEAT, SEAT made a number of acquisitions and issued additional SEAT shares as consideration in such acquisitions. For U.S. GAAP purposes Telecom Italia recognized a gain of €398 million associated with the dilution effect the issuance of the new shares had on Telecom Italia' s shareholding. Italian GAAP only required adjustments to stockholders' equity.

- Offsetting these gains was a write down in goodwill associated with an impairment charge of €7,966 million based upon SFAS 121, *Accounting for the Impairment of Long Lived Assets and for Long Lived Assets to be Disposed of.* Due to the decline in the price of SEAT shares at December 31, 2000 and further analysis performed by Telecom Italia, which indicated that the fair value of SEAT was less than the carrying value of the investment, the goodwill related to the investment was considered impaired. Under U.S. GAAP, the fair market value of the SEAT acquisition was €16,024 million, including acquisition goodwill of €13,834 million. In addition, the historical financial statements of SEAT already included goodwill of €2,769 million. Under Italian GAAP, as a result of the treatment being split between purchase and pooling accounting, Telecom Italia recorded goodwill of €6,796 million. For Italian GAAP purposes there was no similar impairment charge.

- *Subsidiary Stock Conversions.* In connection with TIM and SEAT exchanging ordinary shares for savings shares held by their respective shareholders, the holders of the savings shares were required to pay a cash premium as part of the exchange. The transactions resulted in a net increase in the book value of TIM and SEAT which, under U.S. GAAP, resulted in a non-operating gain of €2,212 million, increasing net income. Under Italian GAAP this gain was accounted for as an equity movement and had no impact on the statement of operations.

In addition to the foregoing, the reversal of certain provisions, (primarily relating to TIM) not allowable for U.S. GAAP purposes (an increase in U.S. GAAP net income of €407 million) was largely offset by the reversal of the gain recognized under Italian GAAP on the sale of the real estate assets (a reduction in net income of€315 million).

The aggregate impact of the foregoing, together with the other adjustments discussed in Note 26 to Notes to the Consolidated Financial Statements, resulted in the increase in U.S. GAAP net income in 2000 compared to Italian GAAP net income.

Stockholders' Equity, net of minority interest

Stockholders' equity under U.S. GAAP in 2000 were€19,118 million compared with €18,821 million under Italian GAAP. Although the overall impact on stockholders' equity of the U.S. GAAP adjustments was not material, certain adjustments were material and certain line items on the U.S. GAAP condensed consolidated balance sheet were materially impacted.

Total assets as of December 31, 2000 under Italian GAAP were €65,515 million compared with €71,528 million under U.S. GAAP, a difference of €6,013 million. Substantially all of the difference is attributable to the higher levels of goodwill recorded for U.S. GAAP purposes (€18,071 million under U.S. GAAP compared to €10,299 million under Italian GAAP, an increase of€7,772 million), mainly attributable to the SEAT acquisition and acquisitions made by SEAT. In addition, the different accounting treatment of the real estate transaction under U.S. GAAP resulted in buildings with a historical carrying value of €2,381 million being recorded on the balance sheet. This was offset by a reduction in net fixed assets of €2,704 million attributable to Nortel Inversora Group which is accounted for under U.S. GAAP in accordance with the equity method.

With respect to liabilities, the material impact from the U.S. GAAP adjustments relates to long-term debt. Long-term debt increased from €8,268 million under Italian GAAP to €12,466 million under U.S. GAAP. The increase in long-term debt is due to the following:

- *SEAT Put/Call Option Financing.* Pursuant to the various agreements relating to the put/call transactions with Huit II entered into in 2000, U.S. GAAP considers these transactions as the acquisition financing of a minority equity interest. As a result, U.S. GAAP requires Telecom Italia to record additional long term debt of €2,985 million. Such amount is also included as part of the overall purchase price of the SEAT acquisition.

- *Real Estate Transaction.* Under U.S. GAAP the sale of the 60% interest in IM.SER to unrelated third parties, together with certain dividends paid by IM.SER to its shareholders, including Telecom Italia, is treated as a secured borrowing resulting in an increase in long-term debt of €2,692 million.

- *Nortel Inversora Group.* The increases in long-term debt described above were partially offset by a reduction in long-term debt of €1,535 million attributable to Nortel Inversora Group which is accounted for under U.S. GAAP in accordance with the equity method.

Cautionary Statement for Purposes of the "Safe Harbor" Provisions of the United States Private Securities Litigation Reform Act of 1995. The foregoing discussion in "Item 5. Operating and Financial Review and Prospects" and the following discussion under "—Quantitative and Qualitative Disclosures About Market Risk" contains forward-looking statements which reflect management's current views with respect to certain future events and financial performance. Actual results may differ materially from those projected or implied in the forward-looking statements. Further, certain forward-looking statements are based upon assumptions of future events which may not prove to be accurate. The following important factors could cause Telecom Italia's actual results to differ materially from those projected or implied in any forward-looking statements:

- the continuing impact of increased competition in a fully liberalized market, including competition from global and regional alliances formed by other telecommunications operators, in Telecom Italia's core domestic fixed-line and wireless markets;

- Telecom Italia' s ability to introduce new services to stimulate increased usage of its fixed and wireless networks to offset declines in its fixed line business due to market share loss and pricing pressures;
- the impact of regulatory decisions and changes in the regulatory environment;
- the impact of the economic crisis in Argentina, the slowdown generally in Latin American economies and the slow recovery of economies generally on Telecom Italia' s international business focused on Latin America and on its foreign investments and capital expenditures;
- the continuing impact of rapid changes in technologies;
- the impact of political and economic developments in Italy and other countries in which Telecom Italia operates;
- the impact of fluctuations in currency exchange and interest rates;
- Telecom Italia' s ability to implement successfully its 2002-2004 Industrial Plan, including the rationalization of its corporate structure and the disposition of Telecom Italia' s interests in various companies;
- Telecom Italia' s ability to successfully achieve its debt reduction targets;
- Telecom Italia' s ability to successfully roll-out its UMTS networks and services and to realize the benefits of its investment in UMTS licenses and related capital expenditures;
- Telecom Italia' s ability to realize the benefits of the merger of SEAT and Tin.it;
- SEAT' s ability to implement successfully its internet strategy;
- Telecom Italia' s ability to achieve cost reduction targets in the time frame established or to continue the process of rationalizing its non-core assets; and
- the impact of litigation or decreased mobile communications usage arising from actual or perceived health risks or other problems relating to mobile handsets or transmission masts.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The following discussion should be read in conjunction with the "Summary of Accounting Policies" in the notes to the consolidated financial statements and in conjunction with Note 28 to the consolidated financial statements, which provides a summarized comparison of the nominal amounts, carrying values and market values of derivative and non-derivative financial instruments and other information relating to those instruments. In the normal course of business, the financial position of the Group is routinely subjected to interest rate and foreign exchange rate risks. These market risks principally relate to the Group's outstanding debt and non-Euro denominated assets and liabilities. The Group does not enter into derivative transactions for trading or speculative purposes. The following discussion is based on the amounts of indebtedness as derived from our Italian GAAP financial statements. See footnote 28 for a further discussion of items which, for purposes of U.S. GAAP, are considered to be debt.

Debt Policy

The Group's debt used to support the financing of its domestic business and international expansion (and the expanding geographic breadth of its business) contains an element of market risk from changes in interest and currency rates. With respect to interest rates applicable to medium and long-term debt, the Group's policy is to utilize both floating rate and fixed rate with different ranges of maturity. The Group's policy is intended to optimize the cost of funding/risk exposure mix, utilizing as providers of funds domestic and international capital markets and supranational agencies such as the European Investment Bank. The Group policies address the use of financial derivatives, including the approval of counterparties and the investment of excess liquidity. These policies are intended to minimize financial risks and obtain more favorable terms from the counterparts. In addition, Telecom Italia has a centralized treasury that provides assistance to its subsidiaries worldwide and usually operates as the Group's main banker, allocating resources according to the needs. The centralized treasury also gives support in negotiating credit lines and financial operations in general.

The table below sets forth, for the periods indicated, the aggregate principal amount of long-term debt (including current portion) payable in each year through 2006 and thereafter.

	2002	2003	2004	2005	2006	Thereafter	As of December 31, 2001 Total	As of December 31, 2000 (pro forma)
				(millions of Euro)				
Fixed Rate Debt	648	768	627	303	5,502	2,365	10,213	2,043
Floating Rate Debt....	1,021	2,178	1,644	1,768	258	670	7,539	5,923
Total	1,669	2,946	2,271	2,071	5,760	3,035	17,752	7,966

The table below sets forth, for the periods indicated, the aggregate principal amount of long-term debt outstanding at year-end (excluding current portion of long-term debt) and the average interest rate, broken down by type of loan. As of December 31, 2001 the fair value of such outstanding debt amounted to about €16,117 million. The financial debt's market value is estimated on the basis of the present value of the future cash flows.

	Year ended December 31						
	2001	2002	2003	2004	2005	2006	Thereafter
	(millions of Euro, except for percentages)						
Long-Term Fixed Rate Debt	8,535	8,397	8,026	7,900	2,398	2,313	2,287
Average Fixed Rate	5.07%	5.00%	4.96%	4.97%	4.93%	7.68%	7.70%
Long-Term Floating Rate Debt Swapped into Fixed Rate Debt	1,114	184	178				
Average Swapped into Fixed Rate	5.94%	4.97%	4.96%				
Average Total Fixed Rate	5.18%	5.00%	4.96%	4.97%	4.93%	7.68%	7.70%
Floating Rate Debt	6,434	4,556	2,662	895	637	582	514
Total Long-Term Debt	16,083	13,137	10,866	8,795	3,035	2,895	2,801

As of December 31, 2001, approximately 77% of the Group's long term debt was denominated in Euro, while the remainder, about €3,660 million, was denominated in foreign currencies primarily US dollars, Pound Sterling, Brazilian Reais and Chilean peso. After taking into account the Company's derivative financial instruments, the Company's long-term debt is not materially exposed to fluctuations in foreign exchange rates. At December 31, 2001, approximately 41% of the long-term debt carried a floating rate.

Market Risk Policy

The Group's policy regarding market risk consists of the following:

- The Centralized Treasury determines the maximum level of interest rate and foreign exchange rate risk to which the Group should be exposed. A Supervisory Committee meets on a regular basis to monitor the activities and the level and value of the current market risk exposures. The Centralized Treasury, operating as a service center, supplies financial services and actively supports to the Group subsidiaries according to their requirements and local circumstances.

- The Group uses derivative financial instruments to manage these risks as discussed below and does not, in the ordinary course, enter into such instruments on a speculative basis. It is the Group's policy to retain any such instruments until maturity.

- The Group continually evaluates the credit quality of counterparties to minimize the risk of non-performance. Any such derivative financial instruments are entered into with major banks or financial institutions.

Financial Instruments

Interest Rate and Foreign Exchange Risk Management

Telecom Italia Group seeks to minimize market risk of its operating and financing activities and according to the evaluation of its exposures, selectively enters into derivatives instruments. Since Telecom Italia's corporate objective is pursued through its commercial operations, meaning the sale of media and telecommunications services, unwanted foreign exchange and interest rate exposures are normally hedged, provided the risks would affect Telecom Italia's cash flows.

The Group is exposed to market risks arising from changing in interest rates, primarily in the Euro zone, in the United States and in Latin America. The Group defines the optimal mixture of fixed and floating-rate debt in each currency, and enters into financial derivatives to adjust their risk profile to the defined target mixture. Interest rate swaps ("IRS") and interest rate options ("IRO") are therefore used to reduce the interest rate exposure on fixed-rate and floating-rate bank loans and bonds. Telecom Italia Group uses cross-currency-interest rate swaps ("CIRS") and foreign currency forwards to convert foreign currency loans – mainly US dollar and Euro – into the functional currencies of the various subsidiaries. As a result of these hedge activities, Telecom Italia Group as of December 31, 2001 was not subject to any material foreign exchange risk in its financial indebtedness nor in its commercial operations.

To determine the market value of the financial derivatives, Telecom Italia Group uses various pricing models. The market value of interest rate swaps and of cross currency and interest rate swaps reflects the present value difference between the fixed rate to be paid/received and the interest rate assessed on the basis of the market trend having the same expiry date as the swap. The CIRSs also reflect the difference between the foreign exchange rate at the closing of the swap and the market rate as of December 31, 2001. The market value of the cross currency and interest rate swaps depends also on the difference between the reference foreign exchange rate at the trade date and the foreign exchange rate at the valuation date.

With regard to IRSs and IROs, they involve or can involve the exchange of flows of interest calculated on the applicable notional principal amount at the agreed fixed or variable rates at the specified maturity date with the counterparties. This amount does not represent the amount exchanged between the parties and therefore does not constitute a measure of exposure to credit risk, which is instead limited to the amount of interest or interest differentials to be received at the interest date.

The same applies to CIRSs which involve the exchange of capital, in the respective currencies of denomination, in addition to the settlement of periodic interest flows, at maturity and eventually at another date.

The counterparties to derivative contracts are generally highly rated banks and financial institutions and such counterparties are continually monitored in order to minimize the risk of non-performance.

The following tables give a description of the Group financial derivative contracts outstanding as of December 31, 2001 to hedge the debt positions.

(millions of Euro)	Notional amount/ Capital exchanged at 12/31/2001	Market value of derivatives at 12/31/2001 (a)	Market value of underlying debt positions at 12/31/2001 (b)	Market value of debt including related derivatives at 12/31/2001 (c)=(b-a)	Market value of derivatives at 12/31/2000 (pro forma)
Interest rate swaps and interest rate options..	5,979	(35)	5,998	6,033	26
Cross-currency and interest rate swaps..	1,847	(16)	1,767	1,783	25

	Interest Rate Derivative Instruments							
	(millions of Euro)							
	Maturities							
IRS	**2002**	**2003**	**2004**	**2005**	**2006**	**Thereafter**	**Total**	**Fair Value**
EURO interest rate Swaps....................								
Receive variable, pay fixed								
Amount	155	568	6	624	-	-	1,353	1,350
Average pay rate..................................	4.65%	3.84%	4.25%	5.27%	-	-		
Average receive rate............................	Euribor 3m	Euribor 3m	Euribor 3m	Euribor 3m	-	-		
EURO Interest rate Swaps								
Receive variable, pay variable								
Amount		1,400	231	238	215		2,084	2,067
Average pay rate..................................		Euribor 3m+33.85bp	Euribor 6m Set in arrears	Euribor 6m Set in arrears	Euribor 6m Set in arrears			
Average receive rate (1),(2),(3),(4)		Euribor 3m+66.5bp	Rolint, Robot	Rolint, Robot, Rendint, Rendibot	Rolint, Robot, Rendint, Rendibot			
EURO interest rate Swaps....................								
Receive fixed, pay variable								
Amount				300			300	302
Average pay rate..................................				Euribor 3m+108bp				
Average receive rate............................				-				
U.S.$ interest rate Swaps								
Receive variable, pay fixed								
Amount				153			153	159
Average pay rate..................................				-				
Average receive rate............................				U.S.$ Libor 3m				
BRL Interest rate Swaps								
Receive variable, pay fixed								
Amount		15					15	15
Average pay rate..................................		16.04%						
Average receive rate............................		103%CDI*(5)*						
Options/Collars								
EURO interest rate collar.....................		700					700	696
Average cap strike rate (purchased)......		-						
Average floor strike rate (sold)............		-						
U.S.$ interest rate collar.......................								
Amount		267		85			352	362
Average cap strike rate (purchased)......		4.70%		7.0%				
BRL interest rate collar.........................								
Amount...	22						22	27
Average cap strike rate (purchased).......	18.0%							
Swaption								
Amount		1,000					1,000	1,020
Average Strike		5.54%						
Total							5,979	5,998

(1) The Rolint is a customary domestic Italian parameter for medium/long-term debt. The average interest rate on the financings as of December 31, 2001 was 5.96%.
(2) The Robot is a customary domestic Italian parameter for medium/long-term debt. The average interest rate on the financings as of December 31, 2001 was 4.95%.
(3) The Rendint is a customary domestic Italian parameter for medium/long-term debt. The average interest rate on the financings as of December 31, 2001 was 5.21%.
(4) The Rendibot is a customary domestic Italian parameter for medium/long-term debt. The average interest rate on the financings as of December 31, 2001 was 4.78%.
(5) The CDI is the customary domestic Brazilian parameter of overnight interest rate. The rate applied to the transaction was 103% of CDI. As of December 31, 2001 this rate was around 19% per annum.

Foreign Exchange Derivative Instruments
(millions of Euro)

Cross Currency Interest Rate Swap	Maturities 2002	2003	2004	2005	2006	Thereafter	Total	Fair Value
Receive Fixed GBP, pay Fixed EURO								
Amount	78						78	72
Average pay rate	4.50%							
Average receive rate	7.0%							
Receive variable GBP, pay Fixed EURO								
Amount		234					234	232
Average pay rate		3.76%						
Average receive rate		Libor GBP +4.6 bp						
Receive variable GBP, pay variable EURO								
Amount			78				78	78
Average pay rate			Euribor 3m + 11 bp					
Average receive rate			Libor GBP 3m +10 bp					
Receive Fixed U.S.$, pay variable BRL								
Amount	463	9	25	41			538	497
Average pay rate (1)	CDI	CDI	CDI	CDI				
Average receive rate	U.S.$ fixed	U.S.$ fixed	U.S.$ fixed	U.S.$ fixed				
Currency forward								
Buy U.S.$/Sell EURO								
Amount	9	13					22	25
Forward rate	0.90	0.80						
Buy U.S.$/Sell BRL								
Amount	218						218	200
Forward rate	2.634							
Buy U.S.$/Sell UF (CLP)								
Amount	543	107	29				679	663
Forward rate	0.0387	0.04345	0.0446					
Total							1,847	1,767

(1) The CDI is the customary domestic Brazilian parameter of overnight interest rate. As of December 31, 2001 this rate was around 19% per annum.

On December 31, 2001 there were also hedges on short term treasury operations in Sogerim for a notional amount of €368 million while in Telecom Italia S.p.A. there were hedging operations on short term debt through Currency Forwards for a notional amount of €11 million and Forward Rate Agreements for €300 million.

The Group also entered into derivative contracts to hedge the interest rate and foreign currency risk on its financial assets. As of December 31, 2001, Softe had entered into Interest Rate Swaps on bond investments for a notional amount of about €272 million and Currency Forwards on short term treasury operations for about €1,812 million.

Telecom Italia Group regularly assesses financial market risks and has established policies to manage and mitigate the adverse effects of these exposures. As a result, the Group does not anticipate any material losses in these areas.

Item 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

Directors

The following are the members of the Board of Directors of Telecom Italia as of June 10, 2002. All of the directors were elected at the Telecom Italia shareholders' meeting held on November 7, 2001. The shareholders meeting was called following the resignation of the previous Board of Directors following Olimpia's acquisition of a 28.7% stake in Olivetti. At that meeting the number of directors was set at 15.

Name	Age	Position	Appointed
Marco Tronchetti Provera	54	Chairman (1)	2001
Gilberto Benetton	61	Deputy Chairman(1)	2001
Enrico Bondi	67	Director and Chief Executive Officer(1)	2001
Carlo Orazio Buora	56	Director and Chief Executive Officer(1)	2001
Umberto Colombo(2)	74	Director	2001
Francesco Denozza(2)	55	Director	2001
Luigi Fausti(3)	72	Director	2001
Guido Ferrarini(2)	51	Director	2001
Paolo Maria Grandi	47	Director	2001
Natalino Irti(3)	66	Director	2001
Gianni Mion	58	Director	2001
Massimo Moratti	57	Director	2001
Carlo Alessandro Puri Negri	49	Director	2001
Pier Francesco Saviotti	59	Director	2001
Roberto Ulissi(4)	39	Director	2001

(1) Appointed by the Board of Directors on November 7, 2001.
(2) Elected by minority shareholders and considered independent directors by the Company.
(3) Although put forward by Olivetti, the Company considers these directors as independent as they are not majority shareholders nor are they parties to the agreements among the Olimpia shareholders nor do they have economic ties which would impair their independent judgment with regard to the Telecom Italia Group, the executive Directors, the majority shareholder or the various parties of the aforementioned pacts.
(4) Appointed by the Treasury pursuant to the Privatization Law and the special powers of the State included in Telecom Italia Bylaws and considered independent by the Company.

As of June 10, 2002, the Secretary of the Board of Directors was Francesco Chiappetta.

Pursuant to the Privatization Law and the special powers of the State included in the Telecom Italia Bylaws, the Treasury has the right to appoint one director of Telecom Italia. Pursuant to the Public Concessions, prior to their conversion into licenses (see "Item 4. Information on the Company—Regulation—Public Concessions") the Ministry of Communications had the right to designate one director of Telecom Italia. As of now, no such power is retained by the Ministry of Communications.

Pursuant to a shareholders' agreement between Pirelli and Edizione Holding dated August 7, 2001 (as amended on September 14, 2001 and on February 13, 2002), and to an agreement among Pirelli, IntesaBCI and Unicredito dated October 24, 2001 (collectively, the "Shareholders Agreements") Edizione Finance International S.A. ("Edizione Finance"), a company 100% owned by Edizione Holding, which was subrogated in Edizione Holding's rights and obligations, may designate one-fifth of the members of the Board of Directors available for nomination (not including the members of the Board appointed by minority shareholders and government agencies) and the Deputy Chairman, who will hold the legal representation in the Company. One member of the Board is appointed at the request and designation of IntesaBci and one member of the Board is appointed at the request and designation of Unicredito.

Moreover, pursuant to the Shareholders Agreements, Pirelli pledged, to the extent allowed by law, that no decision will be made by the Board of Directors without the favorable vote of at least one of the Board members appointed by Edizione Finance (if present) on the following points of business:

- individual investments greater than €250 million;
- purchase, sale and deeds of disposition for any reason whatsoever of controlling and connecting shareholdings with an individual value of more than €250 million;
- deeds of disposition for any reason whatsoever of businesses or assets individually greater than €250 million;
- proposals to call a Shareholder's Extraordinary Meeting;
- transactions between the Olivetti group and the Pirelli group for amounts individually greater than €50 million; and
- transactions with related parties.

For a description of the transactions that involved Pirelli, Edizione Holding, IntesaBCI and Unicredito in acquiring a stake in Olivetti through Olimpia and the underlying agreements, please see "Item 4. Information on the Company—Business—Significant Developments during 2001—The Pirelli-Olimpia Transaction".

Pursuant to Articles 10 and 13 of Telecom Italia's Bylaws, the Board of Directors is appointed by the Shareholders' Meeting through the "*voto di lista*" system (as described below) and is responsible for the ordinary and extraordinary management of Telecom Italia. The Board of Directors consists of not less than seven members and not more than 15 members. The Telecom Italia Shareholders' Meeting held on November 7, 2001 set the number of directors at 15 and this number will not be changed until the Shareholders' Meeting resolves to do so. Directors may serve for a maximum term of three years, they may be re-elected and there is no statutory age limit for their eligibility. The Shareholders Meeting held on November 7, 2001 resolved that the current Directors of Telecom Italia will remain in office for a three-year term (from 2001 to the Annual shareholders Meeting called to approve the Telecom Italia financial statements for the year ended December 31, 2003).

If during the term of the Board of Directors one or more directors ceases from office for any reason, the Board of Directors will appoint replacements by a resolution approved by the Board of Statutory Auditors. The directors so appointed will remain in office until the next Shareholders' Meeting. The directors appointed by such Shareholders' Meeting will remain in office for the same term as the other members already in office at the time of their appointments.

The Board of Directors appoints from its members a Chairman, if the Shareholders' Meeting has not previously done so, and may appoint one Deputy Chairman, both of whom may be reappointed. The Board of Directors may also appoint one or more Chief Executive Officers and determine his/their administrative powers. The Chief Executive Officer's term of office ends with the term of the Board of Directors which appoints him. The Chairman and the Chief Executive Officer are Telecom Italia's legal representatives and in case of the Chairman's absence, for any reason, the Deputy Chairman will replace him.

Corporate Governance

The Company's Board of Directors conformed to the recommendation made by Borsa Italiana in respect of adopting rules of self-discipline for the corporate bodies, and adopted the Telecom Italia code of self-discipline. Such code provides, among other things, that an audit and corporate governance committee and a remuneration committee be set up in the framework of the Board of Directors.

Moreover, in October 2000, the ordinary shareholders approved certain rules regulating shareholders' meetings.

Audit and Corporate Governance Committee

Currently the members of the audit and corporate governance committee are directors Roberto Ulissi (chairman), Guido Ferrarini and Natalino Irti. The audit and corporate governance committee works closely with the Board of Statutory Auditors.

Such committee:

(a) evaluates the adequacy of the internal control system;

(b) evaluates the work plan prepared by those in charge of internal control and receives periodical reports from same;

(c) evaluates the proposals formulated by the independent audit firms to obtain appointment as auditors, as well as the audit work plan and the conclusions described in the letter of recommendations. To this end, as advised by the Board of Directors, the Committee monitors the application of accounting principles;

(d) informs the Board of Directors, at least every six months, at the time of the approval of the annual and semiannual financial statements, on the activities carried out and the adequacy of the system of internal control; and

(e) oversees the observance and periodical updating of the rules for corporate governance and compliance with the code of conduct, if any.

At the beginning of 2002, the committee approved the organizational decision to concentrate the internal audit activities of Telecom Italia, TIM and Seat, in a specific consortium company, which led to the creation of In.Tel.Audit Societá Consortile a.r.l. The project led to the repositioning and reorganization of the system of internal control by taking into account the complexity of the Group, in addition to the new requirements set forth by Legislative Decree of June 8, 2001 No. 231/2001 ("Decree 231") with regard to the administrative responsibility of business entities with respect to the offenses committed by its employees and its agents. The revision of the internal control system is continuing, but the committee concluded that it can be considered adequate, an evaluation that was shared by the Board of Directors at the time of approving the draft 2001 financial statements. At that time, the committee agreed with the Company to adopt a code of ethics which is currently under study.

During 2001 this committee met six times.

Remuneration Committee

Currently the members of the remuneration committee are Luigi Fausti (Chairman), Umberto Colombo and Pier Francesco Saviotti.

The remuneration committee formulates proposals for the Board of Directors regarding compensation of Directors who hold specific responsibilities as well as the criteria for compensation of Telecom Italia's top management. Part of the compensation of executive directors is tied to achievement of budget targets and the committee also considers issues relating to the Group's stock option plans.

Executive Officers

As of June 10, 2002, the executive officers of Telecom Italia and their respective ages, positions and year of appointment as executive officers were as follows:

Name	Age	Position	Appointed
Oscar Cristianci	60	Head of Latin America Operations	2001
Central Functions			
Alberto Borgia	49	Head of Investor Relations	2001
Gustavo Emanuele Bracco	54	Head of Human Resources	2001
Francesco Saverio Bruno	47	Head of International Subsidiaries	2001
Andrea Camanzi	53	Co-Head of Public and Economic Affairs	1999
Aldo Cappuccio	53	Head of Corporate and Legal Affairs	2002
Francesca Di Carlo	38	Head of Mergers & Acquisitions	2001
Armando Focaroli	57	Chairman of IN.TEL.AUDIT	2001
Luciano Gallo Modena	53	Head of Security	2001
Andrea Granelli	41	Head of Venture Capital and CEO TILAB	2000
Enrico Parazzini	58	Head of Finance, Administration and Control	2001
Riccardo Perissich	60	Head of Public and Economic Affairs	2001
Gian Carlo Rocco di Torrepadula	59	Head of Communication and Image	2001
Germanio Spreafico	49	Head of Purchasing	2001
Operational Activities:			
Arrigo Andreoni	58	Head of Information Technology Group	2001
Salvatore Sardo	49	Head of Real Estate and General Services	2001
Business Units:			
Paolo Dal Pino	39	Head of Internet and Media Business Unit and CEO SEAT	2001
Marco De Benedetti	39	Head of Mobile Business Unit and CEO TIM	1999
Salvatore Pinto	44	Head of Telespazio Business Unit and CEO Telespazio	2001
Riccardo Ruggiero	41	General Manager of T.I. and Head of Domestic Wireline Business Unit	2001
Giuseppe Tronchetti Provera	34	Head of Information Technology Market Business Unit	2002

Board of Statutory Auditors

As of June 10, 2002, the following table lists the members of the Telecom Italia Board of Statutory Auditors, including Telecom Italia Alternate Auditors, with their respective positions and year of appointment. The present Telecom Italia Board of Statutory Auditors was appointed on July 3, 2000.

Name	Position	Appointed
Paolo GERMANI(1)	Chairman	2000
Mario BOIDI(3)	Auditor	2000
Paolo GOLIA(4)	Auditor	2000
Fabrizio QUARTA(2)	Auditor	2000
Gianfranco ZANDA(3)	Auditor	2000
Leonida LIUNI(3)	Alternate Auditor	2000
Enrico BIGNAMI(4)	Alternate Auditor	2000

(1) Appointed by the Treasury.
(2) Designated by the Ministry of Communications. Reappointed in 2000. Member of Statutory Auditors Committee since 1999.
(3) Reappointed in 2000. Members of Statutory Auditors Committee since 1997.
(4) Elected by minority shareholders.

The Board of Statutory Auditors verifies the observance of the law and the bylaws and verifies the observance of the best administration principles, the adequacy and reliability of corporate structures, internal audit procedures and accounting system, and the adequacy of instructions given by the Company to its subsidiaries. The Board of Statutory Auditors must receive timely disclosures, at least on a quarterly basis, from the Board of Directors about the company business and significant transactions performed by the company and its subsidiaries, including potential conflict of interests issues. Auditors must inform the CONSOB of any irregularity they detect in the course of their duties. Statutory auditors are required to attend Shareholders' Meetings, Board of Directors meetings and Executive Committee meetings.

The Statutory Auditors are appointed by the Shareholders Meeting. The statutory auditors serve for a three-year term, may be reappointed and may be removed from their office for just cause and upon a resolution approved by the competent court. According to the law if shareholders have to elect more than three regular Statutory Auditors at least two must be elected by minority shareholders. A minimum of two statutory auditors can call Executive Committee meetings, Board of Directors' meetings and the company's shareholders meetings.In case any of the statutory auditors ceases for any reason to serve in such capacity, the older alternate auditor automatically replaces him until the next Shareholders' Meeting, at which a replacement will be appointed by the shareholders.

Pursuant to Article 17 of Telecom Italia's Bylaws, the Shareholders' Meeting appoints the Board of Statutory Auditors through the "voto di lista" system, which is described below. Telecom Italia's Board of Statutory Auditors is composed of not less than five and not more than eight regular auditors, as determined by a resolution of the shareholders meeting; two alternate auditors are also appointed. The Board of Statutory Auditors appoints among its members a Chairman. See "Item 10. Additional Information—Description of Bylaws and Capital Stock—Capital Stock—Voto di Lista". Statutory auditors cannot be members of more than five Boards of Statutory Auditors of listed companies on Italian Stock Exchange (excluding Telecom Italia and its subsidiaries).

External Auditors

The financial statements of Telecom Italia are required to be audited by an independent auditing firm whose assignment has to be ratified by the Shareholders' Meeting that approves the annual financial statements. The Shareholders' Meeting resolution authorizing such appointment must be furnished to CONSOB together with the Board of Statutory Auditors' opinion on the appointment. Suchappointment is for three years and the Shareholders' Meeting may not appoint the same external auditors for more than three consecutive three-year terms.

Italian audit principles require that, in cases of corporate groups, the audit firm of the parent company should carry out the audit of the group's most important entities in terms of the nature of operations, in such a way that it can act as main group audit firm and express a professional evaluation of the financial statements in their entirety. For this reason and to optimize and simplify audit operations, Reconta Ernst & Young ("REY") has been selected as the audit firm for the majority of Olivetti group companies.

Therefore on June 12, 2001 the Shareholders' Meeting revoked "on just grounds" the assignment previously conferred to PricewaterhouseCoopers S.p.A. ("PwC"), in view of the fact that otherwise REY could not be qualified as the main audit firm for the Olivetti group. The early revocation of the assignment of PwC was contemplated in the agreement among Telecom Italia and PwC entered into in September 1999.

Following the revocation, the Shareholders' Meeting conferred to REY an assignment for the complete accounting audit of the financial statements of Telecom Italia, the consolidated financial statements of the Group and a limited review for the half-year report in individual and consolidated form for the 3-year period 2001, 2002 and 2003.

Biographical Data

The following are the selected biographical data of the Directors and the Executive Officers.

Directors

Marco Tronchetti Provera: Marco Tronchetti Provera was born in Milan, on January 18, 1948. Mr. Tronchetti Provera has been Telecom Italia Chairman since September 27, 2001. Mr. Tronchetti is also Chairman and CEO of Pirelli S.p.A., Chairman of Pirelli & C, of Pirelli & C Real Estate and of Olimpia S.p.A., and Vice-Chairman and CEO of Olivetti S.p.A.. Mr. Tronchetti Provera began his career in 1973 working in the family maritime transport business and establishing a financial holding company. In 1986 he joined the Pirelli Group as a managing partner of Pirelli & C. In 1988 he was appointed CEO and General Manager of the Société Internationale Pirelli S.A., Basle, a position he held until 1992. He is also Chairman of CAMFIN S.p.A., Vice Chairman of Confindustria, Director of Luigi Bocconi University, Chairman of the Council for Relations between Italy and the United States, member of the European Round Table of Industrialists, of Gruppo Italiano Trilateral Commission, International Advisory Board of Allianz, International Council of J.P. Morgan and of New York Stock Exchange European Advisory Committee.

Gilberto Benetton: Gilberto Benetton was born in Treviso, on June 19, 1941. Mr. Bennetton has been Telecom Italia Deputy Chairman since September 27, 2001. Mr. Benetton is also Vice Chairman of Olivetti and Olimpia S.p.A.. He began his activity in 1965 with his brothers Giuliana, Luciano and Carlo; Bennetton Group is active in 120 countries in the world. Chairman of Edizione Holding, Autogrill S.p.A., Benfin S.p.A., CFI S.p.A., Edizione Property S.p.A., Edizione Alberghi S.p.A., Ragione s.a.p.a. of G. Benetton & C., Verde Sport S.p.A., Vice Chairman of Fondazione Benetton, CEO of Regia S.r.l. and Immobiliare Marca S.r.l., Director of Benetton Group S.p.A., Area Nord Concessionaria di Pubblicità, Banca Antoniana Popolare Veneta, Impresa Tipografica Veneta, Interbanca S.p.A., Schemaventotto S.p.A., Sep S.p.A., Società Finanziaria Editrice San Marco, HMS Host Corp., Lloyd Adriatico S.p.A., Autostrade S.p.A., Beni Stabili S.p.A. and Autospistas C.E.S.A. He is also Chairman of the Asolo Golf Club (sport association), the Asolo Golf Club S.r.l. and Asolo Golf Investimenti S.p.A..

Enrico Bondi: Enrico Bondi was born in Arezzo, on October 5, 1934. Mr. Bondi has been Director and Chief Executive Officer of Telecom Italia since July 31, 2001 and CEO of Olivetti. Since August 1, 2001 he also served as Chairman of Telecom Italia Mobile S.p.A., since October 12, 2001 he took over as Chairman of Telespazio and since December 2001 also of Seat Pagine Gialle. Since April 8, 2002 he is Director of Olivetti Tecnost. Mr. Bondi began his career in 1957 at Montedison, working for the Resins Research Institute in Castellanza as Head of the Agriculture Products Division Fertilizer Research Center at Porto Marghera, and subsequently as Head of Product and Process Improvement. In 1973, he moved to the Vernici Italiane company (IVI) to become Head of Research and Development. In 1975, he was appointed Head of Research and Development at the SNIA Chemicals Division. In 1980, he took over management of the Chemicals Division, becoming CEO of subsidiary companies in the sector, including Caffaro and Tecnopolimeri. In 1986, he took over responsibility for the SNIA Defense and Space Division. In 1990, he joined Fiat as Head of the Defense and Space Division, working under the Industrial Components arm of the company. In 1991, he was appointed CEO of Gilardini S.p.A., the company in charge of

Group operations in the industry. In 1993, Mr. Bondi returned to the Compart Montedison Group as CEO of Montedison S.p.A.. The positions he held at the Group include: Chairman of Edison S.p.A.;CEO of Ferruzzi Finanziaria (later Compart S.p.A.) and Deputy Chairman of Fondiaria Assicurazioni S.p.A.. He was also a Board Member of Beghin-Say S.A., Cerestar S.A., Cereol S.A. and Provimi S.A., and Chairman of the Montedison Community and Innovation Foundation, and Chairman of Fondazione Montedison Comunita' Innovazione.

Carlo Orazio Buora: Carlo Buora was born in Milan, on May 26, 1946. Mr. Buora has been Chief Executive Officer of Telecom Italia since November 7, 2001, and currently is Deputy Chairman of TIM S.p.A. and Olimpia S.p.A. He is also CEO and General Director of Pirelli S.p.A. where he was first Executive Officer of Finance and Administrative and CEO of Olivetti. Mr. Buora began his career in 1972 in Banca Nazionale del Lavoro Group, then in 1979 he went to Merloni Group where he became Chief of the Finance and Administration department. In 1982 he went to Snia BDP/FIAT Group as Finance Executive Officer and Vice General Manager of Telettra S.p.A.. In 1989 he also became General Director of Benetton Group. Mr. Buora is also General Partner of Pirelli & C, Director of Pirelli & C Real Estate, of Olivetti Tecnost, of HDP S.p.A., F.C. Internazionale S.p.A. and Mediobanca.

Umberto Colombo: Umberto Colombo was born in Livorno, on December 20, 1927. He is Director of Impregilo S.p.A.. Mr. Colombo has been Director of Telecom Italia since November 7, 2001. Mr. Colombo is also Chairman of Novamont S.p.A., Alcantara S.p.A., and Kemyx S.p.A., Director of Eni S.p.A. (Chairman in 1982-83), ACEA S.p.A., Snia S.p.A., UTET S.p.A., FB Ambiente S.p.A., SAES Getters S.p.A. and of Energy Conversion Devices. Mr. Colombo has been Chairman of ENEA (1983-93) and Minister for "University and Scientific and Technologic Research (1993-94). Member of the Executive Committee of the Club of Rome, Honorary Trustee of the Aspen Institute of Humanistic Studies (United States), Member of China Council for International Cooperation on Environment and Development, of Lincei Academy, of XL Academy, European Academy, European Academy for Science, Arts and Letter, Academies of Engineering of Sweden, of Switzerland, United States, United Kingdom, Japan, American Academy of Arts and Sciences, Third World Academy of Sciences and New York Academy of Sciences. Author of several publications. Received "honoris causa" a PHD degree from Madras University and Mendeleyev University (Moscow) in engineering and a chemical engineering degree from Genoa University.

Francesco Denozza: Francesco Denozza was born in Turin, on October 5, 1946. Mr. Denozza has been Director of Telecom Italia since November 7, 2001. Mr. Denozza is also Professor of Commercial Law at University of Milan School of Law. As an expert of corporate and antitrust law, he has advised Telecom Italia and TIM in dealing with the National Regulatory Agency and with the Antitrust Authority. Mr Denozza is the author of several publications.

Luigi Fausti: Luigi Fausti was born in Ancona, on March 9, 1929. Mr. Fausti has been Director of Telecom Italia since November 7, 2001. He is also Director of MONRIF S.p.A.. Mr. Fausti began his career in 1947 in Banca Commerciale Italiana where he was Executive Officer and General Director of many branches and in 1990 he became CEO of the Bank, in 1994 Vice-Chairman and CEO, in 1997 Chairman and in 1999 Honorary Chairman. Received "honoris causa" an economics degree from Naples University.

Guido Ferrarini: Guido A. Ferrarini was born in Genoa on August 8, 1950. Mr. Ferrarini has been Director of Telecom Italia since June 12, 2001. Mr. Ferrarini is also Director of Erg S.p.A., of Grandi Navi Veloci S.p.A. and of European Corporate Governance Institute Bruxelles. He is professor of Financial Markets Law at the University of Genova School of Law, Director of Center of Law and Finance, legal expert and lawyer, Member of Scientific Committee of CONSOB, Member of Board of Trustees IASC Foundation of London, Advisor of the Corporate Governance Committee of Borsa Italiana S.p.A., Co-director of Rivista delle Societá Giuffrè, Honorary professor of University College School of Law, London. Author of several publications.

Paolo Maria Grandi: Paolo Maria Grandi was born in Milan, on November 7, 1954. Mr. Grandi has been Director of Telecom Italia since November 7, 2001. Mr. Grandi began his career in 1979 in Credito Italiano and in 1982 went to Mediocredito Lombardo where he was responsible for the General Director offices. Mr. Grandi is also General Director of IntesaBci and head of Private Equity Fund, Director of Atos S.P.A., Car World Italia S.p.A., DE-TA S.p.A., ECO S.p.A., Euromilano S.r.L., of Eutron S.p.A., of Idra Partecipazioni, Idra Presse S.p.A., Intesa E-LAB, Musicland S.p.A., Reno De Medici S.p.A., of Termomeccanica S.p.A. and UTET S.p.A.

Natalino Irti: Natalino Irti was born in Avezzano, on April 5, 1936. Mr. Irti has been Director of Telecom Italia since November 7, 2001. Mr. Irti is also Vice-Chairman of Assonime, professor of Civil Law of University of Rome "La Sapienza" Law School, Member of Lincei Academy, Director of legal reviews and publications. Author of several publications.

Gianni Mion: Gianni Mion was born in Vó, a town near Padoa, on September 6, 1943. Mr. Mion has been Director of Telecom Italia since November 7, 2001 and he is Director of TIM S.p.A., Seat Pagine Gialle S.p.A., Olivetti S.p.A. and Olimpia. Mr. Mion is also CEO of Edizione Holding S.p.A., Schemaventotto S.p.A., Chairman of Alfa S.p.A., Edizione Realty Corp., Director of Benetton Group S.p.A., Autogrill S.p.A., Edizione Property, 21 Investimenti, Autostrade S.p.A., Sagat S.p.A., Interbanca S.p.A., Banca Antoniana Popolare Veneta, Alpi Eagles S.p.A., Assonime, Aiscat, Edizione Finance International S.A., Edizione Participations S.A., Edizione Alberghi, Grandi Stazioni S.p.A., Host Marriot Services Corporation, Eurostazioni S.p.A., 21 Partners Soc. Di Gestione del Risparmio S.p.A., 21 Network S.p.A., Verde Sport S.p.A. and Volley treviso S.p.A. He is also General Partner of Schematrentadue S.r.l.

Massimo Moratti: was born in Boscochiesanuova, a town near Verona, on May 16, 1945. Mr. Moratti has been Director of Telecom Italia since November 7, 2001. Mr. Moratti is also General Partner of Angelo Moratti – di Gianmarco e Massimo Moratti & C. S.a.p.a., CEO and Director of Saras S.p.A. Raffinerie Sarde, Chairman of F.C. Internazionale Milano S.p.A., of Sarint S.A., Director of Interbanca S.p.A., and of Pirelli S.p.A.

Carlo Alessandro Puri Negri: Carlo Alessandro Puri Negri was born in Genoa, on July 11, 1952. Mr. Puri Negri has been Director of Telecom Italia since November 7, 2001. Mr. Puri Negri is also Chairman of Aon Italia S.p.A., Vice Chairman and CEO of Pirelli & C. Real Estate S.p.A., Vice Chairman of CAMFIN S.p.A., Pirelli & C. Ambiente S.p.A., Director of Pirelli S.p.A., Olimpia S.p.A., Olivetti S.p.A., General Partner of Pirelli & C. S.p.A., General Director of Pirelli & C. S.p.A., Representative of the Labour Unions of Pirelli & C. S.p.A.

Pier Francesco Saviotti: Pier Francesco Saviotti was born in Alessandria, on June 16, 1942. Mr. Saviotti has been Director of Telecom Italia since November 7, 2001. Mr. Saviotti began his career in Banca Commerciale Italiana where he became Executive Officer and General Manager of many branches and in 1997 became General Director and in 1998 CEO and Director of the Bank. Mr. Saviotti is also Director of Stefanel S.p.A., Profit- Progetti Finanziari Televisivi S.p.A., TOD' S S.p.A., Danieli S.p.A., and of Linificio and Canapificio Nazionale S.p.A.

Roberto Ulissi: Mr. Ulissi was born in Rome on August 20, 1962. Mr. Ulissi has been Director of Telecom Italia since June 12, 2001. Mr. Ulissi is General Manager, Head of the Directorate IV of the Department of the Treasury of the Ministry of the Economy and Finance (Responsible for Banking Financial Markets and Legal Affairs) and Contract professor of Banking Law at the faculty of economics University of Cassino, Director of F.S. S.p.A., of MEFOP S.p.A. and alternate member of the Board of Auditors of ENEL S.p.A. Mr. Ulissi is and has been a member of several other committees and Board of Directors. He has published studies related to corporate and banking law. He is and has been a member of several commissions and boards involved in corporate and banking law and financial markets both at national and EU level.

Executive Officers

For the biographical data of Mr. Bondi and Mr. Buora see above under "Directors".

Arrigo Andreoni: Mr. Andreoni was born in Casorate Primo, near Pavia, Italy, on February 5, 1944. On January 15, 2002, Mr. Andreoni was appointed Head of Information Technology of Group in Telecom Italia. Since 21 November 2001 he is Chairman and CEO of I.T. Telecom. Mr. Andreoni began his career in 1969 at the Montedison Group, where he worked until 1993 in a number of positions at different group companies. Until 1972, he worked at Montedison´s Information Systems unit. In 1973, he transferred to software house Datamont, where he remained until 1981, gaining a number of promotions in his specific field, particularly industrial automation and technical applications. From 1981 to 1983, he worked at the Group´s Tecnimont engineering company as EDP manager, before being appointed Director of Information Technology Europe at Himont, a joint venture between Montedison and Hercules. Mr. Andreoni joined the Pirelli Group in 1993 as IT Coordinator for the tires business. In 1994, he was appointed Manager of Information Technology Worldwide. From 1994, he served as General

Manager of Pirelli Informatica, of which he became CEO in 2001, a position he held until he joined the Telecom Italia Group, where from 1 October 2001 to 14 January 2002 he was Head of I.S. and Technology. Mr. Andreoni is currently a member of the Board of Directors of the following affiliates of Telecom Italia S.p.A. : Chairman of NetIkos S.p.A., Netsiel S.p.A., Saritel S.p.A. and Telesoft S.p.A. and Director of Finsiel S.p.A., Scuola G. Reiss Romoli S.p.A., Sogei S.p.A., Telecom Italia Lab S.p.A. and Webegg S.p.A.

Alberto Borgia: Mr. Borgia was born in Florence, Italy, on August 30, 1952. On October 1, 2001 he joined the Telecom Italia Group as Head of the Investors Relations Department. Mr. Borgia began his career in the commercial department of the Centro Factoring (a financial institution of the Italian Savings Banks) in 1978. In 1979 he received a degree in Banking Management at SDA – Luigi Bocconi University. In the same year he became Head of the Milan commercial office. In 1982 he moved to Fiscambi, a holding company of the Toro Assicurazioni group, as Head of the Factoring department. In 1985 he joined Pirelli spa as Head of the Italian corporate finance department. In 1988, he was appointed as Head of the South American corporate finance activities. In 1992 he became Head of the subsidiaries' corporate finance activities. From 1992 until 1995 he was involved in the Pirelli Group turn around. In 1996 he was appointed Head of Pirelli Investors Relations department.

Gustavo Emanuele Bracco: Mr. Bracco was born in Turin, Italy, on May 18, 1948. On October 1, 2001, he became Head of Telecom Italia Group Human Resources. Mr. Bracco began his career at Fiat in 1972, working for the Trade Union Relations Central Management. In 1976, he was appointed Personnel Manager at the Mirafiori factory. In 1977, he transferred to Toro Assicurazioni as Head of Industrial Relations and Labour Disputes, under the aegis of Central Personnel Management. He joined the Turin Industrial Union in 1979, where he worked until 1982, initially at the Research Office before moving to the Trade Union Service, where he rose through the ranks to the position of Head. Between 1983 and 1987, he worked at Cinzano, Saiag and Carello, with responsibility for Personnel and External Relations. In 1988, he returned to the Fiat Group as Head of Personnel and Organization at the Engine Control Division. He took on the same role at CEAC in 1991 and at Fidis in 1994. He was appointed Head of Group Trade Union Relations in 1996. In 1998, Mr. Bracco went to work in London for New Holland as Head of Personnel and Organization, a position he subsequently filled in Chicago for Case-New Holland. He joined Pirelli in December 2000 as Group Head of Human Resources.

Francesco Saverio Bruno: Mr. Bruno was born in Naples on June 9th, 1955. Chief of International Subsidiaries in Telecom Italia since May 2002. He began his career in 1979 at Sirti in the technical/sales division. In 1982 he joined the Telecom Italia Group, first in STET – Strategic Planning and Development Department, where he was involved in the assessment of international partnership agreements, then in different companies of the Group (STET S.p.A., STET International S.p.A., and Telecom Italia S.p.A.), where with increasing responsiblities he was in charge of M&A activities related to specific acquisition initiatives in the telcommunications sector (wireline, mobile, data, Internet). In December 2001 he appointed Head of Telecom Italia Group International Operations department, where he manages TI's international wireline/wireless operations in Latin America and Europe.

He is a member of the Board of Directors of Telecom Italia International, 9Telecom (France), Etecsa (Cuba), Telekom Austria and Telekom Serbia.

Andrea Camanzi: Mr. Camanzi was born in Alfonsine, near Ravenna in Italy, on February 2, 1949. He graduated in Economics at the Bologna University in July 1999. He is the Senior Vice President of Public and Regulatory Affairs at Telecom Italia. Prior to joining Telecom Italia, from 1996 to 1999 he held the position of Senior Vice President of Legal, Public and Regulatory Affairs at Olivetti. From 1993 to 1996 he worked as Vice President for European Affairs at Olivetti based in Brussels. Between 1989 and 1993, he worked as Senior Vice President for Eastern and Central Europe at Olivetti.

Aldo Cappuccio: Mr. Cappuccio was born in Trieste, Italy on April 26, 1949. Mr. Cappuccio has been Head of Telecom Italia Corporate and Legal Affairs since March 12, 2002. Mr. Cappuccio began his career in 1976 and worked as a freelance civil lawyer for ten years. In 1986 he joined Assicurazioni Generali, where he worked until 2001 in positions of increasing responsibility, rising from Deputy Director in Charge of Legal Consulting to Central Director of Group Legal Affairs, with supervision over the Privacy Service. Mr. Cappuccio is also member of the Board of Directors of Seat Pagine Gialle.

Oscar Cristianci: Mr. Cristianci was born in Buenos Aires, Argentina on September 27, 1942. Mr. Cristianci has been CEO Telecom Italia Latin America Operations since February 2002. He began his career in 1968 at the Pirelli Argentina Group as Internal Auditor. Over the next 33 years he was promoted as follows: in 1974 he became Director Administration Corporate, in 1980 Director of A&Finance Pirelli Neumaticos, in 1985 CEO in 1993 CEO Pirelli Pneus Brasil in 1994 CEO Pirelli Pneus South America, in 1997 Vice President Pirelli Pneumatici S.p.A., in 2001 CEO Pirelli Cables & Energy S.p.A., in 2002 moved from Pirelli Cables & Energy S.p.A. to Telecom Italia Group.

Paolo Dal Pino: Mr. Dal Pino was born in Milan, Italy, on June 26, 1962. Mr. Dal Pino became CEO of Seat PG in July 2001. Since October 1, 2001 he has been in charge of the Telecom Italia Group Internet & Media Business Unit. He began his career in 1986 at the Fininvest Group as assistant to the Fininvest S.p.A. Planning and Control Manager. He moved in 1987 to the Mondadori S.p.A Group to take up the same post. In 1988, he was promoted to Administration, Finance and Control Manager at the Verkerke Group, headquartered in Holland, where he worked until 1990. In 1990 he joined the Espresso Group, where he was promoted through the ranks until he left the company in 2001. In 1990, he worked as Controller for "Editoriale La Repubblica" and in 1995, he became Administration, Finance and Control Manager; he was Managing Director and founder of Kataweb SpA, the Group Internet business holding company, and General Manager of the "Divisione Repubblica", as well as a member of the Board. He has sat on the board of many Espresso Group companies, including Manzoni and Finegil. In addition, he was a member of the ANSA Executive Committee. Mr. Dal Pino joined the Telecom Italia Group as CEO of Seat Pagine Gialle in July 2001. He is currently an Alumni member of the Council for US/Italy Relations, as well as a member of the Bocconi University Advisor Program.

Marco De Benedetti: Marco De Benedetti was born in Turin on September 9, 1962. On July 2, 1999 he was appointed TIM Chief Executive Officer. Mr. De Benedetti began his career with the marketing department of Procter & Gamble. From 1987 to 1989, he worked in Merger and Acquisitions for Wasserstein, Perella & Co, a New York merchant bank. He joined Olivetti in 1990 as assistant to Chief Executive Officer of Olivetti System & Networks. He was later promoted to Marketing and Services Manager. In December 1992, he was appointed General Manager of Olivetti Portugal. In September 1994, he became Chief Executive Officer of Olivetti Telemedia, subsequently also taking on the chairman's role. In October 1996, he was named Chairman of Infostrada. In 1997, he was appointed company Chief Executive Officer. Since March 1998 he has served as Olivetti Group Central Manager for Telecommunications Strategies. Mr. De Benedetti is also Chairman of TIM Brasil S.A., Deputy Chairman of IS-TIM Telecomunikasyon Hismetleri S.A., Director of TIM International N.V., IN.TEL.AUDIT Società Consortile di Revisione Interna Gruppo Telecom Italia a.r.l. AUNA S.A. and also director of Cofide S.p.A. and of Virata Inc.

Francesca Di Carlo: Ms. Di Carlo was born in Rome, Italy, on October 18, 1963. Ms. Di Carlo has been Head of Mergers and Acquisitions for the Telecom Italia Group since November 2001. Ms. Di Carlo began her career in 1987 with the SG Warburg Group (now UBS Warburg) for whom she worked in London and Milan until 1993, specializing predominantly in mergers and acquisitions regarding Italian companies and international groups. In 1994, she joined the Telecom Italia Group as Head of Investor Relations for Telecom Italia and TIM. In 1998, she took charge of Financial Planning, and in 1999 became Head of Acquisitions and Disposals, a position she held until this latest appointment. Ms. Di Carlo is currently a Board member of Italtel S.p.A., Italtel Holding S.p.A., Consodata S.A., 9Telecom Reseau S.A., Stream S.p.A., Telimm S.p.A., Telecom Italia International, Webegg S.p.A..

Armando Focaroli: Mr. Focaroli was born in Milan, Italy, on May 20, 1945. Mr. Focaroli has been Head of Telecom Italia Group Internal Auditing since 1 October 2001. He began his career in 1970 at Price Waterhouse (now PricewaterhouseCoopers), where he worked until 1977. In 1977, he joined Montedison, where he was in charge of Auditing Programs and Models until 1978. In 1979, he took over responsibility for Corporate Auditing. Between 1980 and 1987, he worked at Peat Marwick & Mitchell (now KPMG). In 1987, he returned to Montedison as Head of Administrative Systems and Procedures, a position he held until 1989, when he joined the Pirelli Group as Head of Auditing. He worked at Pirelli until his most recent appointment.

Luciano Gallo Modena: Luciano Gallo Modena was born in San Damiano D'Asti, Italy, on September 19, 1948. Mr. Modena was appointed Head of Telecom Italia Group Security in October 2001. He began his career in

1969 as an Officer in the "Carabinieri Army" in the departments of "Contrasto Criminalità Comune" and "Antiterrorismo", in 1980 he was responsible of one of the security deparments of Fiat Auto, in 1987 he became Security Director of the Alfa Romeo Group, in 1991 he was responsible of the Security of Group "BPD Difesa e Spazio", in 1994 he became Director of Security, General Services and Purchasing of Ferruzzi Montedison Group and CEO of Trantor, a company of the same group.

Andrea Granelli: Andrea Granelli was born in Bergamo, Italy, on November 13, 1960. Since March 21, 2002 he has been Head of Venture Capital of the Telecom Italia Group and, since February 2001, he has managed Telecom Italia Lab, of which he was appointed CEO in January 2001. Mr. Granelli's early career included, in 1986, a spell as head of office automation at CESI (Centro Elettrotecnico Sperimentale, ENEL). In 1987 he took over information technology planning and control at Montedison Group company Iniziativa ME.T.A.'s Strategy Office. From 1988 to 1989 Mr. Granelli worked at Fimedit (an Iniziativa ME.T.A./Ferruzzi Group finance and banking sector holding company), where he managed the sales network IT system. Between 1989 and 1995 he worked at McKinsey & Company as Senior Engagement Manager. In 1995 he oversaw all Business Process Reengineering operations at the company's Italian office. He began working for Vieo On Line in 1995. In 1996 he was responsible for all company operations, including the company's acquisition by Telecom Italia. In 1996 when TIN (Telecom Italia Net) was created through the merger of Telecom On Line and Vido On Line, Mr. Granelli was appointed sales director at the new company. In 1997 he became head of the "Mass Market Interactive Services" Business Unit, responsible for TIN commercialization. In May 1999 he became head of Telecom Italia Internet Management, and was subsequently named Tin.it CEO. From April 2000 to February 2001 he ran the Telecom Italia Group's Venture Capital and Innovation Business Unit, which subsequently became Telecom Italia Lab.

Enrico Parazzini: Mr. Parazzini was born in Milan, Italy, on March 18, 1944. He became Head of Telecom Italia Group Finance, Administration and Control on October 1, 2001. Mr. Parazzini began his career in 1968 as a Junior Auditor at Arthur Andersen. In 1969, he was hired by the Finance Department at General Electric. In 1970, he joined Honeywell Information Systems Italia. Over the next 20 years he was promoted through the company, holding the positions of Financial Planning Manager from 1975 to 1980, Administration and Control Manager from 1981 to 1986, and Chief Financial Officer from 1987 to 1990. In 1991, after Honeywell sold its business to the Bull Group, Mr. Parazzini was appointed General Manager of Administration, Control, IT Systems and Logistics. He joined Pirelli as Group Controller in May 1992. He took active part in the process of group restructuring, with special reference to reform of the planning and control system. Between 1996 and 1999, he was Head of Administration, Group Acquisitions and Risk Management. He was appointed Chief Financial Officer of the Cables and Systems division in 2000. Mr. Parazzini is currently a Board member of IT Telecom, Seat PG, Finsiel, IMMSI, Italtel, Italtel Holding, TI Lab, and Chairman of Telecom Italia International. Since 1994 he has worked as a visiting lecturer on the Multinational Group Planning and Control Course at the "Luigi Bocconi" University of Milan.

Riccardo Perissich: Mr. Perissich was born in Milan, Italy, on January 24, 1942. Mr. Perissich took over responsibility for Telecom Italia Group Public and Economic Affairs on October 1, 2001. After gaining initial job experience at Italconsult S.p.A between 1962 and 1964, in 1966 he took over responsibility for European community studies at the International Affairs Institute of Rome, of which he was later became Deputy Director. In 1970 Mr. Perissich went to work for the European Community Commission. During his employment there, until 1988, he served as Cabinet Chief to four Commission Members. In 1988 he was appointed Deputy Director-General of the Internal Market and Industrial Affairs DG. In 1990, he became Director General of the Industry DG, a position he held until he moved to Pirelli S.p.A. in 1994. From 1994, he worked as Public and Economic Affairs Manager for Pirelli S.p.A., and sat on the company´s Board of Directors. He is a director of Tim. Mr. Perissich is currently Deputy Chairman of Assolombarda, UIR (Unione Industriali di Roma) and a member of the Assonime Chairman´s Committee. He is also a Board member of the European Oncology Institute and of Enciclopedia Treccani, a Director and Executive Committee Member of ISPI, a member of the International Institute for Strategic Studies (London), the International Affairs Institute (Rome) and the Aspen Institute of Italy (Rome).

Salvatore Pinto: Mr. Pinto was born at Torre Annunziata, near Naples, Italy, on November 27, 1957. Mr. Pinto became CEO of Telespazio in May 2001. Since October 1, 2001, he has been in charge of the Telecom Italia Group Telespazio Business Unit. He began his career in 1983 with the STET Group, where he worked as a

CAE/CAD Project Leader in Milan for the Italtel/GTE/Telettra Consortium. In 1987, he moved to Italcable, where he took over responsibility for telecommunications software. It was in 1987 that he joined Olivetti. Until 1992 he held a range of positions at the company. Between 1992 and 1993, he was Country Sales Manager for Tandem Computers of Milan. He joined Pirelli in 1993 as Sales Manager Italy, before going on to become OEM Worldwide Sales Manager. He returned to Tandem Computers in 1994 as CEO. During this time he was a member of the task force working on the Compaq sale, as well as serving as CEO of Twinsoft, a joint venture between Tandem and the Marben Group. In 1996 he was appointed Olivetti-Olsy Area Manager for Italy, North Africa and the Middle East, and took a seat on the Board of Olivetti Ricerca. In March 1998, he was named CEO of Olivetti-Wang Global. He became CEO of the IPM Group in January 1999. The many positions Mr. Pinto has held include serving as a member of the Anasin Management Committee. He is Vice President of Esoa, the association of European satellite operators.

Gian Carlo Rocco di Torrepadula: Mr. Rocco di Torrepadula was born in Rome, Italy, on January 17, 1943. Appointed head of Telecom Italia Group Communication & Image in October 2001. He began his career in 1968 at the Pirelli Group where he was promoted through various positions in the areas of Licensing, Commercial Services, Economic Studies Office and since 1979 Communication.

Riccardo Ruggiero: Mr. Ruggiero was born in Naples, Italy, on August 26, 1960. Since October 1, 2001 Mr. Ruggiero has been Head of the Telecom Italia Group Domestic Wireline Business Unit. On May 7, 2002 he was appointed General Manager of Telecom Italia. He began his career in 1986 as a Sales Manager at Fininvest S.p.A. Between 1988 and 1990, he worked as the Sales and Marketing Manager for AT&T Italia. He joined the Olivetti Group as assistant to the CEO in 1990. He remained with the Group until 1995, during which time he covered a number of positions. In 1992, he became Vice President International Customers and Communications Sales Development worldwide for the Oliservice Organization; in 1994, Vice President Olivetti Telemedia Sales and Marketing Development. In 1996, he was appointed CEO of Infostrada - with responsibility for Market, Infrastructure and Human Resources - before taking over the same position at Italia On Line. He continued in both posts until 2001. In July 2001, Mr. Ruggiero joined the Telecom Italia Group as Head of the Telecom France Business Unit, with the brief of managing and developing Group business on the French market through the company´s participating interests.

Salvatore Sardo: Mr. Sardo was born in Turin, Italy, on November 28, 1952. Since October 1, 2001, Mr. Sardo has served as Head of Telecom Italia Group Real Estate and General Services. He began his career in 1976 at Coopers and Lybrand. In 1981, he joined STET as Head of Control and Management for manufacturing activities. In 1991 he was promoted to Joint Central Manager, and a year later, to Central Manager of Planning and Control. Following the merger of STET and Telecom Italia in 1997, he became Telecom Italia Deputy General Manager of Administration and Control, a position he retained the following year after Telecom Italia´s post-privatization restructuring. From 1998 to June 2001, he was Chairman of Seat Pagine Gialle. In October 1999, he took over operational responsibility for Telecom Italia Group Real Estate Operations. Starting November 2000, he took over responsibility for the Real Estate and Services Business Unit. He has served as a regular auditor at Italtel, Finsiel and Telecom Italia. He has been a Director and Chairman of many companies, and qualified as an Auditor General on 21 April 1995. He is currently Chairman of the Board of EMSA S.p.A., EMSA Servizi S.p.A., where he is also CEO, Telemaco and IM.SER, and he is also CEO of IMMSI S.p.A.

Germanio Spreafico: Mr. Spreafico was born in Lecco, Italy on September 20, 1952. He was appointed Head of Telecom Italia Group Purchasing on October 1, 2001. He began his career in 1977 at the Pirelli Financial Division, where he worked for 10 years, during which time he was promoted through various positions in domestic and international finance and ultimately took charge of Italian market financial operations. Subsequent to this he moved to the Cable sector, initially as Chief Financial Officer of the Italian company, before taking on the same role for the French company. In 1997, he became Chief Financial Officer of the Group Cable Industry Holding Company, where he also took on the position of Chief Purchasing Officer. At the present time, Mr. Spreafico is Vice Chairman of Pirelli Cavi & Sistemi S.p.A, the holding company for the Pirelli Group Cable division, of which he was Head of Administration and Control and, from February 2000, Head of Purchasing.

Giuseppe Tronchetti Provera: Mr. Tronchetti Provera was born in Rome, Italy, on April 3, 1968. He has been head of the Telecom Italia Group Information Technology – Market Business Unit since January 15, 2002.

Mr. Tronchetti Provera began his career at McKinsey & Company, where for five years he worked as a Senior Management Consultant at a number of offices across Europe, working in industries such as air transport, energy, mobile telephony, steel, television media and insurance. In 1997, he founded Cam Tecnologie, of which he is CEO. The company develops technologies and products for the Energy Industry and the Environment. He is also Director of Camfin Spa. Since 1999, he has served as Vice Chairman of the Kyoto Club. He sits on the boards of Malgara Chiari & Forti S.p.A., Negroni S.p.A., and FSB S.p.A. He is currently Board member of Banksiel, Finsiel, Insiel e Sogei.

Employees

At December 31, 2001 the Group employed 109,956 persons, an increase of 2,785 employees compared to 107,171 at December 31, 2000 pro forma. The increase of 2,785 units is mainly due to the changes in the scope of consolidation (especially for the increases of 1,749 units in Internet and media and of 1,464 units in Mobile Services as well as the inclusion of the Entel Chile group which led to an increase of 4,681 employees) and a reduction of 5,460 units at Telecom Italia due to personnel turnover. The main component of the turnover refers to the termination of employment at the Telecom Italia level, partly as a result of employee cutbacks under Law No. 223/1991 following agreements with the labor unions in March and July 2000 and September 2001.

On January 1, 2000, the "*Fondo di previdenza per il personale addetto ai pubblici servizi di telefonia*" (FPT) or Telephone Employees Pension Fund was abolished pursuant to the provisions of art. 41 of Law No. 488 of December 23, 1999 (the 2000 Finance Bill). From that date, those holding positions in this fund will be registered in the obligatory general insurance fund, with separate accounting in the "Employees Pension Fund", and the rules of the abolished fund will continue to be applied. For the additional financial requirements necessary pursuant to specific FPT rules, an extraordinary contribution to INPS is required for the three years 2000-2002, amounting to approximately €77.5 million for each year to be charged to the companies which have employees registered in the abolished fund. Telecom Italia Group's contribution currently is and will be charged on an accrual basis over the three year period.

Approximately 2% of the Group's employees held executive positions at December 31, 2001.

Group employees within Italy are represented by two categories of national unions, one for managerial staff and one for non-managerial staff. Employment agreements in Italy are generally collectively negotiated between the national association of telecommunications and manufacturing/installation/IT companies and the national unions. Renewals of collectively negotiated contracts are subject to certain general guidelines agreed between the Italian Government and trade unions generally including that salary increases may not exceed agreed upon inflation rates. Individual companies may enter into additional collective contracts with their employees based on, and following, the guidelines set out by the national collective agreements.

Employment contracts for managerial staff are ruled by a national collective agreement renewed in May, 2000. The compensation clauses of such agreement expired in December 2001, the remainder of the agreement will expire in December 2003.

Group personnel is covered by the general social security system for health care and pension plans on the basis of each category. Group employees may elect to be covered by additional health care and pension plans available to Telecom Italia personnel. So far approximately 65,000 Group employees (70% of the employees entitled) adhered to the pension fund for telecommunications workers ("Telemaco").

The following table represents the personnel of the Group at December 31, 2001 broken down by geographical areas and function:

	Manager	Professional	White-collar	Blue-collar	Total
Italy	2,003	4,962	75,196	8,467	90,628
Europe excluding Italy	230	1,068	5,796	716	7,810
North America	3	19	38	2	62
South America	193	924	10,250	73	11,440
Asia	1	4	11		16
Group Total	2,430	6,977	91,291	9,258	109,956

The following table represents the personnel of the Group at December 31, 2001 by Business Unit:

	Number of employees at end of period	
	2001	**2000 (pro forma)**(1)
Domestic Wireline	58,406	62,782
Mobile Services	16,721	15,257
Internet & Media	9,264	7,515
International Operations	7,307	2,572
IT Services	11,288	12,005
Satellite Services	1,196	1,206
TILAB	1,422	1,287
Sub-total	105,604	102,624
Other activities and eliminations	4,352	4,547
Consolidated Total	109,956	107,171

(1) Gives pro forma effect to the consolidation of the Nortel Inversora Group on an equity basis at year end 2000.

COMPENSATION OF DIRECTORS AND OFFICERS

The total compensation paid or still due by Telecom Italia or by any of Telecom Italia subsidiaries in 2001 to (i) the members of the Board of Directors was €20,112 thousand, of which €17,941 thousand was due to the members of the Board of Directors who resigned in 2001; (ii) the executive officers was €38,450 thousand (1), of which €30,870 thousand was paid to executive officers who are no longer employed by companies of the Group and employees who no longer qualify as executive officers but were executive officers at certain periods of 2001 (the amount of €38,450 thousand (1), includes termination payments paid to certain executive officers of the Company); and (iii) the members of the Board of Statutory Auditors was €656 thousand.

The following table lists the Directors and the Board of Statutory Auditors of Telecom Italia during 2001 and their respective compensation as of December 31, 2001. The compensation relates only to the period of 2001 in which they served as set forth below.

Board of Directors

Name	Position	Period	Compensation Base	Bonus	Other Compensation	Other Cash Compensation
				(thousands of Euro)		
Marco Tronchetti Provera	Chairman	Sept. 27, 2001 – Dec. 31, 2001	457(2)			
Gilberto Benetton	Deputy Chairman	Sept. 27, 2001 – Dec. 31, 2001	26		6(3)	
Enrico Bondi	Director and Chief Executive Officer	July 31, 2001 – Dec. 31, 2001	866(2)		69(4)	
Carlo Buora	Director and Chief Executive Officer	Sept. 27, 2001 – Dec. 31, 2001	320(2)		4(5)	
Umberto Colombo	Director	Nov. 7, 2001 – Dec. 31, 2001	26			
Francesco Denozza	Director	Nov. 7, 2001 – Dec. 31, 2001	17			
Luigi Fausti	Director	Nov. 7, 2001 – Dec. 31, 2001	26			
Guido Ferrarini	Director	June 12, 2001 – Dec. 31, 2001	83		52(6)	
Paolo Grandi	Director	Nov. 7, 2001 – Dec. 31, 2001	17(7)			
Natalino Irti	Director	Nov. 7, 2001 – Dec. 31, 2001	26			
Gianni Mion	Director	Nov. 7, 2001 – Dec. 31, 2001	17(8)		13(9)	
Massimo Moratti	Director	Nov. 7, 2001 – Dec. 31, 2001	17			
Carlo Alessandro Puri Negri	Director	Nov. 7, 2001 – Dec. 31, 2001	17			
Pier Francesco Saviotti	Director	Nov. 7, 2001 – Dec. 31, 2001	26			
Roberto Ulissi	Director	June 12, 2001 – Dec. 31, 2001	86(10)			
Board of Statutory Auditors						
Paolo GERMANI	Chairman	Jan. 1, 2001 – Dec. 31, 2001	136(10)			
Mario BOIDI	Statutory Auditor	Jan. 1, 2001 – Dec. 31, 2001	97			
Paolo GOLIA	Statutory Auditor	Jan. 1, 2001 – Dec. 31, 2001	97			

Name	Position	Period	Compensation Base	Bonus	Other Compensation	Other Cash Compensation
				(thousands of Euro)		
Fabrizio QUARTA	Statutory Auditor	Jan. 1, 2001 – Dec. 31, 2001	97			
Gianfranco ZANDA	Statutory Auditor	Jan. 1, 2001 – Dec. 31, 2001	97		132(11)	

(1) Bonus compensation represents 17% of executive officers' total compensation. Such bonus compensation is determined by the Chairman or the Chief Executive Officer respectively, for their own structure and is normally based upon group and individual performance targets, set at the beginning of each fiscal year. Group targets are usually based on economical and financial performances. Individual targets derive from functional responsibilities and particular goals set for each business unit. In 2001 Telecom Italia reserved €166,220 as supplemental retirement benefits for its executive officers.

(2) The amount includes the remuneration ex art. 2389, section 2, of the Italian Civil Code.

(3) Remuneration as director of SEAT.

(4) Remuneration as Chairman of SEAT, TIM and Telespazio which was paid to the Company.

(5) Remuneration as Deputy Chairman of TIM which was paid to the Company.

(6) Remuneration as director and committee member of TIM.

(7) Remuneration paid to Banca Intesa.

(8) Remuneration paid to Edizione Holding.

(9) Remuneration as director and committee member of SEAT and director of TIM which was paid to Edizione Holding.

(10) Remuneration for the post not received by the person but paid over to the Administration Fund of the entity for which he works.

(11) Remuneration for the post of chairman of the Board of Statutory Auditors of the subsidiary IT Telecom and Statutory Auditor in the subsidiaries Finsiel, IMMSI, Telespazio and TIM.

OPTIONS TO PURCHASE SECURITIES FROM REGISTRANT OR SUBSIDIARIES

Stock option plan

The extraordinary shareholders' meeting held on June 12, 2001 granted the Board of Directors, for a maximum period of five years from the date thereof, the power to further increase the Company's share capital by payment, in one or more instalments and to issue new Shares, which will rank *pari passu* for dividends, to be offered for subscription to senior managers and to other employees of Telecom Italia, its subsidiaries or controlling companies, up to a maximum of Euro 40,150,000 (which corresponds to the issuance of a maximum of 73,000,000 Shares).

On July 27, 2001 the Board of Directors approved a Stock Option Plan involving approximately 1,400 managers and professional employees employed by companies in the Group, selected on the basis of special responsibilities and/or expertise.

This initiative follows those already begun in 1999 and 2000 and described in the notes to the financial statements of those years.

The common factor to all these initiatives is the assignment of personal and non-transferable *inter vivos* rights that can be used to purchase an equal number of new Shares against payment. The 2001 plan - which does not involve employees of the TIM and SEAT groups since these companies are listed on the stock exchange and have their own Stock Option Plans - led to the assignment of 67,025,000 options to purchase Shares at the price of €10.488 (equal to the arithmetic average of the official prices of Telecom Italia Ordinary Shares on Telematico during the period June 27 to July 27, 2001). The exercise of the options, which are subdivided into two separate lots, each equal to half the options attributed, is subject to the achievement of performance targets correlated to the best average trend of Telecom Italia shares compared to that of the Dow Jones EuroStoxx TLC share index in certain periods. However, the achievement of the targets relating to the second lot means that the options in the first lot can be exercised.

The following table summarizes the key features of the Stock Option Plan in force in 2001:

	2001 Plan			2000 Plan			1999 Plan		
	Number of options	Exercise price	Market price	Number of options	Exercise price	Market price	Number of options	Exercise price	Market price
	(Euro, except number of options)								
Rights existing at 1/1/2001	-	-	-	51,430,000	13.815	11.902	11,411,500	6.791	11.902
New rights assigned during the year............	67,025,000	10.488	10.702	-	-	-	-	-	-
Rights exercised during the year............	-	-	-	-	-	-	1,496,350	6.791	11.904
Rights expired and not exercised during the year	-	-	-	-	-	-	-	-	-
Rights expired during the year due to termination of service/other reason	575,000	10.488	9.076	860,000	13.815	11.590	68,500	6.791	11.426
Rights existing at 12/31/2001..................	66,450,000	10.488	9.713	50,570,000	13.815	9.713	9,846,650	6.791	9.713
Of which exercisable at 12/31/2001..............	-	-	-	15,173,333	13.815	-	4,258,550	6.791	-

Plan	Exercise price (in Euro)	Number of rights assigned at December 31, 2001 and exercisable from				
		2001	2002	2003	Total	Maximum duration of options
1999	6.791	4,258,550	5,588,100	-	9,846,650	3 years beginning from each year
2000	13.815	15,173,333	15,173,333	20,223,334	50,570,000	5 years beginning from each year
2001	10.488	-	33,225,000	33,225,000	66,450,000	5 years beginning from each year

As far as the 2000 plan is concerned, because the exercise price was significantly higher than the current price of the shares, on March 26, 2002 the Board of Directors approved a new stock option plan with an exercise price of €9.665 (equal to the arithmetic average of the official prices of the Shares on Telematico during the period February 26 to March 26, 2002), reserved to executives who have been assigned options referring to the 2000 plan and were still working for the Company, subject to their voluntary relinquishment of the 2000 plan, with the aim of recapturing the goals of management incentives and retention, which are fundamental to stock option plans.

Item 7. MAJOR SHAREHOLDERS AND RELATED-PARTY TRANSACTIONS

MAJOR SHAREHOLDERS

As a result of the Olivetti Offer and subsequent market purchases, Olivetti controls, as of June 10, 2002, 54.95% of the Shares of Telecom Italia. In 2001 Olimpia became the largest shareholder in Olivetti, (see "Item 4 Information on the Company — Business — Significant Developments during 2001 — The Pirelli-Olimpia Transaction") with a stake of 28.7%.

There are no arrangements known to the Company the operation of which may result in a change in control of the Company.

The following table shows certain information, as of June 10 , 2002, about the ownership of the Company's Shares and Savings Shares by the Company's directors and executive officers as a group and by the members of the Board of Statutory Auditors as a group.

Title of Class	Owner	Number owned	% of class
Share	Directors and executive officers as a group (15 Directors and 21 Executive Officers)	18,656	0.00035
	Board of Statutory Auditors as a group (5 persons)	-	-
Savings Shares	Directors and executive officers as a group (15 Directors and 21 Executive Offers)	1,000	0.00005
	Board of Statutory Auditors as a group (5 persons)	-	-

As of December 31, 2001 the members of the Board of Directors who resigned in 2001 held 283,500 Shares, 514,625 TIM shares and 3,683,940 SEAT shares. The following table shows the ownership of Shares, Savings Shares, TIM shares and SEAT shares by the members of the Board of Directors as of December 31, 2001. As of December 31, 2001 the members of the board of statutory auditors did not hold any Shares, Saving Shares, TIM shares or SEAT shares.

Name	Company	Number of shares held at end of prior year	Number of shares purchased	Number of shares sold	Number of shares held at the end of 2001
Board of Directors					
Marco Tronchetti Provera					
Gilberto Benetton					
Enrico Bondi					
Carlo Buora					
Umberto Colombo					
Francesco Denozza					
Luigi Fausti	TIM ordinary shares	50,000(1)			50,000
Guido Ferrarini					
Paolo Grandi					
Natalino Irti	TIM ordinary shares	11,000(1)			11,000
Gianni Mion					
Massimo Moratti					
Carlo Alessandro Puri Negri					
Pier Francesco Saviotti	TIM ordinary shares	10,000(1)			10,000
Roberto Ulissi					

(1) Shares held from November 7, 2001, date of appointment to the Board of Directors.

Continuing Relationship with the Treasury

Prior to the privatization of Telecom Italia in November 1997 (the "Privatization"), the Treasury owned 44.71% of the outstanding Shares and 0.62% of the outstanding Savings Shares. After completion of the Privatization, the Treasury continued to own 5.17% of the outstanding Shares and 0.62% of the outstanding Savings Shares of Telecom Italia. The Treasury has stated its intention to sell its Telecom Italia Shares. As of June 20, 2002, the Treasury retains a 3.46% of the outstanding Shares of Telecom Italia.

The Treasury continues to be in a position to exert certain powers with respect to Telecom Italia through the exercise of the special powers included in Telecom Italia's Bylaws. See "Item 10. Additional Information—Description of Bylaws and Capital Stock—Capital Stock—Limitations on Voting and Shareholdings—Special Powers of the State" for a description of such special powers see "Item 6. Directors, Senior Management and Employees".

Following the issuance by the EU of a directive on May 4, 1999, on February 11, 2000, the Italian Government issued a decree (the "Golden Share Decree"), on the exercise by the Italian Government of certain special powers with respect to privatized companies. Pursuant to the Golden Share Decree, the Italian Government can use its special powers to protect the vital interests of the State and respond to indispensable reasons of general interest, including public law and order, public security, public health and national defense. The Italian Government will exercise such special powers in compliance with the principles of Italian and European Community laws, and in any case in line with the objectives of the privatization process, and the protection of competition and the market and having regard for non-discrimination principles. Such powers must be suitable and proportional to achieving the indispensable objectives of general interest described above. The Golden Share Decree provides that the Italian Government may exercise its special powers to prevent acquisitions of shares of privatized companies if such acquisitions (i) are not transparent and would not ensure full disclosure with respect to controlling share ownerships of the companies whose shares are being acquired and the objectives and industrial plans proposed by the buyers of the target companies, (ii) compromise the liberalization and market competition or are not in line with the company's privatization goals, or entails situations of conflict of interests which could compromise the company's mission with respect to the objectives of public interest, (iii) entail objective risks of being affected by criminal organizations, or involve the company in unlawful activities, (iv) jeopardize conservation of the special powers of the State, or (v) represent a considerable risk of serious harm to the vital interests of the State described above, including the supply of essential raw materials and goods, the supply of essential public services and the security of related installations and networks and, further, the development of advanced technological sectors.

The aforementioned special powers granted to the Italian Government by the Company's Bylaws must be exercised according to the terms and in compliance with the principles provided for by the Golden Share Decree.

RELATED-PARTY TRANSACTIONS

The Group enters into transactions with affiliates, and various related parties. The following related party transactions relate to transactions between Telecom Italia and its subsidiaries and the Group's unconsolidated subsidiaries and affiliated companies as well as the members of the Board of Directors and the companies in which they hold corporate office or significant responsibility. Transactions between members of the Group are excluded as they are eliminated on consolidation. All such transactions are within the Group's normal operations and were conducted on an arm's length basis in accordance with specific regulatory provisions.

For purposes of comparison, the 2001 related party transactions reflected in the statement of operations are also compared to the 2000 pro forma amounts to give effect to the consolidation of the Nortel Inversora group (Nortel Inversora and the controlled Telecom Argentina group) using the equity method instead of the proportional consolidation method.

The following related party transactions are reflected in the statement of operations for the years ended December 31, 2001, 2000 and 1999:

- *Operating revenues:* comprise mainly revenues from Astrolink (€296 million in 2001), Brazil Telecom (€120 million in 2001), Nortel Inversora group (€119 million in 2001, €163 million in 2000 pro forma, €81 million in 2000 and €91 million in 1999), Teleleasing (€82 million in 2001 and €113 million in 2000), Auna group (€63 million in 2001 and €57 million in 2000), Stream (€55 million in 2001, €102 million in 2000 and €79 million in 1999), Lottomatica (€53 million in 2001, €58 million in 2000 and €44 million in 1999) and SEAT (€211 million in 2000 and €159 million in 1999). In the aggregate, operating revenues were €881 million in 2001 (€919 million in 2000 pro forma, €837 million in 2000 and €557 million in 1999).

- *Cost of materials and other external charges*: refers mainly to rent payable to IM.SER (€199 million in 2001 and €23 million in 2000) and Telemaco Immobiliare (€77 million in 2001), TLC service costs from Etec S.A. Cuba (€79 million in 2001 and €24 million in 2000) and Entel Chile group (€40 million in 2000) and cost of materials and other external charges from Siemens Informatica (€80 million in 2000 and €38 million in 1999), SEAT (€61 million in 2000 and €91 million in 1999) and Teleleasing (€59 million in 2000). In the aggregate, cost of materials and other external charges accounted for €586 million in 2001 (€377 million in 2000 and €242 million in 1999).

- *Other income, net*: relates mainly to cost recoveries for personnel on loan to some foreign unconsolidated subsidiaries and affiliated companies. In the aggregate other income, net accounted for €25 million in 2001 (€19 million in 2000 and €26 million in 1999).

- *Financial income and expense, net*: refers to accrued interest income on loans made to certain foreign unconsolidated subsidiaries and affiliated companies (€22 million in 2001), interest expense payable to Teleleasing (€30 million in 2001 and €31 million in 2000) for financial leasing transactions and dividends received from the Eutelsat satellite consortium (€64 million in 2000). In the aggregate, financial income and expense, net was negative for €8 million in 2001 (positive for €54 million in 2000 and €19 million in 1999).

The following related party transactions are reflected on the balance sheets as of December 31, 2001 and 2000:

- *Loans in long-term investments*: refers mainly to loans granted to Bouygues Décaux Télécom (BDT) (€108 million at December 2001 and €102 million at December 2000) and other foreign unconsolidated subsidiaries and affiliated companies. In the aggregate such loans were €119 million at December 2001 (€138 million at December 31, 2000).

- *Trade accounts receivables and other current assets*: comprises mainly receivables from Auna group (€90 million at December 31, 2001 and €48 million at December 31, 2000), Stream (€82 million at December 31, 2001 and €23 million at December 31, 2000), Telekom Srbija (€56 million net of provision at December 31, 2001 and €66 million at December 31, 2000), Nortel Inversora group (€21 million net of provision at December 31, 2001, €44 million at December 31, 2000 pro forma and €22 million at December 31, 2000), Teleleasing (€18 million at December 31, 2001), Golden Lines International (€25 million at December 31, 2000), IM.SER (€46 million at December 31, 2000), Consortium CSIA (€13 million at December 31, 2000) and Etec S.A. (€13 million at December 31, 2000). In the aggregate trade accounts receivables and other current assets were €430 million at December 31, 2001 (€350 million at December 31, 2000 pro forma and €328 million at December 31, 2000).

- *Trade accounts payable and other current liabilities*: pertains mainly to supplier relationships connected with investments and transactions. In particular, they comprise trade accounts payable to Italtel group (€173 million at December 31, 2001 and €277 million at December 31, 2000), Siemens Informatica (€51 million at December 31, 2001 and €38 million at December 31, 2000), Teleleasing (€42 million at December 31, 2001 and €22 million at December 31, 2000), advances from Consorzio Telcal (€85 million at December 31, 2001), Entel Chile group (€41 million at December 31, 2000), Telekom Srbija (€23 million at December 31, 2000), Golden Lines International (€17 million at December 31, 2000), Auna group (€13 million at December 31, 2000), Etec S.A. (€11 million at December 31, 2000) and Telekom Austria group (€10 million at December 31, 2000). The item also includes payables to Astrolink (€95 million at December 31, 2000) for capital contributions payable. In the aggregate trade accounts payable were €485 million at December 31, 2001 (€834 million at December 31, 2000).

- *Long-term and short-term debt*: refers mainly to payables for finance leases to Teleleasing (€522 million at December 31, 2001 and €554 million at December 31, 2000) and a payable by Softe from Olivetti Finance N.V. (€600 million at December 31, 2001), payables to IM.SER (€81 million at December 31, 2000), Webegg (€29 million at December 31, 2000) and Italtel group (€20 million at December 31, 2000). In the aggregate long-term and short-term debt were €1,170 million at December 31, 2001 (€692 million at December 31, 2000).

- *Short-term financial receivables*: refers mainly to short-term loans receivable from Stream (€122 million at December 31, 2001 and €55 million at December 31, 2000), IS Tim (€29 million at December 31, 2001), Telekom Srbija (€23 million at December 31, 2001 and €21 million at December 31, 2000) and from the affiliates of SEAT (€60 million at December 31, 2000). In the aggregate short-term financial receivables were €213 million at December 31, 2001 (€175 million at December 31, 2000).

- *Long and short-term contracts*: refers mainly to activities on behalf of Consorzio Telcal for the Telematico Calabria Plan (€110 million at December 31, 2001). In the aggregate such long and short-term contracts accounted for €116 million at December 31, 2001 (€71 million at December 31, 2000).

- *Guarantees and collateral:* include sureties given on behalf of the Auna group (€510 million at December 31, 2001), IS Tim (€228 million at December 31, 2001), Stream (€86 million at December 31, 2001), Retevision Movil (€1,658 million at December 31, 2000), Italtel group (€177 million at December 31, 2000) and the affiliates of SEAT (€162 million at December 31, 2000) as well as collateral given on behalf of IS Tim (€147 million at December 31, 2001). In the aggregate such guarantees and collateral accounted for €1,261 million at December 31, 2001 (€2,420 million at December 31, 2000).

- *Capital expenditures*: mainly consist of acquisitions telephone exchanges from the Italtel group (€567 million in 2001 and €184 million in 2000) and information and computer projects from Siemens Informatica (€31 million in 2001 and €32 million in 2000). In the aggregate investments in fixed and intangible assets accounted for €665 million in 2001 (€234 million in 2000).

SEAT

In connection with the 2000 SEAT-Tin.it transaction, Telecom Italia contributed to its ownership of the Italian White Pages to Tin.it, including the assignment of its contracts with SEAT relating to the production of and advertising in White Pages in Italy. Under the terms of the contracts, prior to the acquisition of the controlling interest in SEAT, the Group including Tin.itpaid SEAT for the production and printing of the White Pages and received advertisement royalties from SEAT. Subsequent to the acquisition of the controlling interest in SEAT, these contracts have been terminated and the revenues and expenses no longer exist. The amounts relating to these transactions are disclosed in the relevant sections above.

Parent company

Pursuant to a tender offer in 1999, Olivetti our majority shareholder gained, through its subsidiary Tecnost, a controlling interest in Telecom Italia, and as at December 31, 2001 holds approximately 55 per cent of Telecom Italia. Dividends of €891 million and €13 million were paid to Olivetti and Olivetti Finance, respectively, in 2001 (€888 million was paid to Tecnost - then merged into Olivetti - in 2000 and €396 million in 1999).

Pirelli group

Related party transactions in 2001 also include those by the Telecom Italia Group with the Pirelli group. Pirelli has a 60% interest in Olimpia, which owns approximately 28.7% of the share capital of Olivetti.

The following related party transactions are reflected in the statement of operations for the year ended December 31, 2001:

- *Operating revenues:* mainly refers to telephone services (€6.9 million).

The following related party transactions are reflected on the balance sheet as of December 31, 2001:

- *Trade accounts receivables and others*: mainly refers to the above-mentioned telephone services (€0.6 million).

- *Trade accounts payable and others*: mainly pertain to the supply contracts connected with supplier relationships (€6.4 million).

- *Capital expenditures*: mainly consist of purchases of telecommunications cables (€21.5 million).

Directors and Executive Officers

The following comments concern the relationships between Telecom Italia and companies in which the directors of Telecom Italia (who resigned in the second half of 2001) held specific positions, as well as relationships with key managers and/or directors of the Group' s companies whoresigned in the meantime:

- based on a contract signed on March 15, 2000 by Telecom Italia, Huit II, Huit (now TI Media) and its shareholders, and Lorenzo Pelliccioli, regarding the integration of Tin.it into SEAT, and futhermore, by virtue of previous agreements, Lorenzo Pelliccioli (the then CEO of SEAT who resigned in the second half of 2001) became a stockholder of Huit II in July 2000 through a capital increase of 1.05% reserved for him. Consequently, the number of SEAT shares held by Telecom Italia, indirectly through Huit, was proportionally reduced. Lorenzo Pelliccioli later sold the stake in Huit II to the parent company Huit. Telecom Italia, as a shareholder in Huit, contributed €19 million to the total benefit received by Lorenzo Pellicioli;

- in April 2001, Telecom Italia Lab (a 100%-owned subsidiary of Telecom Italia), joined with the Ramius Capital Group, an American investment management company (in which the then director, Peter Cohen, was the CEO), to set up an United States-registered venture capital fund called Saturn Venture Partners which targets investments in fixed and mobile TLC technologies and service infrastructures. The fund's participants also included the companies TIM, Olivetti and Hopa, in which the then Chairman Roberto Colaninno and the then director Emilio Gnutti were shareholders and directors;

- the law firm of Studio Bonelli, Erede, Pappalardo in which the then Deputy Chairman of Telecom Italia Mr. Sergio Erede was the senior partner, has performed professional legal services on behalf of Telecom Italia and some companies in the Group. The Group paid legal fees to this law firm totaling €16 million in 2001 (€5 million in 2000 and €0.9 million in 1999);

- in March 2001, Telecom Italia purchased a 12.3% stake in Netesi S.p.A.– with headquarters in Milan and operating in the area of on-line applications services – by subscribing to a first tranche of new shares issued for a capital increase for an investment of approximately €6.2 million. In September 2001, Telecom Italia's stake rose to 17.98% following a successive increase in share capital. Netesi's shareholders included, among others, Omniaholding (a related party of Telecom Italia, through the then Chairman Roberto Colaninno);

- in August 2001, Huit II, a subsidiary of Telecom Italia, purchased - by exchanging 186 million Seat Pagine Gialle ordinary shares - a 100% stake in ISM S.r.l. (owned by Messrs. Ainio and Gualandri, both of whom were managers and directors of companies in the Group in service at the time), a company that holds – through the subsidiary Vertico N.V. - a 33.3% stake in Matrix S.p.A.;

- furthermore, two executives of Telecom Italia (in service at the time) purchased a building each from Telecom Italia, paying the market price.

Item 8. FINANCIAL INFORMATION

Historical Financial Statements

See Items 18 and 19 for a list of financial statements and other financial information filed with this report.

LEGAL PROCEEDINGS

General

Group companies are involved in a number of legal proceedings in the ordinary course of their business; most legal proceedings are related to credit collection of unpaid customers bills. In addition, proceedings involving alleged abuses of market-dominating positions against Telecom Italia and other antitrust proceedings are pending before Italian competition and regulatory authority. Other than as described herein, neither the Company nor any of its subsidiaries is a party to any proceedings and no such proceedings are known by the Company to be contemplated by governmental authorities or third-parties, which, if adversely determined, could have a material adverse effect on the Group's consolidated financial position or results of operations.

Social Security Charges

The Company is a party, together with INPS, to a dispute, concerning the Company's calculation of the social security charges to be paid by the companies in the telecommunications sector of the Group in respect of employees of such companies. Pursuant to Law 58/1992, those Group companies are required to ensure that all personnel employed on February 20, 1992 are covered by the Italian pension fund for telecommunications employees ("FPT"), for their entire retirement benefit, including sums due in respect of prior employment in other companies. The employees involved are those employed on that date by the Company, SIP, Italcable and Telespazio, as well as the employees passed from ASST to Iritel. Law 427/1993 subsequently established that contributions to cover these benefits are to be recorded in the financial statements of the Company in the financial year they are paid over to the FPT in 15 equal annual installments in arrears.

The dispute between the Group and INPS concerns two principal issues. The first concerns whether interest on the 15 annual installments (at the rate of 5% per annum) should accrue from February 20, 1992, as INPS maintains, or from the date INPS notifies the companies involved of the total sum payable, as the Group companies maintain. The second dispute concerns the status of the Group company employees who, on February 20, 1992 had outstanding applications to INPS to join the FPT under the terms of Law 29/1979. The Group companies maintain that the payments relating to those employees should be calculated as provided under Law 29/1979, pursuant to which the applications had been made, regardless of the fact that INPS had not yet acted on those applications. Under Law 29/1979, such amounts would be calculated on the basis of the wage amount as of the date the employee made his or her application, rather than as of February 20, 1992 and would be based on an amount equal to 50% (rather than 100%) of the mathematical reserves required to back the pension involved.

To resolve these disputes, the Company and INPS have agreed to submit test cases involving a limited number of employees to the trial courts and have further stipulated that the losing party at the trial court level would be allowed only to appeal a single appeal to the *Corte di Cassazione* (Italy's highest court of appeal) for a final determination of the issues involved and that this determination would be considered as binding for all the employees employed by Group companies on February 20, 1992 and not just those involved in the test case.

Regarding the second issue of the dispute, the trial judges have now decided the merits of seven test cases; the Group has won three cases (June 23, 1995; November 23, 1998; and March 8, 1999), while INPS has won the others (July 5, 1996; June 13, 1997; and September 28, 1998). The disputing parties have appealed the decisions of the trial judges to the *Corte di Cassazione*. The *Corte di Cassazione* rejected one of the appeals on the basis that in labor disputes the intermediary step of the Court of Appeals cannot be skipped. As a consequence, according to Italian civil procedure, the trial judgment concerning the first test case won by the Group cannot be appealed, as well as the below mentioned decision of the Court of Appeals of Turin (January 27, 2000) and the one of the trial court delivered on March 8, 1999, because of the expiration of the Italian statute of limitations. Moreover, the parties have appealed the other trial judgments to the Court of Appeals. On November 22, 1999, the *Corte di Cassazione* confirmed the decision of the trial judge concerning the second test case (July 5, 1996) and on January 27, 2000, INPS won the appeal pending in the Court of Appeals of Turin against the judgment delivered on November 23, 1998.

As for the first issue of the dispute, INPS won the first test case submitted to the trial judge in Turin, whose decision was reversed by the Court of Appeals on September 4, 1997; finally, on April 5, 2000, the *Corte di Cassazione* rejected the appeal of INPS, confirming the judgment of the Court of Appeals. On the same issue the Group won two other cases both pending in the trial court in Rome (December 4, 1997; March 3, 1999); on May 5, 2000, the decision concerning the first of these cases was confirmed by the Court of Appeals and by the *Corte di Cassazione*. On April 24, 2002, the Court of Appeals confirmed the decision concerning the other case.

Pending final resolution by the *Corte di Cassazione* of the test cases, the companies of the Group have agreed to make the required annual payments requested by INPS, subject to later adjustment in the event of a final determination favorable to them, and INPS has agreed to pay the pensions of the employees involved.

While the full amount of the Group companies' exposure under Law 58/1992 can only be estimated, given the large number of employees involved, each of whose individual situations (including the impact of pension contributions made in respect of those employees during periods of employment with other companies) may vary, management estimates that the aggregate liability as of December 31, 2001 relating to such contributions for principal will range from approximately €960 million to approximately €1,284 million (€334 million of which has already been paid) net of the amount of €656 million already recorded by Iritel and presently appearing in Telecom Italia's and TIM's financial statements following the Telecom Merger.As of December 31, 2001 INPS had submitted formal requests for about 97% of the employees whose change in insurance status will result in a charge to Telecom Italia.

The remaining liability for obligations under Law No. 58/1992, to be paid in fifteen annual installments on the basis of the formal requests made by INPS on December 31, 2001 and the interpretation of said requests, amounts to €1,347 million, divided as follows:

- €910 million for the principal amount (except for the portion attributable to former Iritel employees);

- €437 million in accrued interest.

The amount referring to 2001 and charged to the statement of operations under "Other income and expense, net" amounts to €155 million, including accrued interest.

Pre-amortization interest (including that relating to the employees of the former Iritel), subsequent to the agreement between INPS and Telecom Italia, was paid by Telecom Italia (with reserve) in fifteen equal annual deferred installments, including interest at an annual rate of 5%, up to the end of 1999, for a total amount of €112 million. In compliance with the ruling of the *Corte di Cassazione*, No. 4242 of April 5, 2000, which upheld Telecom Italia's position, payment of the above-described interest and accrued interest related thereto was suspended as from June 2000 (for a residual amount of €407 million). As a result of the above decision Telecom Italia will proceed to reach an agreement with the above-named institution to work out the recovery of the sums paid by the company up to 1999, equal to €112 million plus 5% interest.

During 2001, Telecom Italia paid INPS the above-mentioned charges also on behalf of other Group companies - mainly TIM and TILAB - for those employees transferred and covered by the obligation of a uniform insurance status under Law No. 58/1992, recovering the amounts paid from these same companies.

Furthermore, in connection with law 1369/1960 INPS has claimed the payment by Telecom Italia of social charges of approximately €31 million for the failure to make such payment by two outside contractors of Telecom Italia which subsequently became insolvent. Telecom Italia claimed in court the illegitimacy of INPS requests. Telecom Italia has appealed one ruling and INPS still has time to appeal the second ruling. Telecom Italia also successfully contested in court an injunction of INPS to pay €15 million. Numerous disputes are also pending in connection with the treatment of workers formerly employed by outside contractors of Telecom Italia; the total of all such claims is, approximately, €35 million.

Galactica Dispute

At the end of May 2001 a dispute arose between Telecom Italia and the Internet Service Provider Galactica S.p.A. (currently in liquidation) for wrongful termination by Telecom Italia of an agreement concerning the testing of an Internet flat-rate access service. In this connection – after appeals were urgently presented to a civil court and to the Milan Court of Appeal under Law No. 287/1990, with one upheld and the other turned down—Galactica sued Telecom Italia for the alleged illegality of withdrawal, claiming damages and challenging Telecom Italia not to interrupt the distribution of the service. In February 2002, Galactica claimed further damages for approximately €51.7 million caused by the alleged unfair competition practices of Telecom Italia. In addition, the proceedings brought before the National Regulatory Authority concluded with no agreement having been reached.

Disputes Concerning Shareholders' Resolutions

The disputes arising from the resolution with which the Shareholders' Meeting on January 14, 2000 authorized the buy-back of Savings Shares through a tender offer and subsequent acquisitions on the stock market, concluded on January 10, 2001, are still pending at the first degree court.

In particular, certain shareholders filed a claim for damages against Olivetti, the Company, as well as the Chairman and Deputy Chairman pro tempore of the Company, for a total of €18.9 million. The claim is based on the alleged non-fulfillment of the commitments contained in the offering document relating to the takeover and exchange bid by Olivetti and Tecnost for Telecom Italia in 1999, and also for the resolutions passed by the shareholders' meeting of January 14, 2000, especially in relation to the mandate to purchase Treasury Savings Shares on the open market, as set forth by applicable laws, subsequent to the end of the period of the offer. This same resolution was contested by another shareholder who pleaded that the proposal put to the shareholders' meeting had been changed from the one deposited prior to the shareholders' meeting.

With regard to the expiry of the deadline established for launching the voluntary conversion of Savings Shares into Shares, the proceedings opposing the resolutions passed at the shareholders' meeting of May 3, 2001, which involved the authorization to establish a subsidiary for the purpose of acquiring Telecom Italia ordinary shares, through a tender offer, as well as the offer to convert savings shares against payment, has been abandoned.

Inquiry by the Attorney General's office of Turin

Telekom Srbija

In the first quarter of 2001 Italian newspaper reports alleged that improper payments were made in connection with the Company investment in Telekom Srbija. On June 9, 1997, Telecom Italia and OTE, the Greek telecommunications company, entered into a stock purchase agreement with Serbian PTT, at that time the sole shareholder of Telekom Srbija, as part of the privatization of the Serbian telecommunications sector. At that time Telecom Italia was controlled by the Italian government. Under the terms of the contract, Telecom Italia acquired a 29% interest in Telekom Srbija for approximately €457 million and OTE acquired a 20% interest for approximately €345 million.

In February 2001, the Attorney General's Office of Turin ordered the start of a preliminary investigation into the transaction. Telecom Italia immediately made all the documentation and figures relating to the above-mentioned transaction available to the judicial authorities. Under Italian law and regulations, Telecom Italia's statutory auditors and its external auditors PwC were required to investigate the matters relating to the alleged improper payments. On the basis of the tests and procedures performed, with the full cooperation of the responsible corporate officers of Telecom Italia, the audit firm and the statutory auditors stated that no facts had emerged, at the time, which could call into question the correctness of the statutory financial statements and consolidated financial statement of Telecom Italia at December 31, 1997, 1998 and 1999, or for fiscal year ended December 31, 2000. Law No. 99/02 dated May 21, 2002 established a specific Parliamentary Commission on Telekom Srbija.

SEAT

In July 2001, the Company was asked by the attorney general's office of Turin to present documentation mainly concerning the transactions for the acquisition of SEAT and the merger of Tin.it-SEAT.

The Company has provided full cooperation to the authorities conducting the investigation.

Universal service

Omnitel and Infostrada appealed to the Administrative Court, or TAR, of Lazio against the ruling by the National Regulatory Authority against Telecom Italia to cancel Resolution No. 8/00/CIR regarding the "Application of the sharing mechanism for the net cost of the universal service for 1999". See "Item 4. Information on the Company—Regulation".

Under this resolution, part of the cost was recognized as being an "unfair burden" for Telecom Italia. As a consequence of this, it was divided among Omnitel, Infostrada and TIM. Omnitel and Infostrada have not yet paid their share (totaling €9 million) to the special fund set up by the Ministry of Communications, thus preventing it from paying the whole amount owed to Telecom Italia (€27 million).

In January 2001, the TAR ruled in favor of the appeal presented by Omnitel, but only in relation to procedural issues. The judgment is still pending.

In February 2002, appeals were presented before the TAR of Lazio by Omnitel Pronto Italia and Wind to annul, after suspension, the efficacy of the resolution issued by the National Regulatory Agency with regard to the sharing of the cost of the universal service for the year 2000.

The plaintiffs contested the legality of the resolution for the lack of an inquiry and for not having had access to the documentation resulting from the consultancy commissioned by the National Regulatory Agency on the analysis of the net costs.

Omnitel also asked for the case to be referred to the Court of Justice of the European Community, for a preliminary interpretation, in order to ascertain the correct interpretation of EU directives, and, secondly, the non-application of Italian law.

SEAT – De Agostini Arbitration

De Agostini has initiated arbitration proceedings against SEAT, Matrix, Buffetti and Finanziaria Web for the alleged nonfulfillment of the framework agreement of September 20, 2000, with regard to SEAT's obligation to acquire the Finanziaria Web S.p.A. shares still held by the De Agostini Group (40% of Finanziaria Web S.p.A.'s share capital; the remaining 60% of Finanziaria Web S.p.A.'s shares are held by SEAT).

Effectively, De Agostini Group maintains that all the conditions stipulated in the contract for executing the agreement were fulfilled, whereas SEAT maintains that this is not true and that, in any case, the fact that market conditions changed rendered the acquisition excessively onerous.

The De Agostini Group is asking for specific performance of the framework agreement and that the Finanziaria Web shares should be transferred to SEAT for the amount originally agreed of €700 million, with payment beginning in June 30, 2003, as well as the payment of unspecified damages.

Infostrada/Albacom—Telecom Italia: services with access in ADSL technology and RING services

On April 27, 2001, the Italian Antitrust Authority, pursuant to a complaint made by Infostrada alleging unfair practices of Telecom Italia relating to ADSL technologies, ruled that Telecom Italia had abused its dominant position in the ADSL and xDSL market and fined Telecom Italia €59 million. Telecom Italia appealed the ruling and the fine to the Regional Administrative Tribunal, or TAR, of Lazio. The TAR of Lazio dismissed the appeal but reduced the fine to €29 million. Although Telecom Italia has paid the fine, it appealed the ruling to the Italian administrative court of appeals (*Consiglio di Stato*).

As a result of complaints made by Infostrada and Albacom, the Court of Appeals of Rome, on August 16, 2000, issued a restraining order prohibiting Telecom Italia to "promote and/or offer and/or directly conclude contracts for RING services and their equivalent, under whatever name". Telecom Italia subsequently appealed this order, but its appeal was dismissed on February 13, 2001. Although the restraining order was withdrawn on April 5, 2001, the case is proceeding on the merits. Other telecommunications operators have claimed that they suffered damages as a consequence of Telecom Italia's alleged unfair trade practices. The total amount of damages claimed amounts to approximately €351 million.

Acquisition of Cecchi Gori Communications

In relation to litigation following the sale of TeleMonteCarlo television network, or TMC, through a sale and purchase agreement among SEAT, Cecchi Gori Media Holding Group S.r.l. and Cecchi Gori Group FIN.MA.VI. S.p.A. ("Cecchi Gori Group") on August 6, 2001, the Cecchi Gori Group filed a proceeding with the civil court of Milan asking for the rescission of the pledge agreement by which Cecchi Gori Group granted a security interest in Cecchi Gori Communications S.p.A.'s ordinary shares to SEAT.

On July 31, 2001, Cecchi Gori Group, enforcing an arbitration clause, commenced an arbitration proceeding against SEAT claiming rescission, invalidity or termination of the purchase and sale agreement of Cecchi Gori Communications S.p.A. and claiming damages.

The Board of Arbitration was established in October 2001 and set itself the deadline of December 31, 2002 as the date by which the proceedings must be completed.

The Cecchi Gori Group parties have also challenged, in the civil court of Rome, the validity of a resolution of the Ordinary and Extraordinary shareholders' meeting of Cecchi Gori Communications S.p.A. (on April 27, 2001), which approved the company's annual report, resolved to cover the losses for the year 2000 and increased its share capital. On December 11, 2001, the hearing on the merits was concluded. On June 13, 2002, the court rejected the complaints filed by the Cecchi Gori Group.

Fee Concerning Article 20, Section 2 of Law No. 448 of December 23, 1998

Telecom Italia, Tim, Wind and Omnitel contested, before the TAR Lazio, the Ministerial Decree of March 21, 2000 introducing Italian Law No. 448 dated December 23, 1998, which, on January 1, 1999, established a new license fee in place of the concession fee, the amount of which progressively declines until 2003. The TAR Lazio asked to the administrative offices of the Ministries of the Treasury and of Communications to consign a documented report of clarification regarding the correspondence that had taken place with the European Commission in connection with the approval of the above-mentioned law. Furthermore, with regard to extraordinary appeals presented by Infostrada and Albacom to the Head of State, asking for the annullement of the above-mentioned Decree, the Council of State brought the case before the European Court of Justice, raising the question of the non-compatibility of the fee with Community regulations relating to telecommunications. Following the dispute, Telecom Italia and Tim did not pay the amount that theywere ordered to pay for 2000 (equal to € 307 million and € 179 million respectively). The TAR of Lazio decided to bring the case introduced by Telecom Italia and TIM to the European Court of Justice.

Investigation on Equality of Treatment

In April 2001, pursuant to an investigation relating to equality of treatment in the Italian telecommunications market commenced in July 2000, the Italian National Regulatory Agency ruled that Telecom Italia violated certain competition and telecommunications regulations. The sanction is expected to be a fine in an amount still to be quantified, but which Telecom Italia expects will not exceed €150, 000. In June 2001, Telecom Italia filed a complaint with the TAR of Lazio against the National Regulatory Agency's ruling. In a hearing in July 2001 the TAR of Lazio declined to suspend the effectiveness of the ruling. The merits on the case are still to be decided.

Nortel Inversora

In April 2001, a shareholder of Nortel filed a complaint requesting its appearance before the civil court of Buenos Aires to try to reach an agreement in relation to alleged irregularities in resolutions approved by the Nortel shareholders' meeting of January 19, 2001. The resolutions at issue were those that approved the financial statements as of September 30, 2000. Under Argentine law, the attempt to reach an agreement is a prerequisite to the initiation of formal litigation proceedings. The parties did not resolve their dispute in their appearance before the Buenos Aires civil court. Therefore, the plaintiff served process on Nortel for the commencement of litigation proceeding on the merit.

In August 2001, the same shareholder of Nortel filed another complaint requesting its appearance before the Buenos Aires civil court to try to reach an agreement in relation to alleged irregularities in resolutions approved by the Nortel shareholders' meeting of April 26, 2001. The resolutions at issue were those that approved the financial statements as of December 31, 2000. The parties did not resolve their dispute in their appearance in the Buenos Aires civil court. No service of process has yet been made on Nortel for the proceeding on the merit.

In September 2001, upon the request of the abovementioned shareholder of Nortel, a precautionary relief order was issued by the Buenos Aires civil court providing for: (i) an injunction against the effectiveness of the shareholders' meetings of Nortel dated January 19, 2001 and April 26, 2001, which approved the conduct of Nortel's directors for the periods September 30, 1999 to September 30, 2000 and October 1, 2000 to December 31, 2000, and (ii) the nomination of a special supervisor directly reporting to the judge the status of Nortel's business. Nortel has appealed against this order. On May 28, 2002, the judge revoked the precautionary measure under point (ii) above and disposed the attachment (*embargo*) of the shares in Nortel owned by the plaintiff.

Wholesale Telecom Corporation

In March 1999, Telecom Italia filed a lawsuit in the United States District Court for the Southern District of Florida against Wholesale Telecom Corporation ("WTC") to recover U.S.$13 million, plus interest, for switched transit communications services provided by Telecom Italia to WTC. WTC filed an answer and counterclaim in August 1999 and in June 2000, asserting counterclaims against Telecom Italia. WTC's counterclaim sought compensatory damages of at least U.S.$10 million and punitive damages of at least U.S.$50 million, plus interest.

The claim is for breach of contract, with WTC alleging (i) that Telecom Italia breached the terms of the agreement with respect to prices, quality of service, and invoicing; and (ii) tortious interference with contract by Telecom Italia.

Furthermore, WTC filed a third-party complaint in August 1999 against Telemedia International U.S.A., Inc. ("TMI U.S.A."), an indirect, wholly-owned subsidiary of Telecom Italia that operates telecommunications networks in the United States. WTC has asserted claims for conspiracy and tortious interference with contract, contending that TMI U.S.A. interfered with WTC's contract with Telecom Italia. In the third-party complaint, WTC seeks compensatory damages in excess of U.S. $10 million and punitive damages in excess of U.S.$50 million. TMI moved to dismiss WTC's third-party complaint. The district court dismissed WTC's conspiracy claim, but refused to dismiss the claim for tortuous interference with contract. TMI U.S.A. has appealed this decision. The district court's order was affirmed on appeal in April 2001. The claim for tortious interference together with the claims by WTC against Telecom Italia are pending before the United States District Court for the Southern District of Florida. The discovery stage ended and the case is ready for trial (according to the calendar that shall be decided by the judge).

SIN/Solpart

A complaint was filed against SIN (now Telecom Italia International) in August 2001 with the civil court of Curitiba (State of Paraná, Brazil) by a shareholder of Brazil Telecom ("Brazil Telecom"). The plaintiff seeks a preliminary restraining order suspending SIN's veto rights in respect of certain corporate actions of Solpart, the holding company of Brazil Telecom. SIN had been granted veto rights in respect of such actions pursuant to a shareholders' agreement dated July 19, 1998.

The plaintiff claims that SIN was not entitled to exercise its veto rights, first, because of a conflict of interest; and second, because in exercising its veto, SIN would have allegedly abused its power in relation to the acquisition of certain licenses for telecommunications services held by Companhia Riograndense de Telecomunicações ("CRT") and improperly prevented Brazil Telecom from participating in an auction for those licenses.

The plaintiff's request for a preliminary restraining order suspending the exercise of the veto rights was denied by the judge, and the judge's ruling was affirmed on appeal.

The plaintiff has not yet served process on SIN for the commencement of litigation proceedings on the merits.

Brazil Telecom

In April 2001, Brazil Telecom filed suits against Telecom Italia, SIN, and the two directors of Brazil Telecom nominated by Telecom Italia.

Such Suits have been filed in order to obtain compensation for the alleged damages that Brasil Telecom would have suffered following the purchase of CRT (Companhia Riograndense de Telefonia) and the failure to participate in the Servicio Movel Pessoal auction. The judge has been asked to quantify the damages.

The first hearing shall be held on August 6, 2002.

Chase Manhattan Bank

A complaint was filed in June 2000 in the U.S. District Court for the District of Delaware by The Chase Manhattan Bank ("Chase"), now JPMorgan Chase Bank, in connection with an U.S.$800 million financing granted by Chase to Iridium Operating LLC, a subsidiary of Iridium LLC in 1998. Iridium LLC filed for Chapter 11 bankruptcy protection on August 13, 1999. The complaint seeks to enforce a commitment to purchase, under certain circumstances, additional capital of Iridium LLC by certain interest holders of Iridium LLC. The complaint asserts that the commitment to purchase additional capital was pledged as collateral to Chase in connection with the above referenced financing. Chase amended its complaint in February 2001 to assert additional claims for alleged fraud and misrepresentation against the defendants.

Telecom Italia directly held approximately a 3.8% interest in Iridium LLC until October 1996. In November 1996 Telecom Italia contributed its interest in Iridium LLC to Iridium Italia S.p.A., a company owned by Telecom Italia (30% interest), TIM (35% interest) and Telespazio (35% interest).

On April 5, 2002, the Magistrate Judge issued an Order granting Telecom Italia's motion to dismiss. Such Order has been objected by Chase on April 19, 2002.

STET Hellas Dispute

In December 1996, Mobitel, a company of the Greek Interamerican group (now Demco Reinsurance), a minority shareholder of STET Hellas and, at that time, its exclusive representative, initiated arbitration proceedings at the Paris International Chamber of Commerce. Mobitel claims its right to receive commissions on outgoing traffic generated by the subscribers it had signed up and on incoming traffic generated by calls received by Stet Hellas customers from the fixed telephone network of OTE and that was generated by customers in default of payment allegedly derived from negligent behaviour of Stet Hellas in dealing with customers. The alleged total loss is approximately U.S.$38 million. Mobitel and the Greek Interamerican group have also requested damages for a total of U.S.$172 million following the dissolution of their exclusive representative contract.

STET Hellas and Telecom Italia, which took over from Stet International (formerly the guarantor of STET Hellas and, as such, a party to the contracts) presented a counterclaim for an amount of about U.S.$210 million, mainly to cover the damages suffered as a result of the loss of the acquisition of market share caused by Mobitel's breach.

In October 2000, a partial award was given which, in principle, agreed with Mobitel's request for commissions on STET Hellas's revenues from incoming traffic; in November 2001, the Board of Arbitration rejected Telecom Italia and STET Hellas' claim that the Board of Arbitration did not have jurisdiction but that the ordinary Greek courts had exclusive jurisdiction concerning the decision over the amounts claimed, since the Arbitration Board had only been asked to decide on the obligation to pay, a matter which the Board of Arbitration had already decided.

Afterwards, a series of legal actions took place and on January 15 and 31, 2002, Mobitel claimed damages as follows: U.S.$19.6 million plus interest of U.S.$9.6 million for the commission on revenues generated by all calls (including incoming calls) made by customers acquired by Mobitel; U.S.$8.8 million plus interest for the Company's failure to achieve a 45% market share; and claim for the damages as a result of the breach of the agreement amount to U.S.$109.4 million.

As of January 30, 2002 STET Hellas quantified its claim against Mobitel as follows: €22.7 million for bad debts; U.S.$255.4 million for the loss of market share as a result of the failure of Mobitel and Interamerican to fulfil their obligations; and to U.S.$611.2 million plus the legal interest for damages and loss of income incurred for the illegal termination by Mobitel of the distribution and sales agreement with the Company.

Item 9. LISTING

The principal trading market for the Shares and the Savings Shares is on Telematico, an automated screen trading system managed by Borsa Italiana. (See "—Securities Trading in Italy").

Ordinary and Savings Share ADSs, each representing respectively ten Shares and ten Savings Shares, have been quoted on the NYSE since July 27, 1995. JPMorgan Chase Bank is the Company's Depositary issuing ADRs evidencing the Ordinary Share ADSs and the Savings Share ADSs.

The table below sets forth, for the periods indicated, reported high and low official prices of the Shares on Telematico and high and low closing prices of Ordinary Share ADSs on the NYSE. Beginning January 4, 1999, the Shares began trading on Telematico in euro. The prices for 1998 have been restated (based on the Fixed Euro/ Lira Exchange Rate of Lit. 1, 936.27 = €1.00 established on December 31, 1998) as if the Shares had been trading in euro since the beginning of the period.

	Telematico		NYSE	
	High	**Low**	**High**	**Low**
	(€)		**(U.S.$)**	
1998:				
First quarter	7.43	5.87	79 7/16	63 7/16
Second quarter	8.02	6.46	87 7/8	70 1/8
Third quarter	8.17	5.81	89 3/16	67 1/8
Fourth quarter	7.43	4.69	87 1/4	54 3/8
1999:				
First quarter	9.99	7.58	113	87 5/8
Second quarter	10.19	9.34	110	97 7/16
Third quarter	11.13	8.21	113 6/16	86 3/16
Fourth quarter	14.15	7.86	141 14/16	83 7/16
2000:				
First quarter	19.74	12.19	16 12/16	123 4/16
Second quarter	16.60	13.20	152 8/16	119 11/16
Third quarter	15.40	12.05	145 1/16	105
Fourth quarter (1)	14.02	11.59	121 14/16	97 8/16
2001:				
First Quarter	13.65	10.68	127.50	95.55
Second Quarter	12.55	9.69	113.25	83.00
Third Quarter	10.93	6.51	94.50	60.00
Fourth Quarter	9.99	8.14	90.35	75.50
2002:				
January	9.83	9.19	88.75	79.60
February	9.46	8.69	82.10	75.18
March	9.89	9.51	87.35	81.75
April	9.51	8.84	83.64	77.63
May	9.25	8.35	85.00	76.05
June (through June 21)	8.55	7.78	78.66	74.60

(1) The official prices of Shares and Savings Shares and Ordinary and Savings Share ADSs for the periods prior to and including November 10, 2000 are not comparable to the official prices of these shares and ADSs in the following periods due to the effect of the demerger of Tin.it, which became effective on November 10, 2000.

At the close of business on June 21, 2002, there were 4,016,236 Ordinary Share ADSs outstanding held by 111 registered holders.

The table below sets forth, for the periods indicated, reported high and low official prices of the Savings Shares on Telematico and high and low closing prices of the Savings Share ADSs on the NYSE for the period following such date. Beginning January 4, 1999, the Savings Shares began trading on Telematico in euro. The prices for 1998 have been restated (based on the Fixed Euro/Lira Exchange Rate of Lit. 1, 936.27 = €1.00 established on December 31, 1998) as if the Savings Shares had been trading in euro since the beginning of the period.

	Telematico		NYSE	
	High	**Low**	**High**	**Low**
	(€)		**(U.S.$)**	
1998:				
First quarter	5.74	4.09	61 1/2	45
Second quarter	5.79	4.51	60 1/4	52
Third quarter	5.56	3.55	58 1/4	46 5/16
Fourth quarter	5.55	3.33	64	39 1/2
1999:				
First quarter	6.59	5.40	74 1/4	60
Second quarter	5.67	4.62	62 3/4	50
Third quarter	5.77	4.78	58 8/16	51
Fourth quarter	6.09	4.42	62	48 4/16
2000:				
First quarter	8.86	5.69	85	60 4/16
Second quarter	7.24	6.28	69	58 8/16
Third quarter	7.56	6.12	71	55
Fourth quarter (1)	6.65	5.82	58 8/16	52 4/16
2001:				
First quarter	7.03	5.59	63.38	52.50
Second quarter	7.08	5.19	61.00	45.94
Third quarter	5.99	3.73	50.50	37.50
Fourth quarter	6.01	4.57	52.29	49.00
2002:				
January	6.06	5.61	53.04	51.10
February	5.94	5.35	50.51	47.51
March	6.36	6.00	55.96	54.88
April	6.33	5.94	57.00	52.50
May	6.05	5.64	54.74	54.00
June (through June 21)	5.69	5.14	50.32	50.32

(1) The official prices of the Shares and Savings Shares and Ordinary and Savings Share ADSs for the periods prior to and including November 10, 2000 are not comparable to the official prices of these shares and ADSs in the following periods due to the effect of the demerger of Tin.it, which became effective on November 10, 2000.

At the close of business on June 21, 2002, there were 85,124 Savings Share ADSs outstanding held by 9 registered holders.

Fluctuations between the euro and the U.S. dollar will affect the dollar equivalent of the price of the Share and the Savings Shares on Telematico and the price of the Ordinary Share ADSs and the Savings Share ADSs on the New York Stock Exchange. On June 20, 2001, the Noon Buying Rate for the euro was U.S.$0.8901 = €1.00.

Securities Trading in Italy

Since July 1994, all Italian equity securities have been traded on Telematico except for those of certain smaller companies and cooperative banks traded on *Mercato Ristretto* under certain specific rules concerning trading hours and procedures and for those of high growth companies traded on *Nuovo Mercato*.

Telematico operates under the control of CONSOB, the public authority charged, among other things, with regulating securities markets and all public offerings of securities in Italy, and is managed by Borsa Italiana a joint stock company previously owned by the Treasury, sold through a tender offer to authorized intermediaries.

Securities transactions on Telematico are settled on a cash basis. Cash transactions are settled on the third business day following the trading date. Borsa Italiana issues a daily official list with certain information on transactions in each listed security, including the volume traded and the high and low prices of the day. No "closing price" is reported, but an "official price" calculated as a weighted average price of all trades effected during the trading day and a "reference price" calculated as a weighted average price of the last 10% of the trades effected during such day are published. Effective July 1, 2002, the reference price will be the equal to the closing auction price. The Bank of Italy clearing system assists with the settlement of transactions and the delivery of securities traded.

Residents of Italy and non-residents through their authorized agents may purchase or sell shares on Telematico, subject to satisfying (i) in case of sales, either the Margin or the Deposit, and (ii) in case of purchases, the Margin. "Margin" means a deposit equal to 100% of the agreed price, and "Deposit" means a deposit of an equal number of the same shares as those sold. If in the course of a trading day the price of a security fluctuates by more than 5% from the last reported sale price (or 10% from the previous day's reference price or from the opening auction price, as the case may be), an automatic five-minute suspension is declared. In the event of such a suspension, effect is not given to trades agreed but not confirmed before the suspension. In addition, Borsa Italiana has the authority to suspend trading in any security in response to extreme price fluctuations or for other reasons.

Starting May 15, 2000 the most liquid shares traded on Telematico, including the Shares and the TIM ordinary shares, have been traded on "Mercato After Hours", an automated screen trading system managed by Borsa Italiana. "Mercato After Hours" operates, from 6.00 p.m. to 8.30 p.m. on every trading day, substantially under the same rules as Telematico except that the price of any security may not fluctuate by more than 3.5% from the reference price of said securities on Telematico on the same day.

American style call and put options are traded on the derivative market managed by Borsa Italiana which currently include the Shares, the Savings Shares and the TIM ordinary shares.

Effective July 1, 1998, the Italian financial markets have been regulated by the Draghi Law, which has embodied (with significant amendments and integrations) most of the contents of Delegated Law No. 415 of July 23, 1996. With the Draghi Law, the Italian Government has introduced new laws and regulations governing some aspects of the financial sector and, in particular: (i) brokers and firms managing financial instruments; (ii) the Italian regulated Stock Exchanges; (iii) the offering to the public of financial instruments; (iv) public tender offers; (v) some aspects of corporate governance of listed companies; and (vi) insider trading. The Draghi Law contains framework provisions which have been implemented by specific regulations.

Clearance and Settlement of Telecom Italia Shares

Legislative Decree No. 213 of June 24, 1998 ("Dematerialization Decree") provided for the dematerialization of financial instruments publicly traded on regulated markets including treasury bonds. From July 9, 1998, all companies that issue financial instruments that are publicly traded on regulated markets must inform Monte Titoli, a centralized securities clearing system owned by certain of the major Italian banks and financial institutions, which will open an account in the name of each company in its register.

Beneficial owners of Shares and Savings Shares must hold their interests through specific deposit accounts with any participant having an account with Monte Titoli. The beneficial owners of Shares and Savings Shares held with Monte Titoli may transfer their shares, collect dividends, create liens and exercise other rights with respect to those Shares and Savings Shares through such accounts and may no longer obtain physical delivery of share certificates in respect of their Shares and Savings Shares. All new issues of Shares and Savings Shares and all other transactions involving Shares and Savings Shares must settle electronically in book-entry form.

Shares and Savings Shares are accepted for clearance through Euroclear and Clearstream. Holders of shares may elect to hold such Shares and Savings Shares through Euroclear or Clearstream (outside the United States).

Item 10. ADDITIONAL INFORMATION

EXCHANGE CONTROLS AND OTHER LIMITATIONS AFFECTING SECURITY HOLDERS

Foreign Investment and Exchange Control Regulations in Italy

There are no exchange controls in Italy. Residents of Italy may hold foreign currency and foreign securities of any kind, within and outside Italy. Non-residents may invest in Italian securities without restriction and may export cash, instruments of credit and securities, in both foreign currency and euro, representing interest, dividends, other asset distributions and the proceeds of dispositions. There are no limitations on the right of non-resident or foreign beneficial owners to vote their Shares except as provided for all Telecom Italia shareholders by law. See "—Description of Bylaws and Capital Stock—Capital Stock—Limitations on Voting and Shareholdings".

Updated reporting and record-keeping requirements are contained in recent Italian legislation which implements an EU Directive regarding the free movement of capital. Such legislation requires that transfers into or out of Italy of cash or securities in bearer form in excess of €10,329.14 be reported in writing to the Ufficio Italiano Cambi (the Italian Exchange Office) by residents or non-residents that effect such transfers, or by credit institutions or other intermediaries that effect such transactions on their behalf. In addition, credit institutions and other intermediaries effecting such transactions on behalf of residents or non-residents of Italy are required to maintain records of such transactions for five years, which may be inspected at any time by Italian tax and judicial authorities. Non-compliance with these reporting and record-keeping requirements may result in administrative fines or, in the case of false reporting and in certain cases of incomplete reporting, criminal penalties. The *Ufficio Italiano Cambi* will maintain reports for a period of ten years and may use them, directly or through other government offices, to police money laundering, tax evasion and any other crime or violation.

Certain additional procedural requirements are imposed for tax reasons. Non-corporate residents of Italy effecting transfers to and from Italy in excess of €10,329.14 in one year must disclose them in their annual tax declarations. Non-corporate residents must also give details in their tax declarations of financial assets held outside Italy at the end of the fiscal year and of transfers in excess of €10,329.14 to, from, within and between foreign countries in connection with such assets during the fiscal year. No declaration is required in respect of foreign investments and foreign income-earning assets that are exempt from income tax or subject to withholding tax in Italy. Such disclosure requirements do not apply (i) if the total value of the investments and assets at the end of the taxable period or the total amount of the transfers effected during the year is not greater than €10,329.14 or (ii) in respect of foreign investments, foreign assets or transfers within the EU (except for transfer from or to Italy). For corporate residents there is no requirement for such a declaration because their financial statements (on the basis of which their tax returns are prepared) already contain the information.

There can be no assurance that the present regulatory environment in or outside Italy will endure or that particular policies presently in effect will be maintained, although Italy is required to maintain certain regulations and policies by virtue of its membership in the EU and other international organizations and its adherence to various bilateral and multilateral international agreements.

DESCRIPTION OF BYLAWS AND CAPITAL STOCK

Bylaws

Object

Telecom Italia's objects are described in Article three of Telecom Italia's bylaws. Such objects are:

- to install and operate fixed or mobile equipment and installations for the purpose of providing and operating licensed telecommunications services for public use, and to carry out the activities directly or indirectly related thereto;
- to hold interests in other businesses falling within the scope of the above stated corporate object or otherwise related thereto;
- to control and provide the strategic, technical, administrative and financial coordination, overseeing and managing the financial activities of controlled companies and businesses, and carrying out all transactions related thereto.

Directors

There are no provisions in Telecom Italia bylaws relating to the power of a director to vote on a proposal in which such director is materially interested, the power of a director to (in the absence of an independent quorum) vote compensation to itself or any member of its body, the borrowing powers exercisable by a director and how such powers can be varied, the retirement of a director under an age limit requirement and the number of shares required for director's qualification. Such powers and requirements are governed by applicable Italian law.

Under Italian law:

- where a director (either directly or on behalf of third parties) has an interest in any specific transaction, which is in conflict with the interest of the company, such director is obliged to disclose this situation to the Board of Directors and the Board of Statutory Auditors and to abstain from voting;
- the compensation of directors and of members of the Executive Committee, if any, is determined by the bylaws or resolved upon by the shareholders in the ordinary meeting. Telecom Italia shareholders approved and fixed an overall compensation for the whole Board of Directors, the allotment of this overall compensation among its members is decided by the Board itself; and
- the Board of Directors grants specific positions to any of its members in compliance with the bylaws of the company; such positions include, among others, those of Chairman and Chief Executive Officer. The remuneration corresponding to such positions is then defined by the Board of Directors in its discretion, after acknowledging the opinion of the Board of Statutory Auditors. For the specific compensation provisions of Mr. Colaninno, the Former CEO of the Company please see "Item 6. Directors, Senior Management and Employees—Compensation of Directors and Officers".

There are no provisions in Italian law that set age or shareholding requirements for directors' qualification.

Capital Stock

General

As of June 20, 2002, the full paid-in capital stock amounted to €4,023,716,540.80 and was constituted by 5,262,726,231 Shares and 2,053,122,025 Savings Shares, each of €0.55 par value.

At the extraordinary shareholders' meeting held on May 3, 2001 Telecom Italia's share capital was converted from lire into euros by rounding up the par value of the shares, from Lit. 1,000 (approximately €0.52) to €0.55, partially through the cancellation of 112, 998, 070 Savings Shares held in treasury. For a maximum period of five years from the date of the shareholders resolution authorizing the transaction (December 15, 1998 subsequently amended on August 10, 2000 and May 3, 2001) the Board of Directors has the power to increase the Company's share capital by payment on one or more installments and to issue new Shares, which will rank for dividend *pari passu*, to be offered for subscription to executives of Telecom Italia or its subsidiaries, up to a maximum of €40,150,000 (which corresponds to the issuance of 73,000,000 Shares, with a par value of €0.55 each), at a price determined by the Board of Directors for each capital increase, within the limits permitted by law.

In partial implementation of the authorization granted by the shareholders on December 15, 1998, the Board of Directors:

- on December 17, 1999 passed a resolution to increase the share capital by payment of up to a maximum of €9,127,470, (such amount being the result of the conversion and recalculation of the previous lire amount following the May 3, 2001 shareholders' meeting), by issuing a maximum of 16,595,400 Shares (of which 7,594,600 were issued as of June 20, 2002);

- on June 12, 2001 passed a resolution to increase the share capital by payment of up to a maximum of €8,398,500 by issuing a maximum of 15,270,000 Shares;

- on March 26, 2002 passed a resolution to increase the share capital by payment of up to a maximum of €3,025,000, by issuing a maximum of 5,500,000 Shares.

See "Item 6. Directors, Senior Management and Employees—Options to Purchase Securities from Registrant or Subsidiaries".

The extraordinary shareholders' meeting held on June 12, 2001 granted the Board of Directors, for a maximum period of five years from the date thereof, the power to further increase the Company's share capital by payment, in one or more installments and to issue new Shares, which will rank for dividends pari passu, to be offered for subscription to senior managers and to other employees of Telecom Italia or its subsidiaries or controlling companies, up to a maximum of €40,150,000 shares (which corresponds to the issuance of a maximum of 73,000,000 Shares).

In partial implementation of the authorization granted by the shareholders on June 12, 2001, the Board of Directors:

- on March 26, 2002 passed a first resolution to increase the share capital by payment of up to a maximum of €33,236,500, by issuing a maximum of 60,430,000 Shares;

- on March 26, 2002 passed a second resolution to increase the share capital by payment of up to a maximum of €6,490,000, by issuing a maximum of 11,800,000 Shares.

See "Item 6. Directors, Senior Management and Employees—Options to Purchase Securities from Registrant or Subsidiaries". In consideration of the authorization granted by the shareholders' meeting on December 15, 1998 (for the part not yet executed) and on June 12, 2001 the maximum authorized share capital amounts to €4,099,839, 510.80, constituted by 5,401,131,631 Shares and 2,053,122,025 Savings Shares.

Classes of shares

According to Italian law, Savings Shares may not be issued for an amount which, including other preferred shares, if any, exceeds one-half of the Company's share capital.

Pursuant to Telecom Italia's bylaws any reduction in share capital made for the purpose of absorbing losses is applied to the par value of the Shares until they have been reduced to zero and only then is the par value of the Savings Shares reduced. If, as a consequence of capital reduction, the Savings Shares exceed half of the Company's share capital, such excess must be eliminated within the following two years.

Form and Transfer

The Dematerialization Decree provides for the dematerialization of financial instruments publicly traded on regulated markets, including treasury bonds.

As a result, Shares and Savings Shares must be held with Monte Titoli. Most Italian banks, brokers and securities dealers have securities accounts as participants with Monte Titoli, and beneficial owners of Shares and Savings Shares may hold their interests through special deposit accounts with any such participant. The beneficial owners of Shares and Savings Shares held with Monte Titoli may transfer their Shares, collect dividends and exercise other rights (including voting rights) with respect to those shares through such accounts. Such shares held by Monte Titoli are transferred between beneficial owners by appropriate instructions being given to the relevant participants associated with Monte Titoli to debit the account with the bank of the vendor and to credit the account with the bank of the purchaser.

Voting rights relating to Shares and Savings Shares that have not been deposited with Monte Titoli may be exercised only by depositing them with an authorized intermediary, with the subsequent issuance of the necessary certification. The Company may be requested to perform the functions of an intermediary.

Each person owning a beneficial interest in Shares and Savings Shares held through Euroclear or Clearstream must rely on the procedures of Euroclear or Clearstream, respectively, and of institutions that have accounts with Euroclear or Clearstream to exercise any rights of a holder of shares. Holders may request Euroclear or Clearstream to transfer their Shares and Savings Shares to an account of such holder with a participant of Monte Titoli, in which case such holders may transfer their shares, collect dividends and exercise other shareholder rights through that participant. Any such transfer through that participant is not subject to Italian transfer tax if non-Italian parties are involved. See "Item 10.—Description of Bylaws and Capital Stock—Taxation".

Meetings of Shareholders

Holders of Shares are entitled to attend and vote at ordinary and extraordinary shareholders' meetings ("Shareholders' Meetings"). At any Shareholders' Meeting, each holder is entitled to cast one vote for each Share held. Votes may be cast personally or by proxy. Holders of Shares can also vote by mail.

Shareholders' Meetings are called by the Company's Board of Directors when required by law or the shareholders or deemed necessary. A minimum of two statutory auditors can call the Company's shareholder meetings.

Shareholders' Meetings must be convened at least once a year. At these ordinary meetings, holders of Shares (i) approve the annual accounts, (ii) appoint directors and statutory auditors and determine their remuneration, when necessary, and (iii) vote on any business matter submitted by the directors. Extraordinary Shareholders' Meetings may be called to pass upon proposed amendments to the Bylaws, capital increases, mergers, dissolutions, issuance of debentures, appointment of receivers and similar extraordinary actions. The notice of a Shareholders' Meeting may specify up to two meeting dates for an ordinary Shareholders' Meeting and up to three meeting dates for an extraordinary Shareholders' Meeting ("calls").

An ordinary Shareholders' Meeting is duly constituted on first call with the attendance of at least 50% of the outstanding Shares, while on second call there is no quorum requirement. In either case, resolutions are approved by holders of the majority of the Shares represented at a duly called meeting.

Extraordinary Shareholders' Meetings are duly constituted with the attendance of more than one-half or one-third or one-fifth of the company's share capital shareholders, on the first call, second call and third call, respectively. The favorable vote of at least two-thirds of the Shares represented at the meeting is necessary for the resolution approval. Resolutions concerning capital increases with the exclusion or limitation of subscription rights must always be approved by holders of more than 50% of the shares outstanding, irrespective of the call in which the resolution is taken.

The annual accounts of the Company are submitted for approval to the annual Shareholders' Meeting, which must be convened within six months after the end of the financial year to which they relate. Shareholders are informed of all Shareholders' Meetings to be held by publication of a notice in *Gazzetta Ufficiale* at least 30 days before the date fixed for the meeting. In the case of a Shareholders' Meeting that is called at the request of the minority shareholders or a Shareholders' Meeting called to approve the liquidation of the Company, the notice period is reduced to 20 days. The notice period is reduced to 15 days if the Company is subject to a tender offer and a Shareholders' Meeting is called to consider defensive actions against such tender offer (in which case resolutions must be approved by at least 30% of the holders of the voting shares outstanding at all calls of the Shareholders' Meeting). The notice must also be published in at least one national daily newspaper.

To attend any Shareholders' Meeting, holders of Shares must be in possession of appropriate certification issued by an authorized intermediary. Special arrangements with the Depositary may be required for the beneficial owner of ADRs representing ADSs to attend Shareholders' Meetings and exercise voting rights with respect to underlying Shares. See "—Description of American Depositary Receipts—Voting of Deposited Securities".

Shareholders may attend the meeting by proxy using a power of attorney. Any one proxy cannot represent more than 200 shareholders. A proxy may be appointed only for one single meeting (including, however, the first, second and third call) and may be substituted only by the person expressly indicated in the form. The proxy can neither be a director, statutory auditor, employee of the company or of one of its controlled subsidiaries, nor a controlled company or the independent auditors of Telecom Italia or shareholders, directors, statutory auditors or employees of such independent auditors.

Votes by proxy may be solicited and collected for the shareholders' meetings of listed companies. Proxy solicitation provisions allow individuals (so-called consignors), to promote, through special brokers, the soliciting of votes by proxy at shareholders' meetings. The ownership—including joint ownership—of at least 0.5% (such reduced limit was introduced by CONSOB for Telecom Italia and other listed companies; the general ownership requirement is 1%) of the company's voting share capital (registered in the shareholders' register for at least six months) is a requisite for becoming a consignor. Soliciting brokers may be investment companies, banks, asset management companies and joint-stock companies, with soliciting votes by proxy as their only corporate object.

Shareholders associations composed of at least 50 people, each with no more than 0.1% voting share capital, may collect proxies among their group. In order to facilitate such operation among employee shareholders, the Bylaws provides that special spaces will be made available to such shareholders associations where information about solicitation can be made available and proxy collection operations can be carried out.

Votes may also be cast by mail. The "vote by mail" system is essentially based on the following principles: (a) the notice calling the shareholders' meetings must specify that shareholders can vote by mail and must describe the procedures they have to follow; (b) the notice must also be sent to the centralized securities depositary system which will in turn distribute the notice to the depositary banks; (c) shareholders wishing to vote by mail must send the company a certification issued by the depositary banks certifying their shareholding and a special form (so called ballot) made available to such purpose by the issuer, which has to comply with specific CONSOB requirements; (d) such special forms are kept by the Chairman of the Board of Statutory Auditors until the votes are counted; (e) votes cast by mail must be delivered to the company at least 48 hours prior to the Shareholders' Meeting; and, finally, (f) votes cast by mail remain valid for the second and third calls of the meeting and can be revoked by a written declaration until the day before the meeting.

The shareholders' meetings may be called when requested to the Board of Directors by shareholders representing at least 10% of a company's share capital, while action against directors, statutory auditors and general managers may be promoted by shareholders representing at least 5% of the Company's share capital and who have been registered for at least six months. The Board of Directors can decide, in the best interest of the Company, not to call a shareholders' meeting despite the request of the shareholders. The shareholders can appeal the decision of the Board to the Court, and the Court can issue a decree ordering the call of the meetings. The Board of Directors does not have the discretion to ignore a request to call a shareholders' meeting if such request is made by shareholders representing at least 20% of the company's share capital.

Although holders of Savings Shares are not entitled to vote in meetings of holders of Shares, they are entitled to attend special meetings of holders of Savings Shares ("Special Meetings") and to appoint a joint representative (the "Joint Representative") to represent them, with respect to the Company.

The Joint Representative, who is appointed by the Special Meetings or, in default, by the President of the Court, is entitled to (i) inspect certain corporate books of the Company, (ii) to attend the Shareholders' Meetings and (iii) to challenge in court the resolutions adopted by such meetings. The Joint Representative is appointed for a maximum three-year term and, according to the Bylaws, is kept informed by the Company regarding corporate events that can affect the price trend of Savings Shares. The saving shareholders Meeting held on October 31, 2001 appointed Mr. Carlo Pasteris as joint Representative for a three year period ending on October 31, 2004.

Special Meetings may be called when deemed necessary or upon request by saving shareholders representing at least 1% of the outstanding Savings Shares either by the Joint Representatives or by the Company's Board of Directors in order to (a) appoint and revoke the Joint Representative, (b) approve the resolutions of the Shareholders' Meetings that may affect the rights of Savings Shares, (c) set up an expense fund for the coverage of costs incurred in protecting rights of the Saving Shareholders, (d) negotiate possible disputes with the Company; and (e) resolve other issues relating to their position as holders of Savings Shares. To adopt resolutions related to (a), (c) and (e) above, a favorable vote of at least 20% of the Savings Shares is required at Special Meetings held on the first call, a favorable vote of at least 10% is required at Special Meetings held on the second call, and a favorable vote of at least a majority of the Savings Shares present is required at Special Meetings held on the third call. To adopt resolutions related to (b) and (d) above, a favorable vote of at least 20% of the Savings Shares is required at all calls of the Special Meetings.

To attend any Special Meeting, the holders of Savings Shares must be in possession of an appropriate certification issued by an authorized intermediary. Special arrangements with the Depositary may be required for the beneficial owner of ADRs representing Savings Share ADSs to attend Special Meetings and exercise voting rights with respect to underlying Savings Shares. See "—Description of American Depositary Receipts—Voting of Deposited Securities".

Dividend Rights

Holders of Savings Shares are entitled each year to a distribution with respect to such year's net profits in the amount of 5% of the par value of their shares. If with respect to any year a lesser amount is paid, the entitlement to payment of the shortfall is carried over for two successive years. In the event that dividends are paid to holders of Shares, holders of Savings Shares have a preferential right to receive a dividend per share that is 2% of the par value of the Savings Shares greater than that received by holders of the Shares.

Subscription Rights

New Shares and/or Savings Shares may be issued pursuant to a resolution of holders of Shares at any extraordinary Shareholders' Meeting. Pursuant to Italian law, shareholders (including holders of Savings Shares) are entitled to subscribe for new issues of Shares and/or Savings Shares, debentures convertible into Shares and/or Savings Shares and rights to subscribe for Shares and/or Savings Shares in proportion to their respective shareholdings.

Subject to certain conditions principally designed to prevent dilution of the rights of shareholders, subscription rights may be waived or limited by resolution taken by an extraordinary Shareholders' Meeting by the affirmative vote of holders of more than 50% of the Shares outstanding. This majority is required at the first, second and third call.

The shareholders can adopt a resolution, at an extraordinary Shareholders' Meeting, to convert available reserves into additional share capital. In such case, either the par value of all outstanding Shares is identically raised or the Shares resulting from the increase in share capital are allocated to the shareholders in proportion to their ownership before the increase without further contribution or payment from the shareholder.

Liquidation Rights

Subject to the satisfaction of all other creditors, holders of Shares are entitled to a distribution in liquidation. Holders of Savings Shares and preferred shares, if any, are entitled to a preferred right to distribution from liquidation up to their par value. No liquidation dividend is payable to the holders of other classes of shares until such preferential right has been satisfied in full. Thereafter, if there are surplus assets, holders of all classes of shares rank equally in the distribution of such surplus assets. Shares rank *pari passu* among themselves in a liquidation.

Purchase of Shares or Savings Shares by the Company

The Company may purchase its own Shares or Savings Shares subject to certain conditions and limitations. Such purchases must be authorized by a Shareholders' Meeting and made only out of retained earnings or distributable reserves as shown on the most recent financial statements approved by the Shareholders' Meeting. The par value of the Shares or Savings Shares purchased by the Company, including the Shares or Savings Shares, if any, held by the Company's subsidiaries may not exceed 10% of the Company's share capital. The Company may purchase its own Shares or Savings Shares either on the market or through a tender offer, according to the terms and conditions agreed with Borsa Italiana.

A corresponding reserve equal to the purchase price of such Shares or Savings Shares has to be created on the Company's balance sheet. Such reserve is not available until such Shares or Savings Shares are sold or disposed of or canceled by the Company. Shares or Savings Shares purchased and held by the Company or one of its subsidiaries may be disposed of only pursuant to a resolution of the Company's or, if applicable, its subsidiary's Shareholders' Meeting.

Neither the Company nor any company under its control may vote or subscribe for new Shares or Savings Shares of the Company. These subscription rights accrue to the other holders so long as such Shares or Savings Shares are held by the Company or a company under its control. The Shares or the Savings Shares, as long as they are owned by the Company, are not entitled to receive dividends.

On November 7, 2001, the shareholders' ordinary meeting of Telecom Italia granted Telecom Italia's Board of Directors authorization for the buyback of Shares or Savings Shares, or both, up to a maximum amount of €1.5 billion, provided however that the total number of shares acquired shall not exceed 10% of registered capital. The share buyback may be undertaken on one or more occasions within a period of 18 months, starting from November 7, 2001, and will be undertaken in accordance with conditions agreed with the Italian Stock Exchange in order to guarantee equal shareholders' treatment. The purchase price of each share must be neither 15% higher nor 15% lower than the average of the reference prices recorded by the Italian Stock Exchange in the three trading days preceding each individual transaction. The disposal of the shares purchased pursuant to the share buy-back program is not subject to any time limit. Disposal of the shares may take place in one or more transactions and the shares may be disposed of by sale or exchange, including public offers and offers to shareholders, employees, directors and certain agents of Telecom Italia. The shares purchased pursuant to the share buy-back may also be disposed of within the framework of any stock option or share incentive plans. In the case of a sale, the sale price may not be less than the lowest purchase price; the shares may also be disposed of by coupling them with bonds or warrants. The sale price limit will not be applicable to disposal of shares in respect of employees, directors or collaborators of Telecom Italia, within the framework of any share incentive plans or stock option plans.

As of June 15, 2002, 2,981,200 Shares and 10,350,000 Savings Shares were purchased.

Reporting Requirements and Restrictions on Acquisitions of Shares

Pursuant to Italian securities regulations any acquisition or sale of an interest in excess of 2%, 5%, 7.5%, 10% and all higher multiples of five, in the voting shares of a listed company, must be notified to the listed company and to CONSOB within five trading days (defined as days on which Borsa Italiana is open) following the acquisition or sale. CONSOB must make such information public within three trading days from the notification.

For purposes of the disclosure requirements referred above: (i) a person's holding must include both the shares owned by such person, even if the voting rights belong or are assigned to third parties, and the shares whose voting rights belong or are assigned to such person; (ii) a person's holding shall also include both the shares owned by nominees, trustees or subsidiary companies and the shares of which the voting rights belong or are assigned to such persons; (iii) shares registered in the names of or endorsed to trustees and those whose voting rights are assigned to an intermediary in connection with collective or individual portfolio management services are not to be attributed to the persons controlling the trustee or the intermediary.

For the purposes of the disclosure requirements for 5%, 10%, 25% 50% and 75% thresholds, the calculation of holdings shall also include issued and subscribed shares that a person may buy or sell on his own initiative, either directly or through nominees, trustees or subsidiary companies. Shares that may be acquired by exercising conversion rights or warrants shall be included in the calculation only if the acquisition can be made within sixty days.

Shareholder agreements concerning the voting shares of a listed company must be notified to CONSOB and to the company if they include agreements on the exercise of voting rights and/or duties of consultation before voting. The same rule applies when the shareholder agreements concern the shares issued by a non-listed company that controls a listed company. The notification must include the share ownership of all parties filing it. When listed companies change their share capital, they must notify CONSOB and Borsa Italiana of the amount of the share capital and the number and classes of shares into which it is divided. CONSOB and Borsa Italiana must make the information available to the public no later than the day following the notification. The notification shall be made no later than the day following the event causing such modification or the day following the filing of the amended bylaws.

Any holdings by a listed company of an interest in excess of 10% in the voting shares of an unlisted company must be notified to CONSOB and to the company. The reduction of the participation within the 10% threshold must be notified to the company only. Notifications to CONSOB must be made within 30 days from the approval by the Board of Directors of the half-year and the annual reports; notifications to the company whose shares are being acquired or sold must be made within seven days from the transaction which results in exceeding or going within the 10% threshold. Such information must be made public when the half-year and the annual reports are deposited. For purposes of calculating the interest threshold above, the following unlisted companies shares must be taken into account: (i) shares owned by a listed company even if the voting rights belong to a third party; and (ii) shares attributing voting rights to a listed company if such voting rights grant the listed company dominant or significant voting powers.

In accordance with Italian antitrust laws and regulations, the Antitrust Authority is required to prohibit acquisitions of sole or joint control over a company that would create or strengthen a dominant position in the domestic market or a significant part thereof. However, if the acquiring party and the company to be acquired operate in more than one Member State of the EU and exceed certain revenue thresholds, the antitrust approval of the acquisition falls within the exclusive jurisdiction of the European Commission. See "Item 4. Information on the Company—Regulation—Competition Law".

Limitations on Voting and Shareholdings

There are no limitations imposed by Italian law or by the Bylaws of Telecom Italia on the rights of non-residents of Italy or foreign persons to hold or vote the Shares other than those limitations described below, which apply equally to all owners of Shares.

Special Powers of the State

Telecom Italia's Bylaws include special powers granted to the State as permitted by the Privatization Law. See "Item 7. Major Shareholders and Related-Party Transactions—Continuing Relationship with the Treasury".

The special powers included in Telecom Italia's Bylaws are as follows:

Approval of Material Acquisitions of Shares. The State has the authority to approve or disapprove of the acquisition of material interests in the share capital of Telecom Italia (which is defined as 3% of the voting share capital). The Board of Directors is required to notify all such acquisitions to the Ministry of the Treasury. Until approval, the purchaser of the Shares may not vote the Shares and in case of disapproval or the expiration of the 60-day term within which the Minister of the Treasury has to make a decision. Short of approval by the Minister of the Treasury, the purchaser is obligated to resell the Shares within one year.

Approval of Material Voting Agreements. The State has the authority to approve or disapprove of voting agreements involving a material amount of voting share capital (5% of the voting share capital or any lesser percentage as may be established by decree of the Minister of the Treasury). CONSOB is required to notify the Ministry of the Treasury of any voting agreements reported to it. Until approval, the shareholders participating in the voting agreement may not vote the Shares and in case of disapproval or the expiration of the 60-day term within which the Minister of the Treasury is required to make a decision without approval, the voting agreement is nugatory. Resolutions adopted with the decisive vote of shareholders linked by a shareholders' agreement which, although not approved by the Treasury, is demonstrated by the shareholders' behavior during the meeting may be challenged and voided.

Veto Power over Major Changes. The State has veto power on resolutions to dissolve the company, approve mergers, demergers or disposition of the business, transfer the registered office abroad, change the corporate purposes or amend or modify the Minister of the Treasury's special powers.

Board of Directors and Board of Statutory Auditors Representation. The State has the power to appoint to the Board of Directors one director and to appoint to the Board of Statutory Auditors one member.

The foregoing special powers, which became effective on July 15, 1997, were granted to the Minister of the Treasury and will remain in effect, until such time as the process of liberalization of the telecommunications industry has reached a sufficiently advanced stage and the National Regulatory Agency has become firmly established. The determination that these conditions have been met shall be made by means of a decree of the Italian Prime Minister.

Voto di Lista

Pursuant to Telecom Italia's Bylaws, the election of directors and statutory auditors, other than those appointed pursuant to the special powers described above, is made through the "*voto di lista*" system. The "*voto di lista*" system is primarily aimed at ensuring that minority shareholders are represented on the Board of Directors and Board of Statutory Auditors. For the Board of Statutory Auditors, representation of minority shareholders is mandatory.

By the "*voto di lista*" system, the Board of Directors is elected on the basis of lists or slates of candidates presented by the shareholders or by the outgoing Board of Directors; candidates are listed by means of progressive numbers. Each shareholder may submit only one slate, and each candidate may appear only on one slate. Only those shareholders who alone or together with other shareholders hold a total number of Shares representing at least 1% of the share capital entitled to vote at the Shareholders' Meeting may submit slates. Each person entitled to vote may vote for only one slate. Four-fifths of the directors to be elected are chosen from the slate that obtains a majority of the shareholders' vote in the progressive order in which they are listed on the slate. The remaining directors are chosen from the other slates; the votes obtained by the various slates are successively divided by one, two, three or four, depending on the number of directors to be chosen, and the quotients obtained are assigned progressively to candidates on each of these slates, in the order respectively specified on the slate. The quotients thus assigned to the candidates on the various slates are arranged in a single decreasing order. Those candidates who have obtained the highest quotients are elected to the Board of Directors.

The election of the Board of Statutory Auditors is governed by the same procedures used for the election of the Board of Directors as far as presentation, filing and publication of slates are concerned. If the Board of Statutory Auditors is composed of three members one member of the Board of Statutory Auditors must be taken from the minority slate that obtains the largest number of votes. Two members must be taken from the minority slates if the Board of Statutory Auditors is composed of more than three members.

DESCRIPTION OF AMERICAN DEPOSITARY RECEIPTS

The Company has entered into two Deposit Agreements among the Company, JPMorgan Chase Bank, as depositary, and the registered Holders from time to time of ADRs issued thereunder. The first such Deposit Agreement, dated as of February 14, 1995, provides for the deposit of Shares in registered form, par value €0.55 each and the issuance of the Ordinary Share ADSs; the second such Deposit Agreement, dated as of February 24, 1995 provides for the deposit of Savings Shares in registered form, par value €0.55 each and the issuance of the Savings Share ADSs. Because these agreements are otherwise substantially identical, such agreements (including all exhibits and amendments thereto) are referred to herein as the "Deposit Agreement", deposited Shares as well as deposited Savings Shares are referred to as "Shares", and the Ordinary Share ADSs or Savings Share ADSs, as the case may be, are referred to as the "ADSs". The following is a summary of the material provisions of the Deposit Agreement. This summary does not purport to be complete and is qualified in its entirety by reference to the Deposit Agreement. Copies of the Deposit Agreement are available for inspection at the principal office of the Depositary in New York (the "Principal New York Office"), which is presently located at 60 Wall Street, New York, New York 10260. Terms used herein and not otherwise defined shall have the respective meanings set forth in the Deposit Agreement.

ADRs evidencing ADSs are issuable by the Depositary pursuant to the terms of the Deposit Agreement. Each ADS represents, as of the date hereof, the right to receive ten Shares (in the case of each Ordinary Share ADS) or 10 Savings Shares (in the case of each Savings Share ADS) in each case deposited under the Deposit Agreement (together with any additional Shares deposited thereunder and all other securities, property and cash received and held thereunder at any time in respect of or in lieu of such deposited Shares, the "Deposited Securities") with the Custodian, currently the Milan office of JPMorgan Chase Bank (together with any successor or successors thereto, the "Custodian"). An ADR may evidence anynumber of ADSs. Only persons in whose names ADRs are registered on the books of the Depositary will be treated by the Depositary and the Company as Holders.

Deposit, Transfer and Withdrawal

In connection with the deposit of Shares under the Deposit Agreement, the Depositary or the Custodian may require the following in form satisfactory to it: (a) a written order directing the Depositary to execute and deliver to, or upon the written order of, the person or persons designated in such order an ADR or ADRs evidencing the number of ADSs representing such deposited Shares (a "Delivery Order"); (b) proper endorsements or duly executed instruments of transfer in respect of such Deposited Securities; (c) instruments assigning to the Custodian or its nominee any distribution on or in respect of such Deposited Securities or right to subscribe for additional Shares or indemnity therefor; and (d) proxies entitling the Custodian to vote such Deposited Securities until registered in its name. At the request, risk andexpense of any holder of Shares, and for the account of such holder, the Depositary may receive certificates for Shares to be deposited, together with any other documents and payments required under the Deposit Agreement, for the purpose of forwarding such Share certificates to the Custodian for deposit thereunder. As soon as practicable after the Custodian receives Deposited Securities pursuant to any such deposit or pursuant to any distribution upon Deposited Securities or change affecting Deposited Securities, the Custodian shall present such Deposited Securities for registration of transfer into the name of the Custodian or its nominee, to the extent such registration is practicable, at the cost and expense of the person making such deposit (or for whose benefit such deposit is made) and shall obtain evidence satisfactory to it of such registration. Deposited Securities shall be held by the Custodian for the account and to the order of the Depositary at such place or places and in such manner as the Depositary shall determine. The Depositary agrees to instruct the Custodian to place all Shares accepted for deposit into a segregated account separate from any Shares of the Company that may be held by such Custodian under any other depositary receipt facility relating to the Shares. Deposited Securities may be delivered by the Custodian to any person only under the circumstances expressly contemplated in the Deposit Agreement. Neither the Depositary nor the Custodian shall lend Deposited Securities.

After any such deposit of Shares, the Custodian shall notify the Depositary of such deposit and of the information contained in any related Delivery Order by letter, first class airmail postage prepaid, or, at the request, risk and expense of the person making the deposit, by cable, telex or facsimile transmission. After receiving such notice from the Custodian (or such other evidence as the Company may accept), the Depositary, subject to the Deposit Agreement, shall execute and deliver at the designated transfer office in the Borough of Manhattan, the City of New York (the "Transfer Office"), to or upon the order of any person named in such notice, an ADR or ADRs registered as requested and evidencing the aggregate ADSs to which such person is entitled.

Subject to the terms of the Deposit Agreement, the Depositary may so issue ADRs for delivery at the Transfer Office only against deposit with the Custodian of: (a) Shares in form satisfactory to the Custodian; (b) rights to receive Shares from the Company or any registrar, transfer agent, clearing agent or other entity recording Share ownership or transactions; or (c) other rights to receive Shares (until such Shares are actually deposited pursuant to (a) or (b) above, "Pre-released ADRs") only if (i) Pre-released ADRs are fully collateralized (marked to market daily) with cash or U.S. government securities held by the Depositary for the benefit of Holders (but such collateral shall not constitute Deposited Securities), (ii) each recipient of Pre-released ADRs agrees in writing with the Depositary that such recipient (a) owns such Shares, (b) assigns all beneficial right, title and interest therein to the Depositary, (c) holds such Shares for the account of the Depositary and (d) will deliver such Shares to the Custodian as soon as practicable and promptly upon demand therefor and (iii) all Pre-released ADRs evidence not more than 20% of all ADSs (excluding those evidenced by Pre-released ADRs). The Depositary may retain for its own account any earnings on collateral for Pre-released ADRs and its charges for issuance thereof. At the request, risk and expense of the person depositing Shares, the Depositary may accept deposits for forwarding to the Custodian and may deliver ADRs at a place other than its office. Every person depositing Shares under the Deposit Agreement represents and warrants that such Shares are validly issued and outstanding, fully paid, non-assessable and free of preemptive rights, that the person making such deposit is duly authorized so to do and that such Shares are not restricted securities as such term is defined in Rule 144 under the Securities Act. Such representations and warranties shall survive the deposit of Shares and issuance of ADRs.

Subject to the terms and conditions of the Deposit Agreement, upon surrender of ADRs in form satisfactory to the Depositary at the Transfer Office, the Holder is entitled to delivery at the Custodian's office of the Deposited Securities at the time represented by the ADSs evidenced thereby. At the request, risk and expense of the Holder of an ADR, the Depositary may deliver such Deposited Securities at such other place as may have been requested by the Holder.

Distributions on Deposited Securities

Subject to the terms and conditions of the Deposit Agreement, to the extent practicable, the Depositary will distribute by mail to each Holder entitled thereto on the record date set by the Depositary therefor at such Holder's address shown on the ADR Register, in proportion to the number of Deposited Securities (on which the following distributions on Deposited Securities are received by the Custodian) represented by ADRs evidenced by such Holder's ADSs:

(a) Cash. Any U.S. dollars available to the Depositary resulting from a cash dividend or other cash distribution or authorized portion thereof ("Cash"), on an averaged, if possible, or other practicable basis, subject to appropriate adjustments for (i) taxes withheld, (ii) such distribution being impermissible or impracticable with respect to certain Holders, and (iii) deduction of the Depositary's expenses in (1) converting any foreign currency to U.S. dollars by sale or in such other manner as the Depositary may determine to the extent that it determines that such conversion may be made on a reasonable basis, (2) transferring foreign currency or U.S. dollars to the United States by such means as the Depositary may determine to the extent that it determines that such transfer may be made on a reasonable basis, (3) obtaining any approval or license of any governmental authority required for such conversion or transfer, which is obtainable at a reasonable cost and within a reasonable time and (4) making any sale by public or private means in any commercially reasonable manner.

(b) Shares. (i) Additional ADRs evidencing whole ADSs representing any Shares available to the Depositary resulting from a dividend or free distribution on Deposited Securities consisting of Shares (a "Share Distribution") and (ii) U.S. dollars available to it resulting from the net proceeds of sales of Shares received in a Share Distribution, which Shares would give rise to fractional ADSs if additional ADRs were issued therefor, as in the case of Cash.

(c) Rights. (i) Warrants or other instruments in the discretion of the Depositary after consultation with the Company, to the extent practicable, representing rights to acquire additional ADRs in respect of any rights to subscribe for additional Shares or rights of any nature available to the Depositary as a result of a distribution on

Deposited Securities ("Rights"), to the extent that the Company timely furnishes to the Depositary evidence satisfactory to the Depositary that the Depositary may lawfully distribute same (the Company has no obligation to so furnish such evidence), or (ii) to the extent the Company does not so furnish such evidence and sales of Rights are practicable, any U.S. dollars available to the Depositary from the net proceeds of sales of Rights as in the case of Cash, or (iii) to the extent the Company does not so furnish such evidence and such sales cannot practicably be accomplished by reason of the non-transferability of the Rights, limited markets therefor, their short duration or otherwise, nothing (and any Rights may lapse).

(d) Other Distributions. (i) Securities or property available to the Depositary resulting from any distribution on Deposited Securities other than Cash, Share Distributions and Rights ("Other Distributions"), by any means that the Depositary may deem equitable and practicable, or (ii) to the extent the Depositary deems distribution of such securities or property not to be equitable and practicable, any U.S. dollars available to the Depositary from the net proceeds of sales of Other Distributions as in the case of Cash. Such U.S. dollars available will be distributed by checks drawn on a bank in the United States for whole dollars and cents (any fractional cents being withheld without liability for interest and added to future Cash distributions).

To the extent that the Depositary determines in its discretion that any distribution is not practicable with respect to any Holder, the Depositary, after consultation with the Company, may make such distribution as it so deems practicable, including the distribution of foreign currency, securities or property (or appropriate documents evidencing the right to receive foreign currency, securities or property) or the retention thereof as Deposited Securities with respect to such Holder's ADRs (without liability for interest thereon or the investment thereof)

There can be no assurance that the Depositary will be able to effect any currency conversion or to sell or otherwise dispose of any distributed or offered property, subscription or other rights, Shares or other securities in a timely manner or at a specified rate or price, as the case may be.

Disclosure of Interests

To the extent that the provisions of or governing any Deposited Securities may require disclosure of or impose limits on beneficial or other ownership of Deposited Securities, other Shares and other securities and may provide for blocking transfer, voting or other rights to enforce such disclosure or limits, Holders and all persons holding ADRs agree to comply with all such disclosure requirements and ownership limitations and to cooperate with the Depositary in the Depositary's compliance with any Company instructions in respect thereof, and the Depositary will use reasonable efforts to comply with such Company instructions.

Record Dates

The Depositary shall, after consultation with the Company, if practicable, fix a record date (which shall be as near as practicable to any corresponding record date set by the Company) for the determination of the Holders who shall be entitled to receive any distribution on or in respect of Deposited Securities, to give instructions for the exercise of any voting rights, to receive any notice or to act in respect of other matters and only such Holders at the close of business on such record date shall be so entitled.

Voting of Deposited Securities

Upon receipt of notice of any meeting or solicitation of consents or proxies of holders of Deposited Securities the Depositary will, unless otherwise instructed by the Company, promptly thereafter, mail to all Holders a notice containing (i) the information (or a summarythereof in a form provided by the Company) included in any such notice received by the Depositary, including the agenda for the meeting, (ii) a statement that the Holders as of the close of business on a specified record date will be entitled, subject to applicable provisions of Italian law and of the Company's Certificate of Incorporation and Bylaws (any such provisions will be adequately summarized in such notice in a form provided by the Company), to instruct the Depositary as to the exercise of voting rights, if any, pertaining to the number of Deposited Securities represented by their respective ADSs, (iii) a statement as to the manner in which such instructions may be given, and (iv) a statement (in a form provided by the Company) as to the arrangements required in order to request that the Depositary obtain the issue of such proper document as would permit the Holder to vote the underlying Deposited Securities in the name of the said Holder. Upon the written delivery of instructions by a Holder on such record date, received on or before the date established by the Depositary for such purpose, the Depositary shall endeavor insofar as practicable and permitted under the provisions of or governing the Deposited Securities represented by the ADSs, including without limitation Italian law and the Certificate of Incorporation and Bylaws of the Company to cause to be voted the Shares represented by the ADSs evidenced by such Holder's ADRs in accordance with any instructions set forth in such request. In addition, in accordance with Italian law and the Certificate of Incorporation and Bylaws of the Company, a precondition for exercising any voting rights with respect to any Shares is that such Holder deposit in a blocked account established for such purpose the relevant ADS at least five days prior to the date of the related shareholders' meeting.

The Depositary also agrees that, upon written request of a Holder received on or before the date established by the Depositary for such purpose, requesting that the Depositary obtain the issue of the proper document to enable him to vote, it shall use its reasonable efforts to obtain the issuance of such document as early as reasonably practicable prior to such meeting.

The Depositary shall not itself vote or attempt to exercise the right to vote that attaches to Deposited Securities other than in accordance with instructions received from a Holder as set forth above.

A Holder desiring to exercise voting rights on the basis of the document referred to above with respect to the Shares represented by its ADSs may do so by (a) depositing its ADRs in a blocked account with the Depositary until the completion of such meeting and (b) instructing the Depositary to (i) furnish the Custodian with the name and address of such Holder, the number of ADSs represented by ADRs held by such Holder and any other information required in accordance with Italian law or the Company's Certificate of Incorporation and Bylaws and (ii) notify the Custodian of such deposit.

The Depositary and the Company may modify or amend the above voting procedures or adopt additional voting procedures from time to time as they determine may be necessary or appropriate to comply with mandatory provisions of Italian law and the Certificate of Incorporation and Bylaws of the Company and interpretations thereof. There can be no assurance that such amendments, modifications or additional voting procedures will not limit the practical ability of Holders to exercise voting rights in respect of the Shares represented by the ADSs.

Under Italian law, shareholders at Shareholders' Meetings may modify the resolutions presented for their approval by the Board of Directors. In such case Holders who have given prior instructions to vote on such resolution will be deemed to have elected to have abstained from voting on any such revised resolution.

When the Company makes its annual accounts available at its offices in connection with a general meeting of shareholders at which a vote will be taken on such accounts, the Company will deliver to the Depositary and the Custodian copies of such accounts. Until such meeting, the Depositary will make available copies of such accounts for inspection at the office of the Depositary in New York, the office of the Custodian in Milan, Italy and any other designated transfer offices.

The Depositary and the Company agree to use reasonable efforts to make and maintain arrangements to enable Holders to vote the Shares underlying their ADRs.

Inspection of Transfer Books

The Deposit Agreement provides that the Depositary or its agent will keep books at its Transfer Office for the registration, registration of transfer, combination and split-up of ADRs, which at all reasonable times will be open for inspection by the Holders and the Company for the purpose of communicating with Holders in the interest of the business of the Company or a matter related to the Deposit Agreement.

Reports and Other Communications

The Deposit Agreement, the provisions of or governing Deposited Securities and any written communications from the Company, which are both received by the Custodian or its nominee as a holder of Deposited Securities and made generally available to the holders of Deposited Securities, are available for inspection by Holders at the offices of the Depositary and the Custodian and at the Transfer Office. The Depositary will mail copies of such communications (or English translations or summaries thereof) to Holders when furnished by the Company.

On or before the first date on which the Company makes any communication available to holders of Deposited Securities or any securities regulatory authority or stock exchange, by publication or otherwise, the Company shall transmit to the Depositary a copy thereof in English or with an English translation or summary. The Company has delivered to the Depositary, the Custodian and any Transfer Office, a copy of all provisions of or governing the Shares (other than copies of Italian law) and any other Deposited Securities issued by the Company or any affiliate of the Company, if any, and, promptly upon any change thereto, the Company shall deliver to the Depositary, the Custodian and any Transfer Office, a copy (in English or with an English translation) of such provisions (other than copies of Italian law) as so changed.

Changes Affecting Deposited Securities

Subject to the terms of the Deposit Agreement and the ADRs, the Depositary may, in its discretion, upon consultation with the Company, if practicable, amend the ADRs or distribute additional or amended ADRs (with or without calling ADRs for exchange) or cash, securities or property on the record date set by the Depositary therefor to reflect any change in par value, split-up, consolidation, cancellation or other reclassification of Deposited Securities, any Share Distribution or Other Distribution not distributed to Holders or any cash, securities or property available to the Depositary in respect of Deposited Securities from (and the Depositary is hereby authorized to surrender any Deposited Securities to any person and to sell by public or private sale any property received in connection with) any recapitalization, reorganization, merger, consolidation, liquidation, receivership, bankruptcy or sale of all or substantially all the assets of the Company, and to the extent the Depositary does not so amend the ADRs or make a distribution to Holders to reflect any of the foregoing, or the net proceeds thereof, whatever cash, securities or property results from any of the foregoing shall constitute Deposited Securities and each ADS evidenced by ADRs shall automatically represent its *pro rata* interest in the Deposited Securities as then constituted.

Amendment and Termination of Deposit Agreement

The ADRs and the Deposit Agreement may be amended by the Company and the Depositary, provided that any amendment that imposes or increases any fees or charges (other than stock transfer or other taxes and other governmental charges, cable, telex and facsimile transmission and delivery charges incurred at the request of persons depositing, or Holders delivering Shares, ADRs or Deposited Securities, transfer or registration fees for the registration of transfer of Deposited Securities on any applicable register in connection with the deposit or withdrawal of Deposited Securities and expenses of the Depositary in connection with the conversion of foreign currency into U.S. dollars), or that shall otherwise prejudice any substantial existing right of Holders, shall become effective 30 days after notice of such amendment shall have been given to the Holders. Every Holder of an ADR at the time any amendment so becomes effective shall be deemed, by continuing to hold such ADR, to consent and agree to such amendment and to be bound by the Deposit Agreement and the ADRs as amended thereby.

The Depositary shall, at the written direction of the Company, terminate the Deposit Agreement and the ADRs by mailing notice of such termination to the Holders at least 30 days prior to the date fixed in such notice for such termination. The Depositary may likewise terminate the Deposit Agreement if at any time 90 days shall have expired after the Depositary shall have delivered to the Company a written notice of its election to resign and a successor depositary shall not have been appointed and accepted its appointment within such 90 days. After the date so fixed for termination, the Depositary and its agents will perform no further acts under the Deposit Agreement and the ADRs, except to advise Holders of such termination, receive and hold (or sell) distributions on Deposited Securities and deliver Deposited Securities being withdrawn. As soon as practicable after the expiration of six months from the date so fixed for termination, the Depositary shall sell the Deposited Securities and shall thereafter (as long as it may lawfully do so) hold in a segregated account the net proceeds of such sales, together with any other cash then held by it under the Deposit Agreement, without liability for interest, in trust for the *pro rata* benefit of the Holders of ADRs not theretofore surrendered. After making such sale, the Depositary shall be discharged from all obligations in respect of the Deposit Agreement and the ADRs, except for any indemnification obligations to the Company and to account for such net proceeds and other cash. After the date so fixed for termination, the

Company shall be discharged from all obligations under the Deposit Agreement except for its obligations to the Depositary and its agents.

Charges of Depositary

The Depositary may charge each person to whom ADRs are issued against deposits of Shares, including deposits in respect of Share Distributions, Rights and Other Distributions, and each person surrendering ADRs for withdrawal of Deposited Securities, U.S. $5.00 for each 100 ADSs (or portion thereof) evidenced by the ADRs delivered or surrendered. The Company will pay all other charges and expenses of the Depositary and any agent of the Depositary (except the Custodian) pursuant to agreements from time to time between the Company and the Depositary, except (i) stock transfer or other taxes and other governmental charges (which are payable by Holders or persons depositing Shares), (ii) cable, telex and facsimile transmission and delivery charges incurred at the request of persons depositing, or Holders delivering Shares, ADRs or Deposited Securities (which are payable by such persons or Holders), (iii) transfer or registration fees for the registration of transfer of Deposited Securities on any applicable register in connection with the deposit or withdrawal of Deposited Securities (which are payable by persons depositing Shares or Holders withdrawing Deposited Securities; there are no such fees in respect of the Shares as of the date of the Deposit Agreement) and (iv) expenses of the Depositary in connection with the conversion of foreign currency into U.S. dollars (which are paid out of such foreign currency). These charges may be changed as permitted in the Deposit Agreement.

Liability of Holders for Taxes

If any tax or other governmental charge shall become payable by or on behalf of the Custodian or the Depositary with respect to an ADR, any Deposited Securities represented by the ADSs evidenced thereby or any distribution thereon, such tax or other governmental charge shall be paid by the Holder thereof to the Depositary. The Depositary may refuse to effect any registration, registration of transfer, split-up or combination or, only for those reasons set forth in General Instruction I.A.(1) of Form F-6 under the Securities Act, any withdrawal of Deposited Securities until such payment is made. The Depositary may also deduct from any distributions on or in respect of Deposited Securities, or may sell by public or private sale for the account of the respective Holder any part or all of such Deposited Securities (after attempting by reasonable means to notify the Holder thereof prior to such sale), and may apply such deduction or the proceeds of any such sale in payment of such tax or other governmental charge, the respective Holder remaining liable for any deficiency, and shall reduce the number of ADSs evidenced thereby to reflect any such sales of Shares.

In connection with any distribution to Holders, the Company or its agent will remit to the appropriate governmental authority or agency all amounts (if any) required under applicable law to be withheld and remitted by the Company or such agent and owing to such governmental authority or agency by the Company or such agent; and the Depositary and the Custodian will remit to the appropriate governmental authority or agency all amounts (if any) required to be withheld and remitted by the Depositary or the Custodian and owing to such authority or agency by the Depositary or the Custodian. The Depositary shall forward to the Company or its agent such information from its records as the Company may request to enable the Company or its agent to file necessary reports with governmental authorities or agencies. In the event that the Depositary determines that any distribution in property other than cash (including Shares and rights to subscribe therefor) is subject to any tax or other governmental charge which the Depositary is obligated to withhold, the Depositary may by public or private sale dispose of all or a portion of such property (including Shares and rights to subscribe therefor) in such amounts and in such manner as the Depositary deems necessary and practicable to pay any such taxes or charges and the Depositary shall distribute the net proceeds of any such sale or the balance of any such property after deduction of such taxes or charges to the Holders entitled thereto as in the case of a distribution of Cash.

The Depositary and the Company agree to use reasonable efforts to make and maintain arrangements to enable persons that are considered United States residents for purposes of applicable law to receive any rebates, tax credits or other benefits (pursuant to treaty or otherwise) relating to distributions on the ADSs to which such persons are entitled. Notwithstanding the above, the Company may, by written notice to the Depositary, modify or withdraw the procedures described in this paragraph (including by ceasing to pay to the Depositary any amounts in respect of refunds of Italian withholding taxes), to the extent the Company determines that its participation in the refund process is no longer lawful or practical.

See "—Taxation" for additional information on tax issues relating to ADRs.

General Limitations

The Depositary, the Company, their agents and each of them shall: (a) incur no liability (i) if any present or future law, regulation, the provisions of or governing any Deposited Security, act of God, war or other circumstance beyond its control shall prevent, delay or subject to any civil or criminal penalty any act which the Deposit Agreement or the ADRs provides shall be done or performed by it, or (ii) by reason of any exercise or failure to exercise any discretion given it in the Deposit Agreement or the ADRs; (b) assume no liability except to perform its obligations to the extent they are specifically set forth in the ADRs and the Deposit Agreement without gross negligence or bad faith; (c) be under no obligation to appear in, prosecute or defend any action, suit or other proceeding in respect of any Deposited Securities or the ADRs; or (d) not be liable for any action or inaction by it in reliance upon the advice of or information from legal counsel, accountants, any person presenting Shares for deposit, any Holder, or any other person believed by it in good faith to be competent to give such advice or information. The Depositary, its agents and the Company may rely and shall be protected in acting upon any written notice, request, direction or other document believed by them in good faith to be genuine and to have been signed or presented by the proper party or parties. The Depositary and its agents will not be responsible for any failure to carry out any instructions to vote any of the Deposited Securities (provided such action or omission is in good faith), for the manner in which any such vote is cast or for the effect of any such vote. The Depositary and its agents may own and deal in any class of securities of the Company and its affiliates and in ADRs. The Company has agreed to indemnify the Depositary and its agents under certain circumstances and the Depositary has agreed to indemnify the Company against losses incurred by the Company to the extent such losses are due to the negligence or bad faith of the Depositary.

Prior to the issue, registration, registration of transfer, split-up or combination of any ADR, the delivery of any distribution in respect thereof, or, subject to the last sentence of this paragraph, the withdrawal of any Deposited Securities, and from time to time, the Company, the Depositary or the Custodian may require: (a) payment with respect thereto of (i) any stock transfer or other tax or other governmental charge, (ii) any stock transfer or registration fees in effect for the registration of transfers of Shares or other Deposited Securities upon any applicable register and (iii) any applicable charges; (b) the production of proof satisfactory to it of (i) the identity and genuineness of any signature and (ii) such other information, including without limitation, information as to citizenship, residence, exchange control approval, beneficial ownership of any securities, compliance with applicable law, regulations, provisions of or governing Deposited Securities and terms of the Deposit Agreement and the ADRs, as it may deem necessary or proper; and (c) compliance with such regulations as the Depositary may establish consistent with the Deposit Agreement. The Depositary shall provide to the Company, promptly upon its written request, copies of any such proofs of citizenship or residence or other information referred to in (b) above so requested. The issuance of ADRs, the acceptance of deposits of Shares, the registration, registration of transfer, split-up or combination of ADRs or, subject to the last sentence of this paragraph, the withdrawal of Deposited Securities may be suspended, generally or in particular instances, when the ADR register or any register for Deposited Securities is closed or when any such action is deemed necessary or advisable by the Depositary or the Company. Notwithstanding any other provision of the Deposit Agreement or the ADRs, the withdrawal of Deposited Securities may be restricted only for the reasons set forth in General Instruction I.A.(1) of Form F-6 (as such instructions may be amended from time to time) under the Securities Act.

Governing Law

The Deposit Agreement is governed by and shall be construed in accordance with the laws of the State of New York.

JPMorgan Chase Bank

The Depositary is JPMorgan Chase Bank, a New York banking corporation, which has its principal office located in New York, New York. JPMorgan Chase Bank is a commercial bank offering a wide range of banking and trust services to its customers in the New York metropolitan area, throughout the United States and around the world.

The Consolidated Balance Sheets of J.P. Morgan Chase & Co. Incorporated ("J.P. Morgan"), the parent corporation of JPMorgan Chase Bank , are set forth in the most recent Annual Report and Form 10-Q. The Annual Report, Form 10-K and Form 10-Q of J.P. Morgan are on file with the SEC.

The Articles of Association of JPMorgan Chase Bank and Bylaws together with the annual report, Form 10-K and Form 10-Q of J.P. Morgan are available for inspection at the Principal New York Office of the Depositary.

TAXATION

Unless otherwise indicated, for purposes of the following discussion regarding taxation the Shares and the Savings Shares are collectively referred to as the "Telecom Italia Shares."

Italian Taxation

The following is a summary of certain Italian tax consequences of the purchase, ownership and disposition of Shares, Savings Shares or ADRs as at the date hereof. It does not purport to be a complete analysis of all potential tax matters relevant to a decision to hold Shares, Savings Shares or ADRs. For purposes of Italian law and the Italian-U.S. income tax convention (the "Treaty"), holders of American Depositary Shares which are evidenced by ADRs will be treated as holders of the underlying Shares or Savings Shares, as the case may be.

Income Tax

Savings Shares, Shares and ADRs. Under Italian law dividends paid to holders of Savings Shares and applicable ADRs who are not Italian residents and do not have a permanent establishment in Italy to which dividends are connected are subject to a 12.5% withholding tax.

With respect to dividends paid to beneficial holders of Shares and ADRs who are not Italian residents and do not have a permanent establishment in Italy to which dividends are connected, Italian law provides for a 27% withholding tax on dividends paid.

Under Italian law, all shares of Italian listed companies have to be registered in a centralized deposit system. With respect to dividends paid in connection with shares held in the centralized deposit system managed by Monte Titoli, such as Telecom Italia Shares, instead of the 27% or 12.5% withholding taxes mentioned above, a substitute tax will apply at the same tax rates as the above-mentioned withholding taxes. This substitute tax is levied by the Italian authorized intermediaries participating in the Monte Titoli system and with whom the securities are deposited and also by non-Italian authorized intermediaries participating, directly or through a non-Italian centralized deposit system, in the Monte Titoli system.

Non-resident holders of Shares and ADRs have the right to recover, up to four-ninths of the 27% substitute tax on their dividend income, the income tax paid in their home country on the same dividend income providing adequate evidence, within 48 months from the date of payment of the foreign income tax.

These refunds are normally subject to extensive delays. In addition, these refunds are an alternative to seeking any relief from double taxation under the Treaty.

U.S. resident owners of Shares and ADRs may be entitled to reduced rates of tax on their dividends under the Treaty. Under circumstances where a U.S. resident owner is the actual beneficiary of the dividends and the dividends paid are not connected with a permanent establishment in Italy through which the U.S. resident owner carries on a business or with a fixed base in Italy through which the U.S. resident owner performs independent personal services, the Treaty provides that Italian taxes cannot exceed 15% of gross dividends.

To qualify for the reduced tax rate afforded by the Treaty, a beneficial owner of Shares or ADRs must provide the intermediary with which the shares are deposited and which participates in the Monte Titoli system with the following:

(i) a declaration by the beneficial owner containing all the data identifying this person as the beneficial owner and establishing the existence of all the conditions necessary for the application of the Treaty; and

(ii) a certification (Form 6166) issued by the U.S. Internal Revenue Service that states that the beneficial owner is a U.S. resident for tax purposes. The certification is valid until March 31 of the year following the submission.

The time for processing requests for certification by the U.S. Internal Revenue Service normally is six to eight weeks. Accordingly, in order to be eligible for the procedure described below, eligible ADR holders should begin the process of obtaining Form 6166 as soon as possible after receiving instructions from the Depositary on how to claim the reduced rate provided by the Treaty.

The Depositary' s instructions, which will be sent to all ADR holders before the dividend payment date, will specify certain deadlines for delivering to the Depositary any documentation required to obtain the reduced rate provided by the Treaty, including the certification that the eligible ADR holders must obtain from the U.S. Internal Revenue Service. In the case of ADRs held through a broker or other financial intermediary, the required documentation should be delivered to such financial intermediary for transmission to the Depositary. In all other cases, the eligible ADR holders should deliver the required documentation directly to the Depositary.

If the holder of Shares or ADRs fails to obtain the reduced rate provided by the Treaty, a refund equal to the difference between the Treaty rate and the Italian 27% tax must be claimed directly from the Italian tax authorities. Extensive delays have been encountered by U.S. residents seeking payments directly from the Italian authorities pursuant to the Treaty.

In the case of dividends derived by a U.S. partnership, the reduction of the tax rate under the Treaty is only available to the extent such dividends are subject to U.S. tax in the hands of the partners.

Transfer Tax

No transfer tax is payable upon the transfer of Telecom Italia Shares through Telematico. Other types of transfers of shares listed on Telematico and ADSs are also exempted from the payment of transfer tax provided that the parties entering into the agreement pursuant to which the transfer takes place are (i) banks, Italian securities dealing firms ("SIMs") exchange agents or (ii) banks, SIMs or exchange agents on the one hand, and non-residents on the other hand or (iii) banks, SIMs or resident or non-resident exchange agents, on the one hand, and investment funds on the other hand. In any other case, transfer tax is currently payable at the following rates:

- €0.072 per €51.646 (or any fraction) of the price at which the shares or ADSs are transferred when the transfer is made between private individuals directly or through an intermediary that is not a bank, SIM or exchange agent;

- €0.026 per €51.646 (or any fraction) of the price at which the shares or ADSs are transferred when the transfer is made either (i) between bank, SIM or exchange agent and a private individual or (ii) between private individuals through a bank, SIM or exchange agent; and

- €0.006 per €51.646 (or any fraction) of the price at which the shares or ADSs are transferred when the transfer is made between banks, SIMs or exchange agents.

The mere change of the depositary (*e.g.*, Euroclear, Clearstream, Monte Titoli, DTC or the Depositary) not involving a transfer of the ownership of the transferred shares will not trigger the Italian transfer tax.

Capital Gains Tax

Under Italian law, capital gains tax ("CGT") is levied on capital gains realized by non-residents from the disposition of shares in companies resident in Italy for tax purposes even if those shares are held outside of Italy. Capital gains realized on the sale of qualified shareholdings (as described below) are subject to CGT at a rate of 27%. All other capital gains are subject to CGT at a rate of 12.5%. Capital gains realized by non-resident holders on the sale of non-qualified shareholdings in companies listed on a stock exchange and resident in Italy for tax purposes are not subject to CGT.

In addition, with respect to these non-resident holders, Telecom Italia could require a simple declaration in which they have to declare that they are U.S. residents for tax purposes.

A "qualified shareholding" consists of securities that (i) entitle the holder to exercise more than 2% of the voting rights of a company with shares listed on a stock exchange (as is Telecom Italia's case) or 20% of the voting rights of other companies, in each case in the ordinary meeting of the shareholders or (ii) represent more than 5% of the share capital of a company with shares listed on a stock exchange (as is Telecom Italia's case) or 25% of the share capital of other companies.

The relevant percentage is calculated taking into account the holdings sold during a 12-month period. Where losses exceed gains, they can be carried forward for up to the fourth taxable period.

Pursuant to the Treaty, a U.S. resident will not be subject to CGT unless the Telecom Italia Shares or ADRs form part of the business property of a permanent establishment of the holder in Italy or pertain to a fixed base available to a holder in Italy for the purpose of performing independent personal services. U.S. residents who sell Telecom Italia Shares or ADRs may be required to produce appropriate documentation establishing that the above mentioned conditions of non-taxability pursuant to the Treaty have been satisfied if CGT would otherwise be applicable.

Inheritance and Gift Tax

A tax reform has abolished the Italian inheritance tax, effective 2001.

Gift tax is payable on transfers of shares of Italian companies by reason of donation, regardless of the residence of the donor and even if the shares are held outside Italy, the application of Italian gift tax depends upon the value of the gift and the relationship between the donee and the donor.

There is currently no gift tax convention between Italy and the United States.

United States Federal Income Taxation

The following summary describes the material U.S. federal income tax consequences of the acquisition, ownership and sale of Telecom Italia Shares, including Telecom Italia Shares represented by American Depositary Shares evidenced by ADRs, that are generally applicable to U.S. holders who own Telecom Italia Shares or ADRs as capital assets. For these purposes, you are a U.S. holder if you are:

- a citizen or resident of the United States for U.S. federal income tax purposes;
- a corporation, or other entity taxable as a corporation, organized under the laws of the United States or of any political subdivision of the United States; or
- an estate or trust the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source.

This discussion is based on the tax laws of the United States currently in effect, including the Internal Revenue Code of 1986, as amended, Treasury Regulations, administrative announcements, and judicial decisions, as well as the Italian-U.S. income tax convention (the "Treaty"). These laws may change, possibly with retroactive effect. This discussion does not address U.S. state, local or non-U.S. tax consequences. This discussion is based in part upon representations of the Depositary and assumes that each obligation provided for in, or otherwise contemplated by, the Deposit Agreement and any related agreement will be performed in accordance with its respective terms. The U.S. Treasury has expressed concerns that parties to whom ADRs are pre-released may be taking actions that are inconsistent with the claiming, by U.S. holders of ADRs, of foreign tax credits for U.S. federal income tax purposes. Accordingly, the analysis of the creditability of Italian taxes described below could be affected by future actions that may be taken by the U.S. Treasury.

Please note that this discussion does not address all of the tax consequences that may be relevant in light of your particular circumstances. In particular, it does not address purchasers subject to special rules, including:

- partnerships;

- persons subject to the alternative minimum tax;
- tax-exempt entities;
- dealers and traders in securities or foreign currencies;
- insurance companies;
- financial institutions;
- persons who own the Telecom Italia Shares or ADRs as part of an integrated investment, including a straddle, hedging or conversion transaction, comprised of the Telecom Italia Shares or ADRs and one or more other positions for tax purposes;
- persons whose functional currency is not the U.S. dollar; or
- persons who actually or constructively own 10% or more of the Company's voting stock.

Please consult your tax advisors with regard to the application of U.S. federal income tax laws to the Telecom Italia Shares or ADRs, and any tax consequences arising under the laws of any state, local or non-U.S. taxing jurisdictions. For U.S. federal income tax purposes, holders of ADRs evidencing American Depositary Shares will be treated as owners of the underlying Shares or Savings Shares, as the case may be, represented by those American Depositary Shares and the discussion of U.S. federal income tax consequences to holders of ADRs applies as well to holders of the underlying Shares or Savings Shares, as the case may be.

Taxation of dividends

Distributions made with respect to the Telecom Italia Shares or ADRs, before reduction for any Italian tax withheld, will generally constitute foreign source dividend income for U.S. federal income tax purposes to the extent such distributions are made from the Company's current or accumulated earnings and profits, as determined in accordance with U.S. federal income tax principles. You will not be entitled to claim a dividends-received deduction for dividends paid on the Telecom Italia Shares or ADRs. The amount of any cash distribution paid in euros, including the amount of any Italian tax withheld, will be equal to the U.S. dollar value of such euros on the date of receipt by the Depositary in the case of U.S. holders of ADRs, or by the U.S. holder in the case of U.S. holders of Telecom Italia Shares, regardless of whether the payment is in fact converted into U.S. dollars. Gain or loss, if any, recognized on the sale or other disposition of such euros will be U.S. source ordinary income or loss. The amount of any distribution of property other than cash will be the fair market value of such property on the date of distribution.

Subject to certain limitations and restrictions, Italian taxes withheld from distributions at the rate provided in the Treaty will be eligible for credit against a U.S. holder's U.S. federal income tax liability. Italian taxes withheld in excess of the rate provided in the Treaty will generally not be eligible for credit against a U.S. holder's federal income tax liability. Furthermore, you will not be allowed a foreign tax credit for foreign taxes withheld on distributions if you:

- have held the Telecom Italia Shares or ADRs for less than a specified minimum period during which you are not protected from risk of loss;
- are under an obligation to make related payments with respect to positions in "substantially similar or related property"; or
- hold the Telecom Italia Shares or ADRs in arrangements in which your expected economic profit, after non-U.S. taxes, is insubstantial.

The limitation on foreign taxes eligible for credit is calculated separately with respect to specific classes of income. For this purpose, dividends the Company distributes with respect to the Telecom Italia Shares or ADRs will generally constitute "passive income" or, in the case of certain U.S. holders, "financial services income". You should consult your tax advisor concerning the foreign tax credit implications of the payment of these withholding taxes.

Taxation of capital gains

You will recognize capital gain or loss for U.S. federal income tax purposes on the sale or exchange of Telecom Italia Shares or ADRs in the same manner as you would on the sale or exchange of any other shares of stock held as capital assets. As a result, you will generally recognize capital gain or loss for U.S. federal income tax purposes equal to the difference between the amount realized and your adjusted basis in the Telecom Italia Shares or ADRs. The gain or loss will generally be U.S. source income or loss. You should consult your own tax advisor about the treatment of capital gains, which may be taxed at lower rates than ordinary income for non-corporate taxpayers, and capital losses, the deductibility of which may be limited.

Information Reporting and Backup Withholding

You may, under certain circumstances, be subject to information reporting and backup withholding with respect to dividends or the proceeds of any sale, exchange or redemption of ADRs or Telecom Italia Shares unless you:

- are a corporation or come within certain other exempt categories, and, when required, demonstrate this fact, or

- provide a correct taxpayer identification number, certify that you are not subject to backup withholding and otherwise comply with applicable requirements of the backup withholding rules.

Any amount withheld under these rules will be creditable against your U.S. federal income tax liability if you provide the required information to the U.S. Internal Revenue Service. If you are required to and do not provide a correct taxpayer identification number, you may be subject to penalties imposed by the U.S. Internal Revenue Service.

Item 11. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

See "Item 5. Operating and Financial Review and Prospects—Quantitative and Qualitative Disclosure About Market Risk".

Item 12. DESCRIPTION OF SECURITIES OTHER THAN EQUITY SECURITIES

Not applicable.

PART II

Item 13. DEFAULTS, DIVIDEND ARREARAGES AND DELINQUENCIES

Not applicable.

Item 14. MATERIAL MODIFICATION TO THE RIGHTS OF SECURITY HOLDERS AND USE OF PROCEEDS

Not applicable.

Item 15. [Reserved]

Item 16. [Reserved]

PART III

Item 17. FINANCIAL STATEMENTS

Not applicable.

Item 18. FINANCIAL STATEMENTS

Reference is made to Item 19 for a list of all financial statements filed as part of this Annual Report.

Item 19. FINANCIAL STATEMENTS AND EXHIBITS

(a) Financial Statements

(b) Exhibits

1.1 Bylaws of the Company.

2.1 Deposit Agreements.

(a) Deposit Agreement dated as of February 14, 1995, as amended, among the Company, Morgan Guaranty Trust Company of New York (now JPMorgan Chase Bank), as Depositary and the holders from time to time of American Depositary Receipts representing Ordinary Shares of the Company. *

(b) Deposit Agreement dated as of February 28, 1995, as amended, among the Company, Morgan Guaranty Trust Company of New York (now JPMorgan Chase Bank), as Depositary and holders from time to time of American Depositary Receipts representing Savings shares of the Company. *

*2.2 Plan of Merger, dated as of March 24, 1997, between the Company and Telecom Italia S.p.A.**

*4.1 Public Telecommunications Licenses.***

(a) Decision No. 820/00/CONS of 22.11.2000

Individual license for installation and supply of public telecommunications networks and for the provision to the public of a voice telephony service (*modifications to the concessions and annexed conventions, ex SIP, Iritel and Italcable*).

(b) Decision No. 821/00/CONS of 22.11.2000

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* Incorporated by reference to the Exhibits filed with the Company's Registration Statement on Form 20-F/A on July 27, 1995 (Registration No. 1-13882).

** Incorporated by reference to the Exhibits filed with the Company's Registration Statement on Form 20-F/A on June 29, 2001.

Authorization for supply of network and satellite communication services (*modification to the concession and annexed* convention *ex Telespazio*).

(c) Decision No. 738/00/CONS of 15.11.2000

Individual licence for establishment and operation of a network of coastal stations to provide mobile maritime services and ground stations to provide mobile service via Inmarsat satellites (*modification to the concession and annexed convention ex Intel*).

(d) Decision No. 737/00/CONS of 15.11.2000

Individual license for establishment and operation of on board radio electrical stations and supply of mobile maritime services and mobile service via satellite through Inmarsat terminals (*modification to the concession and annexed convention ex SIRM*).

10(a) *Reports and consents of Auditors*

(i) Consent of Reconta Ernst and Young S.p.A., Independent Accountants, dated June 25, 2002, relating to the independent audit report on the consolidated financial statements of Telecom Italia S.p.A. for the fiscal year ended December 31, 2001;

(ii) Consent of PricewaterhouseCoopers S.p.A., Independent Accountants, dated June 25, 2002, relating to the independent audit report on the consolidated financial statements of Finsiel *Consulenza e Applicazioni Informatiche* S.p.A. for the fiscal year ended December 31, 2001;

(iii) Consent of Deloitte & Touche Sociedad de Auditores y Consultores Limitada, Independent Accountants, dated June 24, 2002, relating to the independent audit report on the consolidated financial statements of Empresa Nacional de Telecomunicaciones S.A. for the fiscal year ended December 31, 2001;

(iv) Consent of KPMG Austria GmbH and Grant Thornton - Jonasch & Platzer, Independent Accountants, dated June 24, 2002, relating to the independent audit report on the combined consolidated financial statements of Mobilkom Austria A.G. for the fiscal year ended December 31, 2001;

(v) Consent of KPMG Austria GmbH and Grant Thornton - Jonasch & Platzer, Independent Accountants, dated June 24, 2002, relating to the independent audit report on the consolidated financial statements of Telekom Austria A.G. for the fiscal year ended December 31, 2001;

(vi) Consent of PricewaterhouseCoopers, Independent Accountants, dated June 24, 2002, relating to the independent audit report on the financial statements of IS - TIM Telekomunikasyon Hizmetleri A.S. for the fiscal year ended December 31, 2001;

(vii) Consent of PricewaterhouseCoopers S.p.A., Independent Accountants, dated June 25, 2002, relating to the independent audit report on the consolidated financial statements of Telecom Italia S.p.A. for the fiscal year ended December 31, 2000;

(viii) Consent of Arthur Andersen S.p.A., Independent Accountants, dated June 25, 2002, relating to the independent audit report on the consolidated financial statements of Telecom Italia Mobile S.p.A. for the fiscal year ended December 31, 2000;

(ix) Consent of Arthur Andersen S.p.A., Independent Accountants, dated June 25, 2002, relating to the independent audit report on the consolidated financial statements of Telecom Italia S.p.A. for the fiscal year ended December 31, 1999;

(x) Consent of Deloitte & Touche S.p.A., Independent Accountants, dated June 24, 2002, relating to the independent audit report on the consolidated financial statements of Finsiel *Consulenza e Applicazioni Informatiche* S.p.A. for the fiscal year ended December 31, 1999;

(xi) Consent of Deloitte & Touche S.p.A., Independent Accountants, dated June 24, 2002, relating to the independent audit report on the consolidated financial statements of Sirti S.p.A. for the fiscal year ended December 31, 1999;

(xii) Consent of PricewaterhouseCoopers S.p.A., Independent Accountants, dated June 24, 2002, relating to the independent audit report on the consolidated financial statements of Italtel S.p.A. for the fiscal year ended December 31, 1999.

SIGNATURE

Pursuant to the requirements of Section 12 of the Securities Exchange Act of 1934, the registrant certifies that it meets all the requirements for filing on Form 20-F and has duly caused this Annual Report to be signed on its behalf by the undersigned, thereunto duly authorized.

TELECOM ITALIA S.p.A.

By: /s/ Carlo Orazio Buora
Chief Executive Officer

Dated June 28, 2002

RECONTA ERNST & YOUNG

Corso Vittorio Emanuele II, 83
10128 Torino

Tel. (011) 5161611
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REPORT OF INDEPENDENT AUDITORS

To the Shareholders of
Telecom Italia S.p.A.

We have audited the accompanying consolidated balance sheet of Telecom Italia S.p.A., a subsidiary of Olivetti S.p.A., as of December 31, 2001, and the related consolidated statements of operations, shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the financial statements of certain consolidated subsidiaries and affiliated companies accounted for by the equity method of accounting, which statements reflect total assets and revenues constituting nine per cent and seven per cent, respectively, of the related consolidated totals. Those statements were audited by other auditors whose reports have been furnished to us, and our opinion, insofar as it relates to the data included for these companies, is based solely on the reports of those other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the reports of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Telecom Italia S.p.A. at December 31, 2001, and the consolidated results of its operations and its cash flows for the year then ended, in conformity with accounting principles established by the Italian accounting profession, which differ in certain respects from those followed in the United States (see Notes 26, 27 and 28 to the consolidated financial statements).

As described in Note 1 to the consolidated financial statements, effective January 1, 2001, the Company changed its method of accounting for its interest in the Nortel Inversora Group from the proportional consolidation method to the equity method.

Reconta Ernst & Young S.p.A.

Turin, Italy
June 19, 2002

Reconta Ernst & Young S.p.A.
Sede Legale: 00196 Roma - Via G. D. Romagnosi 18/A
Capitale Sociale € 1.043.330,00 i.v.
Iscritta alla S.O. del Registro delle Imprese presso la C.C.I.A.A. di Roma
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TELECOM ITALIA S.P.A.
CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2000 AND 2001

Millions of Euro

	December 31, 2000	December 31, 2001
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents (Note 4)	1,305	765
Marketable securities (Note 4)	2,456	2,191
Receivables (Note 5)	8,451	8,504
Inventories (Note 6)	725	636
Other current assets (Note 7)	3,458	4,640
TOTAL CURRENT ASSETS	16,395	16,736
Fixed assets	65,914	66,023
Less — accumulated depreciation	(42,489)	(44,266)
FIXED ASSETS, NET (Note 8)	23,425	21,757
INTANGIBLE ASSETS, NET (Note 9)	16,037	16,197
OTHER ASSETS (Note 10):	9,658	7,980
Investments in affiliates	7,598	6,586
Treasury stock	662	-
Securities	6	86
Other receivables	1,392	1,308
TOTAL ASSETS	65,515	62,670
LIABILITIES AND STOCKHOLDERS' EQUITY		
CURRENT LIABILITIES:		
Short term debt (Note 11)	15,136	9,114
Payables, trade and other (Note 12)	10,103	10,583
Accrued payroll and employee benefits	1,089	898
Accrued income taxes	295	150
Other accrued liabilities (Note 13)	859	1,200
TOTAL CURRENT LIABILITIES	27,482	21,945
LONG TERM DEBT (Note 11)	8,268	16,083
RESERVES AND OTHER LIABILITIES:		
Deferred income taxes	201	35
Other liabilities (Note 14)	2,716	3,948
Employee termination indemnities (Note 15)	1,319	1,350
TOTAL LIABILITIES	39,986	43,361
STOCKHOLDERS' EQUITY:		
Share capital (Note 16)	3,835	4,023
Additional paid-in capital	1,803	1,812
Reserves, retained earnings and profit (loss) of the year (Note 17)	13,183	7,687
Total stockholders' equity before minority interest	18,821	13,522
Minority interest	6,708	5,787
TOTAL STOCKHOLDERS' EQUITY	25,529	19,309
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	65,515	62,670

The accompanying notes to the consolidated financial statements are an integral part of these financial statements

TELECOM ITALIA S.P.A.
CONSOLIDATED STATEMENTS OF OPERATIONS
FOR THE YEARS ENDED DECEMBER 31, 1999, 2000 AND 2001

Millions of Euro

	1999	2000	2001
Operating revenues	27,104	28,911	30,818
Other income (Note 19)	516	426	417
Total revenues	27,620	29,337	31,235
Cost of materials	2,477	2,259	1,972
Salaries and social security contributions	4,977	5,025	4,666
Depreciation and amortization	5,339	5,647	6,275
Other external charges (Note 20)	9,586	10,790	12,171
Changes in inventories	(130)	(277)	58
Capitalized internal construction costs	(1,062)	(912)	(581)
Total operating expenses	21,187	22,532	24,561
Operating income	6,433	6,805	6,674
Financial income (Note 21)	555	847	1,076
Financial expense (Note 22)	(1,466)	(2,470)	(5,031)
Other income and (expense), net (Note 23)	(507)	(214)	(3,452)
Income (loss) before income taxes and minority interests	5,015	4,968	(733)
Income taxes (Note 24)	(2,606)	(2,020)	(925)
Net income (loss) before minority interests	2,409	2,948	(1,658)
Minority interest	(672)	(920)	(410)
Net income (loss)	1,737	2,028	(2,068)

The accompanying notes to the consolidated financial statements
are an integral part of these financial statements

TELECOM ITALIA S.P.A.
CONSOLIDATED STATEMENTS OF CASH FLOW
FOR THE YEARS ENDED DECEMBER 31, 1999, 2000 AND 2001

Millions of Euro

	1999	2000	2001
OPERATING ACTIVITIES:			
Net income (loss)	1,737	2,028	(2,068)
Minority interest	672	920	410
Depreciation and amortization	5,339	5,647	6,275
Net change in deferred taxes	(87)	51	(166)
(Gains) losses on disposals of fixed assets, intangibles and other long-term assets	60	(1,091)	(330)
Write-downs of fixed assets, intangibles and other long-term assets	614	1,134	4,039
Net change in other liabilities	(320)	704	1,232
Net change in reserve for employee termination indemnities	96	(177)	31
Changes in operating assets and liabilities	(279)	(3,776)	372
Other movements, net	151	112	(193)
Net cash flows from operating activities	7,983	5,552	9,602
INVESTING ACTIVITIES:			
Investments in fixed assets	(3,875)	(3,889)	(4,254)
Investment grants	66	27	22
Addition to goodwill	(567)	(9,109)	(1,174)
Addition to other intangible assets	(1,012)	(4,010)	(2,736)
Addition to other long-term assets	(1,300)	(3,001)	(3,093)
Changes in consolidation area (net cash flow from acquisitions and disposals)	-	77	17
Proceeds from sale, or redemption value, of intangible assets, fixed assets and long-term investments	549	4,311	1,439
Net cash flows used in investing activities	(6,139)	(15,594)	(9,779)
FINANCING ACTIVITIES:			
Changes in short-term debt	242	9,841	(6,068)
Increase in long-term debt	767	1,457	10,816
Repayment of and other changes to long-term debt	(1,334)	(1,754)	(2,254)
Paid in capital in subsidiaries	41	4,174	240
Dividends paid	(1,693)	(3,049)	(3,097)
Net cash flows from (used in) financing activities	(1,977)	10,669	(363)
Increase (decrease) in cash and cash equivalents	(133)	627	(540)
CASH AND CASH EQUIVALENTS:			
Beginning of year	811	678	1,305
End of year	678	1,305	765

The accompanying notes to the consolidated financial statements are an integral part of these financial statements

TELECOM ITALIA S.P.A.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 1999, 2000 AND 2001

Millions of Euro

	Attributable to Telecom Italia				Attributable to minority interest	
	Share Capital	Additional Paid in Capital	Reserves, retained earnings and Profit (loss) of the year	Total	Reserves, retained earnings and profit (loss) of the year	Total
BALANCES AS OF JANUARY 1, 1999	3,833	1,772	10,742	16,347	2,083	18,430
Dividends paid (Euro 0.1446 per ordinary share and Euro 0.1549 per savings share)	—	—	(1,095)	(1,095)	(355)	(1,450)
Distribution of reserves	—	—	—	—	(243)	(243)
Exercise of stock options	2	31	—	33	—	33
Consolidation on a line by line basis of Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes	—	—	—	—	559	559
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	23	23	27	50
Net income	—	—	1,737	1,737	672	2,409
BALANCES AS OF DECEMBER 31, 1999	3,835	1,803	11,407	17,045	2,743	19,788
Dividends paid (Euro 0.3114 per ordinary share and Euro 0.3218 per savings share)	—	—	(2,327)	(2,327)	(722)	(3,049)
Changes in consolidation area	—	—	370	370	1,076	1,446
Conversion of TIM's savings share	—	—	1,671	1,671	2,498	4,169
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	34	34	193	227
Net income	—	—	2,028	2,028	920	2,948
BALANCES AS OF DECEMBER 31, 2000	3,835	1,803	13,183	18,821	6,708	25,529
Effect of change in method of accounting for the investment in the Nortel Inversora Group	—	—	—	—	(837)	(837)
Dividends paid (Euro 0.3125 per ordinary share and Euro 0.3238 per savings share)	—	—	(2,309)	(2,309)	(788)	(3,097)
Exercise of stock options	1	9	—	10	—	10
Contribution by stockholders'	—	—	128	128	102	230
Cancellation of treasury stock and re-denomination of capital stock in Euro	187	—	(898)	(711)	—	(711)
Entel Chile group acquisition	—	—	—	—	358	358
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	(349)	(349)	(166)	(515)
Net income (loss)	—	—	(2,068)	(2,068)	410	(1,658)
BALANCES AS OF DECEMBER 31, 2001	4,023	1,812	7,687	13,522	5,787	19,309

The accompanying notes to the consolidated financial statements
are an integral part of these financial statements

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Note 1 — Form And Content of the Consolidated Financial Statements

The consolidated financial statements of Telecom Italia S.p.A. ("Telecom Italia") and its subsidiaries (the "Group") are prepared on the basis of the accounts of Telecom Italia and the financial statements of individual consolidated companies as of December 31, 2001 as approved by their respective Boards of Directors, adjusted, where necessary, to conform with the accounting policies adopted by Telecom Italia. The accounting policies are consistent with the Italian law related to consolidated financial statements interpreted and integrated by the accounting principles established or adopted by the Italian Accounting Profession (collectively, "Italian GAAP").

Italian GAAP differs in certain material respects from U.S. generally accepted accounting principles ("U.S. GAAP"). The effects of these differences on stockholders' equity as of December 31, 2000 and 2001 and on consolidated net income (loss) for each of the three years in the period ended December 31, 2001 are set forth in Note 26.

The consolidated financial statements and related notes as presented herein reflect certain reclassifications and disclosures to conform to an international presentation format, which differs from Telecom Italia's financial statements and disclosures which are prepared in accordance with Italian legal requirements. The format presented does not result in any modification of stockholders' equity and net income (loss) as reported on an Italian GAAP basis.

The consolidated financial statements of the Group include the financial statements of Telecom Italia and all Italian and foreign subsidiaries in which Telecom Italia holds, directly or indirectly, more than 50% of the voting capital or has dominant influence (effective control). Effective in 1999, Telecom Italia was acquired by Olivetti S.p.A. ("Olivetti"), an Italian company. As of December 31, 2001 Olivetti owned 54.96% of Telecom Italia.

Beginning with the consolidated financial statements for the year ended December 31, 2001, Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group), which in 2000 were consolidated proportionally as permitted by art. 37 of Legislative Decree No. 127/1991, have been accounted for using the equity method. Prior to 2000 the Nortel Inversora group had been accounted for by the equity method. The equity method of accounting for this investment provides a better representation since Telecom Italia owns a 50% voting interest in Nortel Inversora, which holds a 54.74 % interest in Telecom Argentina (the operating company) resulting in Telecom Italia indirectly owning 27.37% (voting shares) of the operating company, Telecom Argentina. This accounting change affected the classification of various amounts in the financial statements but had no effect on consolidated stockholder's equity of the Telecom Italia Group at January 1, 2001 nor on its consolidated net income (loss) for any period presented. However, it did have an effect on the classification of financial statement line items in the consolidated balance sheet and statement of operations. The tabulation below shows the effects on certain financial statements line items if the accounting change were applied retroactively to 2000.

Increase (decrease) - Amounts in millions of Euro

Balance sheet items	**December 31, 2000**	**Statement of operations items**	**Year ended December 31, 2000**
Current Assets	(722)	Total Revenues	(1,766)
Fixed assets, net	(2,704)	Operating Income	(364)
Intangible assets, net	(466)	Financial income and expense, net	168
Other assets	362	Other income and (expense) net	30
Long-term debt	(1,535)	Income before income taxes and minorities	(166)
Reserves and other liabilities	(186)	Income Taxes	110
Minority interest	(837)	Net income before minority interests	(56)
Total Stockholders equity	(837)	Minority interest	56

The affiliated companies in which Telecom Italia holds, directly or indirectly, between 20% and 50% of the voting rights, including jointly controlled companies, are accounted for under the equity method. Other minor investments, those in which the percentage of ownership is below 20%, are stated at cost.

The significant changes in the composition of the Group in recent years are:

- In March 1999, the Group acquired for approximately Brazilian Reais 705 million a further stake in the Brazilian companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes increasing its percentage ownership from 25.9% to 51.79% of the voting rights of each company.

- In August 1999, Telecom Italia and France Telecom, which jointly (50/50) already held a 65% ordinary stake in Nortel Inversora, acquired the remaining 35% (17.5% each) from Perez Companc and JP Morgan (25% and 10%, respectively). For this further stake Telecom Italia paid approximately U.S.$ 265 million. Nortel Inversora is the holding company that now owns a controlling stake (54.74%) in Telecom Argentina.

- In April 2000, Telecom Italia purchased 50 million of Telecom Italia Mobile ("TIM") ordinary shares at a price of Euro 636 million, in order to increase its own interest in the company.

- In June 2000 the Group and Globo Organizacoes signed a strategic agreement in the Internet sector. The agreement involved the acquisition by Telecom Italia of 30% of the registered capital of GLB Servicos Interativos, an Internet company belonging to Globo Group, for U.S.$ 810 million cash.

- In November 2000 Telecom Italia, through its French subsidiary 9Télécom Reseau S.A., completed its acquisition of 95.5% of Jet Multimedia S.A., the French hosting services company. Total cash consideration was Euro 810.65 million.

- In November 2000, TIM acquired a 56.6% stake in Digitel S.A., a Venezuelan mobile operator. The amount paid for this acquisition was approximately U.S.$ 363 million.

- In November 2000, TIM acquired a further 37.96% stake in Maxitel S.A., the Brazilian wireless operator with a B-Band license, operating in the northeastern states of Minas Gerais, Bahia and Sergipe. The aggregate amount paid to acquire the stake was approximately U.S.$. 240 million. As a result of this acquisition, TIM controls 90% of Maxitel S.A. ordinary shares as of December 31, 2001.

- In November 2000, Telecom Italia tendered its 49.1% stake in Sirti S.p.A. into the public tender offer of Wiretel S.p.A. Telecom Italia received total consideration of Euro 162 million for its stake.

- In November 2000 Telecom Italia and Seat Pagine Gialle ("SEAT") completed the demerger of Telecom Italia by way of transfer to SEAT of 8.168% of the share capital of Tin.it S.p.A. owned by Telecom Italia and the subsequent merger of the remaining 91.832% of Tin.it with SEAT. As of December 31, 2001 Telecom Italia owns, directly and indirectly, approximately 55% (approximately 60% as of December 31, 2000) of SEAT's ordinary share capital.

- On December 1, 2000, Telecom Italia contributed a going concern including a portion of its real estate portfolio to IM.SER. S.p.A. and subsequently sold 60% of this company to Beni Stabili (45%), a leading Italian real estate operator and Lehman Brothers (15%). As a result of the transaction, Telecom Italia received approximately Euro 2.7 billion in cash.

- On December 6, 2000, Telecom Italia sold 80.1% of Italtel S.p.A. to a group of investors led by Clayton, Dubilier & Rice and Cisco Systems. In connection with this sale, Sogerim S.A., a wholly owned subsidiary of Telecom Italia, on behalf of Telecom Italia, retained the 19.9% stake in Italtel not sold by Telecom Italia.

- On December 18, 2000 the Group signed an agreement to bring its investment in Entel Chile to 54.76% by acquiring the shares held by Chilquinta group and the Matte group for cash. The overall cost of the acquisition was U.S.$ 905 million. Entel Chile group operates in the sectors of fixed and mobile telephone services, data-transmission and Internet-access services.

- In February 2001, SEAT acquired a 54.5% stake in Consodata S.A. ("Consodata"), a French company listed on Paris's Nouveau Marché. This acquisition was made through the issuance by SEAT of 63,789,104 of its ordinary shares in exchange for Consodata shares held by certain funds and management, followed by the contribution by SEAT to Consodata of its business information activity. In June 2001, SEAT exchanged 1,084,913 Consodata shares for a 100% stake in Pan Adress GmbH, a German company operating in the direct marketing sector. Furthermore, in August 2001, as a result of a public exchange offer through the issuance by SEAT of 95,706,000 of its ordinary shares in exchange for 5,981,625 Consodata shares, SEAT's stake in Consodata increased to 90.74%. Consodata operates in business information sector in the French market.

- In April 2001, SEAT increased its (direct and indirect) stake in Telegate A.G. to 64.53% after acquiring Telegate Holding's remaining (48.63%) share capital, through the issuance by SEAT of 150,579,625 of its ordinary shares in exchange for Telegate Holding shares. Telegate operates in the sector of Directory Assistance, and is the second-largest operator in Germany after Deutsche Telekom.

- In August 2001, Huit II, a subsidiary of Telecom Italia, exchanged 186,000,000 Seat Pagine Gialle shares for 100% of ISM, a company which holds 33.3% of the share capital of Matrix, through the subsidiary N.V. Vertico. After this transaction, the Telecom Italia Group controls Matrix with a 56.88% stake. Matrix operates in the Internet sector.

- In December 2001, Telecom Italia's stakes in the former satellite consortia companies Eutelsat, Intelsat, Inmarsat and New Skies Satellites were transferred to a new company (Mirror International Holding Sarl, "Mirror"), of which 70% was subsequently acquired by the Lehman Brothers Merchant Banking II L.P. closed fund with a minority stake acquired by Intesa BCI and Interbanca. As a result of the sale, Telecom Italia received Euro 450 million in cash and recorded in the consolidated financial statements a capital gain, before taxes, of Euro 170 million.

The groups Seat Pagine Gialle, Jet Multimedia, Mageos Explorer (formerly Europe Explorer) and Maxitel and the companies Corporacion Digitel and Eustema, whose balance sheets were only consolidated at December 31, 2000, have now been fully consolidated line-by-line, including the statement of operations for 2001.

Sirti group and Italtel group, disposed of during the last part of fiscal 2000, were consolidated only in the statement of operations for the period from January 1, 2000 to September 30, 2000, while in 1999 they were consolidated for the entire year.

The consolidation principles applied by Telecom Italia are as follows:

- The assets and liabilities of the companies consolidated on a line-by-line basis are included in the consolidated financial statements after eliminating the carrying value of the investments against the related stockholders' equity.

- Differences arising on elimination of the investments against the fair value of the related stockholders' equity of the subsidiaries at the date of acquisition are treated as follows:

  - if positive, they are recorded as "goodwill" in intangible assets and amortized on a straight line basis over the period estimated to be benefited and, in any case, not more than a period of 15 years;

  - if negative, they are recorded in stockholders' equity as "consolidation reserve", or, when the amount is due to expectations of unfavorable financial results, to "other liabilities (consolidation reserve for future risks and charges)".

- All significant intercompany transactions are eliminated, together with the unrealized intercompany profits included in inventory.

- Unrealized intercompany profits, included in fixed assets and intangible assets, which arise from intraGroup sales of goods and services at market prices are eliminated, along with the related tax effects. Such sales, net of intercompany profits, are reclassified under the heading of capitalized internal construction costs in the accompanying consolidated statements of income.

- The minority stockholders' share of the equity and net income (loss) of consolidated subsidiaries, calculated using financial statements reflecting the Group's accounting principles, are classified separately in the consolidated stockholders' equity and the statement of operations for the year.

  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 operations and the year-end exchange rate to the items of the balance sheet. The difference arising from the translation of beginning stockholders' equity and the net result for the year at the year-end exchange rate is recorded in the reserves under consolidated stockholders' equity.

  For those consolidated subsidiaries and affiliated companies that use inflation accounting to eliminate distorting effects of inflation on the financial statements, these inflation adjusted financial statements have been translated at the year-end exchange rates for inclusion in the consolidation. The companies in the Group that apply inflation accounting principles are Corporacion Digitel C.A. (Venezuela), Finsiel Romania S.r.l. (Romania) and IS TIM Telekomunikasyon Hizmetleri A.S. (Turkey).

  With respect to the deterioration of the economic situation in Argentina, which led to significant exchange fluctuations after parity with the US dollar was abandoned, monetary assets and liabilities denominated in foreign currencies were adjusted in the Argentine peso financial statements based on the rate of exchange of

Argentine peso 1.7 = U.S.$ 1 and the foreign exchange loss was recognized in the Argentine peso financial statements. The financial statements expressed in Argentine pesos have been translated into Euro by applying the year end exchange rate to the items of the balance sheet and the foreign exchange loss in the statement of operations and the average annual exchange rate to the remaining individual items in the statement of operations.

- Provisions and value adjustments made by individual consolidated subsidiaries exclusively for the purpose of securing tax benefits allowed by law are also eliminated from the consolidated financial statements.

Note 2 — Regulation

The legal framework for the regulation of the telecommunications sector in Italy has been extensively revised in recent years. This revision includes the liberalization of substantially all telecommunication services including the provision of fixed public voice telephony services and the operation of networks to support the provision of such services, which were opened to competition as of January 1, 1998. Most importantly, the legal framework for regulation of the telecommunications sector in Italy has been completely transformed through the formation of the National Regulatory Agency (“NRA”) in accordance with the Maccanico Law, which implemented the Framework Law, and the adoption of the Telecommunications Regulations by the Italian Government pursuant to Law No. 650 of December 23, 1996 (“Law 650”) and Law No. 189 of July 1, 1997 (“Law 189”) to implement a number of EU directives in the telecommunications sector. The Telecommunications Regulations became effective on October 7, 1997, and have been implemented by specific regulations. The Framework Law in general is aimed at:

- ensuring the improvement of competition and efficiency in the telecommunications sector;
- establishing adequate quality standards;
- ensuring access to telecommunications services in a homogeneous manner throughout Italy;
- defining a clear and transparent tariff system on the “price cap” method which, pursuant to the Maccanico Law, applied to Telecom Italia’s fixed public voice telephony services for up two years from August 1, 1997 (which price cap method was extended by the NRA from August 1, 1999 to December 31, 2002); and
- protecting the interests of consumers and users.

The Telecommunications Regulations completed the liberalization of the provision of all telecommunications services and the operation of all telecommunications networks in Italy, effective from October 7, 1997, except for the provision of fixed public voice telephony services and the operation of telecommunications networks to support provision of such services, which were liberalized as of January 1, 1998. Restrictions on other operators providing telecommunications services, other than fixed public voice telephony services and the operation of telecommunications networks, had been lifted by several previous measures.

The Telecommunications Regulations contain provisions concerning:

- the granting of general authorizations or individual licenses to provide telecommunications services;
- universal service obligations and the mechanism for funding the net cost of such obligations;
- special obligations imposed on operators having significant market power, including the determination of interconnection charges using principles cost orientation;
- numbering, carrier selection and number portability;
- right of way; and
- the essential requirements that must be complied with in the provision of services and when interconnecting between public telecommunications networks.

The NRA has established and will continue to establish detailed regulations governing the telecommunications sector and will monitor their application, while the Ministry of Communications will retain the responsibility for defining telecommunications policy in Italy.

During 1999, 2000 and 2001 the NRA issued several resolutions in order to implement and detail general framework regulation. In particular, provisioning regulation on carrier preselection, interconnection and local loop unbundling/shared access was delivered.

New European Regulatory Framework, that was published on April 2002 and will be transposed in National Laws by July 2003, will change the nature of regulatory and competitive markets scenario, through more liberalization and a decrease of ex ante regulation. Converging markets' regulation will be privileged.

Note 3 — Accounting Policies

The principal accounting policies applied are as follows:

Securities

Marketable securities, including quoted shares of consolidated subsidiaries anticipated to be sold, are valued at the lower of cost or market based on year-end prices quoted on the stock exchange. Write-downs are reversed if the reason for the write-down no longer exists.

Securities classified under non current assets (other assets) are held to maturity and recorded at purchase cost adjusted for the unamortized discount or premium. They are also adjusted for any permanent impairment in value.

Securities acquired under "repurchase agreements", for which the obligation exists to resell them at maturity, are included at purchase cost under current assets. The difference between the sales price and the purchase price is allocated to income as it accrues.

Contracts for the loan of securities 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 current assets" and "short term debt" include, respectively, a receivable and a payable of the same amount at the fixed amount of the contract.

Accounts receivable and payable

Accounts receivable and payable are recorded at their nominal value. Where required, provision is made to write-down the receivables to their estimated realizable value.

An estimate is made for doubtful receivables based upon a review of all outstanding amounts at the period-end. Bad debts are written off during the year in which they are identified.

Accounts receivable and payable in foreign currencies are adjusted to reflect year-end rates with gains or losses on the translation accounted for as "financial income" or "financial expense". Accounts receivable and payable in Argentine pesos were adjusted at the exchange rate of Argentine peso 1.7 = US$ 1.

Foreign currency transactions

Monetary assets and liabilities denominated in foreign currencies have been recorded at the exchange rate in effect at the date of the transaction; such assets and liabilities denominated in foreign currencies are remeasured at the prevailing rate at the balance sheet date, taking into consideration the hedging contracts, and any resulting unrealized losses are charged to income and unrealized gains are credited to income.

Inventories

Inventories are valued at the lower of cost or market. Cost is determined using the LIFO method for raw materials and finished products and the weighted average method for purchased finished goods. Provision is made for potential losses on obsolete or slow-moving raw materials, finished products and other inventories, taking into account their expected future use and estimated realizable value. Contracts covering less than 12 months are valued using the actual cost, while long-term contracts are valued using the percentage completion method. Provision is also made for estimated losses on completion and any other related risks on long-term contracts.

Fixed assets

Fixed assets are stated at purchase or construction cost plus directly attributable expenses. The values are adjusted where specific laws of the country, in which the assets are located, allow or require monetary revaluations.

Depreciation is calculated on a straight line basis over the estimated useful lives of the assets using the following annual rates applied to the historical or revalued costs:

Buildings	3 — 7%
Telecommunication system and equipment	3 — 33%
Machinery and installation	20 — 33%
Industrial and commercial equipment	15 — 25%
Other fixed assets	6 — 33%

The depreciation charge for assets purchased or brought into service during the year is normally determined using rates reduced by 50 percent.

Construction in progress is stated at cost. Ordinary repair and maintenance costs are charged to income in the year they are incurred.

For fixed assets whose value is permanently below the historical cost, net of their accumulated depreciation, the appropriate writedowns are made pursuant to Article 2426, Section 1, item 3 of the Italian Civil Code. Write-downs are reversed if the reason for the write-down no longer exists.

The Group periodically evaluates potential impairment loss relating to long-lived assets, including goodwill, when a change in circumstances occurs by assessing whether permanent diminution in value has occurred. . Impairment is recognized if the recoverable amount falls below its carrying value. In that event, an impairment loss is recognized based on the amount by which the carrying value exceeds the recoverable amount.

Retirements, sales and disposals of assets are recorded by removing the cost and accumulated depreciation from the accounts with any resulting gain or loss reflected in the statement of operations.

Capital grants

Capital grants provided by the Italian government in connection with investments in fixed assets are recorded in the year the grant is formally approved and, in any event, when the right to their receipt is definite. The grants are not subject to any restriction as to use and may not be reclaimed by the government. Capital grants are included in deferred income and recorded in the statement of operations in connection with the gradual depreciation of the assets they refer to.

Intangible assets

Intangible assets are recorded at cost, and amortized on a straight line basis over the period of expected future benefit as follows:

Licenses, trademarks and similar rights	Contract duration (*)
Goodwill	Years to be benefited
Software	Principally in 3 years
Leasehold improvements	Rental contract duration

(*) Only for telecommunications licenses of not more than 15 years.

When full recovery of the investments is not expected, appropriate writedowns of goodwill are made.

Software costs capitalized represent only those costs associated with the development of new software or the enhancement of software when additional functionality is provided. The Company applies the same policy in accounting for web site development costs as for costs of computer software developed or obtained for internal use. All costs of maintaining existing software, costs for the enhancement of software that does not provide for additional functionality, and costs pertaining to the preliminary stage of software development are expensed as incurred.

Employee termination indemnities

The amount of this reserve is determined in accordance with current laws and collective bargaining agreements.

The reserve for termination indemnities shown in the consolidated financial statements reflects the total amount of the indemnities, net of any advances taken, that each employee in the Italian consolidated companies would be entitled to receive if termination were to occur as of the balance sheet date.

Reserves for risks and other charges

Reserves for risks and other charges are recognized when the Group has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources embodying economic benefit will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Research and development costs

Research and development costs are charged to income as incurred. In 1999, 2000 and 2001 gross research and development costs charged to income (before revenue grants) amounted to Euro 331 million, Euro 269 million and Euro 138 million, respectively.

Revenue grants

Revenue grants represent contributions against operating costs mainly provided by the government or other public agencies in connection with research and development costs. They are recorded in the statement of operations in the year they are formally approved and in any event when the right to their receipt is definite. These grants are not subject to any restriction as to use and they may not be reclaimed by the government.

Recognition of revenues and expenses

Revenues and expenses are recorded on the accrual basis.

Revenues are recorded in the statements of income as follows:

i) for telecommunication services companies (both fixed and mobile providers), in the year in which the services are provided.

   Certain revenues deriving from fixed telephone and mobile services are billed in advance and are recognized when services are provided. Revenues deriving from other telecommunications services, principally network access, long distance, local and wireless airtime usage, are recognized based on minutes of traffic processed or contracted fee schedules. Revenues from installation and activation activities are recognized at the date of the installation or activation.

   The revenue and related expenses associated with the sale of wireless handsets and accessories are recognized when the products are delivered and accepted by customers, as this is considered to be a separate earnings process from the sale of wireless services;

ii) for IT software and services and other activities, on the basis of the services rendered during the year;

iii) revenues of the Internet and Media segment are primarily derived from advertising and publishing, sale of office and related products, and internet access and related services. Revenues from the sale of advertising and publishing are recognized in the statement of operations according to the date of publication, which corresponds to the time at which the directories are printed and delivered. Advertising revenue from on-line services is recorded on the date the on-line advertisement is posted to the related web site and advertising revenue from television is recorded on the date at which the advertisement is shown. Revenues from the sale of office and related products are recognized when title transfers, which generally corresponds to the date when products are shipped. Provisions for returns and other adjustments related to sales are provided in the same period the related sales are recorded. Revenues from internet access and related services, primarily subscription services, are recognized over the subscription period on a straight line basis.

Capitalization of interest policy

Interest on construction projects is capitalized when specific borrowings can be attributed to the project.

Income taxes

The companies within the Group are required to pay taxes on a separate company basis. Income taxes currently payable, recorded in accrued income taxes, are provided on the basis of a reasonable estimate of the tax liability for the year of all consolidated companies.

The Group also recognizes deferred income tax assets and liabilities that are determined under the liability method. Income taxes represent the tax effect of temporary differences between the tax and financial reporting bases of assets and liabilities, using enacted tax rates, and the expected future benefit of net operating loss carry forward.

Deferred tax assets and deferred tax liabilities are offset, whenever allowed by local tax laws.

The tax benefit of tax loss carry-forwards is recorded only when there is a reasonable expectation of realization.

Deferred taxes on reserves on which taxation has been deferred, are recorded when such reserves are expected to be distributed or otherwise used and their distribution or utilization will give rise to tax charges.

Accounting for leases

Assets covered by finance lease contracts are recorded in fixed assets and depreciated from the date of the lease contract. The corresponding liability is allocated between short and long term debt. The interest element of the finance lease and the depreciation charge are recorded in the statement of operations. Depreciation is calculated on the same basis as that for similar owned assets.

All other leases are accounted for as operating leases.

Financial derivatives

Financial derivative contracts are used by the Group to hedge exposure to interest rate and foreign currency exchange risks. They are valued consistently with the underlying asset and liability positions and any net expense connected with each single transaction is recognized in the statement of operations.

For financial instruments used to hedge interest rate risks, the interest differentials are recorded in the statement of operations in "financial income" or "financial 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 rate at the date of entering into the contract and the forward rate) is recorded in the statement of operations in "financial income" or "financial expense" based on the accrual principle.

Securitization of accounts receivables

Upon the sale of receivables to the TI Securitization Vehicle S.r.l., the underlying receivables are removed from the balance sheet. The difference between the carrying value of the receivables sold and the consideration received (including the deferred consideration under the deferred purchase price) is charged on the accrual basis to the consolidated statement of operations in "other external charges" or in "financial expense". All expenses to initiate and operate the program are charged to "other external charges". The notes issued under the program are not included in the consolidated balance sheet of Telecom Italia, as they are considered to be legal obligations of TI Securitization Vehicle S.r.l. (see Note 5).

Note 4 — Cash and Cash Equivalents and Marketable Securities

Cash and Cash Equivalents

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Bank and postal accounts	1,299	757
Cash and valuables on hand	5	5
Receivables for sales of securities	1	3
	1,305	765

Marketable Securities

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Marketable equity securities	436	256
Marketable debt securities	2,020	1,935
	2,456	2,191

As of December 31, 2001, marketable equity securities include Euro 247 million (Euro 382 million as of December 31, 2000) of listed shares of consolidated subsidiaries.

Marketable debt securities consist almost entirely of government securities and bonds.

The carrying values of both marketable equity and debt securities have been written down by Euro 291 million to approximate market values at year end.

Note 5 — Receivables

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Trade	8,734	8,711
Reserve for bad debt	(740)	(808)
	7,994	7,903
Unconsolidated subsidiaries	41	33
Affiliated companies	413	567
Parent companies	3	1
	8,451	8,504

Gross trade accounts receivable totaled Euro 8,711 million and consist, for the most part, of receivables for telecommunications services. Receivables are adjusted to estimated realizable value through writedowns. Such writedowns mainly relate to other telecommunications companies. Trade accounts receivable refer, in particular, to Telecom Italia (Euro 4,242 million), TIM (Euro 917 million) and Seat Pagine Gialle group (Euro 885 million).

This caption also includes Euro 1,610 million of receivables from other telecommunications carriers and Euro 122 million of services to be performed by Seat Pagine Gialle representing the advertising commitments undertaken and invoiced by the company for directories that will be published in 2002. The same amount is recorded in payables, trade and other.

In 2000, Telecom Italia S.p.A. sold receivables without recourse, not due on December 31, 2000, to factoring companies for a total of Euro 207 million, with a loss on the sale of Euro 3 million.

During 2001, TIM S.p.A. sold trade accounts receivable under factoring arrangements for Euro 3,297 million (Euro 3,204 million in 2000). At December 31, 2001, receivables sold and not yet due totaled Euro 106 million (Euro 263 million as of December 31, 2000).

During 2001, Telecom Italia began a program (the "Program") for the securitization of receivables generated by the services rendered to the customers of the Telecom Italia Domestic Wireline (TIDW) business unit and the customers of Path.Net (a wholly-owned subsidiary of Telecom Italia, which provides telephone services to the Public Administration). A first tranche of Euro 700 million of Notes was issued in June 2001 by TI Securitisation Vehicle S.r.l., a non-consolidated vehicle company for the Program which operates under Law No. 130/1999. The Program allows the possibility of successive issues of notes all with the same rights and risk profile, up to a total maximum amount of Euro 2 billion.

The transaction, regulated by the aforementioned law, presupposes, usually on a monthly basis, the stipulation of buy-sell contracts containing without recourse clauses between Telecom Italia and Path.Net (assignors) and TI Securitisation Vehicle S.r.l. (assignee), exclusively for outstanding trade accounts receivable. The flow of receipts from the trade accounts receivable covered by the contracts constitutes the funds which the securitization vehicle uses to pay the interest and the principal to the noteholders. Within the framework of TI Securitization Vehicle's disbursement plans and the time frame for the collection of the receivables, the sums received are also used to purchase new receivables generated by the sales activities of the assignor companies.

The price for this transaction, equals to the nominal value of the receivables, net of a discount which takes into account the expenses that TI Securitization Vehicle S.r.l. must bear, will be paid to the assignor company partly as an advanced purchase price, at the time of sale, and partly as a deferred purchase price. The deferred portion, which constitutes the credit enhancement of the transaction, will be paid to the assignor company each time new receivables are sold, subject to the collection of the receivables, and is prudently calculated by the rating agencies on the basis of pre-established estimate of the collection times and the amounts of the credit notes that will eventually be issued. Such estimates, and therefore also the deferred purchase price, will be adjusted monthly on the basis of the effective performance of the receivables (dynamic type of credit enhancement).

As regards the risk of uncollectibility, the assignor company is responsible for the solvency of the debtors on the receivables sold only up to the limit of the amount of the deferred purchase price.

The first issue of notes backed by the securitization of receivables (called Series 2001-1) for a total of Euro 700 million, was divided into three classes having the following characteristics:

- Class A1: Euro 100 million variable rate notes denominated in Euro with a maturity at approximately 18 months (maturing January 25, 2003) with a margin of 19 basis points over the 3-month Euribor;
- Class A2: Euro 150 million variable rate notes denominated in Euro with a maturity at approximately 3 years (maturing July 25, 2004) with a margin of 27 basis points over the 3-month Euribor;
- Class A3: Euro 450 million variable rate notes denominated in Euro with a maturity at approximately 5 years (maturing July 25, 2006) with a margin of 34 basis points over the 3-month Euribor.

These notes have been rated by Fitch, Moody's and Standard & Poor's at AAA/Aaa/AAA, respectively. The high ratings reflect the quality and diversification of the receivable portfolio, the element of over collateralization represented by the dynamic mechanism for managing the deferred purchase price, the legal structure of the transaction and other qualifying aspects of the program. The notes were subscribed to at face value and requests were received from Italy for about 20% of the total amount and the remaining 80% from abroad, particularly Spain, France, the United Kingdom and Germany.

The total amount of the trade accounts receivable sold under the securitization transactions in 2001 was Euro 5.9 billion and solely referred to receivables from residential customers generated by Telecom Italia. At December 31, 2001, the receivables sold and not yet collected amounted to Euro 877 million (of which Euro 684 million were not yet due).

The securitization transaction led to an improvement in consolidated net debt as of December 31, 2001 of about Euro 848 million.

Lastly, under the securitization program, TI Securitisation Vehicle can invest the temporary excess liquidity in Telecom Italia. As of December 31, 2001, the balance of such investments totaled Euro 168 million against which financial payables to TI Securitisation Vehicle, included under "short term debt", have been recorded for the same amount in the consolidated balance sheet.

Note 6 — Inventories

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Raw materials and supplies	21	22
Purchased finished goods	214	253
Work in progress and semi-finished products	13	6
Finished products	2	2
Long and short-term contracts	467	352
Advances to suppliers	8	1
	725	636

Inventories of Euro 245 million (Euro 233 million as of December 31, 2000) are held by companies providing telecommunications services, and Euro 229 million (Euro 217 million as of December 31, 2000) are held by companies providing information technology services and Euro 113 million (Euro 224 million as of December 31, 2000) are held by companies in the satellite sector.

Note 7 — Other Current Assets

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Receivables from banks and other loans	931	591
Receivables from national government and public agencies for subsidies and contributions	42	45
Cash receipts in transit	187	210
Tax receivables	576	1,544
Deferred tax assets	572	949
Prepaid expenses	337	364
Accrued income	72	152
Other	741	785
	3,458	4,640

Receivables from banks and other loans are mainly due to the deferred purchase price related to the securitization of accounts receivable and certain agreements with financial institutions entered into by Telecom Italia for the lending of SEAT shares (“prestito titoli”). A short-term obligation is also recognized for an equal amount. The accounting for such transaction is regulated by the Bank of Italy. The Euro 340 million decrease is mainly related to the partial reimbursement of such securities loans.

The Euro 968 million increase in tax receivables is principally due to Telecom Italia’s current tax receivables, which rose by Euro 943 million, in as much as taxes paid on account in 2001, as of December 31, 2001, proved to be in excess of actual tax requirements.

Deferred tax assets, including those under Other assets (see Note 10), totaled Euro 1,410 million (Euro 996 million as of December 31, 2000), while deferred income taxes amounted to Euro 35 million (Euro 201 million as of December 31, 2000). As a result, net deferred tax assets amounted to Euro 1,375 million (Euro 795 million as of December 31, 2000).

Other current assets includes miscellaneous receivables due from the Italian government and other public institutions and advances to personnel.

Note 8 — Fixed assets, net

Fixed asset balances, net of accumulated depreciation and writedowns and adjusted to eliminate intraGroup profits generated by purchases of internally produced goods and services by the Group, are detailed as follows:

	2000	As of December 31, 2001 Cost	Accumulated Depreciation	Net book value
		(Millions of Euro)		
Land and buildings	2,947	4,491	1,614	2,877
Telecommunications systems and equipment, machinery and installations	18,126	57,082	40,433	16,649
Industrial and commercial equipment	78	987	914	73
Other	836	2,036	1,305	731
Construction in progress and advances to suppliers	1,438	1,427	-	1,427
	23,425	66,023	44,266	21,757

As of December 31, 2001 fixed assets include leased assets with a net book value of Euro 650 million (gross value of Euro 799 million less accumulated depreciation of Euro 149 million).

An analysis of the movements in fixed assets for each of the years is as follows:

	As of December 31, 2000	2001
	(Millions of Euro)	
Balance, at beginning of the year	23,508	23,425
Effect of change in accounting for the Nortel Inversora Group	-	(2,704)
	23,508	20,721
Investments in fixed assets	3,889	4,254
Disposals	(103)	(172)
Sale by Telecom Italia of a portion of its real estate portfolio	(2,392)	-
Depreciation (*)	(4,515)	(4,034)
Write-downs	(11)	(11)
Changes in consolidation area	2,978	1,345
Translation adjustment	71	(346)
Balance, end of the year	23,425	21,757

In 2001, changes in consolidation area mainly refer to the inclusion of the Entel Chile group and consolidation of certain of SEAT’s subsidiaries all of which were acquired in 2001.

(*) A breakdown of depreciation is as follows:

	2000	2001
	(Millions of Euro)	
Buildings	265	152
Telecommunications systems and equipment, machinery and installations	3,844	3,542
Industrial and commercial equipment	49	34
Other	357	306
	4,515	4,034

A detail of investments in fixed assets during each of the years is as follows:

	2000	2001
	(Millions of Euro)	
Domestic wireline	1,917	1,976
Mobile services	1,194	1,547
Internet and media	55	82
International operations	579	427
IT services	83	87
Satellite services	29	27
Telecom Italia Lab	29	12
	3,886	4,158
Other activities and intercompany eliminations	3	96
	3,889	4,254

Note 9 — Intangible Assets

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Licenses, trademarks and similar rights	3,505	4,307
Goodwill	10,299	9,141
Software and other rights	819	1,274
Leasehold improvements	261	231
Work in progress and advances	840	874
Other	313	370
	16,037	16,197

- Licenses, trademarks and similar rights increased by Euro 802 million mainly as a result of the acquisition of new licenses in Brazil and Greece (Euro 1,080 million). This item primarily includes the UMTS license acquired by TIM in Italy (Euro 2,417 million), and the mobile telephony licenses of Maxitel, Stet Hellas Telecommunications, TIM Sao Paulo, TIM Celular Centro Sul, TIM Rio Norte and TIM Perù.

- Goodwill arises mainly due to the acquisition of the controlling interest in Seat Pagine Gialle (Euro 5,882 million) and Entel Chile (Euro 799 million), the increase in ownership of TIM (Euro 798 million), and acquisitions of Corporacion Digitel (Euro 337 million), TDL Infomedia (Euro 310 million) and Holding Media e Comunicazione (Euro 184 million). Goodwill decreased by Euro 1,158 million since the end of 2000, mainly as a result of:

- extraordinary writedowns made in 2001 to adjust the value of the following investments:

	(Millions of Euro)
International operations of the International Operations BU	764
International operations of the Mobile Services BU	392
Operations of Internet and Media BU	147
	1,303

Such write-downs were made on a consistent basis according to the new business plans and market trends and resulted in the conclusion that there was a permanent impairment in the value at which these investments were carried by Telecom Italia;

- amortization charge for the year 2001 amounting to Euro 1,022 million, and

- additions for the year 2001 amounting to Euro 1,174 million (of which Euro 731 million is attributable to Entel Chile).
- Software and other rights principally includes software for telecommunications services.
- Work in progress and advances relate primarily to costs of developing software projects incurred by Telecom Italia, mainly for internal use.

Movements in intangible assets during the year are as follows:

	(Millions of Euro)
Balance, at beginning of the year	16,037
Effect of change in accounting for the Nortel Inversora group	(466)
	15,571
Goodwill	1,174
Other additions	2,736
Amortizations	(2,241)
Disposals	(12)
Writedowns	(1,308)
Changes in consolidation area	311
Translation adjustment and other	(34)
Balance, end of the year	16,197

Other additions mainly refer to capitalization of costs for telecommunications software and new licenses acquired.

Note 10 — Other assets

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Investments in:		
Unconsolidated subsidiaries	21	18
Affiliated companies	7,199	4,764
Other companies	191	145
Advances on future capital contributions	187	1,659
Total investments	7,598	6,586
Treasury stock	662	-
Other securities	6	86
Deferred tax asset	424	461
Other receivables	968	847
	9,658	7,980

Investments in affiliated companies decreased by Euro 2,435 million compared to 2000, as a result of the followings:

	(Millions of Euro)
Balance, at beginning of the year	7,199
Effect of change in accounting for the Nortel Inversora group	390
	7,589
Additions	1,382
Disposals	(711)
Extraordinary writedowns	(1,078)
Valuation using equity method	(1,921)
Changes in consolidation area	(497)
Balance, end of the year	4,764

Extraordinary writedowns relate to Telekom Austria (Euro 225 million), GLB Servicos Interativos (Euro 586 million), Solpart Participacoes (Euro 151 million), Nortel Inversora (Euro 50 million) and other (Euro 66 million).

Such write-downs were made on a consistent basis according to the new business plans and market trends and resulted in the determination that there was a permanent impairment in the value at which these investments were carried by Telecom Italia.

Changes in consolidation area refer to Entel Chile (- Euro 379 million) and Holding Media e Comunicazione (- Euro 118 million); in 2001, such companies, after the acquisition of control, are consolidated on a line by line basis.

The largest investments in affiliated companies are:

- Telekom Austria (Euro 1,460 million; Euro 1,819 million as of December 31, 2000), which operates in the sectors of wireline and mobile telephone services, data-transmission and Internet-access services;
- Auna (Euro 690 million; Euro 509 million as of December 31, 2000), a Spanish holding company that provides fixed and mobile telephone services, data-transmission and Internet-access services;
- Etec S.A. (Euro 551 million; Euro 538 million as of December 31, 2000), the Cuban operator for national and international fixed telephone services and Internet services;
- Mobilkom Austria (Euro 544 million; Euro 586 million as of December 31, 2000), which operates mobile telephone services;
- Solpart Participacoes (Euro 238 million; Euro 461 million as of December 31, 2000), a holding company for fixed local and long-distance telephone services;
- Telekom Srbija (Euro 195 million as of December 31, 2001 and 2000), which operates in the sector of fixed telephone services, data services and mobile telephone services;
- Bouygues Décaux Télécom (Euro 158 million; Euro 172 million as of December 31, 2000), a holding company which controls the investments of the Bouygues group in the telecommunications industry;
- IM.SER (Euro 141 million; Euro 204 million as of December 31, 2000) a real estate management company, which was set up at the end of 2000 following the real-estate spin-off transactions carried out by Telecom Italia;
- Mirror International Holding (Euro 94 million), a holding company to which in December 2001 Telecom Italia contributed its stakes in the former satellite consortia companies Eutelsat, Intelsat, Inmarsat and New Skies Satellites;
- Telemaco Immobiliare (Euro 91 million) a real estate management company, which was set up in May 2001 through the contribution of IM.SER’s “Trading Portfolio” business segment;
- IS TIM (Euro 81 million; Euro 353 million as of December 31, 2000), a company in Turkey which operates mobile telephone services;
- GLB Servicos Interativos is recorded at Euro 24 million (Euro 809 million as of December 31, 2000) following the extraordinary writedown made in 2001; the company operates in the Internet sector in Brazil and owns the "Globo.com" brand;
- Nortel Inversora shows a nil balance as a result of the extraordinary writedown made in 2001; such company was proportionally consolidated in 2000 and accounted for by the equity method in 2001.

Advances on future capital contributions (Euro 1,659 million; Euro 187 million as of December 31, 2000) mainly refer to advances made by Tim International to IS TIM.

Treasury stock (related to 112,998,070 Telecom Italia savings shares) was cancelled subsequent to the bonus increase in share capital at the time the capital was re-denominated in Euro.

Other receivables include the non current portion of the expenses related to the deferral of the premium paid for the put option on the SEAT shares, as well as receivables from affiliated companies, the revalued amount of the tax receivable from the prepayment of the tax on the reserve for employee severance indemnities, loans to employees, loans to other companies and security deposits.

Note 11 — Financial Debt

	As of December 31, 2000	As of December 31, 2001		
	Total	Denominated in Euro	Denominated in Foreign Currency	Total
		(Millions of Euro)		
Short-term debt (*)	15,136	8,534	580	9,114
Long-term debt	8,268	12,420	3,663	16,083
Total financial debt	23,404	20,954	4,243	25,197

(*) Including current portion of long term debt.

The increase in total financial debt at December 31, 2001 is mainly due to dividends paid (Euro 3,097 million), the investments in Turkey (Euro 1,906 million), Brazil and Greece (Euro 1,080 million) and the acquisition of the controlling interest in Entel Chile (Euro 1,858 million), only partly offset by the effect of the de-consolidation of the Nortel Inversora group.

Financial debt denominated in foreign currency as of December 31 of each year is as follows:

	In Foreign Currency (Millions)		(Millions of Euro)	
	2000	2001	2000	2001
U.S.$	4,063	967	4,406	1,097
GBP	253	305	390	502
BRL (Brazil)	1,342	3,235	738	1,582
CLP (Chile)	-	538	-	937
NUEVO SOL (Perù)	-	329	-	109
YEN	8,153	450	72	4
Other			17	12
			5,623	4,243

A grouping of the financial debt by interest rates is as follows:

	As of December 31, 2000	As of December 31, 2001
	(Millions of Euro)	
Up to 2.5%	1,003	988
From 2.5% to 5%	3,873	19,650
From 5% to 7.5%	13,841	2,573
From 7.5% to 10%	1,730	700
Over 10%	2,090	1,050
	22,537	24,961
Non-interest bearing	867	236
	23,404	25,197

The non-interest bearing financial payables relate to certain agreements entered into by Telecom Italia for the lending of SEAT shares ("prestito titoli").

Long-term debt as of December 31, 2001 classified by maturity is as follows (in millions of Euro):

2002 (current portion of long-term debt)	1,669
2003	2,946
2004	2,271
2005	2,071
2006	5,760
Beyond 2006	3,035
	17,752

Financial debt consists of the following:

	As of December 31, 2000	As of December 31, 2001		
	Total	Long term debt	Short term debt	Total
	(Millions of Euro)			
Debt to banks	16,796	3,340	6,895	10,235
Debt to other financial institutions	1,689	1,186	977	2,163
Convertible notes	-	2,500	-	2,500
Notes and bonds	1,814	8,003	180	8,183
Payables to affiliates	691	474	96	570
Note payables	50	220	-	220
Suppliers	272	155	13	168
Other	2,092	205	953	1,158
	23,404	16,083	9,114	25,197

- Debt to banks, of Euro 10,235 million, decreased by Euro 6,561 million compared to December 31, 2000. They are secured by mortgages for Euro 37 million and liens and pledges for Euro 686 million.

- Debt to other financial institutions, of Euro 2,163 million, increased by Euro 474 million compared to December 31, 2000. They refer to loans payable to Cassa Depositi e Prestiti and IRI by Telecom Italia (Euro 489 million), loans payable by Seat Pagine Gialle (Euro 780 million) to Seat Pagine Gialle Finance S.r.l., a corporate vehicle, entirely owned by third parties, operating under Law No. 130/99 on securitization and a payable by Softe (Euro 600 million) to Olivetti Finance N.V.

- Convertible notes includes notes issued by Sogerim in an aggregate principal amount of Euro 2,500 million convertible into TIM or Seat Pagine Gialle shares, with the right of Sogerim to pay off the amount due in cash. These are five-year notes and can be redeemed by the noteholders before maturity at the end of the third year after issue.

- Notes and bonds, which totaled Euro 8,183 million and increased by Euro 6,369 million from December 31, 2000, include the following:

  - on April 10, 2001, notes were issued by Sogerim on international markets in an aggregate principal amount of Euro 6,000 million. The issue was divided into three tranches: the first, for Euro 1,000 million principal amount of floating rate notes, maturing on April 20, 2004; the second, for Euro 3,000 million principal amount of fixed-rate notes, maturing on April 20, 2006; the third, for Euro 2,000 million principal amount of fixed-rate notes, maturing on April 20, 2011;
  - on December 21, 2001, Telecom Italia issued floating rate notes of Euro 1,500 million principal amount (this is the first issue under the Global Medium-Term Note Program with Telecom Italia as the issuer). The maturity date is June 21, 2005 and Telecom Italia can call the notes at an earlier date at par beginning from the second year and at every coupon date for interest thereafter;
  - notes maturing in 2003 issued by the Brazilian companies Tele Nordeste Celular and Tele Celular Sul for Euro 196 million;
  - notes maturing between 2002 and 2021 issued by Entel Chile for Euro 102 million;
  - notes maturing in 2002 issued by Softe through various financial institutions for a total of Euro 174 million;
  - notes maturing between 2009 and 2010 issued by the TDL Infomedia Ltd group for Euro 211 million.

- Payables to affiliates, of Euro 570 million, decreased by Euro 121 million compared to the end of 2000 and are related mainly to Teleleasing (Euro 522 million) for financial lease contracts.

- Notes payable, of Euro 220 million, increased by Euro 170 million and refer to the investment certificates issued by Seat Pagine Gialle as part of the securitization transaction.

- Other, of Euro 1,158 million, decreased by Euro 934 million compared to the end of 2000 and were mainly related to the financial payables of Telecom Italia (Euro 395 million, of which Euro 236 million for the loan of Seat Pagine Gialle ordinary and savings shares and Euro 50 million for medium/long-term financial debt relating to the agreement reached with the Tax Administration over the assessments received in 2001 by Telecom Italia) and TIM group (Euro 670 million, relating to the remaining amounts payable on the UMTS licenses acquired in Italy and Greece and the PCS licenses in Brazil).

Note 12 — Payables, trade and other

	As of December 31,	
	2000	**2001**
	(Millions of Euro)	
Advances from customers	370	388
Trade payables	6,507	6,058
Payables to affiliated companies	580	349
Other taxes payable	632	672
Payables to customers	1,684	1,650
Other	330	1,466
	10,103	10,583

Trade payables decreased by Euro 449 million from December 31, 2000; an amount of Euro 131 million of these payables are secured by pledges on Maxitel shares, owned by TIM International and Bitel, and liens on installations guaranteeing the supply contracts with Ericsson. This item also includes Euro 743 million of amounts due to other telecommunications operators.

Payables to customers consist of deposits paid by customers and pre-billed basic subscriber charges (mainly for January and February), as well as prepaid traffic. The item also includes other liabilities for services to be performed by Seat Pagine Gialle (Euro 122 million).

Other includes payables for Telecommunications license fee totaling Euro 1,034 million. In particular, Telecom Italia and TIM contested the Ministerial Decree dated March 21, 2000 that introduced Law No. 448/1998, which set forth a new license fee as from January 1, 1999 in lieu of the previous concession fee. Consequently, they did not pay the license fee for the year 2000 (Euro 486 million) nor the on-account payment for the year 2001.

Note 13 — Other accrued liabilities

Other accrued liabilities consist of accrued expenses (primarily interest) of Euro 224 million as of December 31, 2000 and Euro 403 million as of December 31, 2001 and deferred income of Euro 635 million as of December 31, 2000 and Euro 797 million as of December 31, 2001. Deferred income includes, among other things, the pre-billed basic charges and rentals of telephone equipment and the unavailable portion of capital grants received.

Note 14 — Other liabilities

	As of December 31,	
	2000	**2001**
	(Millions of Euro)	
Reserve for taxes	159	154
Reserves for pensions and similar obligations	15	49
Reserve for restructuring costs	164	37
Reserve for forward purchase commitments (Put option on SEAT's shares)	-	569
Reserve for contract and other risks and charges	1,229	2,209
Payable to INPS and other accruals	1,149	930
	2,716	3,948

- The reserve for taxes mainly consists of estimated tax liabilities on positions still to be agreed or in dispute.
- The reserve for purchase commitments recorded in 2001 relates to the forward purchase commitment of Seat Pagine Gialle shares connected with the estimate of the nonrecoverability of the original price of the options (See Note 18).
- The reserve for contract and other risks and charges includes:
  - the reserves for contractual risks and other risks of Telecom Italia for a total of Euro 590 million provided in previous years and in the current year, relating to the "2000 IM.SER real estate transaction", the sales of Italtel and Sirti, the sale of the satellite consortiums (Mirror) and the agreement with Vivendi/CanalPlus for transfer of the investment in Stream;
  - the reserve for the losses of subsidiaries and affiliated companies of Euro 603 million for extraordinary provisions recorded on the basis of the strategic guidelines of recent plans;
  - the reserves for the risks of technological revisions and future risks inherent to the regulatory framework of TIM for Euro 465 million.
- Payable to the Italian Social Security Agency ("INPS") and other accruals includes the non current portion of the contributions due for the personnel of IRITEL, the company merged into Old Telecom Italia in 1994 (see Note 18), as well as the deferred capital grants provided by the government.

Note 15 — Employee termination indemnities

Under Italian labor laws and regulations all employees are entitled to an indemnity upon termination of their employment relationship for any reason. The benefit accrues to the employees on a pro-rata basis during their employment period and is based on the individuals' salary. The vested benefit payable accrues interest, and employees can receive advances thereof in certain specified situations, all as defined in the applicable labor contract regulations. The reserve for termination indemnities shown in the consolidated financial statements reflects the total amount of the indemnities, net of any advances taken, that each employee would be entitled to receive if termination were to occur as of the balance sheet date.

The reserve for employee termination indemnities increased by Euro 31 million compared to the end of 2000, as a result of the followings:

	(Millions of Euro)
Balance, at beginning of the year	1,319
Provision for the year	211
Indemnities paid	(127)
Advances	(18)
Other variations	(35)
Balance, end of the year	1,350

Other variations mainly refer to the changes in the scope of consolidation.

Note 16 — Share capital

Share capital increased by Euro 188 million, compared to December 31, 2000. Euro 1 million of this increase is due to the subscription against payment, by executives of the Group, of 1,496,350 ordinary shares, of which 1,022,650 of par value Lire 1,000 each and 473,700 of par value Euro 0.55 each, were purchased under the group's stock option plan. The remaining Euro 187 million relates to the bonus share capital increase following the re-denomination of the share capital into euro. At the extraordinary Shareholders' Meeting of May 3, 2001 a resolution was passed to re-denominate the share capital into euro by re-denominating the par value of the ordinary and savings shares in euro and rounding up the par value of Lire 1,000 to Euro 0.55, which consequently increased share capital by transferring from certain reserve accounts the necessary amounts to bring the share capital amounts in line with the new par value.

After these transactions, the share capital of Telecom Italia as of December 31, 2001 amount to Euro 4,023 million and is fully paid and consists of 5,261,533,481 ordinary shares and 2,053,122,025 savings shares of par value Euro 0.55 each.

Savings shares do not carry voting rights but entitle their holders to preferential rights to receive a dividend per share out of current years' earnings that is 2% of the par value of the savings shares greater than that received by holders of ordinary shares.

Note 17 — Reserves, retained earnings and profit (loss) of the year

	As of December 31,	
	2000	2001
	(Millions of Euro)	
Reserves and retained earnings	11,155	9,755
Net income (loss)	2,028	(2,068)
	13,183	7,687

Reserves, retained earnings and profit (loss) of the year decreased by Euro 5,496 million compared to December 31, 2000. The reduction was due mainly to the payment of 2000 dividends (Euro 2,309 million), the net loss for the year (Euro 2,068 million), the cancellation of 112,998,070 savings shares of treasury stock by Telecom Italia at the time of the re-denomination of share capital in Euro (Euro 662 million at December 31, 2000 in addition to Euro 49 million for purchases in the early months of 2001) as well as the decrease in the value of net equities of some foreign companies as a result of the unfavorable movements in the local currency against the Euro.

Included in reserves and retained earnings are retained earnings of subsidiaries, legal reserves, revaluation reserves and the reserves held on a tax-deferred basis. No income taxes have been provided with respect to such reserves either because they are considered permanently reinvested in the subsidiaries or because the conditions which could give rise to a tax liability are not expected to occur. Legal reserves are not available for payment of dividends.

Note 18 — Commitments, Guarantees and Contingent Liabilities

As of December 31, 2001, the Group has purchase commitments totaling Euro 3,305 million (Euro 4,286 million as of December 31, 2000).

In particular, the purchase commitments mainly refer to:

- Telecom Italia's commitment for the put option on Seat Pagine Gialle shares (Euro 2,985 million) described below. Under the contract stipulated on March 15, 2000 (as subsequently amended and integrated), Telecom Italia gave Huit II a put option on 710,777,200 Seat Pagine Gialle shares at a strike price of Euro 4.2 per share. The contract provided for the exercise of such option after the deed of merger between Seat Pagine Gialle and Tin.it was recorded in the Companies Register. Huit II later transferred the put option to Chase Equity Limited (CEL), together with the ownership of the corresponding Seat Pagine Gialle shares. On December 4, 2000, CEL renegotiated the contract with Telecom Italia, extending the period to five years, with the possibility of exercising the option at an earlier date in April and May 2003, 2004 and 2005. The time extension made it possible to defer the financial impact.
  Stet International Netherlands (a wholly-owned subsidiary of Telecom Italia) then purchased from CEL, through the Liberator Ltd. trust, a call option on 660,777,200 Seat Pagine Gialle ordinary shares with the same expiry date and strike price as the put option, paying a total premium of Euro 747 million. Moreover, for the purpose of transferring the effects of this latter transaction to Telecom Italia, a call option was stipulated, with the same features, between Telecom Italia and Stet International Netherlands.
  On February 25, 2002, Telecom Italia concluded the renegotiation of the December 4, 2000 put and call options with the JPMorgan Chase group.
  In particular, a decision was made to reduce the exercise price of the aforementioned options from Euro 4.2 to Euro 3.4 per share; in view of the reduction, Telecom agreed to pay JPMorgan Chase Euro 569 million at the original expiration date of December 2005, unless Telecom Italia decides to exercise the right to pay the present value of the same amount prior to that date.
  A decision was also made to eliminate the right of either party to exercise the options, which expire on December 6, 2005, except for Telecom Italia's right to exercise part of the call options earlier; the early exercise of the call option per tranche, beginning from December 2004, covers 355 million Seat Pagine Gialle shares.
  At the expiration date the purchase of Seat Pagine Gialle shares will require an entry to record the difference on consolidation equal to the purchase cost, recorded in commitments, less the underlying share of net equity at current values at that date.
  At December 31, 2001, the valuation of the forward purchase commitment of Seat Pagine Gialle shares led to a provision in the reserves for risks and charges (other reserves) of Euro 569 million to cover the estimated non recoverability of the original price to exercise the option. This provision is in line with the cost connected with the above-mentioned revision of the strike price;
- contractual commitment by Telecom Italia Lab S.A. (Euro 113 million) to pay the remaining amounts subscribed to but not yet paid to four mutual funds specialized in financing emerging companies in telecommunication, Internet, Intranet and Broadband networks.

The reduction of Euro 1,521 million from December 31, 2000 is relative to the purchase of Entel Chile for Euro 959 million during the first months of 2001 and Seat Pagine Gialle's commitment to purchase 40% of Finanziaria Web S.p.A. for Euro 700 million. As regards to the latter, Seat Pagine Gialle S.p.A. passed a resolution during 2001 not to proceed on this acquisition, due to the excessive burden that has arisen from the framework agreement dated September 20, 2000 with the De Agostini Group concerning this acquisition, following the unexpected loss of value that occurred among the Internet Business companies.

De Agostini has initiated arbitration proceedings against the SEAT Group, for the alleged nonfulfillment of the framework agreement with regard to this obligation. The De Agostini Group is asking for the specific execution of the framework agreement and therefore that the Finanziaria Web shares should be disposed for transfer to SEAT for the amount originally agreed of Euro 700 million, with payment beginning in June 30, 2003, as well as the payment of unspecified damages. If the Company would be required to pay the full amount, this could be in excess of the fair value in 2003.

As of December 31, 2001, the Group has sale commitments totaling Euro 2,064 million (Euro 76 million as of December 31, 2000). The sales commitments include the Group's commitment for the sale of the investment in the Spanish company Auna (Euro 1,999 million).

As of December 31, 2001, the Group has given guarantees of Euro 1,422 million (Euro 2,931 million as of December 31, 2000). The amount of the guarantees provided is presented net of counter-guarantees received amounting to Euro 567 million (Euro 560 million as of December 31, 2000). Guarantees provided mainly consist of sureties provided by Telecom Italia and TIM on behalf of affiliated companies and others for medium/long-term loan transactions and guarantees on bids to acquire TLC licenses abroad.

As of December 31, 2001, the Group has given collateral of Euro 163 million (Euro 3 million as of December 31, 2000). Collateral provided refers to liens and mortgages on assets of certain companies included in consolidation. In particular, the collateral includes IS TIM shares pledged as guarantees by TIM International for the performance of the obligations covered by the supply contracts signed by IS TIM with Ericsson and Siemens.

The total amount of Telecom Italia commitments as of December 31, 2001 for building rental obligations to be paid to IM.SER under 21-year contracts was Euro 3,678 million. The commitment from 2002 to 2006 is Euro 185 million per year.

Telecom Italia and certain of its subsidiaries are involved in various legal actions. However, in the opinion of the Group's management, the risks relating to such actions will not materially affect the Group's financial position or results of operations.

Pursuant to a law enacted in 1992, Telecom Italia is required to ensure that all personnel employed on February 20, 1992 are covered by the Fondo Previdenza Telefonici ("FPT"), the telephone workers social security fund, for their entire retirement benefit, including sums due in respect to prior employment in other companies. The contributions to cover these benefits are to be computed by INPS (the Italian social security institution), and would be paid in 15 equal annual installments. A subsequent law established that the cost for such contributions should be recorded in the financial statements and be deductible for tax purposes in the respective years as paid. The amount of the liability for the contributions due is not certain as there is disagreement between the Group and INPS as to the computation of the amounts due. The issues are presently being debated in legal proceedings between the parties involved pending in front of the Italian judicial courts. Telecom Italia's management believes that the aggregate liability as of December 31, 2001 relating to such contributions can be estimated to range from Euro 960 million to Euro 1,284 million (of which Euro 334 million has already been paid), net of the residual amount already recorded in 1993 by Iritel and presently appearing in these consolidated financial statements following the IRITEL merger (Euro 656 million).

Pre-amortization interest (including that relating to the employees of the former Iritel), subsequent to the agreement between INPS and Telecom Italia, was paid by the latter - with reservation - in fifteen equal annual deferred installments, including interest at an annual rate of 5%, up to the end of 1999, for a total amount of Euro 112 million. In compliance with the ruling of the Court of Appeals, No. 4242 of April 5, 2000, which upheld Telecom Italia's position, payment of the above-described interest and accrued interest related thereto was suspended as from June 2000 (for a residual amount of Euro 407 million).

Management also believes that the other contributions eventually due will not significantly affect the Group's financial position or future results of operations since, as provided for by the pertinent law, any costs required to be paid will be paid and recorded over a period of fifteen years.

Financial derivatives

The Group uses derivatives mainly for the management of its debt positions, primarily interest rate swaps (IRS) and interest rate options (IRO) to reduce the interest rate exposure on fixed-rate and floating-rate bank loans and bonds, and cross-currency & interest rate swaps (CIRS) and currency forwards to convert various currency loans – mainly in US dollar and Euro – into the functional currencies of the various subsidiaries.

The following table gives a description of the financial derivative contracts used to hedge debt positions of the Group, outstanding as of December 31, 2001.

(in millions of Euro)	**Notional amount/ Capital exchanged as of December 31, 2001**
Interest rate swaps and interest options	5,979
Cross currency and interest rate swaps	1,847

IRSs and IROs involve or can involve the exchange of flows of interest calculated on the applicable notional principal amount at the agreed fixed or variable rates at the specified maturity date with the counterparts. This principal amount does not represent the amount exchanged between the parties and therefore does not constitute a measure of exposure to credit risk, which is instead limited to the amount of interest or interest differentials to be received at the interest date.

The same also applies to CIRSs which involve the exchange of capital, in the respective currencies of denomination, in addition to the settlement of periodic interest flows, at maturity and eventually at another date.

The counterparties to derivative contracts are generally highly rated banks and financial institutions and such counterparties are continually monitored in order to minimize the risk of non-performance.

Besides derivative contracts used as part of the management of debt exposure, as of December 31, 2001, there were IRSs and CIRSs at the Luxembourg subsidiary Softe to hedge investments in notes and for cash management purposes representing a notional principal amount of Euro 2,084 million. Lastly, the subsidiary Sogerim has entered into transactions to hedge funds for cash management purposes for a principal amount of Euro 368 million.

Finally, as of December 31, 2001, Telecom Italia is carrying transactions to hedge interest rate and exchange risks on short-term loans for a total of Euro 311 million, using forward rate agreements for Euro 300 million and currency forwards for Euro 11 million.

Note 19—Other income

	Year ended December 31,		
	1999	2000	2001
		(Millions of Euro),	
Operating grants	20	20	24
Gain on disposal of intangibles and fixed assets	18	10	12
Amount credited to income of capital grants	73	72	73
Miscellaneous income	405	324	308
	516	426	417

In particular:

- operating grants refer chiefly to the amounts received to cover the costs of research, development and technological innovation;
- capital grants recorded in the consolidated statement of operations represent the portion that became available during the year based on the depreciation pattern of the underlying fixed asset;
- miscellaneous income from operations includes, among other things, charges to customers of the telecommunications services companies for the late payment of telephone bills (Euro 112 million in 2001, Euro 110 million in 2000 and Euro 130 million in 1999).

Note 20—Other external charges

	Year ended December 31,		
	1999	2000	2001
		(Millions of Euro)	
Costs of external services rendered	7,380	8,394	9,552
Rents and lease payments	704	798	1,069
Provision for bad debts	363	477	439
Provision for risk	80	119	189
Write-downs of fixed assets and intangibles	73	48	16
TLC license fee	606	572	524
Other provisions and operating charges	380	382	382
	9,586	10,790	12,171

The 2001 increase in costs of external services rendered of Euro 1,158 million was mainly due to the higher costs for the operation and development of mobile telecommunications and the change in the scope of consolidation. In 2000, the increase in costs of external services rendered of Euro 1,014 million was mainly due to the inclusion of the Nortel Inversora group and the increase in the costs of operating and developing mobile telecommunications services.

The 2001 increase in rents and lease payments was mainly due to the higher costs sustained by Telecom Italia on the rentals of buildings sold to IM.SER (Euro 252 million).

Note 21—Financial income

	Year ended December 31,		
	1999	2000	2001
		(Millions of Euro)	
Dividends	60	139	17
Capital gain on sale and other income from equity investments	86	167	137
Interest and capital gains on fixed-income securities	97	105	138
Interest and commission from:			
— unconsolidated subsidiaries and associated companies	15	24	24
— banks	54	74	110
— customers	12	3	2
Gain on foreign exchange	139	196	217
Other	92	139	431
	555	847	1,076

In 2001, "other" includes Euro 298 million of income on hedging contracts and income from the application of inflation accounting principles.

Note 22—Financial expense

	Year ended December 31,		
	1999	2000	2001
		(Millions of Euro)	
Interest and commission paid to:			
— banks, on short and long term loans	351	678	815
— other financial institutions, on short and long term loans	28	59	155
— suppliers	67	32	10
— unconsolidated subsidiaries and associated companies	2	34	31
Interest and other charges on debenture loans	50	148	449
Losses on foreign exchange	164	175	348
Write-downs and equity in losses in unconsolidated subsidiaries, affiliated and other companies, net	565	1,025	1,665
Write-downs of marketable debt and equity securities	-	134	291
Other	239	185	1,267
	1,466	2,470	5,031

Net write-downs and equity in the income and losses in unconsolidated subsidiaries, affiliated and other companies reflects primarily the Group's proportionate share of the results of operations for the Group's equity method investments, including the amortization of goodwill that arose upon the acquisition of such investments (Euro 316 million in 2001, Euro 453 million in 2000 and Euro 184 million in 1999). The higher expenses in 2001 were particularly affected by:

- the losses of IS TIM (Turkey) of Euro 334 million due not only to expenses incurred in conjunction with the start-up phase but also the effects of the currency crisis in Turkey and the application of inflation accounting principles;
- the writedown of Stream (Euro 241 million);
- the losses of the Nortel Inversora group (Euro 238 million), which were related to the economic crisis in Argentina and due mainly to exchange losses on financial payables;

- the writedown of Astrolink of Euro 259 million by Telespazio as the related project was suspended.

In 2000, the increase in net write-downs and equity in the income and losses in unconsolidated subsidiaries, affiliated and other companies was essentially due, other than the above mentioned increase in amortization of goodwill, to the losses incurred by the Maxitel group (Euro 224 million), Stream (Euro 202 million), Auna group (Euro 176 million) and Telekom Austria (Euro 52 million).

Other is mainly related to the provision of Euro 569 million for the forward purchase commitment of Seat Pagine Gialle shares connected with the estimated nonrecoverability of the original price to exercise the option, the portion of interest expenses for the year of Euro 152 million relating to the deferral of the put option on Seat Pagine Gialle shares recorded in prepaid interest expenses and expenses on hedging contracts of Euro 272 million.

Note 23—Other income and expense, net

	Year ended December 31,		
	1999	2000	2001
		(Millions of Euro)	
Provisions and write downs of goodwill and equity investments	-	-	(2,984)
Restructuring costs	(256)	(492)	(380)
Charges as required under Law n. 58/1992 (see Note 18)	(188)	(153)	(155)
Gains on the disposal of investments	26	1,146	392
Other, net	(89)	(715)	(325)
	(507)	(214)	(3,452)

Provision and write-downs of goodwill and equity investments have been made on a consistent basis according to the new business plans and market trends and are analyzed as follows:

- Euro 1,303 million for the writedown of goodwill relating to consolidated companies (9 Telecom group, Entel Bolivia, Entel Chile group, Maxitel group, Tele Celular Sul group, Tele Nordeste Celular group, Tim Brazil, Med-1 group and certain companies in the Seat Pagine Gialle group);
- Euro 1,078 million for the writedown of goodwill relating to companies accounted for by the equity method (GLB Serviços Interativos, Solpart Participacoes, Telekom Austria and the Nortel Inversora group); and
- Euro 603 million for other provisions relating to equity investments.

Restructuring costs are related to expenses for employee cutbacks and layoffs.

In 2001 gains on the disposal of investments mainly arose from the sale of the 70% holding in Mirror International Holding, the company through which the satellite companies were contributed to the Lehman Brothers group (Euro 170 million) and the 30% holding in Mediterranean Nautilus S.A. to the Israeli company F.T.T. Investment (Euro 94 million), the dilution of the investment in Auna (Euro 16 million) and the increase in the net equity of Lottomatica as a result of the capital increase set aside for third parties when it was listed (Euro 35 million). In 2000, gains on the disposal of investments mainly arose from the old divestiture plan of the Group (Euro 969 million), which was related to the sale of 80.1% of the Italtel group (Euro 393 million), the Meie group (Euro 232 million), Teleleasing (Euro 21 million), the Sirti group (Euro 11 million) and the sale of a portion of the real estate portfolio through the sale by Telecom Italia of the 60% of IM.SER (Euro 312 million) to third parties. The remaining gains of Euro 177 million were related to the sale of other investments and intangibles, fixed assets and business segments, of which Euro 55 million came from the sale of the investment in the Bharti group.

In 2001 "other, net" included: i) income from the release of reserves by Telecom Italia recorded in prior years for risks which did not materialize (Euro 120 million mainly relating to the reserve for the contract with Iraq of Euro 62 million and the reserve for corporate restructuring of Euro 50 million); ii) income (Euro 32 million) deriving from the partial cancellation, by the Council of State, of resolution No. 7533/1999 of the Antitrust Authority under which TIM and Omnitel Pronto Italia were levied administrative fines for the alleged violation of antitrust laws relating to the price fixing of fixed-mobile rates; iii) the provision for expenses connected with the Vivendi/Canal Plus agreement for the transfer of the investment in Stream (Euro 248 million); iv) the extraordinary contributions to INPS established by the 2000 Finance Bill for the three years 2000-2002 to meet the higher financial requirements covered by the rules of the Fondo Previdenza Telefonici (FPT) that was abolished and became part of the general "Employee Pension Fund" (Euro 77 million); and v) the costs resulting from the decision to reposition the broadcasting station La7 as a consequence of the closing of a series of contracts (Euro 85 million).

In 2000, "other, net" included: i) the provision made by TIM to the reserve for technological risk (Euro 400 million); ii) the expenses and provisions connected to the transactions for the disposal of investment holdings and the real estate portfolio (Euro 180 million); iii) the extraordinary annual contribution to INPS to meet the higher financial requirements covered by the rules of the FPT fund (Euro 77 million); and iv) the residual amount for the fine of Euro 41 million imposed on TIM by the Antitrust Authority for the alleged violation of rules against price-fixing. This amount was equal to the difference between the original fine (Euro 52 million) and the amount accrued by TIM in the 1999 financial statements (Euro 11 million).

Note 24—Income taxes

Income taxes include the current, deferred and prepaid income taxes of individual consolidated companies.

Income taxes amounted to Euro 925 million (Euro 2,020 million in 2000 and Euro 2,606 million in 1999) as a result of current income taxes of Euro 1,186 million and prepaid income taxes for Euro 261 million.

The 2001 decrease in income taxes (Euro 1,095 million) was due to a reduction in the taxable base caused mainly by the extraordinary provisions and write-downs of Telecom Italia and TIM regarding the valuation of foreign investments.

In 2000 tax as a percentage of income before income taxes was 40.7% compared to 52% in 1999. The reduction in the level of tax as a percentage of income was due to: i) the utilization of the tax benefits on investments made by TIM; and ii) the taxation of gains from the sale of investments and the contribution of a portion of the real estate portfolio by Telecom Italia to IM.SER, the real estate company in which the Group sold a 60% interest, using the substitute equalization tax. The tax rate was also affected by the release of deferred taxes by Telecom Italia in accordance with the application of art. 14 of Law 342/2000. Under this law, the "Reserve for accelerated depreciation" was reclassified and the tax expense for the year was reduced by the excess amount of the "reserve for deferred taxes".

Italian and Foreign income (loss) before taxes are as follows:

	Year ended December 31,		
	1999	2000	2001
	(Millions of Euro)		
Italy	5,314	4,897	2,856
Foreign	(299)	71	(3,589)
	5,015	4,968	(733)

The provision for income taxes consisted of the following in the years ended December 31, 1999, 2000 and 2001:

	Year ended December 31,		
	1999	2000	2001
	(Millions of Euro)		
Current tax expense:			
Italy	2,815	2,289	1,158
Foreign	69	197	28
Total current tax expense	2,884	2,486	1,186
Deferred:			
Italy	(261)	(493)	(254)
Foreign	(17)	27	(7)
Deferred tax expense / (benefit)	(278)	(466)	(261)
Income tax expense	2,606	2,020	925

Net Operating Losses

At December 31, 2000 and 2001, the Company has net operating loss carryforwards of Euro 2,594 million and Euro 5,970 million respectively. Losses as of December 31, 2001 include Euro 599 million attributable to Italian companies, Euro 3,076 million attributable to other European companies, Euro 924 million attributable to Latin American companies and Euro 1,371 million attributable to others. The losses at December 31, 2001 of Euro 5,970 million expire as follows: Euro 1,199 million between 2002 and 2006, Euro 431 million beyond 2006, and Euro 4,340 do not expire.

Utilization of these losses are limited to future earnings of the respective companies. Where it is anticipated that all or a portion of these losses will not be utilized, a valuation allowance has been placed against the related deferred tax asset.

Note 25—Subsequent events

2002 – 2022 notes reserved for employees of the Telecom Italia Group

On January 1, 2002, following the resolution passed at the Board of Directors' Meeting on July 27, 2001, the offer began for subscription to the "Telecom Italia 2002 – 2022 floating rate notes, open special series, reserved for the employees of the Telecom Italia Group, in service and retired", maturing January 1, 2022, for a maximum amount of Euro 1 billion. At the same time, the SIP 1992 – 2010 notes with features similar to the new notes were called for early redemption.

The new notes, which pay gross interest semiannually (payable on January 1 and July 1 of each year not in advance), can be subscribed to over the entire period of the notes until the maximum offer has been entirely subscribed and also contain a right to sell by the noteholder to Telecom Italia that can be exercised at any time at face value; the notes can also be called for early redemption by the Company at each interest payment date at face value, with notice at least three months in advance. As of June 15, about Euro 170 million of notes had been subscribed to and noteholders numbered 10,497.

Issue of notes

In February 2002, Telecom Italia issued an additional aggregate principal amount of Euro 2.5 billion in notes. The issue is divided into two tranches of Euro 1.25 billion each, at a fixed rate of interest, respectively, with maturity dates of February 1, 2007 and February 1, 2012. The Euro 2.5 billion in notes was issued as part of the "Global Note Program" aimed at restructuring the Group's debt. The total amount of the global Note Program, by vote of the Board of Directors on December 18, 2001, was raised from US dollars 10 billion to US dollars 12 billion or the equivalent in other currencies.

Conclusion of the agreement for the revision of the put/call options on Seat Pagine Gialle shares

On February 25, 2002, Telecom Italia and the JPMorgan Chase group signed the definitive agreements relating to the re-negotiation of the put and call options on Seat Pagine Gialle shares; the economic effects of this agreement that have been recognized are disclosed in Note 22 to these financial statements.

Social security contributions in accordance with Law No 58/1191

In a recent verdict, the Supreme Court ruled for the second time that Telecom Italia does not have to pay pre-amortization interest claimed by INPS in application of Law No 58/1992 (regarding the reform of the telecommunications sector). As a result of the above decision, Telecom Italia will proceed to reach an agreement with the above-named institution to work out how to recover the sums paid by the Company for that purpose up to 1999, equal to Euro 112 million, plus 5% interest.

Divestiture program

- **Lottomatica**: on January 18, 2002 Finsiel accepted the tender offer launched by Tyche S.p.A. (De Agostini Group) and tendered its 18.3% stake in the share capital of Lottomatica. The transfer took place on February 5, 2002 resulting in proceeds equal to Euro 212 million.
- **Auna**: on January 15, 2002, Telecom Italia, Endesa, Unión Fenosa and Banco Santander Central Hispano signed an agreement for the sale of Telecom Italia's interest in Auna Operadores de Telecomunicaciones, S.A. ("Auna") for a price of Euro 2 billion in cash. The effectiveness of the agreement is subject to applicable regulatory approvals. The purchasers have granted Telecom Italia a right of first refusal for two years to acquire any shares currently held by the Telecom Italia group which the purchasers may seek to sell during this two-year period. The costs associated with the right of first refusal together with financial advisory fees and other expenses are approximately Euro 150 million, which will result in net proceeds for the Telecom Italia Group of approximately Euro 1.85 billion. Furthermore, in connection with the foregoing Telecom Italia has obtained a pre-emptive right on Amena shares for the same period of time.
- **BDT**: In February 2002, Telecom Italia reached an agreement with Bouygues S.A. to sell TIM International's stake (19.61%) in BDT, the company that controls 55% of the French mobile company Bouygues Télécom for a consideration of approximately Euro 750 million. The transaction was completed on March 28, 2002, realizing a net gain of Euro 484 million, which contributed Euro 266 million to the consolidated net income of the Telecom Italia Group.
- **Stream**: In February 2002, Telecom Italia reached an agreement with News Corporation and Vivendi Universal/Canal+ for the sale of its 50% stake in Stream S.p.A., a multimedia services platform, for a total consideration of U.S.$ 42 million. The agreement, which was subject to regulatory approvals by Italian authorities, provided for the sale of Telecom Italia's 50% stake in Stream to News Corporation (which holds the remaining 50% of Stream) and the successive sale by News Corporation of 100% of Stream to the Vivendi Universal/Canal+. Telecom Italia has agreed to forfeit approximately U.S.$ 80 million of accounts receivable from Stream. The economic effects of this transaction have already been recorded in 2001 as extraordinary provisions.

  On May 13, 2002, the Competition Authority authorized the acquisition of Stream by Canal+/Telepiù, subject to certain conditions aimed at easing entry by new competitors in the pay-TV market, the development of alternative means of transmission, as well as guaranteeing the protection of consumers. On May 15, 2002 Vivendi Universal and Canal+ announced that, due to the conditions imposed by the Antitrust Authority, they would abandon their plan to acquire Stream.

  On June 8, 2002, News Corporation announced that it had signed an agreement with respect to the acquisition of Telepiù by a group of investors headed by News Corporation. This agreement is subject to a number of conditions, including the agreement of Telecom Italia. As of June 19, 2002 the sale of Stream is in discussions.
- **Sale of Interest in Mobilkom and gradual disposal of interest in Telekom Austria**: at the beginning of June 2002, the Group reached an agreement with Telekom Austria for the sale of TIM's 25% stake in Mobilkom, through the acquisition by Telekom Austria from TIM International of 100% of Autel Beiteiligungs GmbH, which owns the participation in Mobilkom. In the same period, the Group also reached an agreement with Telekom Austria's main shareholder, Österreichische Industrieholding AG ("ÖIAG"), for a gradual and coordinated disposal of Telecom Italia's interest in Telekom Austria starting from the second half of 2002.

  TIM International's disposal of its stake in Mobilkom is expected to generate proceeds of approximately Euro 716 million out of which Euro 690 million represents the price of the stake and Euro 26 million represents the dividend for the 2001 financial year. The capital gain for TIM, on a consolidated basis, will correspond to approximately Euro 163 million.

The disposal does not require clearance by the relevant antitrust authorities and is expected to close before the end of June 2002. As a consequence of such disposal, the Mobilkom shareholders' agreement will be terminated.
In conjunction with the Mobilkom transaction, the Group has also reached an agreement with ÖIAG regarding, among others, an amendment to the shareholder agreements relating to Telekom Austria, in which the Group, through Telecom Italia, has approximately a 29.8% stake.
The agreement will permit Telecom Italia International to undertake a gradual, coordinated disposal of its interest in Telekom Austria, and allow ÖIAG to take further steps in its privatization of the Austrian telephone company. Although Telecom Italia and ÖIAG will continue to review strategic alternatives for the sale of their stakes in Telekom Austria, the amended agreement will give them the right to dispose of shares in the public market.

Tiglio Project

On May 24, 2002 the Telecom Italia Group and the Olivetti Group reached an agreement with Pirelli & C. Real Estate S.p.A., Pirelli S.p.A., MSMC Italy Holding B.V. and Popoy Holding B.V. with regard to the so called "Tiglio Project", aimed at integrating real-estate assets and entities of the companies involved with real-estate services and consequently maximizing their value.

According to the terms of the agreement Telecom Italia Group will transfer property, land and staff in charge of real estate asset-management activities to two newly created companies; at a later date a closed-end real-estate fund will receive the above mentioned assets.

In particular, Telecom Italia Group's contribution will be approximately Euro 1,350 million with gross capital gains of approximately Euro 170 million.

The implementation of the project is subject to obtaining the necessary financing and the transfer of 40% of IM.SER real-estate to the Telecom Italia Group.

Buy-back of Telecom Italia stock

By authorization of the ordinary shareholders' meeting of November 7, 2001, the Company, in March, began to buy-back treasury stock on the market according to the terms and in the manner established by existing laws and the shareholders' resolution. As of June 15, 2002, 2,981,200 Shares and 10,350,000 Savings Shares were purchased at an average price of Euro 8.53 per Share and Euro 5.94 per Savings Shares, for a total investment of about Euro 87 million.

Note 26—Reconciliation to Accounting Principles Generally Accepted in the United States

The consolidated financial statements of the Group are prepared in accordance with accounting principles established or adopted by the Italian Accounting Profession described in Notes 1, 2 and 3, which differ in certain significant respects from U.S. GAAP. A summary of the significant differences is as follows:

Goodwill deriving from STET-Old Telecom Italia merger

During 1997, Old Telecom Italia was merged with and into STET (which was renamed Telecom Italia). Under Italian GAAP, the combination was accounted for as a merger and the financial statements reflected the ownership change based on the net book value of the combined entities. For Italian GAAP purposes, the merger was recognized as of January 1, 1997. Under U.S. GAAP, the combination was accounted for as a purchase, effective as of July 18, 1997. The assets and liabilities of Old Telecom Italia were recorded at fair value. The excess of the purchase price over the fair value of net assets was recorded as goodwill. This is being amortized until 2012, which represented the residual license period at the time of the merger.

Purchase method accounting transactions

Several acquisitions, which are required to be accounted for under the purchase method of accounting for U.S. GAAP purposes, have been recorded differently under Italian GAAP:

- Old Telecom Italia formation—Upon the formation of Old Telecom Italia in 1994, Telecom Italia's ownership percentage in the combined companies was diluted. The Italian GAAP financial statements reflected the ownership change impact based on the net book value of the combined entities, while U.S. GAAP required the ownership change to be treated as a purchase, at fair value. For U.S. GAAP purposes, the difference between fair value and book value was being amortized until 2012, which represented the residual license period at the time of the formation.

- Ownership change in Old Telecom Italia—In 1994, Telecom Italia increased its ownership in Old Telecom Italia by receiving previously unissued stock and its Italian GAAP financial statements reflected this transaction as an equity reduction for the excess of the investment over the ownership percentage of Old Telecom Italia's book value. Under U.S. GAAP this excess is recorded as an asset to be amortized over 19 years.

- Investment in Telsi—In 1995, Telecom Italia and Siemens A.G. each contributed assets for a fifty percent non-controlling interest in Telsi Ltd. The Italian GAAP financial statements reflected a gain based on the original book value of the investments contributed while for U.S. GAAP purposes the transaction has been accounted for using the fair market value of the investments contributed. The U.S. GAAP reconciliation reflects the amortization of the underlying basis difference between Telecom Italia's investment in Telsi and Telsi's recorded equity. This was fully amortized at December 31, 1999.

- SEAT has made several acquisitions since it was acquired in 2000. Certain of these acquisitions were made through the issuance of additional SEAT shares for the targets' stock. For purposes of Italian GAAP, these transactions were recorded as equity movements. For purposes of U.S. GAAP, the fair value of the stake received is used to determine the purchase price, if not readily determinable then the fair value of SEAT's stake is used to measure the acquisition price.

For purposes of U.S. GAAP, amortization of goodwill which cease as of January 1, 2002 in accordance with requirements of SFAS n. 142, as discussed in Footnote 28(t).

Revaluation of fixed assets

The Group has revalued its fixed assets as permitted by Italian Law. Under Italian GAAP the depreciation charge is based on the revalued amounts. U.S. GAAP does not permit revaluation of fixed assets and requires depreciation based on historical acquisition cost.

Elimination of intercompany profit on sales of intangible and fixed assets and related depreciation

Until 1993, the Group did not eliminate intercompany profit on sales of intangible and fixed assets. Therefore, certain intangible and fixed assets are valued at the sales amount instead of historical book value. The amounts, principally from manufacturing and installation companies to telecommunication companies, are being depreciated over the useful life of the assets. U.S. GAAP requires the elimination of intercompany profits and requires depreciation based on historical cost.

Capitalization of interest on tangible and intangible assets under construction and related depreciation

The Group capitalizes interest on construction projects only when specific borrowings can be attributed to the project. U.S. GAAP requires interest to be capitalized on both tangible and intangible assets regardless of whether specific borrowings relate to the project. The capitalized interest is being depreciated over the remaining useful life of the assets.

Contributions to telephone workers social security fund

As discussed in Note 18 to these financial statements, pursuant to Italian laws, the Group has not recorded a liability for contributions due to the INPS. U.S. GAAP requires the recognition of a liability when it is probable and can be reasonably estimated. Accordingly, an estimate of the liability is reflected in the U.S. GAAP reconciliations net of any payments made and expensed through the Italian GAAP statement of operations.

Accounting for long-term contracts under the percentage of completion method

Prior to 1999 the Group recognized revenues for its long - term contracts under the completed contract method. In 1999, the Group changed its accounting principle and started accounting for these contracts using the percentage of completion method, consistent with U.S. GAAP.

Investment in stock of subsidiary companies

Telecom Italia Group has purchased, sold and holds stock of certain consolidated subsidiaries and records these investments within current assets. The portion of the earnings, losses and the ownership interest in the net assets associated with such stock is not consolidated under Italian GAAP. The equity securities are recorded at the lower of historical cost or fair value within current assets. Write-downs below historical cost are reversed in subsequent periods up to the original cost, if the fair value of the equity securities increases. Write-downs and any subsequent reversals are recorded in the statement of operations.

Under U.S. GAAP, the value of the investment in subsidiary stock has been adjusted to original cost and has been eliminated upon consolidation. The elimination of the investment results in additional goodwill, the reversal of any write-downs or write-ups taken under Italian GAAP, and the accrual of the incremental income or losses from the additional ownership percentage being consolidated.

SEAT-Tin.it transaction

In 2000, several significant events occurred in connection with the acquisition of a controlling interest in SEAT Pagine Gialle S.p.A. ("SEAT"), giving rise to the following differences. See also Note 28 (f) for further discussion of the SEAT Acquisition.

- In February 2000, the Group announced its intention to acquire a controlling interest in SEAT, the publisher of the Italian yellow pages. The acquisition was made with a combination of cash and the issuance of shares in Telecom Italia's wholly owned internet subsidiary, Tin.it, to SEAT. For purposes of Italian GAAP, the transaction was accounted for as an acquisition using purchase accounting for the cash portion of the acquisition, and as a pooling of interest for the exchange of shares. Goodwill of Euro 6,796 million was created under Italian GAAP. For purposes of U.S. GAAP the acquisition, including the shares exchanged, was accounted for at fair value using the purchase method of accounting. For U.S. GAAP purposes the distribution of the subsidiary's shares to SEAT generated a gain of Euro 6,537 million representing the difference between the fair value of the SEAT shares received and the book value of the subsidiary's shares issued. Additionally, SEAT shares were issued directly to Telecom Italia shareholders in exchange for 8.168 percent of the wholly-owned subsidiary's shares, which has been accounted for as a dividend at fair value, generating a gain of Euro 1,329 million.

- For purposes of Italian GAAP, the SEAT acquisition was considered effective as of December 31, 2000. For purposes of U.S. GAAP, the acquisition was considered effective as of October 1, 2000, the date that operating control of SEAT passed to Telecom Italia. Therefore, an adjustment has been recorded to account for the fourth quarter results of SEAT.

- Under U.S. GAAP purchase accounting requirements, the fair value of the SEAT acquisition was Euro 16,025 million. Included in this amount was acquisition goodwill relating to SEAT of Euro 13,834 million . From the date at which the acquisition was announced until the end of the fiscal year, the market valuations of hi-tech companies, in particular those associated with internet activity, were severely reduced. The share-price reduction was considered a possible indication of impairment, thereby requiring an analysis of a potential impairment of SEAT based upon SFAS 121, as discussed in the U.S. GAAP policy Note 28. Based on this review, an impairment charge of Euro 7,966 million was recorded to U.S. GAAP net income to reduce the value of the SEAT investment.

- As discussed further in Note 28 (f), Telecom Italia entered into a put/call arrangement with a third party in 2000 as part of the acquisition of SEAT. For US GAAP purposes, the put/call was recorded as indebtedness as part of the SEAT acquisition. As discussed in Notes 14 and 18, for Italian GAAP purposes, an accrual of Euro 569 million was provided for in 2001 in relation to this financing. As the debt has already been recorded under US GAAP as part of the purchase price of SEAT, the accrual made under Italian GAAP was reversed.

- After the acquisition of SEAT by the Group, SEAT made additional acquisitions in the fourth quarter of 2000, and throughout 2001. Certain of these acquisitions were done through the issuance of additional SEAT shares for the targets' stock. For purposes of Italian GAAP, these transactions were recorded as equity movements. For purposes of U.S. GAAP, the difference between the fair value of the assets received versus the proportional dilution of the SEAT investment resulted in a gain.

Sale of real estate portfolio

During the year 2000 the Group transferred certain real estate properties to a wholly owned subsidiary ("IM.SER"), 60% of which was then sold to third parties. Concurrent with the sale, the Group entered into a lease agreement for part of the portfolio. After the partial sale of the subsidiary, IM.SER borrowed funds from a syndicate of banks, with the funds being dispersed to the shareholders as a special dividend. For purposes of Italian GAAP, a gain was recognized to the extent of the fair market value of the transferred property over its historical cost for that portion sold to third parties. For purposes of U.S. GAAP, the transfer of the assets to the wholly owned subsidiary, the subsequent lease agreement and the receipt of cash by the Group from the partial sale and the special dividend are treated as a secured borrowing, therefore the gain recorded has been reversed and the real estate retained, along with the additional indebtedness, has been recorded at historical cost. See also Note 28 (o) for a further discussion of the real estate transaction.

Non-capitalizable expenses

The Group entered into several transactions for which certain costs were capitalized under Italian GAAP. These costs include expenses related to the SMH (renamed TIM International) transaction, and costs associated with intangible assets. For purposes of U.S. GAAP, these costs are not considered to be capitalizable, therefore they have been expensed. Subsequent periods' amortization of these expenses is reversed for US GAAP purposes.

Reversal of provisions

During the year 2000, due to the technological changes in the mobile phone industry, TIM determined that the invested cost related to analogic services, and the related network plants and billing systems, was rapidly approaching obsolescence due to the evolution of third generation services. The 2001 Italian GAAP financial statements reflect reserves for Euro 465 million recorded to accrue the estimated costs to modify these systems and/or to reflect their potentially reduced lives. U.S. GAAP requires that certain conditions must be met before reserves can be established and that the lives of fixed assets be evaluated to consider potential changes in the related depreciation period. These conditions, which under U.S. GAAP are stricter and more formal, have not been met. As a result in the U.S. GAAP reconciliation these provisions have been reversed and the remaining lives and related depreciation expense have been revised to reflect the expected remaining useful lives of the assets. For periods subsequent to 2000, charges and reversals of the reserve and the modified depreciation are treated as expenses under US GAAP.

Subsidiary stock conversions

In the course of 2000 two publicly traded subsidiaries, SEAT and TIM, each conducted share conversion offers related to their outstanding savings shares, a non-voting class of shares. As part of the conversion offering, holders of savings shares paid a premium to the applicable subsidiary and in return converted their savings shares to ordinary voting shares. These transactions resulted in a net increase in the book value of each subsidiary over and above Telecom Italia's proportionate investment.

For purposes of Italian GAAP, these gains were accounted for as changes in equity. For purposes of U.S. GAAP, these gains are recognized as non-operating gains in the income statement.

Common control transactions

During 2000, Telecom Italia acquired an additional ownership percentage of TIM by contributing its ownership of SMH (renamed TIM International) to TIM in exchange for new shares issued by TIM. Under Italian GAAP, this transaction resulted in an increase in equity and goodwill. As the timing of this transaction was near December 31, 2000, no amortization of the goodwill was recognized in the Italian GAAP financial statements.

Under U.S. GAAP, transactions between entities under common control require predecessor basis accounting. Therefore, the increase in equity and goodwill has been reversed. For periods subsequent to 2000, the annual amortization of the goodwill arising from this transaction is reversed for US GAAP purposes.

Satellite Transaction

In late 2001, Telecom Italia formed a wholly-owned subsidiary domiciled in Luxembourg (Mirror International Holding or "Mirror") to which it transferred its investments in entities in the satellite sector at an amount equal to the fair value of the investments contributed. Subsequently, 70% of the interest in Mirror was sold to Lehman Brothers Merchant Bank (LBMB), with Mirror subsequently obtaining debt financing. For Italian GAAP purposes this transaction was accounted for as a partial sale of financial assets with a pretax gain of Euro 170 million being recorded. For US GAAP purposes, Mirror is deemed a non-qualifying special purpose entity and the transaction is not accounted for as a sale. Instead, the accounts of Mirror have been consolidated by the Group with an elimination of the related step-up of the assets and an elimination of the gain. The cash received from the debt financing has been reflected as debt and the cash received from the partial sale of the investment has been reflected as minority interest in Mirror.

Derivative Financial Instruments

The Company enters into a number of derivative agreements to manage its risks related to changes in interest rates, foreign currency exchange rates and values of equity investments. The Company's derivative instruments include interest rate swap and collar agreements, cross currency and interest rate swaps, foreign currency options and forward contracts and equity securities options.

The Company's accounting policies related to its derivative financial instruments under Italian GAAP are described as follows:

- *Interest rate swap and collar agreements* – The Company enters into interest rate swap and collar agreements as part of the management of its interest rate exposures. Interest rate differentials to be paid or received as a result of interest rate swap and collar agreements are accrued and recognized as an adjustment of interest expense related to the designated debt.

- *Cross currency and interest rate swaps* – The Company enters into cross currency and interest rate swap agreements to manage its interest rate and foreign currency exchange exposures related to foreign currency denominated debt. The related foreign currency denominated debt and the foreign currency portion of the cross currency and interest rate swap agreements are adjusted using foreign currency exchange rates as of the related balance sheet date. Interest rate differentials to be paid or received as a result of cross currency and interest rate swap agreements are accrued and recognized as an adjustment of interest expense related to the designated debt.

- *Foreign currency options and forward contracts* – The Company enters into foreign currency forward exchange contracts as part of the management of its foreign currency exchange rate exposures related to existing foreign currency denominated assets and liabilities or firm commitments denominated in foreign currencies. The foreign currency forward exchange contracts and the related hedged positions are adjusted using foreign currency exchange rates as of the related balance sheet date and any net expense connected with each single transaction is recognized in the statement of operations. Discounts or premiums on forward contracts are recorded in the statement of operations using the straight-line method over the term of the related contract.

Through December 31, 2000 the Company's accounting policies were as described above for both US and Italian GAAP. Effective January 1, 2001, the Company retained the accounting policies described above for Italian GAAP purposes, but for US GAAP purposes adopted the provisions of Financial Accounting Standards Board Statement No. 133, *"Accounting for Derivative Instruments and Hedging Activities"* (SFAS 133). SFAS 133 requires the Company to recognize all of its derivative instruments as either assets or liabilities in the balance sheet at fair value. The accounting for changes in the fair value of a derivative instrument depends on whether it has been designated and qualifies as part of a hedging relationship and further, on the type of hedging relationship. For those derivative instruments that are designated and qualify as hedging instruments, the Company must designate the hedging instrument, based upon the exposure being hedged, as a fair value hedge, cash flow hedge or a hedge of a net investment in a foreign operation.

For derivative instruments that are designated and qualify as a fair value hedge, the gain or loss on the derivative instrument as well as the offsetting loss or gain on the hedged item attributable to the hedged risk are recognized in current earnings during the period of the change in fair values. For derivative instruments that are designated and qualify as a cash flow hedge, the effective portion of the gain or loss on the derivative instrument is reported as a component of other comprehensive income and reclassified into earnings in the same period or periods during which the hedged transaction affects earnings. The ineffective portion of the gain or loss on the derivative instrument, if any, is recognized in current earnings during the period of change. For derivative instruments that are designated and qualify as a hedge of a net investment in a foreign operation, the gain or loss is reported in other comprehensive income as part of the cumulative translation adjustment to the extent it is effective. Any ineffective portions of net investment hedges are recognized in current earnings during the period of change. For derivative instruments not designated or qualifying as hedging instruments, the gain or loss is recognized in current earnings during the period of change.

Impairment of Long-lived Assets

Under Italian GAAP, the Group recognizes impairments of fixed and long-lived assets when it becomes apparent that there has been a permanent diminution in value. Due to a strategic shift in the Group's priorities in 2001, coupled with a general decrease in asset values in the telecommunications sector, the Group recorded Euro 2,381 million of write-downs to investments, including equity investees.

For US GAAP, the Group employs the guidance provided in SFAS 121, *"Accounting for the Impairment of Long-lived Assets and for Long-Lived Assets to be Disposed Of"*. The application of SFAS 121 requires that, among other things, that an asset be identified and measured at it's lowest level of cash flows for impairment. Therefore, the asset identification and impairment methodology as required by US GAAP as compared to Italian GAAP gave rise to an additional charge of Euro 2,641 million in 2001.

Other

Other is comprised of the following:

Stock options

During 1999, 2000 and 2001, Telecom Italia, TIM, SEAT and Entel Chile awarded shares and granted stock options to certain managers. For purposes of Italian GAAP, the above transactions are treated by the Group as changes in share capital and additional paid-in-capital upon exercise. For U.S. GAAP purposes the Group applies Accounting Principles Board Opinion ("APB") No. 25, "Accounting for Stock Issued to Employees". Under APB No. 25, these transactions are treated as compensation expense for the difference between the quoted market price of the shares and the cost of those shares to the managers. This difference is determined on the "measurement date", which is the first date on which both the ultimate number of shares and the option or award prices are known.

Restructuring reserve

The Italian GAAP financial statements include a restructuring reserve made during the year 2000 as part of a group plan to reduce the workforce and re-train employees. U.S. GAAP requires that certain conditions must be met before a restructuring accrual can be established, as well as the type of costs which can be accrued. Training costs included within the accrual do not meet these conditions, and therefore the U.S. GAAP reconciliation reflects an adjustment to eliminate this amount. For periods subsequent to 2000, any charges to or reversals from the reserve are treated as expenses for U.S. GAAP purposes.

Investments in marketable securities

Telecom Italia Group holds marketable securities both for the purpose of selling them in the near term as well as holding them to take advantage of investment opportunities. As described in Note 4, under Italian GAAP, all investments are carried at the lower of cost or market value. Write-downs below historical cost are reversed in subsequent periods up to original cost if the fair market value of the securities increases.

Under U.S. GAAP, the securities are classified as trading and available for sale, respectively. The Group's "trading securities" are recorded at fair value, with unrealized gains and losses included in earnings. Available for sale securities are carried at fair value, with any unrealized gains or losses reflected in other comprehensive income on a net of tax basis. Declines in fair value that are other than temporary are reflected in current period earnings.

Revenue recognition

Under Italian GAAP, non-refundable activation and installation fees, and their related costs, are generally charged and recognized at the outset of a service contract. Additionally, on-line advertising revenues are recognized at the date the advertisement is first posted. Under U.S. GAAP, up front revenues related to non-refundable fees and certain related direct costs are deferred and recognized over the expected customer relationship period, and on-line advertising revenues are recognized over the life of the advertising period on a straight line basis.

Equity investees

The Group has certain investments in equity investees whereby the periodic accrual of income or loss is recorded on the basis of the Group Italian accounting policies. For purposes of US GAAP, the results of the equity investees are recognized on a US GAAP basis.

Universal service

Telecom Italia provides certain services, known as "universal services", which essentially required the Group to offer telephony services to remote and difficult areas, thereby generating losses due to the high fixed and maintenance costs not being offset by an adequate revenue stream. These universal services have been deemed by the National Regulatory Agency to have benefited new fixed and mobile competitors who have entered the marketplace after the deregulation of the industry. Consequently, the National Regulatory Agency determined the costs of providing these services, based on data provided by Telecom Italia, and allocated a pro rata portion of the costs to various competitors, who were requested to pay such allocated amounts to a fund, a portion of which should be remitted to Telecom Italia. The legality and propriety of the allocated charge has been disputed by the competitors who have initiated litigation with the Ministry of Communications ("Ministry"). Under Italian GAAP, Telecom Italia has accrued revenues related to universal service for Euro 26.77 million and Euro 30.48 million in 2000 and 2001, respectively, as "other income". At December 31, 2001 receivables amounting to Euro 39.09 million remained outstanding. Under US GAAP the revenues for universal services are not recognized until collected due to the uncertainty surrounding the amount of the revenues and the collectibility of the revenues in view of the litigation with the Ministry.

Deferred tax adjustments

The differences between Italian GAAP and U.S. GAAP are primarily related to the tax treatment for capital grants received by the Group prior to 1998 and the deferred taxes established for the basis differences of assets revaluations. Additionally, the Group generally does not recognize the benefit of net operating losses as tax assets or the benefit of other deferred tax assets that are not expected to reverse within three to five years.

Comprehensive Income

Statement of Financial Accounting Standards No. 130 (SFAS 130), *"Reporting Comprehensive Income"* requires disclosure of the components of and total comprehensive income in the period in which they are recognized in the consolidated financial statements. Comprehensive income is defined as the change in equity of a business enterprise arising from transactions and other events and circumstances from non-owner sources. It includes all changes in stockholders' equity during the reporting period except those resulting from investments by and distributions to owners. Unrealized gains and losses on investments classified as "available for sale securities" under U.S. GAAP, the cumulative effect of translation adjustments of foreign subsidiaries and the impact of adopting SFAS 133 related to derivatives have been recognized as a component of comprehensive income.

Treasury stock

Telecom Italia has periodically purchased its own savings shares. Under Italian GAAP, these savings shares have been recorded at historical cost within long-term assets, while under U.S. GAAP, the cost of the acquired shares is shown as a deduction from stockholders' equity. All treasury stocks have been cancelled in 2001.

Equity Investment in Nortel Inversora

Under Italian GAAP, the Company's equity investment in Nortel Inversora was accounted for under the equity method in 1999, the proportional consolidation method in 2000 and the equity method in 2001 (See Note 1). In accordance with U.S. GAAP, the equity investment in Nortel Inversora has been accounted for under the equity method of accounting for all periods presented. Other than the reclassification of minority interests from stockholders' equity under Italian GAAP to minority interests accrual under U.S. GAAP, there is no impact on net income or stockholders' equity as a result of the different accounting treatment under Italian and U.S. GAAP.

Significant differences and the effect of the above on consolidated net income and stockholders' equity are set out below:

	Years ended December 31,		
	1999	2000	2001
	(millions of Euro)		
NET INCOME (LOSS)			
Net income (loss) as reported in the consolidated statements of operations	2,409	2,948	(1,658)
Minority interest	(672)	(920)	(410)
Net income (loss), net of minority interest applicable for U.S. GAAP purposes	**1,737**	**2,028**	**(2,068)**
Items increasing (decreasing) reported net income (loss):			
Goodwill deriving from STET-Old Telecom Italia merger	(194)	(194)	(194)
Purchase method accounting transactions	(58)	(4)	(524)
Revaluation of fixed assets	85	85	58
Elimination of intercompany profit on sales of intangibles and fixed assets and related depreciation	45	41	54
Capitalization of interest on tangible and intangible assets under construction and related depreciation	(62)	(29)	124
Contributions to telephone workers social security fund	39	(2)	73
Accounting for long-term contracts under the percentage of completion method	(29)	-	-
Investment in stock of subsidiary companies	-	77	65
SEAT acquisition	-	7,866	-
Effects of SEAT’s 4th quarter results	-	(182)	-
SEAT put and call amortization	-	(15)	(145)
Reversal of provision on SEAT put option	-	-	569
Gain on subsidiary dilution	-	398	325
Sale of real estate portfolio	-	(315)	(34)
Non-capitalizable expenses	-	(95)	41
Reversal of provisions	-	407	(85)
Subsidiary stock conversions	-	2,212	-
Common control transactions	-	-	14
Satellite transaction	-	-	(130)
Derivative financial instruments	-	-	(73)
Impairment of Long-lived Assets	-	(7,966)	(2,641)
Other	(68)	25	(130)
Net adjustments	(242)	2,309	(2,633)
U.S. GAAP income (loss) before reconciliation effects of income taxes, minority interest and cumulative effect of accounting changes	1,495	4,337	(4,701)
Income taxes:			
Deferred tax adjustments	4	(17)	(154)
Tax effect on reconciling items	(30)	(643)	149
U.S. GAAP income (loss) before reconciliation effect of minority interest and cumulative effect of accounting changes	1,469	3,677	(4,706)
Minority interest on reconciling items	36	(76)	647
Net income (loss) in accordance with U.S. GAAP, before cumulative effect of accounting changes	1,505	3,601	(4,059)
Cumulative effect of accounting changes (net of tax)	-	(79)	20
Net income (loss) in accordance with U.S. GAAP	**1,505**	**3,522**	**(4,039)**

Earnings Per Ordinary Share Amounts in Accordance with U.S. GAAP (*)

	Years ended December 31,		
	1999	**2000**	**2001**
		(Euro)	
Basic EPS - per Ordinary Share amounts in accordance with U.S. GAAP before cumulative effect of accounting changes	0.20	0.48	(0.56)
Diluted EPS - per Ordinary Share amounts in accordance with U.S. GAAP before cumulative effect of accounting changes	0.20	0.48	(0.56)
Basic EPS - per Ordinary Share amounts in accordance with U.S. GAAP	0.20	0.47	(0.56)
Diluted EPS - per Ordinary Share amounts in accordance with U.S. GAAP	0.20	0.47	(0.56)

Earnings Per Savings Share amounts in accordance with U.S. GAAP (*)

	Years ended December 31,		
	1999	**2000**	**2001**
		(Euro)	
Basic EPS - per Savings Share amounts in accordance with U.S. GAAP before cumulative effect of accounting changes	0.21	0.49	(0.55)
Diluted EPS - per Savings Share amounts in accordance with U.S. GAAP before cumulative effect of accounting changes	0.21	0.49	(0.55)
Basic EPS - per Savings Share amounts in accordance with U.S. GAAP	0.21	0.48	(0.54)
Diluted EPS — per Savings Share amounts in accordance with U.S. GAAP	0.21	0.48	(0.54)

(*) The earnings per share amounts have been calculated using the two class method due to ordinary and savings shares being outstanding, as set forth in SFAS No. 128, "Earnings Per Share". Also refer to Note 28 for additional information on earnings per share. The calculations take into account the requirement that holders of savings shares are entitled to an additional dividend equal to 2% of the par value of savings shares, above the dividends paid on the ordinary shares. Prior to 2001, the par value of the savings shares was Lire 1,000 per share, while for 2001, following the resolution of the extraordinary stockholders' meeting held on May 3, 2001, regarding the re-denomination of Telecom Italia's share capital into Euro, the calculations take into account the new par value per share of Euro 0.55. For purposes of these calculations the weighted average number of Shares was 7,421,660,518 as of December 31, 1999, 7,398,247,829 as of December 31, 2000, and 7,314,353,578 as of December 31, 2001.

	As of December 31,	
	2000	2001
	(millions of Euro)	
STOCKHOLDERS' EQUITY		
Stockholders' equity as reported in the consolidated balance sheets	25,529	19,309
Minority interest	(6,708)	(5,787)
Stockholders' equity, net of minority interest	**18,821**	**13,522**
Items increasing (decreasing) reported stockholders' equity:		
Goodwill deriving from STET-Old Telecom Italia merger	2,420	2,226
Purchase method accounting transactions	5,435	5,861
Revaluation of fixed assets	(638)	(580)
Elimination of intercompany profit on sales of intangibles and fixed assets and related depreciation	(231)	(177)
Capitalization of interest on tangible and intangible assets under construction and related depreciation	591	715
Contributions to telephone workers social security fund	(790)	(717)
Investment in stock of subsidiary companies	62	87
SEAT acquisition	5,653	5,653
Effects of SEAT's 4th quarter results	(182)	(182)
SEAT put and call amortization	(15)	(160)
Reversal of provision on SEAT put option	-	569
Sale of real estate portfolio	(315)	(349)
Non-capitalizable expenses	(95)	(103)
Reversal of provisions	407	322
Common control transactions	(211)	(197)
Satellite transaction	-	39
Derivative financial instruments	-	(73)
Impairment of Long-lived Assets	(7,966)	(10,607)
Other	194	(139)
Deferred tax adjustments	99	(55)
Treasury stock	(662)	-
Cumulative effect of accounting changes, net of tax	(79)	22
Tax effect on reconciling items	(1,402)	(1,278)
Minority interests on reconciling items	(1,978)	(1,942)
Stockholders' equity in accordance with U.S. GAAP	**19,118**	**12,457**

Note 27—Condensed U.S. GAAP consolidated financial statements

The condensed consolidated financial statements as of December 31, 2000 and 2001 presented below have been restated to reflect the principal differences between the Group's accounting policies and U.S. GAAP discussed above.

In 2000, the condensed consolidated financial statements also reflect the 50 per cent investment in Nortel Inversora on an equity basis, as opposed to the proportional consolidation method used for Italian GAAP purposes.

	As of December 31,	
	2000	2001
	(millions of Euro)	
ASSETS		
Current assets	15,366	16,944
Fixed assets, net	22,823	23,883
Goodwill	18,071	12,752
Other intangible assets	6,013	9,754
Other long-term assets:		
Deferred tax assets	-	1,206
Other	9,255	7,979
Total assets	71,528	72,518

	As of December 31,	
	2000	2001
	(millions of Euro)	
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities	26,207	21,487
Long-term debt	12,466	21,906
Reserves and other liabilities:		
Deferred tax liabilities	1,096	2,616
Other liabilities	3,760	4,973
Employee termination indemnities	1,319	1,350
Total liabilities	44,848	52,332
Minority interest	7,562	7,729
Stockholders' equity	19,118	12,457
Total liabilities and stockholders' equity	71,528	72,518

	Years ended December 31,		
	1999	2000	2001
	(millions of Euro)		
STATEMENTS OF OPERATIONS			
Operating revenues	27,104	27,535	30,594
Other income	516	403	423
Total revenues	27,620	27,938	31,017
Operating expenses	(21,467)	(21,898)	(25,081)
Impairments on goodwill	-	(7,966)	(3,664)
Operating income/(loss)	6,153	(1,926)	2,272
Financial income and expenses and other income and expense, net	(1,379)	(1,492)	(5,976)
Gains on merger, demerger, subsidiary dilution and share conversions	-	10,476	325
Income (loss) before income taxes	4,774	7,058	(3,379)
Income taxes	(2,633)	(2,524)	(917)
Income (loss) before minority interest and cumulative effect of accounting changes	2,141	4,534	(4,296)
Minority interest	(636)	(933)	237
Income (loss) before cumulative effect of accounting changes	1,505	3,601	(4,059)
Cumulative effect of accounting changes (net of tax)	-	(79)	20
Net income (loss)	1,505	3,522	(4,039)

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Share Capital	Additional Paid in Capital	Reserves, Retained Earnings and Profit of the Year	Total
	(millions of Euro, unless for dividends per share)			
Balance as of January 1, 1999	3,833	1,772	13,540	19,145
Dividends paid (Euro 0.14 per ordinary share and Euro 0.15 per savings share)	-	-	(1,095)	(1,095)
Exercise of stock options	2	62	19	83
Translation adjustments on foreign currency financial statements	-	-	59	59
Equity investments and other minor adjustments	-	-	(38)	(38)
Net income	-	-	1,505	1,505
Balance as of December 31, 1999	3,835	1,834	13,990	19,659
Dividends paid (Euro 0.31per ordinary share and Euro 0.32 per savings share)	-	-	(2,327)	(2,327)
Dividend on demerger of Tin.it	-	-	(1,329)	(1,329)
Exercise of stock options	-	44	-	44
Treasury stock	-	-	(662)	(662)
Marketable securities	-	-	(5)	(5)
Translation adjustments on foreign currency financial statements	-	-	34	34
Equity investments and other minor adjustments	-	-	182	182
Net income	-	-	3,522	3,522
Balance as of December 31, 2000	3,835	1,878	13,405	19,118
Dividends paid (Euro 0.31 per ordinary share and Euro 0.32 per savings share)	-	-	(2,309)	(2,309)
Cancellation of treasury stock and re-denomination of capital stock in Euro	187	-	(898)	(711)
Contribution from by stockholders'	-	-	128	128
Exercise of stock options	1	9	-	10
Translation adjustments on foreign currency financial statements	-	-	(349)	(349)
Other adjustments	-	-	609	609
Net income (loss)	-	-	(4,039)	(4,039)
Balance as of December 31, 2001	4,023	1,887	6,547	12,457

Other Comprehensive Income:

	1999	2000	2001
	(millions of Euro)		
Net income (loss) for the year under U.S. GAAP	1,505	3,522	(4,039)
Translation adjustments on foreign currency financial statements during the year	59	34	(349)
Unrealized gains/(losses) on available for sale securities during the year (net of tax of Euro 3 million)	-	(5)	-
Adoption of derivative accounting (net of tax of Euro 1 million)	-	-	2
Total comprehensive income (loss) under U.S. GAAP	1,564	3,551	(4,386)

Note 28-Additional U.S. GAAP Disclosures

(a) Use of estimates

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(b) Accounting for deferred income taxes

For US GAAP reporting purposes, Telecom Italia follows the provisions of SFAS 109, "Accounting for Income Taxes". In accordance with SFAS 109, Telecom Italia has recognized deferred tax assets and liabilities to reflect the future tax consequences of events that have already been recognized in the consolidated financial statements or income tax returns. Where it is anticipated that all or a portion of a deferred tax asset will not be utilized, a valuation allowance has been placed against it.

Under Italian GAAP deferred tax assets and liabilities are recognized only if there is reasonable certainty that the temporary difference will reverse within the foreseeable future.

The provision for income taxes consisted of the following in the years ended December 31, 1999, 2000 and 2001:

	1999	2000	2001
	(millions of Euro)		
Current	2,885	2,390	1,179
Deferred	(252)	134	(262)
Total provision for income taxes	2,633	2,524	917

The actual provision for income taxes is different from income taxes computed by applying the Italian Statutory Tax rate (41.25% in 1999 and 2000 and 40.25% in 2001), primarily as a result of non-deductible and non-taxable items (goodwill, certain non-recurring gains, asset impairments and other expenses).

The components of the net deferred tax assets (liabilities) as of December 31, 2000 and 2001 are as follows:

	2000	2001
	(millions of Euro)	
Deferred tax assets:		
Intercompany profits	293	298
Accrued pension obligation	289	288
Revaluation of fixed assets	244	218
Provisions	138	713
Net operating losses	-	2,236
Other	485	367
Subtotal	1,449	4,120
Less- valuation allowance	-	(2,145)
	1,449	1,975
Deferred tax liabilities:		
Accelerated depreciation	(148)	-
Capitalization of interest on assets	(214)	(195)
Intangibles assets	(1,227)	(1,236)
Tax suspended reserves in equity	-	(264)
Other	(307)	(328)
Subtotal	(1,896)	(2,023)
Net deferred tax asset/(liability)	(447)	(48)

At December 31, 2001, the Company net operating loss carryforwards amounted to Euro 5,970 million. The gross amounts of such losses and expiration at December 31, 2001, by country are described in the notes to the Italian financial statements. The losses and credits generally expire within a period of five years, or have no expiration date. The majority of the losses are attributable to "start-up companies" without historical profits, and whose future profitability is uncertain. In accordance with SFAS 109, a valuation allowance of Euro 2,145 million has been placed against such losses.

No provision has been made for Italian Corporate taxes, or foreign taxes that may result from future remittances of undistributed earnings of foreign subsidiaries, because it is expected that all such earnings will be permanently reinvested in these foreign operations. It is not practical to estimate the amount of taxes that might be payable on the eventual remittance of these earnings.

(c) Fair value of financial instruments

As required by SFAS No. 107, "Disclosures about Fair Value of Financial Instruments", the Group has estimated, where possible, the fair values of the most significant financial instruments held. The Group has not estimated the value of certain unlisted long-term investments, primarily relating to investments in affiliated companies. The fair value for marketable securities and long-term investments are based on quoted market prices for those instruments or discounted cash flow analysis.

For cash and cash equivalents, financial receivables from banks and short-term debt, the amounts reflected in the consolidated financial statements are reasonable estimates of fair value because of the relatively short period of time between the origination of the investments and the expected realization.

For long-term debt, the fair value was determined by discounting contractual future cash flows using the Group's incremental borrowing rates for similar types of borrowing arrangements. The Company has certain investments for which it is not practicable to estimate fair value due to the lack of quoted market prices and the inability to estimate fair value without excessive costs.

The fair values and carrying amounts of financial instruments are as follows:

	As of December 31,			
	2000		2001	
	Carrying amount	Estimated Fair value	Carrying amount	Estimated fair value
	(millions of Euro)			
Cash & cash equivalents	1,305	1,305	765	765
Marketable securities	2,456	2,492	2,191	2,191
Long- term investments:				
Affiliates:				
Practicable to determine	2,198	1,440	3,377	6,779
Not practicable	5,400	-	3,209	-
Other:				
Practicable to determine	6	6	86	86
Short term debt (excluding current portion of long-term debt)	13,513	13,513	7,445	7,445
Long-term debt (current portion included):				
Floating rates	5,473	5,473	7,539	7,588
Fixed rates	4,418	4,534	10,213	10,198
	9,891	10,007	17,752	17,786

(d) Marketable Securities

The Group's investments consist primarily of investment grade marketable debt and equity securities. For purposes of U.S. GAAP these securities are classified as either held to maturity, trading or available for sale. Held to maturity securities are securities that the Group has the ability and positive intent to hold until maturity, therefore they are carried at amortized cost. Trading securities are recorded at fair value with unrealized gains and losses included in the statement of operations. Available for sale securities are recorded at fair value with the net unrealized gains or losses reported net of tax, in other comprehensive income. For purposes of Italian GAAP, investments are carried at the lower of cost or market value, with any gains or losses reflected in the statement of operations.

The fair value of all portfolios is determined by quoted market prices.

December 31, 2001	Amortized cost (Euro millions)	Unrealized gains (Euro millions)	Unrealized losses (Euro millions)	Fair value (Euro millions)
Trading securities	2,482	-	(291)	2,191
Available for sale	-	-	-	-
Total marketable securities	2,482	-	(291)	2,191

December 31, 2000	Amortized cost (Euro millions)	Unrealized gains (Euro millions)	Unrealized losses (Euro millions)	Fair value (Euro millions)
Trading securities	2,578	37	(126)	2,489
Available for sale	12	-	(8)	4
Total marketable securities	2,590	37	(134)	2,493

(e) Sale of Accounts Receivable

During 2001, the Company began selling trade accounts receivable to a Special Purpose Entity (SPE) in a securitization transaction. In order to fund the purchase of the accounts receivable, the SPE issued Euro Medium Term Asset Backed Notes (Notes) in the amount of Euro 700 million which are secured by the accounts receivable acquired, and has the ability to issue additional Notes up to an aggregate amount of Euro 2 billion. Funds received from the collection of sold accounts receivable may be used to acquire additional accounts receivable from the Company.

Under Italian GAAP, the determination of whether the transfer of accounts receivable represents a sale, the inclusion or exclusion of the SPE in the consolidated financial statements of the Group, and the determination of the amount of gain or loss on the sale is determined by the legal and contractual provisions of the agreement. For U.S. GAAP, the accounting for the transaction is governed primarily by SFAS 140, *"Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities"*. Under the provisions of SFAS 140, the agreement must meet certain defined criteria to qualify as a sale of financial assets, the SPE must meet certain defined criteria to preclude consolidation, and the amount of gain or loss on the sale is determined based on the consideration received, the carrying value of the underlying financial components sold and the fair value of the financial components retained. Even though the underlying rules differ, there was no material difference in the accounting treatment of this transaction between Italian and U.S. GAAP.

Under the terms of the agreement, the SPE charges the Company an initial discount which varies based on the credit profile and other characteristics of each tranche of accounts receivable sold. Additionally, for the purposes of credit enhancement, the SPE withholds a portion of the purchase price as a deferred payment, representing the Company's retained interest in the sold receivables. The amount of deferred payment withheld is adjusted on a monthly basis based on an evaluation of actual collections, delinquencies and other factors. The Company retains the servicing responsibility related to the sold receivables and receives a servicing fee from the SPE which is estimated to approximate the fair value of providing such services.

During 2001, the following cash flows were received from and paid to the SPE (in Euro millions):

Gross trade receivables sold to SPE	5,907
Collections remitted to SPE	(5,030)
Discount	(44)
Remaining retained interest	(337)
Net cash received in advance from SPE	496

At December 31, 2001, the amount of accounts receivable held by the SPE and not yet collected were Euro 877 million. Under U.S. GAAP, the retained interest of Euro 337 million, representing the deferred purchase price not yet received, is included in other current assets, before a provision for doubtful accounts of Euro 29 million, and sales of receivables resulted in a loss of Euro 73 million, consisting of the discount charged by the SPE and the provision booked to adjust the retained credit risks to fair value.

(f) Acquisitions

SEAT Acquisition

On February 10, 2000, Telecom Italia announced that it had reached an agreement to acquire a controlling interest in the Italian yellow page publisher, SEAT (the "SEAT Acquisition"). In addition to its publishing business, SEAT also has Internet and television properties. The SEAT Acquisition was effected in a series of steps and was financed through a combination of cash and the issuance of shares in a wholly owned subsidiary of Telecom Italia, Tin.it, to SEAT. Through a proxy offering and an acquisition from a private investment vehicle ("Huit II"), Telecom Italia paid Euro 6,104 million in August 2000 and Euro 6 million in November 2000 to acquire 1,156 million ordinary shares and 327 million savings shares of SEAT. On November 15, 2000, Telecom Italia distributed shares in its previously wholly owned Internet subsidiary, Tin.it, to SEAT to obtain a further 4,675 million ordinary shares of stock. Concurrent with the shares issued, Telecom Italia distributed 8.168 per cent of Tin.it to SEAT on November 10, 2000, for which SEAT issued new shares directly to Telecom Italia's shareholders. This part of the SEAT Acquisition was accounted for as a dividend to the Shareholders of Telecom Italia at fair market value. On November 20, 2000, Telecom Italia paid Euro 258 million to acquire a further 53 million ordinary shares.

For purposes of Italian GAAP, the cash consideration paid for SEAT's shares was recorded under purchase accounting, the shares of Tin.it exchanged for the controlling interest in SEAT were accounted for based on the pooling basis of accounting, therefore no value was ascribed to this portion of the SEAT Acquisition. For Italian GAAP purposes, the SEAT Acquisition was accounted for as of December 31, 2000. For purposes of U.S. GAAP, the shares of Tin.it exchanged for the controlling interest in SEAT have been accounted for as a purchase. The shares issued to Telecom Italia have been valued using the average quoted market price of the SEAT shares in the period from February 8 to February 14, 2000, including the announcement day of the SEAT Acquisition on February 10, 2000. For purposes of U.S. GAAP, the SEAT Acquisition was considered effective as of October 1, 2000, the date that operating control of SEAT was deemed to have passed to Telecom Italia, and therefore the SEAT Acquisition was accounted for as a purchase as of that date.

As part of the SEAT Acquisition, a put option was granted to minority shareholder Huit II under the agreement relating to the SEAT/Tin.it transaction entered into by, among others, Telecom Italia and Huit II on March 15, 2000. The put option allowed the holders of the option to put approximately 710 million SEAT shares to Telecom Italia at Euro 4.20 per share. The option was exercisable not later than the 12th business day after the completion of the transaction. On December 5, 2000, upon notification from the put holders of their intent to exercise, Telecom Italia entered into a transaction with a company of the Chase Manhattan Group ("Chase"), whereby Chase acquired approximately 710 million SEAT ordinary shares from Huit II along with Huit II's put option to sell such shares to Telecom Italia at the price of Euro 4.20 per share. In addition, the exercise period was lengthened to a maximum of five years and a call option over approximately 660 million shares was granted to Telecom Italia under the same terms and conditions as the put option, with the payment of a premium of approximately Euro 747 million. For purposes of U.S. GAAP, the agreement has been accounted for as the acquisition financing of an additional equity interest, with the amounts due under the agreement included in the purchase price allocation below. The transaction increased the investment in SEAT, including goodwill, by Euro 2,985 million with a corresponding increase in long-term debt. For purposes of Italian GAAP, this acquisition has not been recognized in the financial statements.

The following represents the final purchase price allocation to the fair value of the assets acquired and liabilities assumed.

		(millions of Euro)	
Cash purchase price		6,368	
Fair value of merger transaction and put/call financing of minority interest acquisition		9,607	
Transaction costs		49	
Total consideration	**A)**		16,024
Net tangible and intangible assets acquired		3,639	
Minority interest		(1,449)	
	B)		2,190
Goodwill from acquisition	**(A-B)**		13,834

Like many companies operating in the technology sector, and in particular the Internet, as of December 31, 2000 the share price of SEAT had declined substantially from the date of the SEAT Acquisition announcement, falling to Euro 2.375. The reduction was considered to be an indicator of impairment for purposes of SFAS 121, *Accounting for the Impairment of Long Lived Assets and for Long Lived Assets to Be Disposed Of.*

Based on Telecom Italia's analysis and comparison of the undiscounted cash flow of SEAT, it was apparent that the undiscounted cash flows of SEAT were less than the carrying value of the investment in SEAT, at which point the goodwill related to the investment was considered impaired. Upon an analysis of the SEAT business plan, a discounted cash flow analysis was performed, with the outcome being a Euro 7,966 million reduction to the acquisition goodwill.

The remaining goodwill is being amortized on a straight-line basis over 12 years.

Entel Chile

In December 2000 the Telecom Italia Group signed an agreement to increase its investment in Entel Chile ("Entel") from 26.16% to 54.76% by purchasing shares held by the Chilquinta Group and the Matte Group in a cash transaction. Entel Chile Group operates in the sectors of fixed and mobile telephone services, data-transmission and Internet-access services. Previous to this investment the Group had owned a 26.16% interest in Entel Chile, which in accordance with

U.S. GAAP was accounted for on the equity method. The overall cost of the acquisition was Euro 970 million (U.S.$905 million), with the acquisition completed and accounted for as of April 1, 2001.

Under Italian GAAP, the Entel Chile acquisition was accounted for by the purchase method, with the date of effective control designated as of January 1, 2001. The excess of the acquisition cost over the equity in the net book value of net assets acquired was allocated to goodwill, which is being amortized by the straight-line method over 15 years. Entel Chile has been included in the consolidated financial statements of Telecom Italia from January 1, 2001.

Under U.S. GAAP, the Entel Chile acquisition was accounted for by the purchase method with April 1, 2001 designated as the effective date of the acquisition. The tangible and intangible assets acquired and liabilities assumed were recorded at estimated fair values as determined by the Group's management based on information currently available and on current assumptions about future operations. The Group has prepared preliminary appraisals of the fair values and their estimated remaining useful lives. Accordingly, the allocation of the purchase price is subject to revision, which is not expected to be material, based on the final determination of appraisals and other fair values. The following represents the preliminary purchase price, subject to receipt of the final report, allocation to the fair value of assets acquired and liabilities assumed:

	(millions of Euro)
Purchase price	970
Net tangible and intangible assets acquired	(342)
Goodwill from acquisition	628

The amortization of costs assigned to intangible assets and goodwill is computed by the straight line method over the expected period to be benefited, which is five years for software and 15 years for licenses and goodwill.

For U.S. GAAP purposes, Entel Chile has been included in the consolidated financial statements of Telecom Italia by the equity method of accounting for the 26.16% interest through March 31, 2001 and fully consolidated from April 1, 2001.

Holding Media e Comunicazione (formerly Cecchi Gori Communications)

On August 8, 2000, SEAT purchased 25% of Cecchi Gori Communications S.p.A. ("CGC") for a total of Euro 129 million in cash from Cecchi Gori Communication Media Holdings ("CGCMH"). During 2001, SEAT acquired the remaining 75% of CGC, bringing Group's total investment in CGC totaled Euro 217 million. The operations of CGC have been included in the consolidated financial statements from the date of majority acquisition. The transaction was accounted for as a purchase, using step-acquisition accounting, and the excess cost over the fair value of the identifiable tangible and intangible net assets acquired of Euro 72 million was recorded as goodwill, which is being amortized over 10 years computed on the straight line method.

Consodata

On February 9, 2001, SEAT gained a controlling stake (54.5%) of Consodata S.A. ("Consodata"), a company listed on the Paris Nouveau Marché in the business of information marketing. The acquisition occurred in the following manner: (i) SEAT issued 63,789,104 ordinary shares to the Consoldata shareholders for 3,986,819 Consodata shares, corresponding to 39.27% of the French company's share capital; (ii) SEAT contributed their entire stake (100%) in Giallo Dat@ to Consodata in return for 3,383,520 new ordinary shares (25% of the new post-increase capital of Consodata). On May 30, 2001, SEAT announced a public tender offer in which sixteen new ordinary SEAT shares were offered for each Consodata share. The holders of 5,981,625 Consodata shares, equivalent to approximately 44.19% of the share capital, participated in the offer in which 95,706,000 new ordinary SEAT shares were issued on August 8, 2001. SEAT, therefore, gained a total interest of 90.74% in the new combined entity Consodata-Giallo Dat@. The Company's total investment in Consodata totaled Euro 554 million. The operations of Consodata have been included in the consolidated financial statements from the date of majority acquisition. The transaction was accounted for as a purchase, using step-acquisition accounting, and the excess cost over the fair value of the identifiable tangible and intangible net assets acquired of Euro 514 million was recorded as goodwill, which is being amortized over 10 years computed on the straight line method. The Company performed an impairment review under U.S. GAAP in accordance with its policy described in Note 28 (n), and as a result, recorded a non-cash impairment charge to the goodwill related to Consodata of Euro 457 million in 2001.

Telegate

As of October 1, 2000, SEAT owned 2.2% of Telegate AG, a publicly traded company in Germany, with a fair value of Euro 37 million. During November 2000, the Company acquired an additional 11.34% of Telegate AG and 51.37% of Telegate GmbH, a German holding company. Telegate GmbH directly owns 50.99% of Telegate AG. The acquisition was accomplished through the issuance by SEAT of 147,446,627 ordinary shares for a total purchase price of Euro 758 million. On April 5, 2001, SEAT purchased the remaining 48.63% of Telegate GmbH through the issuance of 150,579,625 new ordinary shares for a purchase price of Euro 309 million. The total investment in Telegate GmbH and Telegate AG totaled Euro 1,104 million. The operations of Telegate GmbH and Telegate AG have been included in the consolidated financial statements from the date of majority acquisition. The transaction was accounted for as a purchase, using step-acquisition accounting, and the excess cost over the fair value of the identifiable tangible and intangible net assets acquired of Euro 1,048 million was recorded as goodwill, which is being amortized over 7 years computed on the straight line method. The Company performed an impairment review under U.S. GAAP in accordance with its policy described in Note 28 (n), and as a result, recorded a non-cash impairment charge to goodwill related to Telegate of Euro 907 million in 2001.

TDL Infomedia

During December 2000, the Company acquired 99.6% of TDL Infomedia Ltd. (TDL) through the issuance of 140,672,537 ordinary shares for a total purchase price of Euro 527 million. The operations of TDL Infomedia Ltd. are included in the consolidated financial statements from the date of acquisition. The transaction was accounted for as a purchase and the excess cost over the fair value of the identifiable tangible and intangible net assets acquired of Euro 443 million was recorded as goodwill, which is being amortized over 15 years computed using the straight line method. The Company has an option to acquire the remaining shares at a price to be determined based on a multiple of the operating results of TDL during 2001 through 2003.

The following table reflects the results of operations on a pro forma basis as if the acquisitions of SEAT and Entel Chile had occurred as of January 1, 2000. The 2000 pro forma results of operations do not include the Euro 7,866 million in non-recurring gains from the distribution of Tin.it's shares or the effects relating to the cumulative effect of accounting changes. The following unaudited pro forma information also excludes the effects of synergies and any other cost saving initiatives related to the acquisitions.

Unaudited	**2000**	**2001**
	(millions of Euro, except per share amounts)	
Revenues	30,096	31,383
Net income (loss)	(3,495)	(4,187)
Earnings per Share:		
Basic EPS — per ordinary share	(0.47)	(0.58)
Basic EPS — per savings share	(0.46)	(0.56)
Diluted EPS — per ordinary share	(0.47)	(0.58)
Diluted EPS — per savings share	(0.46)	(0.56)

(g) Segment information

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services.

With respect to international telecommunications activities, the Group's main operating units are located in Europe and in Latin America where it is already well established in the principal countries. As of December 31, 2001, investments in affiliated companies are located approximately 82% in Europe, approximately 12% in Latin America and the remainder in the rest of the world.

At the beginning of 2001 the Group reorganized its businesses into seven segments. The segment information below for the years 1999 and 2000 has been reclassified to present those years' segments information on a basis consistent with 2001:

Domestic Wireline. This segment includes Telecom Italia Domestic Wireline ("TIDW") which relates to the Italian domestic fixed line voice and data businesses on the fixed network; includes, also, national businesses such as

Atesia, related to call center, telemarketing and market researches and international activities relating to developing networks such as the European, Mediterranean and Latin American fiber optic rings as well as TMI.

Mobile Services. This segment includes national and international mobile telecommunications businesses which are managed by TIM. Beginning in 2001 international mobile operations were consolidated with, and managed by TIM, through TIM International. International mobile operations are concentrated in the Mediterranean Basin and in Latin America.

Internet and Media. This segment includes the SEAT Group which was consolidated with the Telecom Italia Group in results of operations for the first time in 2001 as a result of the Group's controlling acquisition. SEAT manages the Group's internet and media business which arose from the merger of Tin.it and SEAT. This segment includes a multimedia network, whose main business areas include advertising, publishing, information marketing, business information, call center services, the Internet and television.

International Operations. The International Operations segment manages and develops international wireline businesses and certain integrated companies providing fixed and mobile telecommunication services outside of Italy.

Information Technology. This ancillary segment is responsible for all information technology services within the Group, including IT services provided to other segments as well as such services offered to the market.

Satellite Services. The Satellite Services segment is responsible for developing satellite communication systems for voice and data transmission as well as for radio and television broadcasting and earth-observation.

TILAB. The TILAB segment, combines the technological knowledge acquired by CSELT and the venture capital management experience of the Company. The TILAB segment identifies and manages new initiatives, and creates business opportunities for companies of the Group as well as for the external market.

The accounting policies of the segments are the same as those described in the significant accounting policies (Note 3). Information about the Group's segments for the year ended December 31, 1999, 2000 and 2001 are as follows (in millions of Euro):

	Domestic Wireline	Mobile Services	Internet and Media	International Operations	IT Services	Satellite Services	TILAB	Other Activities	Elimination and consolidated adjustments	Consolidated
1999										
Operating revenues										
-Third parties	15,961	8,290	68	365	1,099	229	15	1,077		27,104
-Intersegment (**)	2,488	361	160	29	1,141	87	104	1,845	(6,215)	
	18,449	8,651	228	394	2,240	316	119	2,922	(6,215)	27,104
Operating income	4,045	2,708	(65)	(122)	120	(11)	(47)	(276)	81	6,433
Depreciation and amortization	3,602	1,062	13	89	217	31	20	498	(193)	5,339
Investments in fixed assets	2,172	1,211	14	78	136	29	14	363	(142)	3,875
Identifiable assets	21,985	10,007	128	6,794	1,660	996	152	21,628	(17,292)	46,058
2000										
Operating revenues										
-Third parties	15,304	9,090	179	2,257	1,118	263	21	679		28,911
-Intersegment (**)	2,210	328	84	35	1,020	77	102	1,656	(5,512)	
	17,514	9,418	263	2,292	2,138	340	123	2,335	(5,512)	28,911
Operating income	3,915	2,988	(73)	230	134	(52)	(34)	(237)	(66)	6,805
Depreciation and amortization	3,356	1,258	23	550	197	33	20	351	(141)	5,647
Investments in fixed assets	1,917	1,194	55	579	83	29	29	126	(123)	3,889
Identifiable assets	21,418	17,687	3,951	12,536	1,937	1,217	249	23,703	(17,183)	65,515
2001										
Operating revenues										
-Third parties	15,206	9,963	1,880	1,845	1,246	589	28	61		30,818
-Intersegment (**)	2,085	287	77	34	787	59	106	992	(4,427)	
	17,291	10,250	1,957	1,879	2,033	648	134	1,053	(4,427)	30,818
Operating income	4,379	3,136	31	(268)	162	60	(34)	(407)	(385)	6,674
Depreciation and amortization	3,210	1,469	320	511	151	33	21	244	316	6,275
Investments in fixed assets	1,976	1,547	82	427	87	27	12	113	(17)	4,254
Identifiable assets	20,420	17,018	4,072	8,567	2,168	1,274	281	30,322	(21,452)	62,670

(*) Other activities include only ancillary services.

(**) Intersegment sales consist of sales made between consolidated subsidiaries of the Group belonging to different segment. Such sales between segment are accounted for at selling prices which generally approximate prices to unaffiliated customers.

Information about the Group’s segments by geographic area for the year ended December 31, 1999, 2000 and 2001 are as follows (in millions of Euro):

	Italy	Rest of Europe	Central and South America	Other	Consolidated
1999					
Operating revenues	23,209	1,807	1,329	759	27,104
Identifiable assets	35,162	7,824	2,978	94	46,058
Investments in fixed assets	3,403	133	334	5	3,875
2000					
Operating revenues	23,037	1,843	3,217	814	28,911
Identifiable assets	45,030	10,306	10,140	40	65,516
Investments in fixed assets	2,782	246	861	-	3,889
2001					
Operating revenues	24,863	1,817	2,592	1,546	30,818
Identifiable assets	42,780	12,036	7,798	56	62,670
Investments in fixed assets	2,887	411	955	1	4,254

(h) Stock-Based Compensation

The Group accounts for all stock-based compensation issued under the provisions and related interpretations of Accounting Principles Board Opinion (“APB”) No. 25, “*Accounting for Stock Issued to Employees*.” Certain companies within the Group that have publicly traded stock also issue options to their employees. At the end of 2001, SEAT, TIM and Entel Chile all have some form of stock-based compensation program for employees. These plans are all accounted for under APB No. 25. No stock-based compensation expense was recognized in 1999, however Euro 27.2 million was recognized in 2000 and Euro 7 million in 2001.

In 1999 the Company adopted the 1999 Stock Option Plan, under which 16,595,400 options were granted at an exercise price of Euro 6.79 to key employees. The options issued under the 1999 plan vest annually in three year tranches starting in January 2000 and ending in January 2002, expiring on January 31, 2005. The options granted under this plan are performance based, which performance requires that the average share price of Telecom Italia for the month of December prior to the month of vesting (ie. December 1999, 2000 and 2001) is greater than the grant price. As of December 31, 2000 the first tranches of 4,905,500 options had been vested and exercised, with the second tranche of 5,754,900 becoming exerciseable as the vesting requirements had been met. The performance criteria for the remaining 5,935,000 options had not been met as of December 31, 2001, however the Board of Directors has resolved that the options would become exercisable beginning January 2002, regardless of performance criteria. In 2001 a total of 1,496,350 options were exercised for Euro 7.7 million, with a total of 9,846,650 options outstanding at December 31, 2001. Compensation expense totaling Euro 1.6 million has been recorded in 2001 associated with this option plan.

In 2000 the Board of Directors authorized an additional plan, under which a total of 51,430,000 options were granted at a strike price of Euro 13.815. The options vest ratably in three tranches of 15,460,000 in July of 2001, 2002 and 2003, with an extraordinary tranche of 5,050,000 vesting in July 2003. The plan closes on July 31, 2008. The 2000 plan is also performance based, with the performance criteria based on the ratio of the arithmetic mean of Telecom Italia’s ordinary shares to the ratio of the Dow Jones Eurostoxx Indexes for the Telecommunications sector. If the performance criteria for an option tranche is not met in any particular year, but the performance criteria is met in the subsequent year, the options that had not initially met the performance criteria will be considered vested at that time. The first tranche of options has met the performance criteria; therefore, these options have vested. Due to market conditions the Board of Directors has considered re-pricing the options in the plan, which requires that the 2001 options are also considered to be vested. At the end of 2001 50,570,000 options were outstanding under this plan, however no compensation expense has been recognized in 2001 as the exercise price of the options is below the market price.

In 2001 the Board of Directors approved a new plan, consisting of 67,025,000 options with an exercise price of Euro 10.488 per option. This plan is also subject to certain performance criteria similar to the 2000 plan with vesting through July 2003. Total options outstanding under this plan at the end of 2001 was 66,450,000, no compensation expense was recorded in 2001 for this plan as the exercise price was below the market price

The status of the stock options granted under all Stock Option Plans is as follows:

	Number of Options	Weighted Average price per option
		(Euro)
Balance at December 31, 1998	-	-
Granted	16,595,400	6.79
Exercised	(4,905,500)	6.79
Forfeited	-	-
Outstanding at December 31, 1999	11,689,900	6.79
Granted	51,430,000	13.82
Exercised	-	-
Forfeited	(278,400)	6.79
Outstanding at December 31, 2000	62,841,500	12.54
Granted	67,025,000	10.45
Exercised	(1,496,350)	6.79
Forfeited	(1,503,500)	10.06
Outstanding at December 31, 2001	126,866,650	11.51

The following table summarizes certain information for the stock options granted under the stock option plans, which are outstanding at December 31, 2001:

	Options Outstanding			Options Exercisable	
Range of Grant Prices	Shares	Weighted Average Remaining Life	Weighted Average Grant Price	Shares	Weighted Average Grant Price
(Euro)			(Euro)		(Euro)
6.79	9,846,650	4.13	6.79	9,846,650	6.79
13.82	50,570,000	7.58	13.82	50,570,000	13.82
10.49	66,450,000	7.25	10.49	66,450,000	10.49

SFAS No. 123, "Accounting for Stock-Based Compensation" requires the disclosure of pro forma net income per share as if the Group had adopted fair-value accounting for stock-based awards. The fair value of stock-based awards to employees is calculated using the Black-Scholes option pricing model, with the following weighted average assumptions:

	1999	2000	2001
Expected life (years)	3	2.9	3
Expected volatility	43.76%	40.8%	43.6%
Risk free interest rate	6.05%	5.4%	4.91%
Expected dividend yield	0.49%	1.5%	2.0%

The Group's pro forma earnings per share, had compensation costs been recorded in accordance with SFAS No. 123, are presented below, for all plans:

	1999	2000	2001
	(millions of Euro, except per share amounts)		
Net income (loss) available to each class of shares	1,503	3,483	(4,367)
Basic EPS — per Ordinary Share	0.20	0.47	(0.60)
Basic EPS — per Savings Share	0.21	0.48	(0.59)
Diluted EPS — per Ordinary Share	0.20	0.47	(0.60)
Diluted EPS — per Savings Share	0.21	0.48	(0.59)

The effects of applying SFAS No. 123 in this pro forma disclosure should not be interpreted as being indicative of future effects.

(i) Capitalization of interest expense

The Group capitalizes interest expense on both tangible and intangible assets under construction. The Group is currently capitalizing interest expense on acquired UMTS licenses, which under US GAAP are considered as construction in progress. Amortization of the assets, including the capitalized interest costs, will begin when the assets are put in service. The Group incurred Euro 1,870 million interest cost in 2001 of which Euro 236 million was capitalized.

(j) Transactions with subsidiary stock

Occasionally Telecom Italia will sell shares in its controlled subsidiaries in the public market. Gains and losses recognized on these transactions are recognized as non-operating in the statement of operations.

(k) Earnings per Share

In accordance with SFAS No. 128, "Earnings per Share", Basic earnings per share is computed by dividing income available to ordinary shareholders by the weighted average number of ordinary shares outstanding. The computation of diluted earnings per share is increased to include any potential ordinary shares. The effects of any potential ordinary shares are omitted when the effects of including them is anti-dilutive. Potential ordinary shares include options, warrants and convertible securities. In 2001, no potential ordinary shares were considered dilutive, therefore basic and diluted shares were the same.

The computations of basic and diluted earnings per share for the years ended December 31, 1999, 2000 and 2001, prepared in accordance with U.S. GAAP, are as follows:

	1999	2000	2001
	(Thousands of Euro, except per share amounts)		
Basic EPS(*)			
Net Income/(loss)	1,505,524	3,521,926	(4,039,156)
Less: Euro 0.010 in 1999 and 2000 and Euro 0.011 in 2001 premium payable to savings shares	(22,374)	(22,086)	(22,586)
	1,483,150	3,499,840	(4,061,742)
Weighted average number of shares (millions)	7,422	7,398	7,314
Basic EPS — ordinary shares	0.200	0.473	(0.555)
Add: Euro 0.010 in 1999 and 2000 and Euro 0.011 in 2001 premium payable to savings shares (**)	0.010	0.010	0.011
Basic EPS — savings shares	0.210	0.483	(0.544)
Diluted EPS(*)			
Weighted average number of shares (millions)	7,422	7,398	7,314
Dilutive effect of stock options (millions)	6	21	-
Diluted weighted average number of shares (millions)	7,428	7,419	7,314
Diluted EPS — ordinary shares	0.200	0.472	(0.555)
Add: Euro 0.010 in 1999 and 2000 and Euro 0.011 in 2001 premium payable to savings shares (**)	0.010	0.010	0.011
Diluted EPS — savings shares	0.210	0.482	(0.544)

(*) Calculated under the two class method considering distributed and undistributed earnings.

(**) This takes into account the par value of Lire 1,000 per share as of December 31, 1999 and 2000; following the resolution of the extraordinary stockholders' meeting held on May 3, 2001, regarding the re-denomination of Telecom Italia's share capital into Euro, the new par value per share as of December 31, 2001 is equal to Euro 0.55.

(l) Effects of Regulation

As discussed in Note 2, Telecom Italia is subject to the regulatory control of the NRA with additional oversight provided by numerous laws, decrees and codes. The rate-making methodology is currently being redesigned. It is anticipated that the final method will allow Telecom Italia to recover a certain level of costs (subject to price caps), but not necessarily its specific cost of providing service. Accordingly, U.S. GAAP, as described in SFAS No. 71, “Accounting for the Effects of Certain Types of Regulation”, that relates to an entity whose rates are regulated on an actual cost basis, is not currently applicable to these financial statements.

(m) Supplemental disclosure of cash-flow information

Cash and cash equivalents

Cash and cash equivalents represent highly liquid investments that are readily convertible to cash and have original maturities of 90 days or less.

Other Information

	1999	2000	2001
		(millions of Euro)	
Changes in Operating Assets and Liabilities			
Marketable securities	(9)	(1,121)	265
Receivables	(388)	(238)	(53)
Inventories	(70)	305	89
Other current assets	(330)	(2,200)	(708)
Payables, trade and other	593	(469)	774
Accrued payrolls and employee benefits	(28)	294	(191)
Accrued income taxes	(102)	(316)	(145)
Other accrued liabilities	55	(31)	341
	(279)	(3,776)	372
Cash Paid During the Year For:			
Interest	553	790	930
Income taxes	2,766	2,273	2,072

(n) Impairment of Long-lived Assets

For U.S. GAAP purposes, the Group assesses the potential impairment of certain long-lived assets, including goodwill, under the provisions of SFAS No. 121, “Accounting for the Impairment of Long-lived Assets and for Long-lived Assets to be Disposed Of”. In applying SFAS No. 121, the Group assesses potential impairments whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable or if the price of the assets has had considerable market depreciation. The recoverability of an asset’s carrying value is initially determined by comparing the undiscounted cash flows of the asset to its carrying value. If, after the initial assessment, an impairment is deemed to exist, then the Company estimates the fair value of the asset based on discounted cash flows, independent appraisals or quoted market prices, if available. Any excess of carrying value over estimated fair value is written off and recorded as an expense in current period earnings. Investments in equity method investees are also reviewed for potential impairment based on events which indicate the carrying amount may not be recoverable and are written down to fair value if the impairment is deemed to be “other than temporary”. As described in footnote 28 (f), in 2000 the Group acquired SEAT, a company operating in the Internet and publishing sectors. In 2000, Telecom Italia took a charge of approximately Euro 7,966 million in the initial year of the acquisition due to the decrease in asset prices for that sector in 2000. In 2001, Telecom Italia took additional impairment charges of Euro 5,022 million, Euro 2,496 million of which was again related to SEAT.

(o) Sale of Real Estate portfolio

In late 2000, the Group transferred a going concern including a portion of their real estate portfolio to a wholly owned subsidiary, IM.SER, at the fair market value of Euro 2,900 million. The assets’ net book value on the date of transfer was Euro 2,392 million. Subsequently, the Group sold 60% of their interest in IM.SER to third parties for cash in the amount of Euro 1,740 million. Telecom Italia subsequently leased back 90% of the buildings contributed to IM.SER. In total Telecom Italia received cash in the amount of Euro 2,700 million, which came from both the sale of the investment and a cash dividend distribution from IM.SER, with the distribution of funds being provided by IM.SER’s borrowing from a consortium of banks. Under Italian GAAP, a pre-tax gain for the amount of Euro 312 million was recorded in the consolidated financial statements.

Under U.S. GAAP, the transfer of the assets to the wholly owned subsidiary, the subsequent lease agreement and the receipt of cash by the Group from the partial sale and the special dividend are considered to be secured borrowings. This type of accounting treatment requires that the buildings continue to be reflected in the consolidated financial statements and depreciated based on their historical net book value. Additionally, the gain recognized under Italian GAAP on the partial sale of the subsidiary is reversed for U.S. GAAP purposes. The balance sheet of the Group at

December 31, 2001 under U.S. GAAP reflects an increase in long-term debt of Euro 2,520 million, an increase in buildings of Euro 2,202 million (net of the depreciation from the date of transfer) and a reduction in investments for Euro 200 million.

(p) Satellite transaction

In 2001 Telecom Italia formed a wholly-owned subsidiary domiciled in Luxembourg (Mirror International Holding or "Mirror") to which it transferred certain investments in entities in the satellite sector at their fair market values of Euro 550 million. Mirror subsequently obtained a non-recourse loan of Euro 217 million from a merchant bank, which was subsequently disbursed to Telecom Italia, leaving Telecom Italia with net equity of Euro 333 million in Mirror under Italian GAAP. Subsequent to the loan, 70% of the equity in Mirror was sold to the same merchant bank for a total of Euro 233 million, providing Telecom Italia a total of Euro 450 million in cash from the partial disposal of the satellite shareholdings. In the consolidated Italian financial statements the transaction has been accounted for as a sale, with a gain of Euro 170 million being recognized on the sale of 70% of the assets and the remaining 30% interest in Mirror being recorded as an equity investment. For Italian GAAP purposes the remaining equity investment was considered impaired for Euro 40 million at December 31, 2001.

Under US GAAP the structuring of the transaction was considered a securitization, with Mirror being deemed a non-qualifying special purpose entity, therefore the requirements for sales recognition accounting were not met. Consequently, US GAAP requires that (i) the equity investments transferred to Mirror should continue to be reflected in the consolidated financial statements of Telecom Italia at historical cost, (ii) the gain of Euro 170 million and the valuation allowance of Euro 40 million recognized for Italian GAAP purposes should not be recognized and (iii) the accounting for the Euro 450 million of cash received by Telecom Italia be reflected in the consolidated balance sheet as additional bank debt of Euro 217 million and minority interest of Euro 233 million, representing the debt of Mirror and the cash received from LBMB for its purchase of 70% of Mirror from Telecom Italia.

(q) Derivative Financial Instruments

The Company's derivative financial instruments at January 1, 2001 and December 31, 2001 consist of interest rate swap and collar agreements, cross currency and interest rate swaps, foreign currency options and forward contracts and equity securities options. Under SFAS No. 133, effective January 1, 2001, all such derivatives have been recognized on the balance sheet at fair value. Under the transition provisions of SFAS No. 133, the initial recognition of the fair value of derivative instruments was treated as a cumulative effect of a change in accounting principle in either current period earnings or as other comprehensive income depending on the previous nature and hedge designation of the derivative. As the Company did not formally designate its derivative instruments as hedges upon the adoption of SFAS No. 133, subsequent changes in the fair value of the derivative instruments have been recognized as a component of current period earnings according to the requirements of SFAS No. 133 described above.

As a result of adopting SFAS No. 133, effective January 1, 2001, the Company recognized pre-tax gains of Euro 27 million and Euro 7 million as a cumulative effect of a change in accounting principle in current earnings and accumulated comprehensive income, respectively. The cumulative effect of adoption reflected as accumulated comprehensive income will be amortized over the lives of the related derivative instruments on a straight-line basis. During the year, the Company recognized pre-tax losses in current period earnings related to changes in the fair value of its derivative financial instruments of Euro 77 million and pre-tax gains in current period earnings of Euro 4 million for the amortization of the cumulative effect of adoption recorded in accumulated comprehensive income. The net loss of Euro 73 million is included in the accompanying 2001 U.S. GAAP basis statement of operations. For U.S. GAAP purposes, as of December 31, 2001, the Company has recorded net derivative liabilities of Euro 6 million, additional long-term debt of Euro 30 million and pre-tax accumulated comprehensive income of Euro 3 million under the requirements of SFAS 133. Of the accumulated comprehensive income of Euro 3 million at December 31, 2001, Euro 3 million will be amortized to current period earnings in 2002.

(r) Convertible Opera Notes

In March 2001 the Group issued, through its 100% owned finance subsidiary Sogerim, Senior Unsecured Guaranteed Exchangeable Out Performance Equity, Redeemable in Any-Asset ("OPERA") Notes, which bear interest at 1% per year, mature in 2006 and are fully and irrevocably guaranteed by Telecom Italia S.p.A.. The Opera Notes are exchangeable for ordinary shares of Telecom Italia controlled subsidiaries TIM or SEAT. During the exchange period ending 10 business days before March 15, 2006, the holders of the Opera Notes have the right to exchange such notes for either SEAT or TIM shares, with the initial exchange ratios being Euro 1,000 nominal amount of Opera Notes for 232.5581 SEAT ordinary shares (giving SEAT share exchange ratio value of Euro 4.30 per share) or 90.9091 TIM ordinary shares (giving TIM share an exchange ratio value of Euro 11.00 per share). On March 15, 2004, the holders of Opera Notes have an option to cause any remaining Opera Notes then outstanding to be redeemed, at the Accreted

Principal amount , plus accrued interest. At maturity any remaining outstanding Opera Notes will be redeemed at 117.69% of their original principal amount, representing a yield to maturity of 4.25% for unredeemed notes.

Sogerim has the option of honoring the exchange request in shares made by the holders of the Opera Notes, or giving in exchange the cash value of the shares calculated at 95% of the simple arithmetic average of the quoted market price of the shares, or settle the exchange in any combination thereof.

Sogerim has the option to call the Opera Notes in whole, but not in part, after March 15, 2004 at the accreted principal amount plus accrued interest up to, but excluding the date of the redemption, if the cash value of either the TIM exchange property or the SEAT exchange property is equal to or greater than 120% of the aggregate accreted principal amount of the Opera Notes for at least 20 dealing days during any 30 consecutive dealing days.

The notes contain certain restrictive covenants including, but not limited to, restrictions related to the Company's ability to incur debt senior to the Opera Notes. The covenants do not restrict dividends or loans to the Company.

At December 31, 2001 no holders of the Opera Notes has requested exchange of the Notes for either the shares of SEAT or TIM. The quoted market prices of SEAT and TIM at December 31, 2001 were Euro 0.92 and Euro 6.23, respectively. For the year ended December 31, 2001, Sogerim accrued interest on the nominal amount of the Opera Notes outstanding at the rate of 4.25%, the stipulated yield rate assuming the Opera Notes will be held to maturity in 2006.

(s) Lease Commitments

The following is a summary of all future minimum lease payments as of December 31, 2001 (in millions of Euro):

	Finance Leases
2002	60
2003	71
2004	53
2005	45
2006	41
Thereafter	345
Present value of future minimum lease payments	615
Less current portion	(60)
Long term portion	555

(t) New Accounting Standards

In June 2001, the FASB issued statement of Financial Accounting Standards (SFAS) No. 141, "Business Combinations" ("SFAS 141"), and SFAS No. 142, "Goodwill and other Intangible Assets" ("SFAS 142"). SFAS 141 supersedes APB Opinion 16, "Business combinations", and SFAS No. 38, "Accounting for Pre-acquisition Contingencies of Purchased Enterprises". The new pronouncement requires that the purchase method of accounting be used for all business combinations initiated after June 30, 2001, and changes the criteria for recognizing intangible assets apart from goodwill. SFAS 142 supersedes APB Opinion 17, "Intangible Assets", and addresses how intangibles acquired individually or as part of a group, should be accounted for upon acquisition. The statement prescribes the necessary accounting for both identifiable intangibles and goodwill acquired in a business combination after initial recognition. SFAS 142 requires that goodwill, including amounts associated with equity method investments, and indefinite lived intangible assets no longer be amortized upon adoption of this statement, but instead these assets must be tested for impairment at least annually. Amortization of definite lived intangibles will continue over their useful life. For U.S. GAAP reporting, the provisions of SFAS 141 apply to all business combinations initiated after June 30, 2001. The provisions of SFAS 142 are required to be applied starting with fiscal years beginning after December 15, 2001, except for the non amortization provisions for goodwill and indefinite – lived intangible assets acquired after June 30, 2001, which will be subject immediately to provisions of this statement. As a result of adopting these new standards effective January 1, 2002, the Company has ceased amortizing existing goodwill which would have resulted in amortization expense of Euro 1,291 million in 2002. The Company has completed Step 1 of the transition phase outlined in SFAS n. 142. Based on the Company's review, the range of possible impairment from implementation of the new standard is approximately Euro 600 million to Euro 950 million.

In July 2001, the FASB issued SFAS 143, "Accounting for Asset Retirement Obligations". The objective of this statement is to provide accounting guidance for legal obligations associated with the retirement of long-lived assets. SFAS 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred and accreted to its settlement amount over the expected life. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset and subsequently depreciated over the asset's useful life. The statement is effective for financial statements issued for fiscal years beginning after June 15, 2002. Telecom Italia is currently determining the impact of the adoption of SFAS 143 on its results of operations, financial positions and cash flows.

In October 2001, the FASB issued SFAS 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." This new standard supersedes SFAS 121, "Accounting for the Impairment of Long-Lived Assets and for the Long-Lived Assets to be Disposed Of", providing one accounting model for the review of asset impairment other than for goodwill and indefinite life intangible assets. SFAS 144 retains the current requirement to recognize an impairment loss only if the carrying amounts of long-lived assets to be held and used are not recoverable from their expected undiscounted future cash flows and exceeds their fair value. However, goodwill is no longer required to be allocated to these long-lived assets when determining their carrying amounts. SFAS 144 requires that a long-lived asset to be disposed of other than by sale be considered held and used until it is disposed of, requiring the depreciable life to be adjusted as a change in accounting estimate. For financial statement presentation purposes, the criteria used to classify long-lived assets to be disposed of by sale have changed from SFAS 121. However, the statement continues to require that the amortization and depreciation of all long-lived assets to be disposed of by sale cease, and that these assets be recorded at the lower of their carrying amount or fair value less cost to dispose.

Statement 144 also supersedes the section of APB Opinion 30 "Reporting the Results of Operations - Reporting the Effects of Disposal of a Segment, and Extraordinary, Unusual and Infrequently Occurring Events and Transactions" which prescribes reporting for the effects of a disposal of a segment of a business. Discontinued operations are no longer measured on a net realizable value basis, and future operating losses are no longer recognized before they occur. The statement also broadens the definition of a discontinued operation to include a component of an entity. The provisions of SFAS 144 are effective for financial statements issued for fiscal years beginning after December 15, 2001, and interim periods within those fiscal years. Telecom Italia is currently determining the impact of the adoption of SFAS 144 on its results of operations, financial position and cash flows.

(u) Related party transactions

The Group enters into transactions with affiliates, and various related parties. The following related party transactions relate to transactions between Telecom Italia and its subsidiaries and the Group's unconsolidated subsidiaries and affiliated companies as well as the members of the Board of Directors and the companies in which they hold corporate office or significant responsibility. Transactions between members of the Group are excluded as they are eliminated on consolidation. All such transactions are within the Group's normal operations.

The following related party transactions are reflected in the statement of income for the years ended December 31, 2001, 2000 and 1999:

- *Operating revenues:* comprise mainly revenues from Astrolink (Euro 296 million in 2001), Brasil Telecom (Euro 120 million in 2001), Nortel Inversora group (Euro 119 million in 2001, Euro 81 million in 2000 and Euro 91 million in 1999), Teleleasing (Euro 82 million in 2001 and Euro 113 million in 2000), Auna Group (Euro 63 million in 2001 and Euro 57 million in 2000), Stream (Euro 55 million in 2001, Euro 102 million in 2000 and Euro 79 million in 1999), Lottomatica (Euro 53 million in 2001, Euro 58 million in 2000 and Euro 44 million in 1999) and SEAT (Euro 211 million in 2000 and Euro 159 million in 1999). In the aggregate, operating revenues were Euro 881 million in 2001 (Euro 837 million in 2000 and Euro 557 million in 1999).

- *Cost of materials and other external charges*: refers mainly to rent payable to IMSER (Euro 199 million in 2001 and Euro 23 million in 2000) and Telemaco Immobiliare (Euro 77 million in 2001), TLC service costs from Etec S.A. Cuba (Euro 79 million in 2001 and Euro 24 million in 2000) and Entel Chile Group (Euro 40 million in 2000) and cost of materials and other external charges from Siemens Informatica (Euro 80 million in 2000 and Euro 38 million in 1999), SEAT (Euro 61 million in 2000 and Euro 91 million in 1999) and Teleleasing (Euro 59 million in 2000). In the aggregate, cost of materials and other external charges accounted for Euro 586 million in 2001 (Euro 377 million in 2000 and Euro 242 million in 1999).

- *Other income, net*: relates mainly to cost recoveries for personnel on loan to certain foreign unconsolidated affiliates. In the aggregate other income, net, accounted for Euro 25 million in 2001 (Euro 19 million in 2000 and Euro 26 million in 1999).

- *Interest income and expense, net*: refers to accrued interest income on loans made to certain foreign unconsolidated affiliates (Euro 22 million in 2001), interest expense payable to Teleleasing (Euro 30 million in 2001 and Euro 31 million in 2000) for financial leasing transactions and dividends received from the Eutelsat satellite consortium (Euro 64 million in 2000). In the aggregate, interest income and expense, net, was negative for Euro 8 million in 2001 (positive for Euro 54 million in 2000 and Euro 19 million in 1999).

The following related party transactions are reflected on the balance sheet as of December 31, 2001and 2000:

- *Loans in long-term investments*: refers mainly to loans granted to Bouygues Décaux Télécom (BDT) (Euro 108 million at December 31, 2001 and Euro 102 million at December 31, 2000) and other foreign unconsolidated affiliates. In the aggregate such loans were Euro 119 million at December 31, 2001 (Euro 138 million at December 31, 2000).

- *Trade accounts receivables and other current assets*: comprises mainly receivables from Auna group (Euro 90 million at December 31, 2001 and Euro 48 million at December 31, 2000), Stream (Euro 82 million at December 31, 2001 and Euro 23 million at December 31, 2000), Telekom Srbija (Euro 56 million, net of provision at December 31, 2001 and Euro 66 million at December 31, 2000), Nortel Inversora group (Euro 21 million, net of provision at December 31, 2001, and Euro 22 million at December 31, 2000), Teleleasing (Euro 18 million at December 31, 2001), Golden Lines International (Euro 25 million at December 31, 2000), IM.SER (Euro 46 million at December 31, 2000), Consortium CSIA (Euro 13 million at December 31, 2000) and Etec S.A. (Euro 13 million at December 31, 2000). In the aggregate trade accounts receivables and other current assets were Euro 430 million at December 31, 2001 (Euro 328 million at December 31, 2000).

- *Trade accounts payable and other current liabilities*: pertains mainly to supplier relationships connected with investments and transactions. In particular, they comprise trade accounts payable to Italtel group (Euro 173 million at December 31, 2001 and Euro 277 million at December 31, 2000), Siemens Informatica (Euro 51 million at December 31, 2001 and Euro 38 million at December 31, 2000), Teleleasing (Euro 42 million at December 31, 2001 and Euro 22 million at December 31, 2000), advances from Consorzio Telcal (Euro 85 million at December 31, 2001), Entel Chile group (Euro 41 million at December 31, 2000), Telekom Srbija (Euro 23 million at December 31, 2000), Golden Lines International (Euro 17 million at December 31, 2000), Auna group (Euro 13 million at December 31, 2000), Etec S.A. (Euro 11 million at December 31, 2000) and Telekom Austria group (Euro 10 million at December 31, 2000). The item also includes payables to Astrolink (Euro 95 million at December 31, 2000) for capital contributions payable. In the aggregate trade accounts payable were Euro 485 million at December 31, 2001 (Euro 834 million at December 31, 2000).

- *Long-term and short-term debt*: refers mainly to payables for finance leases to Teleleasing (Euro 522 million at December 31, 2001 and Euro 554 million at December 31, 2000) and a payable by Softe from Olivetti Finance N.V. (Euro 600 million at December 31, 2001), payables to IM.SER (Euro 81 million at December 31, 2000), Webegg (Euro 29 million at December 31, 2000) and Italtel group (Euro 20 million at December 31, 2000). In the aggregate long-term and short-term debt were Euro 1,170 million at December 31, 2001 (Euro 692 million at December 31, 2000).

- *Short-term financial receivables*: refers mainly to short-term loans receivable from Stream (Euro 122 million at December 31, 2001 and Euro 55 million at December 31, 2000), IS Tim (Euro 29 million at December 31, 2001), Telekom Srbija (Euro 23 million at December 31, 2001 and Euro 21 million at December 31, 2000) and from the affiliates of SEAT (Euro 60 million at December 31, 2000). In the aggregate short-term financial receivables were Euro 213 million at December 31, 2001 (Euro 175 million at December 31, 2000).

- *Long and short-term contracts*: refers mainly to activities on behalf of Consorzio Telcal for the Telematico Calabria Plan (Euro 110 million at December 31, 2001). In the aggregate such long and short-term contracts accounted for Euro 116 million at December 31, 2001 (Euro 71 million at December 31, 2000).

- *Guarantees and collateral:* includes sureties given on behalf of the Auna group (Euro 510 million at December 31, 2001), IS Tim (Euro 228 million at December 31, 2001), Stream (Euro 86 million at December 31, 2001), Retevision Movil (Euro 1,658 million at December 31, 2000), Italtel group (Euro 177 million at December 31, 2000) and the affiliates of SEAT (Euro 162 million at December 31, 2000) as well as collateral given on behalf of IS Tim (Euro 147 million at December 31, 2001). In the aggregate such guarantees and collateral accounted for Euro 1,261 million at December 31, 2001 (Euro 2,420 million at December 31, 2000).

- *Capital expenditures*: mainly consist of acquisitions telephone exchanges from the Italtel group (Euro 567 million in 2001 and Euro 184 million in 2000) and information and computer projects from Siemens Informatica (Euro 31 million in 2001 and Euro 32 million in 2000). In the aggregate investments in fixed and intangible assets accounted for Euro 665 million in 2001 (Euro 234 million in 2000).

SEAT

In connection with the 2000 SEAT-Tin.it transaction, Telecom Italia contributed its ownership of the Italian White Pages to Tin.it, including the assignment of its contracts with SEAT relating to the production of and advertising in the White Pages in Italy. Under the terms of the contracts, prior to the acquisition of the controlling interest in SEAT, the Group including Tin.it paid SEAT for the production and printing of the White Pages and received advertisement royalties from SEAT. Subsequent to the acquisition of the controlling interest in SEAT, these contracts have been terminated and the revenues and expenses no longer exist. The amounts relating to these transactions are disclosed in the relevant sections above.

Parent company

Pursuant to a tender offer in 1999, Olivetti S.p.A. ("Olivetti"), our majority shareholder, gained, through its subsidiary Tecnost, a controlling interest in Telecom Italia, and as at December 31, 2001 holds approximately 55 per cent of Telecom Italia. Dividends of Euro 891 million and Euro 13 million were paid to Olivetti and Olivetti Finance, respectively, in 2001 (Euro 888 million was paid to Tecnost - then merged into Olivetti - in 2000 and Euro 396 million in 1999).

Pirelli group

Related party transactions in 2001 also include those by the Telecom Italia Group with the Pirelli group. Pirelli has a 60% interest in Olimpia, which owns approximately 28.7% of the share capital of Olivetti.

The following related party transactions are reflected in the statement of income for the year ended December 31, 2001:

- *Operating revenues:* mainly refers to telephone services (Euro 6.9 million).

The following related party transactions are reflected on the balance sheet as of December 31, 2001:

- *Trade accounts receivables and others*: mainly refers to the above-mentioned telephone services (Euro 0.6 million).

- *Trade accounts payable and others*: mainly pertain to the supply contracts connected with supplier relationships (Euro 6.4 million).

- *Capital expenditures*: mainly consist of purchases of telecommunications cables (Euro 21.5 million).

Directors and Executive Officers

The following comments concern the relationships between Telecom Italia and companies in which the directors of Telecom Italia (who resigned in the second half of 2001) held specific positions, as well as relationships with key managers and/or directors of the Group's companies who also resigned in the second half of 2001:

- based on a contract signed on March 15, 2000 by Telecom Italia, Huit II, Huit (now TI Media) and its shareholders, and Lorenzo Pelliccioli, regarding the integration of Tin.it into SEAT, and furthermore, by virtue of previous agreements, Lorenzo Pelliccioli (the then CEO of SEAT who resigned in the second half of 2001) became a stockholder of Huit II in July 2000 through a capital increase of 1.05% reserved for him. Consequently, the number of SEAT shares held by Telecom Italia, indirectly through Huit, was proportionally reduced. Lorenzo Pellicioli later sold the stake in Huit II to the parent company Huit. Telecom Italia, as a shareholder in Huit, contributed Euro 19 million to the total benefit received by Lorenzo Pellicioli;

- in April 2001, Telecom Italia Lab (a 100%-owned subsidiary of Telecom Italia), joined with the Ramius Capital Group, an American investment management company (in which the then director, Peter Cohen, was the CEO), to set up an United States-registered venture capital fund called Saturn Venture Partners which targets investments in fixed and mobile TLC technologies and service infrastructures. The fund's participants also included the companies TIM, Olivetti and Hopa, in which the then Chairman Roberto Colaninno and the then director Emilio Gnutti were shareholders and directors;

- the law firm of Studio Bonelli, Erede, Pappalardo in which the then Deputy Chairman of Telecom Italia Mr. Sergio Erede was the senior partner, has performed professional legal services on behalf of Telecom Italia and some companies in the Group. The Group paid legal fees to this law firm totaling Euro 16 million in 2001 (Euro 5 million in 2000 and Euro 0.9 million in 1999);

- in March 2001, Telecom Italia purchased a 12.3% stake in Netesi S.p.A. – with headquarters in Milan and operating in the area of on-line applications services – by subscribing to a first tranche of new shares issued for a capital increase for an investment of approximately Euro 6.2 million. In September 2001, Telecom Italia's stake rose to 17.98% following a successive increase in share capital. Netesi's shareholders included, among others, Omniaholding (a related party of Telecom Italia, through the then Chairman Roberto Colaninno);

- in August 2001, Huit II, a subsidiary of Telecom Italia, purchased - by exchanging 186 million Seat Pagine Gialle ordinary shares - a 100% stake in ISM S.r.l. (owned by Messrs. Ainio and Gualandri, both of whom were managers and directors of companies in the Group in service at the time), a company that holds – through the subsidiary Vertico N.V. - a 33.3% stake in Matrix S.p.A.;

- furthermore, two executives of Telecom Italia (in service at the time) had each purchased a building from Telecom Italia, paying the market price.

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers SpA

To the Board of Directors and Shareholders of
Finsiel SpA

We have audited the consolidated balance sheet of Finsiel SpA (an Italian corporation) and its subsidiaries (the "Company") as of December 31, 2001 (all expressed in Euro) and the related consolidated statements of income for the year then ended. These financial statements are the responsibility of the Company's Directors. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Finsiel SpA and its subsidiaries as of December 31, 2001, and the results of their income for the year then ended, in conformity with the Italian law governing consolidated financial statements and generally accepted accounting principles in Italy.

Accounting principles generally accepted in Italy vary in certain significant respects from accounting principles generally accepted in the United States.

PricewaterhouseCoopers SpA

Corrado Testori
(Partner)

Rome, 12 March 2002

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Deloitte & Touche

INDEPENDENT AUDITORS' REPORT

The Board of Directors and Shareholders
Empresa Nacional de Telecomunicaciones S.A.

We have audited the accompanying consolidated balance sheet of Empresa Nacional de Telecomunicaciones S.A. and subsidiaries as of December 31, 2001 and the related consolidated statements of income and cash flows for the year then ended, all expressed in thousands of Chilean pesos. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in Chile and in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Empresa Nacional de Telecomunicaciones S.A. and subsidiaries as of December 31, 2001, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in Chile.

Accounting principles generally accepted in Chile vary in certain significant respects from accounting principles generally accepted in United States of America. The application of the latter would have affected the determination of net income and shareholders' equity as of December 31, 2001 to the extent summarized in Note 36 to the consolidated financial statements.

Deloitte & Touche

Santiago, Chile
January 28, 2002

Deloitte
Touche
Tohmatsu

Independent auditors' report

The Supervisory Board and Stockholders
Mobilkom Austria AG & Co KG and
Mobilkom Austria AG:

We have audited the accompanying combined consolidated balance sheets of Mobilkom Austria AG & Co KG and Mobilkom Austria AG (the "Company" or "Mobilkom") as of December 31, 2001 and 2000, and the related combined consolidated statements of operations, cash flows and changes in stockholders' equity for each of the years in the three year period ended December 31, 2001. These combined consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these combined consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the combined consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the combined consolidated financial statements referred to above present fairly, in all material respects, the financial position of Mobilkom as of December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton – Jonasch & Platzer Wirtschaftsprüfungs- und Steuerberatungs-OHG	KPMG Austria GmbH Wirtschaftsprüfungs- und Steuerberatungsgesellschaft
Grant Thornton – Jonasch & Platzer	KPMG Austria GmbH

Vienna
March 15, 2002

Independent auditors' report

The Supervisory Board and Stockholders
Telekom Austria Aktiengesellschaft

We have audited the accompanying consolidated balance sheets of Telekom Austria Aktiengesellschaft ("Telekom Austria") as of December 31, 2001 and 2000, and the related consolidated statements of operations, cash flows and changes in stockholders' equity for each of the years in the three year period ended December 31, 2001. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Telekom Austria as of December 31, 2001 and 2000, and the results of its operations and its cash flows for each of the years in the three year period ended December 31, 2001, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton – Jonasch & Platzer Wirtschaftsprüfungs- und Steuerberatungs-OHG	KPMG Austria GmbH Wirtschaftsprüfungs- und Steuerberatungsgesellschaft
Grant Thornton – Jonasch & Platzer	KPMG Austria GmbH

Vienna
March 20, 2002

PRICEWATERHOUSECOOPERS

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REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors of
İş-Tim Telekomünikasyon Hizmetleri A.Ş.

We have audited the accompanying balance sheet of İş-Tim Telekomünikasyon Hizmetleri A.Ş. ("İş-Tim") at 31 December 2001 and the related statement of loss, changes in shareholders' equity and cash flows for the year then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of İş-Tim at 31 December 2001 and the results of its operations and its cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Başaran Nas Serbest Muhasebeci
Mali Müşavirlik Anonim Şirketi
a member of
PricewaterhouseCoopers

Murat Sancar, SMMM

Istanbul, 1 February 2002

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers SpA

REPORT OF INDEPENDENT ACCOUNTANTS

To the Board of Directors and
Stockholders of Telecom Italia SpA

We have audited the accompanying consolidated balance sheet of TELECOM ITALIA SpA (an Italian corporation) and its subsidiaries as of December 31, 2000 and the related consolidated statements of operations, of changes in stockholders' equity and of cash flows for the period ended December 31, 2000, all expressed in Euro. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit. We did not audit the consolidated financial statements of Telecom Italia Mobile SpA, a subsidiary which is 54.8 percent owned by the Company, which statements reflect total assets of 17,691 millions of Euro and total revenues of 7,959 millions of Euro as of and for the period ended December 31, 2000. Those statements were audited by other auditors whose report thereon has been furnished to us, and our opinion expressed herein, insofar as it relates to the amounts included for Telecom Italia Mobile SpA, is based solely on the report of the other auditors.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audit and the report of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of TELECOM ITALIA SpA and its subsidiaries as of December 31, 2000, and the results of their operations and their cash flows for the period ended December 31, 2000 in conformity with the Italian law governing consolidated financial statements and generally accepted accounting principles in Italy.

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PRICEWATERHOUSECOOPERS

The accounting principles referred to above vary in certain significant respects from accounting principles generally accepted in the United States of America. The application of the latter would have affected the determination of consolidated net income expressed in Euro for the period ended December 31, 2000 and the determination of consolidated stockholders' equity and consolidated financial position also expressed in Euro at December 31, 2000 to the extent summarized in Note 26 to the consolidated financial statements.

Turin, May 21, 2001

PricewaterhouseCoopers SpA

Sergio Duca
(Partner)

ARTHURANDERSEN

Arthur Andersen SpA
Galleria San Federico 54
10121 Torino

Report of Independent Accountants

To the Board of Directors and Shareholders of
Telecom Italia Mobile S.p.A.:

We have audited the consolidated balance sheets of Telecom Italia Mobile S.p.A. and its subsidiaries as of December 31, 2000, and the related consolidated statements of income for the year ended December 31, 2000, all expressed in Euro. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, which assets reflect approximately 24% of total assets as of December 31, 2000, while consolidated revenues, which refer to Telecom Italia Mobile S.p.A. only, have been fully analyzed by us, being the acquisition of the main subsidiary finalized at year end. Those statements were audited by other auditors whose reports have been furnished to us and our opinion, insofar as it relates to the amount included for those entities, is based solely on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the reports of the other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the consolidated financial statements referred to above give a true and fair view of the financial position of Telecom Italia Mobile S.p.A. and its subsidiaries as of December 31, 2000 and the results of their operations for the year ended December 31, 2000 in conformity with generally accepted accounting principles in Italy.

Turin, Italy
March 22, 2001

Arthur Andersen

ARTHUR ANDERSEN

Arthur Andersen SpA
Galleria San Federico 54
10121 Torino

Report of Independent auditors

To the Shareholders of
Telecom Italia S.p.A.:

We have audited the accompanying consolidated balance sheets of Telecom Italia S.p.A. (formerly STET - Società Finanziaria Telefonica p.a.) and subsidiaries (an Italian corporation) as of December 31, 1999, and the related consolidated statements of income, changes in stockholders' equity and cash flows for the year in the period ended December 31, 1999, all expressed in Euro. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, which statements reflect assets representing approximately 16% of total assets as of December 31, 1999, and operating revenues representing approximately 13% of consolidated operating revenues for the year in the period ended December 31, 1999. Those statements were audited by other auditors whose reports have been furnished to us and our opinion, insofar as it relates to the amounts included for those entities, is based solely on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Telecom Italia S.p.A. as of December 31, 1999, and the results of its operations and changes in its financial position for the year in the period ended December 31, 1999 in conformity with generally accepted accounting principles in Italy.

The accounting principles referred to above vary in certain respects from accounting principles generally accepted in the United States of America ("U.S. GAAP"). A description of these differences and the adjustments required to conform consolidated net income for the year in the period ended December 31, 1999 and consolidated stockholders' equity as of December 31, 1999 to U.S. GAAP are set forth in Note 26 to the consolidated financial statements.

Also, in our opinion, the amounts translated into U.S. Dollars in the accompanying consolidated financial statements as of and for the year ended December 31, 1999, have been computed on the basis set forth in Note 1 to the consolidated financial statements.

Arthur Andersen

Turin, Italy
April 10, 2000

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Deloitte & Touche

REPORT OF INDEPENDENT AUDITORS

To the Shareholders of
FINSIEL - Consulenza e applicazioni informatiche S.p.A.

We have audited the accompanying consolidated balance sheets of FINSIEL - Consulenza e applicazioni informatiche S.p.A. (an Italian corporation) and Subsidiaries as of December 31, 1999 and 1998, and the related consolidated statements of income, changes in stockholders' equity and cash flows for each of the three years in the period ended December 31, 1999 all expressed in Italian Lire. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, which statements reflect assets representing approximately 23% and 22% of total assets as of December 31, 1999 and 1998 respectively, and operating revenues representing approximately 18% of consolidated operating revenues for each of the three years in the period ended December 31, 1999. Those statements were audited by other auditors whose reports have been furnished to us and our opinion, insofar as it relates to the amounts included for those entities, is based solely on the reports of the other auditors.

We conducted our audits in accordance with generally accepted auditing standards in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits and the report of other auditors provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of FINSIEL - Consulenza e applicazioni informatiche S.p.A. and Subsidiaries as of December 31, 1999 and 1998, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 1999 in conformity with generally accepted accounting principles in Italy.

Deloitte & Touche

Rome, Italy
March 15, 2000

Deloitte & Touche

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INDEPENDENT AUDITORS' REPORT

To the Shareholders
of SIRTI S.p.A.

We have audited the accompanying consolidated balance sheet of SIRTI S.p.A. (an Italian corporation) and its subsidiaries as of December 31, 1999 and 1998 and the related consolidated statements of income, cash flows and stockholders' equity for each of the three years ended December 31, 1999, 1998 and 1997 all expressed in Italian Lire. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits. We did not audit the financial statements of certain subsidiaries, which in total represent approximately 12% and 21% of total assets as of December 31, 1999 and 1998, respectively and turnover of approximately 19%, 31% and 24% of consolidated turnover for the years ended December 1999, 1998 and 1997 respectively. Those financial statements were audited by other auditors whose reports have been furnished to us and our opinion, insofar as it relates to the amounts included for such subsidiaries, is based solely on the reports of the other auditors.

We conducted our audits in accordance with auditing standards generally accepted in Italy and in the United States of America. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, based on our audits and the reports of the other auditors, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of SIRTI S.p.A. and its subsidiaries as of December 31, 1999 and 1998 and the results of their operations and changes in their financial position for each of the three years ended December 31, 1999, 1998 and 1997 in conformity with accounting principles generally accepted in Italy.

Deloitte Touche Tohmatsu

Milano Ancona Bari Bergamo Bologna Cagliari Firenze Genova Napoli Parma Roma Torino Treviso Vicenza

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Capitale Sociale Lire [illegible] - Partita IVA / Codice Fiscale [illegible]
Registro delle Imprese Milano n. [illegible] - R.E.A. Milano n. [illegible]

In order to better understand SIRTI Group's consolidated financial statements, attention is drawn to the following information related respectively to the consolidated financial statements as of December 31, 1999, December 31, 1998 and December 31, 1997:

- For the first time as from January 1, 1999, the SIRTI Group, as indicated in the notes to the financial statements, has valued receivables and payables in foreign currency based on year end exchange rates; furthermore, it has recorded long term contracts utilising the stage of completion method, which involves the valuation of remaining contract work to be made in correspondence with the income attributable to the services and works already completed, as well as the recognition of profits and costs for the year in which the work was effected.
  The adoption of the two criteria mentioned above gave rise to a higher net result and higher corresponding net equity, compared to those which would have been recorded had the preceding criteria continued to have been applied, of approximately Lire 5.3 billion (the conversion of the items in foreign currency at end of period exchange rates) and of Lire 17.1 billion (the valuation of long term contracts at presumed income).

- As discussed in the note on inventories in the 1998 and 1997 consolidated financial statements, the SIRTI Group has valued work in progress on long term contracts by applying the completed contract method, which is in agreement with the method used to value production cost and therefore in compliance with the Italian Civil Code.
  Accounting principles generally accepted in Italy also require disclosure of the effects on consolidated revenues, costs, net profit and shareholders' equity of applying this method as opposed to the stage of completion method, which accounts for contractual fees as they accrue.
  If the stage of completion valuation method had been consistently applied, consolidated production value would have been approximately Lire 15 billion higher than the figure shown in the financial statements as of December 31, 1998 and unchanged as of December 31, 1997; hence the consolidated net profit would have been increased by some Lire 8.8 billion in 1998 with no significant effect on the 1997 consolidated net profit; finally, the consolidated shareholders' equity as of December 31, 1998 would have been increased by Lire 14.8 billion, net of the tax effect.

DELOITTE & TOUCHE S.p.A.

Adolfo Mamoli
Partner

March 28, 2000

PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers SpA

AUDITORS' REPORT

To the shareholders of
ITALTEL S.p.A.

1. We have audited the consolidated financial statements of *ITALTEL S.p.A.* as of 31 December 1999. These financial statements are the responsibility of *ITALTEL S.p.A.*'s directors. Our responsibility is to express an opinion on these financial statements based on our audit.

2. We conducted our audit in accordance with the auditing standards and criteria recommended by CONSOB. Those standards and criteria require that we plan and perform the audit to obtain the necessary assurance about whether the financial statements are free of material misstatement and, taken as a whole, are presented fairly. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by the directors. We believe that our audit provides a reasonable basis for our opinion.

3. For the opinion on the consolidated financial statements of the prior period, which are presented for comparative purposes as required by law, reference is made to the report issued by Coopers & Lybrand S.p.A. dated 7 April 1999.

4. In our opinion, the consolidated financial statements of *ITALTEL S.p.A.* as of 31 December 1999 comply with the laws governing the criteria for their preparation; accordingly, they give a true and fair view of the consolidated financial position and of the consolidated results of operations of the Company.

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PRICEWATERHOUSECOOPERS

5. For the purposes of a better understanding of the consolidated financial statements we wish to emphasise the following issues, which are disclosed in the Directors' report on operations and in the notes to the consolidated financial statements:

(a) During the year the Company contributed the business unit Mobile Telecommunications Networks, Radio Systems and Transport Systems to Siemens Information and Communication Networks S.p.A., a new entity specially set up for this purpose and later sold to Siemens group.
The terms and effects of the operation are disclosed in the Directors' report on operations and in the notes to the consolidated financial statements.

(b) Pursuant to the provisions of Accounting Principle No. 25 – The accounting treatment for income taxes – issued *by Consigli Nazionali dei Dottori Commercialisti e dei Ragionieri* (Italian Board of Certified Public Accountants) in March 1999, the Company recorded in the consolidated financial statements deferred tax assets on the temporary differences between the carrying amounts of assets and liabilities and their tax bases for the first time.
The effects of the adoption of the new accounting principle on the result for the year and on shareholders' equity are disclosed in the notes to the consolidated financial statements.

Milan, 13 April 2000

PricewaterhouseCoopers S.p.A.

Enrico Picasso
(Partner)

This report has been translated from the original which was issued in accordance with Italian practice.