FORM 20-F

ANNUAL REPORT

FISCAL YEAR 2000

TELECOM ITALIA

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, 2000
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 euro 0.55 par value each	The New York Stock Exchange
Ordinary Shares of euro 0.55 par value each (the "Shares")	The New York Stock Exchange*
American Depositary Shares, each representing 10 Savings Shares of euro 0.55 par value each	The New York Stock Exchange
Savings Shares of euro 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, its consolidated subsidiaries and its associated companies that are proportionately consolidated.

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 market place, including liberalization of the telecommunications industry, the opening to competition of public voice telephone services and introduction of additional competition in Italy and in Europe, 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 - Risk Factors,” (ii) “Item 4. Information on the Company — Business — Recent Developments”, “— Strategy”, “ — International Investments”, (iii) “Item 4. Information on the Company — Regulation”, (iv) “Item 5. Operating and Financial Review and Prospects” and “Quantitative and Qualitative Disclosures About Market Risk” and (v) “Item 8. Legal Proceedings”, 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 fully liberalized market, including the entry of new competitors, especially global and regional alliances formed by other telecommunications operators, in Telecom Italia’s core fixed-line and wireless markets;
- Telecom Italia’s ability to continue the introduction of 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;
- 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;
- 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 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;
- the Group's ability to realize the benefits of its investment in UMTS licenses and related capital expenditures;
- 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 Group's ability to realize the benefits of the merger of SEAT and Tin.it; and
- SEAT's ability to implement successfully its internet strategy.

In addition to the factors noted above, the ability of the Group to achieve certain of its objectives described herein assumes the continuing rebalancing of the tariff system in order to reduce subsidization of certain tariff categories by other ones and a satisfactory determination on interconnection fees that takes into account both the obligation to provide universal service and the access deficit.

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. 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 was consolidated into TI Lab.
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.
Demerged Activities	means the various publishing, advertising and direct marketing activities formerly conducted by the Group, which were spun off to shareholders effective December 31, 1996.
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, indirectly through Tecnost until December 31, 2000 and directly thereafter.
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.
Tecnost	means Tecnost S.p.A., which before December 31, 2000 was the holding company and controlling shareholder of Telecom Italia. On December 31, 2000 Tecnost was merged with and into Olivetti.
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.
TI LAB	means Telecom Italia Lab S.p.A., 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

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

Domestic competition has been introduced in the principal telecommunications business areas in which Telecom Italia operates, including, most significantly, the provision of fixed line and mobile voice telecommunications services, which was fully liberalized and has been opened to competition since January 1, 1998. 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 have faced 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 December 31, 2000, there were a number of significant competitors offering fixed line services and three other operators offering mobile services. This increased competition has led to declines in the Company market shares, particularly for the provision of international, domestic long distance and mobile communication services, 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 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 other alternative revenue sources. These services included non-voice services such as Internet and data traffic and value added services such as interactive messages allowing users to receive news or do banking, in mobile services. Alternative revenue sources also include increased interconnection traffic from other operators using Telecom Italia's fixed line network. In addition to the steps taken in recent years, Telecom Italia is continuing 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.

Furthermore, Telecom Italia's strategy is based on attaining strong growth in certain areas, particularly Internet and data usage. If these markets do not grow as rapidly as expected, Telecom Italia's business could be adversely affected.

Telecom Italia's business will be adversely affected if it is unable to achieve cost reduction targets in the time frame established or to continue the process of rationalizing its non-core assets.

On September 1, 1999, the board of directors of Telecom Italia approved the guidelines for a restructuring plan intended to reduce group costs. Telecom Italia has already met a number of the interim cost-reduction targets of its plan and has disposed of substantially all of the non-core assets which had been originally identified for sale, as described under "Item 4. Information on the Company — Business — Significant Developments during 2000". Telecom Italia intends to continue to evaluate its portfolio of non-core assets and will continue implementation of its cost reduction plans. However, should Telecom Italia seek to sell additional assets, it may not be able to complete further divestments or it may not be able to receive the expected proceeds due to market conditions or other factors. In addition, Telecom Italia may be unable to achieve its cost reduction targets on a timely basis or its ongoing business operations may be disrupted by implementation of its restructuring plan. If any of these events take place, Telecom Italia may have to amend its current cost reduction plans, which may adversely affect its financial position or 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, publication of telephone directories and provision of subscriber information services, public payphones, free emergency call services and other obligations. In addition, the National Regulatory Agency has identified the Company as an operator having significant market power. 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 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, as of February 2001, 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. A review of telecommunications regulation is currently underway by EU regulators. 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.

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.

Telecom Italia has 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.

Telecom Italia's strategy has focused on:

- consolidating its international presence in two strategic markets: Europe, primarily Southern Europe and Latin America, and expanding selectively in the Mediterranean Basin;
- 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.

Telecom Italia's international expansion program is an important element of its business strategy. This strategy has required significant investments and Telecom Italia invested at the end of 2000 approximately Lit. 1,993 billion (US$ 905 million) for a further 28.61% additional stake in Entel Chile SA and Lit. 1,904 billion (US$ 884 million) for the purchase of three additional wireless licenses in Brazil net of discounts for the restitution of overlapping frequencies and US$810 million for the acquisition of a 30% stake in Globo.com. Aggregate financial investment in international operations during 2000 was Lit. 7,649 billion and additional capital investments will be required in Latin America and Europe to further this business strategy. However, because other major telecommunications companies are following similar strategies or attempting to penetrate the same markets, opportunities are becoming more limited. In addition, licenses for wireless services are frequently subject to minimum prices established by the relevant country or are sold through an auction process which can significantly impact prices. Due to the high level of investment and the significant competitive environment in these international markets, Telecom Italia can give no assurance that it will be able to achieve the expected return on its investment in these markets.

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. 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 affected 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 with 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 acquisition of a controlling interest in SEAT, as well as its international expansion, the Group's total indebtedness at year end 2000 was Lit. 45,317 billion compared with Lit. 19,624 billion at year end 1999. 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 effect 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, Telecom Italia has recently acquired a third generation mobile telephone, or UMTS, license to commence operations of UMTS services in Italy. In addition, TIM has made and may be required to make during the next several years substantial investments in other countries in Europe and Latin America to acquire additional UMTS licenses, to build out UMTS networks and develop related products and services. As of March 31, 2001, TIM has committed to pay Lit. 4,680 billion for its UMTS license in Italy and, through its international subsidiaries, a further Lit. 587.6 billion for UMTS licenses in Spain and Austria (of which approximately Lit. 4,588 billion has already been paid). As a result, TIM's future success is dependent, in large measure, upon the capabilities and widespread market acceptance of UMTS technology in these markets. However, UMTS technology may not develop in a timely manner or, if developed, it may not provide the expected advantages over existing technologies. In addition, demand for UMTS-based services is unproven and may not develop as TIM anticipates. Accordingly, there is no assurance that a significant market for UMTS services will develop or, even if such a market develops, that TIM will be able to achieve its desired sales volume for UMTS services. If UMTS technology is not developed on a timely basis, if it does not deliver the anticipated advantages or gain widespread acceptance, if TIM derives a smaller than expected percentage of its total revenues and profitability from its UMTS-related services, or if TIM is otherwise not able to realize the expected return on its substantial investment in UMTS licenses and technology, its results of operations and financial condition as well as that of Telecom Italia may be materially and adversely affected.

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

Concern has been expressed that the electromagnetic signals from mobile handsets and transmission masts, which serve as antennae for transmitting radio signals, may pose health risks and interfere with the operation of electronic equipment, including automobile braking and steering systems. Actual or perceived risks of mobile handsets or transmission masts, and related negative publicity or litigation could reduce the growth rate of Telecom Italia's mobile communications business, customer base, or average usage per customer. Environmental objections may also impair Telecom Italia's ability to augment its infrastructure, including primarily its mobile and data networks. In addition, those actual or perceived risks may lead to regulatory changes which could impose additional costs or otherwise adversely affect Telecom Italia's business.

Telecom Italia may not be able to realize the benefits of the merger of SEAT and Tin.it

In November 2000, Telecom Italia and SEAT, Italy's yellow pages publisher, completed the merger of SEAT and Tin.it, Telecom Italia's internet division. Following completion of the merger and other transactions, the Company owned, directly and indirectly, approximately 60% of SEAT's ordinary shares. If a recently announced acquisition by SEAT is consummated, the Company's ownership of SEAT ordinary shares could be reduced to approximately 50%. SEAT and Telecom Italia expect that the merger will result in significant synergies, creating a company capable of delivering a full range of Internet services to the consumer and small and medium-sized business markets. However, the integration of the operations, personnel and products of SEAT's directories publishing and Internet operations, the businesses that SEAT has recently acquired and the several businesses comprising Tin.it presents a significant management challenge. This is particularly due to the different products and services offered, and technologies utilized, by the respective businesses. SEAT also intends to form a joint venture with TIM in electronic commerce and content and service offerings using mobile devices. If SEAT is not able to integrate successfully all of these businesses or to form and operate successfully the joint venture, it may not realize the anticipated synergies in full or at all.

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

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 54.96% interest in Telecom Italia's ordinary shares. If Telecom Italia completes its conversion offer and all Savings Shareholders participate in the exchange offer, (please see "Item 4. Information on the Company—Business—Recent Developments—Conversion of Savings Shares for Shares and Tender Offer for Shares") Olivetti's stake in Telecom Italia's ordinary share capital will be reduced to approximately 40%. Nevertheless, Olivetti will still have significant influence in shareholders' meetings since it will retain a relative majority of the Shares. As a result, it would still be 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 by-laws; 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.

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, 2000, Olivetti's total debt was approximately euro 18.5 billion. Although Olivetti's debt is expected to decrease if the exchange offer of Telecom Italia's Savings Shares for Shares is successfully completed and the subsequent tender offer for Telecom Italia's ordinary shares is made, Olivetti's financial position may affect adversely 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—Recent Developments".

RATES OF EXCHANGE

Telecom Italia publishes its Consolidated Financial Statements in Italian lire. References to “lire”, “lira” and “Lit.” are to Italian lire, the lawful currency of Italy, references to “U.S. dollars”, “dollars”, “U.S.$” or “$” are to U.S. dollars, the lawful currency of the United States and references to “€”, “euro” and “Euro” are to the euro, the new single unified currency that was introduced in Italy and 10 other participating member states of the European Union on January 1, 1999 and was also adopted by Greece on January 1, 2001 (collectively the “Member States”).

For convenience only (except where noted otherwise), certain lira figures have been translated into dollars at the rate (the “Lira/Dollar Exchange Rate”) of Lit. 2,201.80 = U.S.$1.00, 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”) for the euro on March 30, 2001 of €1.1371 = $1.00 multiplied by the fixed euro/lira exchange rate (the “Fixed Euro/Lira Exchange Rate”) of Lit. 1,936.27 = €1.00 established on December 31, 1998. These translations should not be construed as a representation that the lira amounts actually represent such dollar amounts or have been or could be converted into dollars at the rate indicated. On June 15, 2001, the Lira/Dollar Exchange Rate was Lit. 2,244 = U.S.$1.00, calculated as set forth above.

Telecom Italia intends to adopt the euro as its reporting currency for its financial statements beginning with fiscal year 2001.

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

Exchange Rates

The last stage of European Monetary Union, hereinafter referred to as EMU, with fixed exchange rates between national currencies and the euro started on January 1, 1999 in participating Member States, including Italy (but not including Greece which joined the last stage of EMU on January 1, 2001). Until January 1, 2002, national currencies of participating Member States, and the euro are both in use, although euro hard currency is not yet available. Participating national currencies will be removed from circulation between January 1, 2002 and February 28, 2002 and replaced by euro banknotes and coins. During the transition period through December 31, 2001, the euro will be available only in “paperless form”, pending the production and release of euro banknotes and coins, while the participating countries’ national currencies will be maintained as non-decimal subdivisions of the euro. The denomination of “legal instruments”, which are legislative and statutory provisions, acts of administration, judicial decisions, contracts, unilateral legal acts, payment instruments other than banknotes and coins, and other instruments with legal effect, is not modified by the introduction of the euro itself and payments originally designated in Italian lire on these instruments will continue to be made in Italian lire, unless otherwise agreed by the parties. As of January 1, 2002, all references to the participating countries’ national currencies contained in legal instruments and not redenominated during the transitional period will be references to the euro.

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

The following table sets forth, for the years 1996-1998, certain information regarding the Noon Buying Rate for the lira and, for 1999, 2000 and 2001, certain information regarding the Lira/Dollar Exchange Rate, using the Noon Buying Rate for euro multiplied by the Fixed Euro/Lira Exchange Rate, expressed in lira per U.S. dollar.

Calendar Period	High	Low	Average(1)	At Period End
1996	1,602	1,496	1,538	1,519
1997	1,841	1,516	1,712	1,769
1998	1,828	1,592	1,737	1,654
1999	1,923	1,639	1,828	1,923
2000	2,341	1,874	2,103	2,062
2001 (through June 15, 2001)	2,298	2,031	2,181	2,244
Monthly Amounts				
December 2000	2,212	2,062		
January 2001	2,109	2,031		
February 2001	2,138	2,061		
March 2001	2,202	2,073		
April 2001	2,197	2,144		
May 2001	2,290	2,167		
June 2001 (through June 15, 2001)	2,298	2,244		

(1) Average of the rates for the last business day of each month in the relevant period except for 2001 for which the date used is June 15, 2001.

Beginning January 4, 1999, the Shares and Savings Shares commenced trading on "Mercato telematico azionario" managed by Borsa Italiana S.p.A. ("Telematico"), 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 will be paid by Telecom Italia in Lit. until 2001 and in euro once the lira ceases to be legal tender in 2002, and exchange rate fluctuations will also 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 Lit. (before 2002) or in euro (2002 and after) on the underlying Telecom Italia Shares and Telecom Italia Savings Shares. See "Item 4. Information on the Company—Business—Recent Developments—Conversion of Savings Shares for Shares and Tender Offer for Shares" and "Item 10. Additional Information—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 for each of the five years in the period ended December 31, 2000 are extracted or derived from the consolidated financial statements of the Company, which have been audited by PricewaterhouseCoopers S.p.A. (only for the year ended December 31, 2000) and by Arthur Andersen S.p.A., independent auditors 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 June 12, 2001. The Group's Consolidated Financial Statements included herein have been approved by the Telecom Italia Board of Directors.

	Year ended December 31,									
	1996		1997(1)		1998(1)		1999(1)	2000(1)(3)		2000
	(in billions of Lit., except per share and per ADS amounts)									(in millions of U.S. dollars, except per share and per ADS amounts) (2)
Statement of Income Data:										
Operating revenues	42,080	(4)	44,990	(4)	48,507	(4)	52,481	55,979		25,424
Other income	762		891		1,085		998	826		375
Total revenues	42,842	(4)	45,881	(4)	49,592	(4)	53,479	56,805		25,799
Cost of materials	3,530		4,627		4,535		4,795	4,373		1,986
Salaries and social security contributions	9,902		9,744		9,665		9,636	9,729		4,419
Depreciation and amortization	10,742		11,311		10,480		10,338	10,933		4,965
Other external charges	12,678	(4)	14,146	(4)	17,552	(4)	18,561	20,893		9,489
Changes in inventories	108		(554)		262		(251)	(537)		(244)
Capitalized internal construction costs	(1,963)		(1,747)		(2,088)		(2,056)	(1,765)		(802)
Total operating expenses	34,997	(4)	37,527	(4)	40,406	(4)	41,023	43,626		19,813
Operating income	7,845		8,354		9,186	(4)	12,456	13,179		5,986
Interest income	1,257		1,002		1,579		1,073	1,636		743
Interest expense	(1,824)		(1,643)		(1,681)		(2,837)	(4,779)		(2,171)
Other income and expense, net	(398)		(942)		133	(4)	(981)	(415)		(188)
Income before income taxes	6,880		6,771		9,217		9,711	9,621		4,370
Income taxes	(3,720)		(3,323)		(3,965)		(5,046)	(3,912)		(1,777)
Net income	3,160		3,448		5,252		4,665	5,709		2,593
Minority interest	(1,428)		(839)		(1,422)		(1,301)	(1,782)		(809)
Net income, after minority interest	1,732		2,609		3,830		3,364	3,927		1,784
Net income per Share(5)	322		346		510		447	530		0.24
Net income per Share ADS(5)	3,220		3,460		5,100		4,470	5,300		2.41
Dividends per Share	130		190		280		603	605	(6)	0.27
Dividends per Savings Share	150		210		300		623	627	(6)	0.28

	Year ended December 31,					
	1996	1997(1)	1998(1)	1999(1)	2000(1)(3)	2000
	(in billions of Lit., except per share and per ADS amounts)					(in millions of U.S. dollars, except per share and per ADS amounts)(2)
Amounts in accordance with U.S. GAAP						
Total revenues	41,248 (4)	45,881 (4)	49,592 (4)	53,479	54,096	24,569
Operating income	8,240	8,605	9,026 (4)	11,913	(3,730)	(1,694)
Income before income taxes . . .	6,768	6,881	8,557	9,243	13,666	6,207
Net income from continuing operations, after minority interest	1,545	1,202	2,954	2,915	6,819	3,097
Income from operations of Discontinued Demerged Activities	90	—	—	—	—	—
Net income, after minority interest	1,635	1,202	2,954	2,915	6,819	3,097
Net income from continuing operations, after minority interest per Share — Basic(7)	287	185	392	387	916	0.42
Net income from continuing operations, after minority interest per Share ADS — Basic (7)	2,873	1,847	3,922	3,869	9,160	4.16
Net income per Share — Basic (7)	304	185	392	387	916	0.42
Net income per Share — Diluted (7)	310	185	392	387	913	0.42
Net income per Share ADS — Basic (7)	3,041	1,847	3,922	3,869	9,160	4.16
Net income per Share ADS — Diluted (7)	3,099	1,847	3,922	3,866	9,134	4.15

	As of December 31,					
	1996	1997(1)	1998(1)	1999(1)	2000(1)(3)	2000
	(in billions of Lit. except ratios and other data)					(in millions of U.S. dollars (2))
Balance Sheet Data						
Total current assets	21,965	22,890	23,595 (8)	24,685	31,745	14,418
Total fixed assets, net	47,663	47,615	45,665	45,518	45,358	20,601
Intangible assets, net	2,818	3,242	3,647	5,299	31,052	14,103
Total assets	75,741	81,583	86,880 (8)	89,181	126,854	57,614
Total short-term debt	3,558	7,310	9,341	9,622	29,307	13,311
Total current liabilities	23,573	29,087	32,656	33,784	53,212	24,168
Total long-term debt	12,891	11,993	10,839	10,002	16,010	7,271
Total liabilities	45,519	48,549	51,195 (8)	50,867	77,423	35,164
Total stockholders' equity before minority interest	17,478	29,911	31,651	33,004	36,443	16,551
Total stockholders' equity	30,222	33,034	35,685	38,314	49,431	22,450
Amounts in accordance with U.S. GAAP						
Total current assets	23,771	23,676	24,514	25,141	29,753	13,513
Total fixed assets, net	45,975	46,461	44,867	44,825	44,192	20,071
Intangible assets, net	4,208	10,330	10,247	11,412	46,633	21,179
Total assets	76,425	88,065	93,151	95,386	138,497	62,901
Total current liabilities	23,573	29,087	32,656	33,784	50,743	23,046
Total long-term debt	12,891	11,993	10,839	10,002	24,138	10,963
Total liabilities	45,676	48,994	52,102	52,101	86,837	39,439
Stockholders' equity (9)	18,267	35,955	37,069	38,065	37,018	16,813
Financial Ratios						
Gross operating margin (Gross operating profit/operating revenues)(%) (10)	48.0	47.5	47.2	45.1	45.4	45.4
Operating income/operating revenues (ROS) (%)	18.6	18.6	18.9	23.7	23.5	23.5
Return on equity (ROE) (%)	10.5	10.9	15.3	12.6	13.0	13.0
Return on investments (ROI) (%)	17.7	18.4	18.5	23.6	18.8	18.8
Net borrowings/Invested capital (debt ratio) (%)	28.5	31.7	30.7	29.1	42.7	42.7
Statistical Data:						
Subscriber fixed lines (thousands) (11)	25,259	25,698	25,986	26,502	27,153	
ISDN equivalent lines (thousands) (12)	341.3	896.8	1,735.3	3,048.9	4,583.5	
Mobile customers (thousands) (13)	5,700.3	9,278.0	14,299.0	18,527.0	21,601.2	
Subscriber fixed lines per full-time equivalent employee (14)	298	317	332	354	409	
Internet subscribers (thousands)		133.4	395.6	1,990.0	3,997.0	

(1) Statement of income data and balance sheet data for each of the years ended December 31, 1997, 1998, 1999 and 2000 are not comparable to 1996 due to the demerger of the Demerged Activities and the Merger. Amounts in accordance with U.S. GAAP for the years ended December 31, 1997, 1998, 1999 and 2000 are not fully comparable with 1996 due to the Merger.

(2) For the convenience of the reader, Italian lire amounts for 2000 have been translated into U.S. dollars using the Lira/Dollar Exchange Rate in effect on March 30, 2001 of Lit. 2,201.80 = U.S.$1.00.

(3) Beginning January 1, 2000, under Italian GAAP, the affiliated company Nortel Inversora and the operationally controlled Telecom Argentina group (Nortel Inversora group) have been consolidated using the proportional method. Under U.S. GAAP, the Nortel Inversora group is accounted for using the equity method. These differences in accounting treatment do not affect net income and stockholders' equity but have an impact on other line items, such as operating revenues and operating expenses, as well as a number of balance sheet line items.

(4) Beginning in 1999 Telecom Italia has changed the way in which it accounts 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 have been increased by the same amount: Lit. 1,558 billion, Lit. 2,174 billion and Lit. 3,042 billion in 1996, 1997 and 1998, respectively. This accounting change has had no impact on reported net income for 1996, 1997 and 1998. In 1998, the item "other external charges" also takes into account additional expenses (Lit. 19 billion) 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 Lit. 29 billion and Lit. 19 billion in 1996 and 1997, respectively.

(5) Net income per Share figures in 1996 have been calculated on the basis of 5,281,212,121 Shares and Savings Shares outstanding. 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. The increase in Shares and Savings Shares outstanding in 1997 is due to the issuance of new Shares and Savings Shares in connection with the Merger. The increase in Shares and Savings Shares outstanding in 1999 is due to the issuance of 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 of Lit. 1,000 per share, while for 2000, following the resolution of the extraordinary shareholders' meeting held on May 3, 2001 regarding the re-denomination of Telecom Italia share capital into euros, the calculations take into account the new par value per share of euro 0.55. Net income per Savings Share was Lit. 342, Lit. 366, Lit. 530, Lit. 467 and Lit. 552 in each of 1996, 1997, 1998, 1999 and 2000, respectively, and net income per Savings Share ADS was Lit. 3,420, Lit. 3,660, Lit. 5,300, Lit. 4,670 and Lit. 5,520 in each of 1996, 1997, 1998, 1999 and 2000, respectively.

(6) Approved at the Annual Meeting of Shareholders held on June 12, 2001. 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, 2000 were clipped on June 18, 2001, while Telecom Italia's dividends for the year ended December 31, 2000 were payable from June 21, 2001.

(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 5,281,212,121 for the year ended December 31, 1996, 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 and 7,398,247,829 for the year ended December 31, 2000. The calculations take into account the requirement that holders of Savings Shares are entitled to an additional dividend of Lit. 20 (based on 2 percent of Savings Share par value) over

dividends on Shares. This takes into account the par value of Lit. 1,000 per share as of December 31, 2000; following the resolution of the extraordinary shareholders' meeting held on May 3, 2001 regarding the re-denomination of Telecom Italia share capital into euros, the new par value per share is euro 0.55. In addition, in accordance with U.S. GAAP, net income per Savings Share — Basic from continuing operations, after minority interest, was, Lit. 307, Lit. 205, Lit. 412, Lit. 407 and Lit. 936 in 1996, 1997, 1998, 1999 and 2000, respectively, and net income per Savings Share ADS — Basic from continuing operations, after minority interest, was Lit. 3,073, Lit. 2,047, Lit. 4,122, Lit. 4,069 and Lit. 9,360 in 1996, 1997, 1998, 1999 and 2000, respectively. In accordance with U.S. GAAP, net income per Savings Share — Basic was Lit. 324, Lit. 205, Lit. 412, Lit. 407 and Lit. 936 in 1996, 1997, 1998, 1999 and 2000, respectively, and net income per Savings Share ADS — Basic was Lit. 3,241, Lit. 2,047, Lit. 4,122, Lit. 4,069 and Lit. 9,360 in 1996, 1997 1998, 1999 and 2000, 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 Lit. 221 billion, while total assets and liabilities were reduced by the same amount of Lit. 734 billion.

(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.

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

(12) Data exclude internal lines.

(13) Includes customers of TACS and GSM services, including holders of Prepaid Cards.

(14) Includes employees of the fixed telecommunications services segment only. Ratio for 1997, 1998, 1999 and 2000 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 total dividends and dividends per Share and per Savings Share paid by Telecom Italia with respect to each of the last five fiscal years are shown below.

	Dividends on Shares				Dividends on Savings Shares			
Year ended December 31,	**Lit. per Share**		**U.S. dollars per Share(1)**	**(in billions of Lit.)**	**Lit. per share**		**U.S. dollars per share (1)**	**(in billions of Lit.)**
1996	130		0.077	498.00	150		0.089	217.03
1997	190		0.11	998.48	210		0.12	454.89
1998	280		0.15	1,471.44	300		0.17	649.84
1999	600	(2)	0.29	3,171.80	623	(2)	0.30	1,333.27
2000	605	(3)	0.27	3,183.10	627	(3)	0.28	1,287.31

(1) Italian Lire amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on the respective payment dates. See "Item 3. Rates of Exchange".

(2) 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 Lit. 6.05 billion was also distributed from the statutory reserve in order to round up such per share amounts.

(3) Approved at the Annual Meeting of Shareholders held on June 12, 2001. 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 business days after the Annual Meeting of Shareholders approving the dividends. Telecom Italia's dividend coupons for the year ended December 31, 2000 were clipped on June 18, 2001, while Telecom Italia's dividends for the year ended December 31, 2000 were payable from June 21, 2001.

Cash dividends will be paid by the Company in Lire until the lira ceases to be legal tender. Once the lira ceases to be legal tender, cash dividends will be paid in euro.

Payment of annual dividends is subject to approval by the shareholders 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 By-laws 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 held with 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 By Laws and Capital Stock".

Arrangements between Euroclear or Clearstream and Monte Titoli S.p.A ("Monte Titoli") permit the shareholders to collect the dividends through Euroclear or Clearstream. Holders of 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 — Description of By Laws and Capital Stock—Taxation". Italian regulations do not contain any specific restrictions on the payment of dividends to non-residents of Italy. See "Item 10. Additional Information — Description of By Laws and Capital Stock—Exchange Controls and Other Limitations Affecting Security Holders".

Pursuant to Italian law, in connection with the payment of dividends, participants of Monte Titoli S.p.A. ("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 exercised the option to receive dividends without 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 — Description of By Laws and Capital Stock—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 (comprising of an Italian public offering and an International and U.S. public offering, collectively, the "Global Offering"), and a private sale to a stable group of shareholders. On February 20, 1999 Olivetti S.p.A. ("Olivetti") announced that it intended to launch a tender offer for all Telecom Italia Shares, which offer commenced on April 30, 1999. On May 21, 1999 Olivetti obtained control of Telecom Italia when approximately 52.12% of Telecom Italia Shares were tendered to Olivetti. As of June 16, 2001 Olivetti owns 54.96% of Telecom Italia Shares. See "— Recent Developments".

The registered offices of Telecom Italia are at Via Bertola 34, 10122 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 2660.

Introduction

At the end of 2000, Telecom Italia was one of the world's largest fixed telecommunications operators, with approximately 27 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 45 million mobile customers (which includes 28.3 million equity customers). 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, as of June 15, 2001, one of four operators with the right to provide DCS 1800 digital mobile telecommunications services. TIM is one of five entities who 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 active mainly in Spain, France, Austria, Greece, Turkey and various countries in Latin America.

Significant Developments during 2000

Completion of SEAT — Tin.it Transaction

The SEAT/Tin.it transaction was completed in November 2000 with the completion of the demerger by way of transfer to SEAT of 8.168% of the share capital of Tin.it owned by Telecom Italia and the subsequent merger of Tin.it with SEAT. In connection with the demerger and merger, SEAT ordinary shares were issued to Telecom Italia and Telecom Italia shareholders. See "Item 5. Operating and Financial Review and Prospects—Consolidated Financial Statements as of and for the Year Ended December 31, 2000—Reconciliation of Italian GAAP to U.S. GAAP" and Notes 26, 27 and 28 of Notes to the Group's consolidated financial statements included elsewhere herein for a discussion of the U.S. GAAP impact of the SEAT/Tin.it transaction. See also "Item 8—U.S. GAAP

Unaudited Pro Forma Condensed Consolidated Statement of Income of Telecom Italia for the year ended December 31, 2000." The combined SEAT/Tin.it company is the largest internet services provider in Italy and has one of Italy's most frequently visited portals and an integrated business-to-business platform. Currently, Telecom Italia owns, directly and indirectly, approximately 60% of SEAT's ordinary share capital. See "— Internet and Media" for more information on SEAT .

SEAT Put Option

On December 5, 2000, Telecom Italia announced that it had reached an agreement with the Chase Manhattan group and Huit II, pursuant to which a company of the Chase Manhattan group 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 a price of euro 4.20 per share. The put option was granted to 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.

Chase Manhattan and Telecom Italia also agreed to extend the put option until December 2005, except that Chase Manhattan may exercise it sooner, in April and May of 2003, 2004 or 2005. The Telecom Italia group also purchased a call option on over 660 million SEAT ordinary shares under the same terms and conditions as the put option with a premium payment of approximately euro 747 million. See "Item 5. Operating and Financial Review and Prospects—Consolidated Financial Statements as of and for the Year Ended December 31, 2000 — Reconciliation of Italian GAAP to U.S. GAAP" and Notes 26, 27 and 28 of Notes to Consolidated Financial Statements included elsewhere herein.

Non-Core Assets Disposal Program

On September 1, 1999 the board of directors of Telecom Italia approved the guidelines for a restructuring plan of certain group assets. This plan intended to rationalize the Group's structure and portfolio with the intention to divest non-strategic holdings, including Italtel (the manufacturing business), Sirti (the installation business), Meie Group (insurance), Teleleasing (leasing services) and part of the Group's real estate assets.

Italtel. As part of its non-core assets disposal plan, 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. Total consideration received by Telecom Italia was Lit. 1,668 billion.

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. Telecom Italia and Sogerim are not involved in the management of Italtel. They have the right to appoint two directors of the Italtel board of directors, which consists of 13 directors.

Italtel is the main Italian manufacturer of telecommunications equipment and until 1999 was a 100% owned subsidiary of Telsi Ltd, a fifty-fifty joint venture of Telecom Italia and Siemens A.G. In 1999 Telecom Italia and Siemens decided to terminate the joint venture by splitting the company in two parts. As a consequence of this decision, in December 1999 Italtel sold to Siemens Beteiligungsverwaltung 100% of Siemens Information and Communication Networks S.p.A., the company which assumed after November 1, 1999 Italtel's activities relating to mobile networks and transmission systems equipment. At that time Telecom Italia acquired the remaining 50% of Telsi, and through Telsi, controlled 100% of Italtel until December 6, 2000.

Sirti. On November 8, 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 Lit. 314 billion for its stake.

Meie Group. 51.2% of Meie Assicurazioni and 51% of Meie Vita was sold to Unipol Assicurazioni S.p.A. for Lit. 670 billion in June 2000.

Teleleasing. 60% of Teleleasing was sold to the Mediobanca Group for approximately Lit. 57 billion in June 2000.

Real Estate Assets. An important element of Telecom Italia's restructuring plan was to realize value on its extensive real estate portfolio. On November 23, 2000, Telecom Italia announced that it had 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. Pursuant to the agreement with Beni Stabili and Lehman Brothers, Telecom Italia sold to its two partners 60% of IM.SER S.p.A., a joint stock company formed by Telecom Italia to hold a portion of its real estate assets. As a result Beni Stabili acquired a 45% interest of IM.SER and Lehman Brothers acquired 15%. On May 16, 2001 Beni Stabili exercised an option to buy the Lehman Brothers' stake in IM.SER. Currently Beni Stabili has a 60% stake in IM.SER and Telecom Italia has a 40% stake.

The real estate portfolio held by IM.SER consisted of 581 properties, totaling 3.7 million square meters, divided into:

- 386 properties ("Real Estate Investment Portfolio"), totaling approximately 2.4 million square meters, located throughout Italy, mainly in the regions of Lombardia (20%), Lazio (14%) and Piemonte (11%). All the properties, including buildings that contain telecommunications equipment, will be leased to Telecom Italia under-long term lease contracts (21 plus 6 years) at market rates; and

- 195 properties ("Real Estate Trading Portfolio"), totaling approximately 1.3 million square meters, located throughout Italy, mainly in the regions of Lazio (19%), Lombardia (16%), Campania (8%) and Piemonte (8%). 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. Such early termination clauses will allow Telecom Italia to vacate approximately 1,000 properties in the next five years.

As a result of the transaction, Telecom Italia received approximately Lit. 5,228 billion in cash.

In May of 2001, IM.SER contributed its Real Estate Trading Portfolio to Telemaco Immobiliare S.p.A. ("Telemaco"), a newly formed company. Following such contribution, IM.SER distributed the shares of Telemaco, to its shareholders. The shareholders of Telemaco are Beni Stabili with a 45% stake, Telecom Italia with a 40% stake and Lehman Brothers with a 15% stake.

Recent Developments

Conversion of TIM's Savings Shares

In December 2000, TIM successfully completed the conversion of its savings shares into ordinary shares. The exchange offer, which required savings shareholders to exchange one savings share plus cash of €3.70 per share, for each TIM ordinary share, resulted in TIM raising €5.3 billion in cash proceeds from the conversion. Holders of 91.56% of the savings shares participated in the conversion. Before the conversion, the savings shares represented 19.06% of the outstanding share capital and following the conversion the savings shares now represent 1.54% of the outstanding share capital. The proceeds from the savings share conversion were primarily used to fund the acquisition of TIM's UMTS license in Italy and for further international expansion.

Conversion of SEAT Savings Shares into SEAT Ordinary Shares

The conversion of SEAT savings shares into ordinary shares, which required holders of savings shares to exchange one savings share plus euro 0.89 for each ordinary share, was formally approved in October 2000, and was completed in December 2000. On completion of the conversion, savings shares now represent only 1.7% of SEAT share capital. As a result of the conversion, SEAT received cash proceeds of €1.122 billion.

Conversion of Savings Shares for Shares and Tender Offer for Shares

On February 5 and 16, 2001, and March 31, 2001, the Board of Directors of Telecom Italia approved a project contemplating the voluntary conversion (the "Conversion") of the Savings Shares in exchange for an equivalent number of Shares plus the cash payment of a Conversion premium per share and the subsequent public tender offer, for Shares (the "Tender Offer") for up to a maximum of 10% of the total outstanding share capital after such voluntary conversion. The Conversion and Tender Offer will be neutral for Telecom Italia from a financial point of view since the proceeds from the Conversion will be used to finance the Tender Offer. If the proceeds from the Conversion exceed the cost of the Tender Offer, the Company intends to distribute the amount of excess proceeds to the shareholders in the form of an extraordinary dividend paid out of distributable reserves. An extraordinary and ordinary shareholders' meeting held on May 3, 2001, approved the Board of Directors' proposal relating to the Conversion and the Tender Offer. The Board of Directors has been granted full authority to decide when to launch the offer for the Conversion (the "Conversion Offer"), with a deadline of December 31, 2001.

The price per Share for the Tender Offer will be equal to the average of the official prices for Shares on Telematico, in a period immediately preceding the date of the Board of Directors meeting that will decide the commencement of the Tender Offer, increased by a premium, but not greater than 25% of the average of such official prices.

Neither the Conversion Offer nor the Tender Offer is currently being made, directly or indirectly in, or by use of the mails of, or by any means or instrumentality of interstate or foreign commerce, or any facilities of a national securities exchange of, the United States of America or any other country where an offer may not be made absent registration or an exemption from registration (together, these other countries, the "Other Countries"). This includes, but is not limited to facsimile transmission, electronic mail, telex, telephone and the internet. Any purported acceptance of the Conversion Offer or the Tender Offer resulting directly or indirectly from a violation of these restrictions will be invalid. Securities may not be offered or sold in the United States of America absent registration or an exemption from registration. The Shares which could be issued pursuant to the Conversion Offer have not been registered under the U.S. Securities Act of 1933, and may not be offered, sold or delivered in the United States of America, absent registration or an exemption from registration.

Group Results for the First Quarter Ended March 31, 2001.

On May 11, 2001 Telecom Italia announced its consolidated results of operations and financial condition for the first quarter ended March 31, 2001 on an Italian GAAP basis. The information in this section should be read in conjunction with Telecom Italia's consolidated financial statements and the notes thereto, included in this Annual Report on Form 20-F for the fiscal year ended December 31, 2000. Results for the three months ended March 31, 2001 are not necessarily indicative of results that may be expected for the entire year.

Consolidated net income after minority interest for the three months ended March 31, 2001 was Lit. 748 billion (Lit. 1,118 billion less minority interest of Lit. 370 billion), a decrease of Lit. 414 billion or 35.6% compared to the three months ended March 31, 2000. This decrease was due largely to increases in goodwill amortization, losses on investments (in particular, Stream, Auna and IS TIM) and higher interest expense.

The consolidated financial results for the first quarter 2001 are not directly comparable to the first quarter of 2000 due to changes in the scope of consolidation which occurred at the end of 2000 and in the first quarter of 2001. In the first quarter, 2001, the Entel Chile group, the Consodata group and the new mobile Brazil subsidiaries (Tim do Brazil, Blucel, Starcel and Unicel) have been consolidated.

Prior to January 1, 2001, Entel Chile group was accounted for under the equity method. The Consodata group was acquired by SEAT in the first quarter 2001. In addition, during the second half of 2000, Telecom Italia completed its acquisitions of SEAT, Jet Multimedia and the Maxitel groups which are now fully consolidated but were not included in the first quarter 2000. In addition, during 2000, Telecom Italia sold its interests in SIRTI and Italtel, so they are included in Telecom Italia's results for the first quarter 2000 but not included in the first quarter 2001.

Telecom Italia's consolidated operating revenues for the three months ended March 31, 2001 were Lit. 14,622 billion, an increase of 7.3% compared to the same period in 2000. This growth was primarily due to the positive performance of the mobile services (TIM group) and significant changes in the scope of consolidation. As of March 31, 2001, Telecom Italia had approximately 27.3 million subscriber fixed lines, including ISDN equivalent lines (a slight increase over the 27.2 million as of December 31, 2000), and TIM had 22.0 million mobile customers compared with 21.6 million and 19.2 million mobile customers as of December 31 and March 31, 2000, respectively.

Telecom Italia's consolidated gross operating profit (as defined in "Item 5—Operating and Financial Review and Prospects—Result of Operations—Gross Operating Profit") increased by 4.7% to Lit. 6,798 billion in the three months ended March 31, 2001 compared to Lit. 6,491 billion in the three months ended March 31, 2000. This growth was substantially attributable to the inclusion of Entel Chile group and the good performance of mobile services, only partly offset by the decrease in gross operating profit at Telecom Italia. Gross operating margin (gross operating profit as percentage of operating revenues) was 46.5% in the three months ended March 31, 2001, compared to 47.6% in the three months ended March 31, 2000.

Telecom Italia's consolidated operating income decreased by 3.6% to Lit. 3,476 billion in the three months ended March 31, 2001 compared to Lit. 3,604 billion in the three months ended March 31, 2000. The decline in operating income was largely due to the increase in depreciation and amortization from Lit. 2,650 billion for the three months ended March 31, 2000 to Lit. 3,137 billion for the three months ended March 31, 2001, an 18.3% increase. Such increase was due to the significant increase in goodwill recorded in the last quarter of 2000 attributable to the acquisition of SEAT and other international investments as well as the inclusion in the scope of consolidation of new subsidiaries (SEAT and certain international companies which were consolidated for the first time in the income statement in the first quarter 2001). Before the goodwill amortization, operating income would have increased by 7.7%.

Consolidated net income before minority interest decreased by 30.1% to Lit. 1,118 billion in the three months ended March 31, 2001 from Lit. 1,599 billion in the three months ended March 31, 2000. Consolidated net income after minority interest, decreased by 35.6% to Lit. 748 billion in the three months ended March 31, 2001 compared to Lit. 1,162 billion in the three months ended March 31, 2000.

Consolidated net income before minority interest was reduced by goodwill amortization of Lit. 638 billion (of which Lit. 587 billion related to Telecom Italia interest), recorded in depreciation and amortization (Lit. 484 billion) and in interest expense (Lit. 154 billion as it relates to investments made and accounted for on an equity basis), which increased by Lit. 477 billion compared to the same period in 2000.

Excluding such effects, net income after minority interest for the period would have been Lit. 1,335 billion, compared to Lit. 1,298 billion in the first quarter of 2000.

In the first three months of 2001, cash flow from operating activities was lower than total capital expenditures and financial investments (Lit. 9,278 billion); as a result, consolidated net financial indebtedness increased from Lit. 36,845 billion as of December 31, 2000 to Lit. 43,391 billion as of March 31, 2001. This increase was principally due to the acquisition of the controlling interest in Entel Chile and the related consolidation, as well as to the international investments made in Brazil and Turkey.

At March 31, 2001, the Telecom Italia group had 119,659 employees, an increase of 4,990 compared to December 31, 2000. This increase is primarily due to the inclusion of Entel Chile in the consolidation (4,638 employees).

Business Units

The following discussion relates to the Group's principal Business Units as they were reorganized at the beginning of 2001 (see "Item 5—Operating and Financial Review and Prospects—Results of Operations — General" for further information). The Company intends to report its business segments on this basis going forward. The discussion relating to TIM gives pro forma effect to the international restructuring placing SMH (international mobile operations) under TIM as if such reorganization occurred on January 1, 2000.

Domestic Wireline. This business unit includes Telecom Italia Wireline services (TIWS) which relates to the Italian domestic fixed line voice and data businesses on the fixed network and national call centers, as well as certain international activities relating to developing networks such as the Mediterranean and Latin American fiber optic rings as well as TMI. The developing networks and TMI were contributed to TIWS as of April 1, 2001. The change between TIWS and the previous segment, Wireline Telecommunications Services Italy, is de minimis.

Mobile. This business unit includes all national and international mobile telecommunications businesses which are now 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 SMH and TIM International.

Internet and Media. This business unit includes the SEAT Group which is consolidated with the Telecom Italia Group in results of operations for the first time in the first quarter 2001. SEAT manages the Group's internet and media business which arose from the merger of Tin.it and SEAT at the end of last year. 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. The international business unit, which previously consisted of substantially all of the international operations, including international mobile operations, now manages and develops international fixed line and certain integrated companies providing fixed-mobile services as well as overseeing the Group's international strategy and activities by coordinating acquisitions and alliances.

Other. The Group's remaining Business Units include IT Telecom Italia, Satellite Services and TI Lab. These business units are largely unchanged from the previous business segments. TI Lab now represents the consolidation of CSELT and the Group's Venture Capital and Innovation unit

Telecom Italia Wireline Services (TIWS)

TIWS gross operating revenues for the three months ended March 31, 2001 were Lit. 7,565 billion, a decrease of 5.8% compared to Lit. 8,033 billion for the three months ended March 31, 2000. The decline is primarily attributable to reduction in average call prices, equivalent to a loss in revenues of almost Lit. 1,000 billion.

Despite the revenue decline, gross operating profit increased by approximately 8% compared to the last quarter of 2000, and by approximately 6% compared to the quarterly average for all of 2000. Compared with the first quarter of 2000, however, gross operating profit increased by only 0.5%. The first quarter 2000 benefitted from higher fixed-mobile tariffs as price reductions were imposed by the National Regulatory Agency in beginning February 17, 2000, and were achieved in a less competitive market scenario.

TIWS improved gross operating profit despite the considerable reduction during the first quarter of 2001 compared to the same period in 2000 in average per-minute prices for voice call traffic in the retail market (a reduction of 23%). This was partially offset:

- by a significant increase in wireline traffic volumes (an increase of 8%) and data transmission (an increase of 9%).

- by major cost reductions (a reduction of Lit. 486 billion) exceeding 11%.

The gross operating margin improved by 3 percentage points, from 45.3% in the first quarter of 2000 to 48.3% in the first quarter of 2001.

Due in part to the success of Telecom Italia's Teleconomy offering (various flat rate tariff programs), which more than 2.8 million customers had subscribed to by April, overall market share at the end of March 2001 was equal to 86%.

Telecom Italia Mobile

TIM group gross operating revenues were Lit. 4,640 billion, a 9.6% increase over pro forma gross operating revenues of Lit. 4,235 billion for the same period in 2000. This increase is principally due to continuing growth at TIM and the change of the scope of consolidation.

Consolidated gross operating profit increased by 10.7% to Lit 2,279 billion in the first quarter of 2001 from Lit. 2,058 billion in the first quarter of 2000. The gross operating margin continued to rise significantly, reaching 49.1% for the first quarter 2001 against 48.6% in the first quarter of 2000. Such increases were mainly attributable to the rationalization and containment of operating costs at TIM which grew more slowly than operating revenues.

At the end of March 2001, the TIM group had a total of more than 43.6 million customers (including 28 million equity customers), not including Telecom Italia Group wireless lines, an increase of more than 2.6 million on the end of 2000.

TIM (parent company) operating revenues in the first quarter of 2001 were Lit. 3,772 billion, an increase of 6.5% over the first quarter of 2000. Revenues from services increased 10.6%. The impact of lower prices was more than offset by greater traffic in minute terms (an increase of 19.3%). During the first quarter of 2001, TIM confirmed its leadership in the value added services (VAS) market, where revenues grew by 70.5% to account for approximately 6.8% of traffic revenues (4.4% in the first quarter of 2000).

TIM gross operating profit was Lit. 2,010 billion, up 13.5%, while gross operating margin reached 53.3%.

SEAT

SEAT was consolidated with Telecom Italia's results of operations for the first time in the three months ended March 31, 2001. SEAT's first quarter 2001 results were affected by the highly seasonal nature of its business (mainly due to the time table for the publication of directories).

In the first quarter of 2001, gross operating revenues were Lit. 564.5 billion, an increase of 122% over the first quarter 2000, owing principally to new acquisitions.

Gross operating profit in the first quarter 2001 amounted to Lit. 43.3 billion, down 13.7% with respect to the first quarter 2000.

Income before income taxes for the first quarter showed a loss of Lit. 132.9 billion. Such result was affected by goodwill amortization of Lit. 71 billion relating to significant acquisitions made by SEAT during the last half of 2000.

Gross operating profit for the Group's internet service provider improved from a loss of Lit. 59 billion in the fourth quarter of 2000 to a loss of Lit.16 billion in the first quarter of 2001. At the end of March 2001 SEAT had 4.4 million Internet users, of whom 1.75 million remained active after 45 days. Average connection time increased by 40% compared to the first quarter of 2000.

International Operations

International Operations (business segment of Telecom Italia, TMI, SIN) is responsible for managing international wireline subsidiaries as well as certain integrated wireless/wireline operators and developing the business of international networks for wholesale customers. Starting from April 1, 2001, "Mediterranean Nautilus", "Latin American Nautilus" and "Pan-European Backbone" projects and TMI have been attributed to "Wireline Services".

Gross operating revenues in the first quarter of 2001 from the International Operations Business Unit increased by 43.3% to Lit. 2,443 billion from Lit 1,705 billion in the first quarter 2000. The increase was principally a result of the inclusion in consolidation of different entities compared to the first quarter of 2000.

Gross operating profit was Lit. 715 billion in the first quarter 2001, an increase of 17.6% from Lit. 608 billion in the first quarter 2000. A significant contribution to this result was due to the improved performance of Entel Chile, which was consolidated for the first time in the first quarter of 2001.

Other Group activities

IT Telecom Italia, the Information Technology Business Unit, had gross operating revenues of Lit. 770 billion in the first quarter of 2001 compared to Lit. 813 billion in the first quarter 2000, a 5.3% decline. IT Telecom Italia's gross operating profit was essentially flat at Lit. 136 billion, despite the above mentioned reduction in revenues.

The Satellite Services Business Unit reported gross operating revenues of Lit. 126 billion in the first quarter of 2001, Lit. 4 billion or 3.1% down from the first quarter 2000 principally due to operations under the auspices of the Astrolink space consortium. This strongly affected gross operating profit which amounted to Lit. 9 billion, and the net loss which amounted to Lit. 9 billion.

TI Lab, the Group's innovation and research Business Unit, had gross operating revenues of Lit. 43 billion, with a negative gross operating profit of Lit. 16 billion and a net loss of Lit. 25 billion.

Summary of Memoranda Released by the Board of Statutory Auditors and by the Board of Directors of Telecom Italia at the Shareholders Meeting of June 12, 2001

Following specific requests by Consob on June 6, 2001 the Board of Statutory Auditors and the Board of Directors of the Company released to the shareholders meeting held on June 12, 2001, two memoranda regarding certain transactions engaged in by the Company and which also had been the subject of comment by the national and international press.

Such memoranda were read in their entirety at the shareholders meeting before the beginning of the discussion of the meeting's agenda. Copies of such memoranda were distributed to the shareholders attending the meeting, to press agencies and published on the Company's web site. An English translation of these memos will be filed with the SEC on a Form 6K as well as published on the Company's web site.

The following is a short summary of the two memoranda. Such summary has neither been prepared nor approved either by the Board of Statutory Auditors or by the Board of Directors, respectively, and therefore must not be considered as an amendment or supplement to the above mentioned documents. Readers are encouraged to refer to the original memos in their entirety.

Memorandum released by the Board of Statutory Auditors

Consob requested the Board of Statutory Auditors to prepare a memorandum on the following:

(A) purchase by SIN, in 1997, of a 29% stake in the ordinary capital of Telekom Srbija ("TS");

(B) SEAT/Tin.it transaction; conflict of interest on the part of Chairman and Chief Executive Officer Roberto Colaninno and Director Emilio Gnutti with regard to the purchase of SEAT shares;

(C) SEAT/Tin.it transaction; compensation package in favor of the Chief Executive Officer of SEAT (the "SEAT CEO");

(D) Other Transactions:

- (i) purchase of TIM shares;
- (ii) agreements entered into with JP Morgan to back up the purchase of Telegate by SEAT in particular through a contract for differences in favor of JP Morgan from Telecom Italia;

(iii) purchase of holdings in Globo.com and Jet Multimedia;

(E) managerial delegation, decision-making structures and internal auditing.

Following Consob's request, the Board of Statutory Auditors prepared a detailed report based on its own investigations and other information previously provided to Consob, correlating them to the report prepared pursuant to Article 153 of Legislative Decree 58/1998. In performing its work the Board of Statutory Auditors had available to it the resources of the Company and interviewed relevant Company officers.

The conclusions set forth in the report of the Board of Statutory Auditors can be summarised as follows:

(A) ***Purchase of a 29% stake in Telekom Srbija*****.** The report considered in detail the events and transactions which led to SIN's investment in Telekom Srbija. After considering such matters the Board of Statutory Auditors found that:

- the methods utilized to transfer the funds for the purchase of the 29% stake in Telekom Srbija were not different than those applied at the time by the Group in similar transactions;
- the valuation methodology used by UBS, which was mandated to provide financial advice and services in respect of the advisability of purchasing a strategic shareholding in Telekom Srbija, were consistent with the traditional valuation practice; the value resulting from the range calculated by UBS took into account a majority premium payable by a strategic investor;
- no events or circumstances have emerged such as to invalidate the accuracy of the financial statements of the Company for the years 1997, 1998, 1999 and, consequently, 2000; and
- at the time of issuing the report, the Board of Statutory Auditors was not aware of risks that may give rise to potential liabilities in the shareholding in Telekom Srbija nor was there evidence indicating that other initiatives should be adopted other than the continuous monitoring of the relevant developments;

(B) ***Potential Conflict of Interest***. With respect to a potential conflict of interest on the part of the Chairman and Chief Executive Officer Roberto Colaninno and Director Emilio Gnutti relating to the purchase of SEAT shares by Telecom Italia in connection with the SEAT/Tin.it transaction deriving from their indirect shareholding in one of the participating companies, the Board of Statutory Auditors acknowledged that such purchase originated from a contract, the effectiveness of which was subject to the approval by the Board of Directors of Telecom Italia, which approval was effectively given in the Board meeting held on March 15, 2000 after Chairman Colaninno and Director Gnutti informed the Board about their theoretical conflict of interest and abstained pursuant to Article 2391 of the Italian Civil Code;

(C) ***Compensation package of SEAT CEO***. The complex contractual structure relating to the granting of a compensation package to the SEAT CEO resulted in the Board of Statutory Auditors concluding that two interpretations were possible: (i) that the cost pertaining to such grant should have been borne by Huit shareholders (a company which indirectly controlled SEAT and in which Telecom Italia was a minority shareholder) other than Telecom Italia, or (ii) that Telecom Italia, based on agreements in place prior to March 15, 2000, had undertaken to bear such cost in proportion to its shareholding in Huit. When considering this matter at a Board meeting on March 30, 2000, the Board of Directors, also due to the complexity, requested that an independent legal opinion be obtained. As of the date of its report, the Board of Statutory Auditors reserved its right to reach a conclusion until it received the requested legal opinion. Such opinion was thereafter rendered by Prof. Piergaetano Marchetti and confirmed the correctness of the procedure followed by Telecom Italia in which it bore the cost of such compensation package in proportion to its shareholding in Huit, as illustrated by the Chairman during the Shareholders Meeting on June 12, 2001;

(D) Other Transactions

(i) ***Purchase of TIM shares***. In its report, the Board of Statutory Auditors noted that certain members of the Board of Directors had expressed reservations about the methods by which the TIM share purchases had been made and how the Board had been informed. The Board of Statutory Auditors suggested that the decision of recording financial instruments in the financial fixed assets should be taken, in accordance with best practice, in a period prior to the purchase and should be the outcome of a "*frame resolution*" which establishes the parameters for such purchases. The Board of Statutory Auditors also suggested reviewing the advisability of identifying a maximum period of time - for example the time elapsing between two successive meetings of the Board of Directors - for purposes of respecting the value limits for operations for which powers were conferred on the Chief Executive Officer.

After noting these recommendations, the Board of Statutory Auditors stated that all of the 88,192,000 TIM shares (ordinary and savings) purchased in the year 2000 were acquired on Telematico. In addition, except for 50 million ordinary shares which were recorded in the financial fixed assets in the financial statements for the year 2000 as they were purchased to reinforce the control in the ordinary share capital of TIM even in light of potential transactions involving an exchange of TIM shares, all of the remaining TIM shares were purchased in the ordinary trading activity and therefore included under the short term assets and valued at the lesser of the purchase cost and the market price at the end of the period. The Board of Statutory Auditors also noted that the purchase of 50 million ordinary shares and their recording in the financial fixed assets were resolved by the Board of Directors on August 10, 2000 and disclosed in the interim report for the six months ended June 20, 2000 and the nine months ended September 30, 2000 and the financial statements for the year 2000;

(ii) Telegate. The contract for differences was provided to support SEAT's acquisition of Telegate. Certain members of the Board of Directors questioned whether Telecom Italia should have entered into such agreement which resulted in the purchase of approximately 53 million SEAT ordinary shares at a price of € 4.861 per share on November 17, 2000, with a response that such undertaking should be considered in the overall context of Telecom Italia's acquisition of a controlling interest in SEAT. The Board of Statutory Auditors concluded that at the very least an interest of the Company is not to be excluded with reference to the transaction in question, and that in any case it should be considered in the wider context of the acquisition of control of Telegate by SEAT and, in its turn, of SEAT by Telecom Italia;

(iii) ***Globo.com and Jet Multimedia***. With regards to the acquisition of Globo.com, the Board of Statutory Auditors noted that the price paid for the transaction fell within the valuation range calculated during the negotiations for such acquisition and that such equity value was estimated on the basis of a business plan prepared using prudential assumptions. The Board of Statutory Auditors also stated that, basically, no elements were identified that led them to consider as "at risk" the company as a going concern, nor were factors likely to lead to a significant deterioration in the value of the asset. In addition, the financial statements of TI WEB SA, a company participating directly in Globo.com, were certified on March 7, 2001, by Arthur Andersen without qualifications, with only a request for information on the valuation of Globo.com in the financial statement closing on December 31, 2000 and that the financial statements of Globo.com were likewise certified, on January 31, 2001, by Arthur Andersen without qualifications.

With regards to the acquisition of Jet Multimedia, the Board of Statutory Auditors noted that the price offered was in the low range of the estimated equity value of the company and that such equity value was estimated on the basis of a business plan prepared using very prudential assumptions. The Board of Statutory auditors also stated that there is no evidence of features that might suggest that the Company is at risk as a going concern, nor of situations that might bring about a significant fall in its asset value and that, in addition, the financial statements of 9Télécom Réseau, Jet Multimedia's direct controlling company, were unconditionally certified by Arthur Andersen and Mazars & Guerard on March 13, 2001.

In any case, the Board of Statutory Auditors expressed its intention to carefully monitor the situation of both Globo.com and Jet Multimedia;

(E) ***Managerial delegation***. The Board of Statutory Auditors stated that the question of delegation of authority is now being concretely addressed by the Company. In keeping with the changes of its organizational system in the form of business units and corporate structures, Telecom Italia is currently reviewing the current system of existing delegations in conjunction with McKinsey. As far as Telecom Italia's internal control system is concerned, the Board of Statutory Auditors observed that such system appears to be adequate. The Internal Auditing staff has considered and adequately evaluated any potential risks and is performing its duties to a professional standard.

Memorandum released by the Board of Directors

Consob requested the Company to prepare a memorandum setting forth the following:

(a) the timing of the decision-making process relating to the SEAT/Tin.it transaction and the powers granted by the Board regarding this transaction;

(b) considerations regarding the methods followed by Chairman Colaninno to declare the existence of his own personal interests and those of Director Gnutti in the aforementioned transaction, since this happened only in the meeting of March 15, 2000 and not in previous ones, during the course of which the basic structure of the transaction had already been approved and the Board had granted specific powers to the Chairman in order to perfect the transaction;

(c) considerations about the Chairman's decision not to inform the Board of Directors and the Statutory Auditors about (i) the specific position of the SEAT Chief Executive Officer, Lorenzo Pellicioli, in the SEAT/Tin.it transaction and (ii) the benefit granted him on the occasion of such transaction;

(d) a chronological description of the various contracts from which Telecom Italia's obligation to attribute an "economic benefit" to the SEAT Chief Executive Officer derived;

(e) the reasons why the provisions of the agreement dated July 7, 1997 and the agreement dated March 8, 1998 (rectius: March 3, 1998), which referred to the aforementioned benefit, were not made public pursuant to art. 122 of Legislative Decree n. 58/1998;

(f) information - for the time being - about possible risks connected with the Telekom Srbija affair, which in the future could result in potential liabilities for the Company.

Abiding by this request, the following statements were made by the Board of Directors:

(a) the decision-making process relating to the SEAT/Tin.it transaction developed through three subsequent Telecom Italia Board of Directors meetings, which took place on February 17, on March 1 and on March 15, 2000. The first two discussed only preliminary issues including, giving a mandate to the Chairman and Chief Executive Officer to define appropriate terms and conditions, and approving a general scheme of the transaction, explicitly reserving that the Board would "finally resolve upon the matter" in a subsequent meeting.

The decision-making process reached the approval of the exact terms of the SEAT/Tin.it transaction in the Board of Directors meeting held on March 15, 2000, as described in the corresponding agreements, including the approval of the contract referring to the sale of SEAT shares from Huit II to Telecom Italia agreed prior to the meeting, which in the absence of such approval would be automatically terminated, thus losing any and all force between its parties;

(b) before the Board of Directors meeting called on March 15, 2000 resolved upon the SEAT/Tin.it transaction, the Chairman and Chief Excutive Officer declared his and Director Gnutti's theoretical conflict of interests, being indirect stakeholders in SEAT and adding they would abstain.

On its part, during such meeting, Telecom Italia's Board of Directors acknowledged the Chairman's and Director Gnutti's theoretical conflict, examined and appraised all relevant terms of the transactions (economic, financial and technical-legal) and then unanimously and unreservedly approved such terms, with the abstention of the Directors in conflict. On the basis of the facts illustrated above, the lawfulness and formal correctness of the Chairman's and Director Gnutti's conduct is clear and evident;

(c) the covenant concerning the economic benefit due to the SEAT Chief Executive Officer was not made the object of a specific review by Telecom Italia's Board of Directors because such benefit did not in any manner have any connection with the integration project ; on the contrary, it stemmed only from "previous agreements", which dated from the privatization of SEAT pursuant to which Telecom Italia agreed to become a shareholder of the company to which the shareholding in SEAT as well as the obligation to grant to Mr. Pellicioli such benefit were referring. In the end, the abovementioned benefit was not a specific advantage granted to Mr. Pellicioli as a result of the integration project, nor could it be discussed taking into account the undertaking already assumed. Therefore it was not necessary that it be the subject of a debate by the Board of Directors while approving the merger itself;

(d) the obligation of Telecom Italia to grant the SEAT Chief Executive Officer the economic benefits is totally unrelated to the SEAT/Tin.it transaction. This benefit originates from certain agreements, the fulfilment of which was compulsory for Otto (the predecessor of Huit, and subsequently for Huit) shareholders, and is justified by the value increase of the SEAT business, since it was conditional upon the achievement of performance targets related to the company and its shares.

Indeed, it is clear that the benefit granted to Mr. Pellicioli was the object of undertakings assumed since 1996, and its practical implementation in 2000, during the SEAT/Tin.it transaction, was not caused by nor dependent on this transaction, but just happened at the same time as (not the integration, that took place in November 2000, but) the sale from Huit II to Telecom Italia of the SEAT shares indirectly owned by the investors. And this circumstance, as described in the memo, was always provided for in the agreements dating from the time of the privatisation of SEAT;

(e) an abstract referring to the shareholding-related contents of the Joint Venture and Shareholders' Agreement dated July 7, 1997 was timely published, but it did not include a specific disclosure of the provision referring to the granting to the SEAT Chief Executive Officer of a "compensation package inclusive of stock option", because this covenant was not deemed to have a shareholding-related nature.

As for the agreement dated March 3, 1998, Telecom Italia had no duty to make a disclosure because Telecom Italia was not a party to the agreement.

Moreover, as far as Telecom Italia knows, the parties of such agreement, almost immediately after executing it, acknowledged that it was impossible to practically implement it and therefore started a parallel process aimed at re-negotiating it, which resulted, in fact, in the execution of the contract dated July 27, 2000, which was properly disclosed and deposited;

(f) with reference to the shareholding owned by Telecom Italia (through its subsidiary SIN) in Telecom Srbija, the Board of Directors confirms that, at present, situations possibly causing future potential liabilities have not been identified.

Corporate Governance Committee

The Board of Directors, which met on June 28, 2001, reinforced the Audit and Corporate Governance Committee of Board of Directors by nominating a third member, Professor Guido A. Ferrarini, Board member appointed by the Shareholders' Meeting on June 12, 2001. Professor Ferrarini will assume the Chairmanship of the Committee. The two other members of the Committee are, Mr Jeffrey Livingston, who represents the foreign investment funds, and Mr Gerard Worms.

Professor of Financial Law at Genoa University, Professor Ferrarini is one of the main experts in financial markets and corporate governance, he participated, among other things, in the writing of the Draghi Law and was corporate governance adviser to Borsa Italiana S.p.A. See “Item 6 — Directors, Senior Management and Employees”.

Securitization of Telephone Bill Receivables

Telecom Italia, on June 27, 2001, closed its first issue of Asset Backed Euronotes securitized by telephone bill receivables for a total value of euro 700 million through a Company controlled securitization vehicle.

The offering consisted of three tranches including euro 100 million at 18 months, euro 150 million at 3 years and euro 450 million at 5 years, issued at floating rates and awarded preliminary ratings of AAA/Aaa/AAA by Fitch, Moody’s and Standard and Poor’s, respectively.

The securitization involves a mechanism for the sale of existing receivables for services supplied to residential and business customers and top customers of Telecom Italia Wireline Services. It is also possible to include analogous receivables from the public administration system. In particular, this initial issue was based on the flow of receivables generated by residential customers.

The issue is part of a program worth a total of euro 2 billion. It falls within the framework of the plan for the medium-long term refinancing of the Telecom Italia debt.

Overview of the Group's Operating Revenues by Major Business Areas

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services. Since 1999 domestic telecommunications services are segmented as follows: fixed line services managed by Telecom Italia, mobile services conducted by TIM and satellite services provided by Telespazio.

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, STET International Netherlands N.V. ("SIN") and STET Mobile Holding N.V. ("SMH").

In late December 2000, Telecom Italia completed the reorganization of its international activities. As a result of the reorganization, Telecom Italia now owns 100% of SIN, the primary vehicle through which the Telecom Italia Group holds its international wireline investments and TIM owns 100% of SMH, the primary vehicle for international wireless investments.

The Group now has a significant presence in the internet media market through SEAT. For purposes of Italian GAAP the results of this segment will only be included in the consolidated statement of income beginning in 2001.

The Group is also present in information technology software and services provided by the companies FINSIEL, Netsiel, Telesoft and Sodalia. As of 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. The companies mentioned, together with the Information Technology function of Telecom Italia, make up the "Information Technology Services" Business Unit. In 2001, their activities will come under the control of Telecom Italia Information Technology, a company 100% owned by Telecom Italia, set up in the second half of 2000 with the aim of ensuring the coordination of the information technology activities distributed throughout the various companies.

The Group sold its manufacturing activities conducted by Italtel and the installation activities conducted by Sirti during 2000, although the results for Italtel and Sirti are included in the Group's consolidated results through September 30, 2000.

At the beginning of 2001 the Group reorganized its business segments. See "Recent Developments—Group Results for First Quarter Ended, March 31, 2001" and "Item 5. Operating and Financial Review and Prospects."

For information concerning the Group's principal capital expenditures and investments for 1998, 1999 and 2000 and the financing of such expenditures and investments see "Item 5. Operating and Financial Review and Prospects—Liquidity and Capital Resources." For information concerning certain investments and divestments during the past three years, see "—Significant Developments during 2000—Non-Core Assets Disposal Program" and "Item 5. Operating and Financial Review and Prospects—Results of Operations—Change in Scope of Consolidation."

The table below sets forth the gross operating and consolidated operating revenues of each major business area and the other activities of the Group (before the reorganization of the business segments at the beginning of 2001) for the last three years and the percentage contributed by such business areas to the Group's consolidated operating revenues:

	Year ended December 31,								
	1998(1)			1999(1)			2000(2)		
	Gross Operating Revenues (3)(4)	Consolidated Operating Revenues (4)(5)	% of Consolidated Operating Revenues	Gross Operating Revenues(3)	Consolidated Operating Revenues(5)	% of Consolidated Operating Revenues	Gross Operating Revenues(3)	Consolidated Operating Revenues (5)	% of Consolidated Operating Revenues
	(in billions of Lit., except percentages)								
Fixed line services Italy	36,292	31,080	64.1	35,856	30,953	59.0	33,723	29,419	52.6
Mobile services Italy	11,904	11,094	22.9	14,425	13,722	26.1	15,352	14,701	26.3
Satellite services	739	534	1.1	619	443	0.8	659	509	0.9
International telecommunications services	1,520	1,273	2.6	3,253	3,069	5.8	7,615	7,435	13.3
IT software and services	2,566	1,916	3.9	3,074	2,127	4.1	3,137	2,164	3.8
Manufacturing(6)	1,975	1,041	2.1	1,776	959	1.8	1,221	385	0.7
Installation(7)	2,165	1,220	2.5	1,501	837	1.6	1,165	772	1.4
Other activities	1,019	349	0.8	1,154	371	0.8	1,307	594	1.0
Total operating revenues	58,180	48,507	100.0	61,658	52,481	100.0	64,179	55,979	100.0

(1) 1998 and 1999 gross operating revenues and consolidated operating revenues of each major business area and other activities of the Group are restated and presented consistent with the presentation of 2000 gross operating revenues and consolidated operating revenues.

(2) Starting from January 1, 2000, under Italian GAAP the Nortel Inversora group has been consolidated using the proportional method. Prior to this year the Nortel Inversora group was accounted for on the equity method.

(3) 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).

(4) Beginning in 1999 Telecom Italia changed the way in which it accounts for revenues from telecommunications services, calculating such revenues gross of interconnection and service charges payable to other operators and service providers. As a result, the gross operating and consolidated operating revenues for the year ended December 31, 1998 have been reclassified. Due to this change, operating revenues from fixed line services Italy and other external charges have been increased by the same amount: Lit. 3,042 billion 1998. This accounting change has had no impact on reported net income for 1998.

(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. Until 1998 Italtel Group was proportionately consolidated at 50%.

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

	Year ended December 31,		
	1998	1999	2000
Subscription and Customers:			
Subscriber fixed lines at period-end (thousands)(1)	25,986	26,502	27,153
Subscriber fixed line growth (%)	1.1	2.0	2.5
Subscriber fixed lines per full-time equivalent employee at period-end(2)	332	354	409
ISDN equivalent lines at period-end (thousands)(3)	1,735	3,049	4,584
Mobile customers at period-end (thousands)(4)	14,299	18,527	21,601
Mobile customers growth per annum (%)	54.1	29.6	16.6
Average revenue per mobile customer per month (Lit.)(5)	77,600	67,600	59,100
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	25.0	32.5	37.5
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants)(%)	36.0	53.1	73.3
Internet subscribers(6)(thousands)	396	1,990	3,997
Traffic:			
Average minutes of use per fixed line subscriber during period(7)	4,259	4,313	4,753
Of which:			
Local traffic during period (in average minutes)(8)	2,628	2,782	3,234
Long distance traffic during period (domestic and international) (in average minutes)	1,631	1,531	1,519
Growth in international incoming and outgoing traffic in minutes(%)(9)	9.5	9.8	5.4
Total mobile outgoing traffic per month (in millions of minutes)	839	1,219	1,569

(1) Data includes multiple lines for ISDN and excludes internal lines.

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

(3) Data excludes internal lines.

(4) TIM only.

(5) Including Prepaid Customers' revenues and excluding equipment sales.

(6) Tin.it only.

(7) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks).

(8) Not including district traffic.

(9) 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.

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. Telecom Italia's international focus will be on Latin America, Europe, primarily Southern Europe and the Mediterranean Basin.

Wireline

The Group's wireline strategy will be driven by data/internet growth, aggressive cost cutting and minimizing market share loss on voice services. 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) and leverage opportunities to retain its client base by enhancing customer loyalty (through billing, CRM and customer contact);
- 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 types of 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 Internet, 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.

In order to accelerate the achievement of such strategic goals in the Internet market, Telecom Italia during 2000 acquired control of SEAT, which included merging Tin.it with SEAT.

The Organizational Structure

The Group's organizational model is based on the clear distinction between the Chairman's staff and the corporate and business activities.

The Chairman's staff includes:

- *General Secretariat*: supports the Chairman and Chief Executive Officer and co-ordinates the Office of the Chairman;
- *Strategy*: supports senior management in identifying and controlling the strategic operations and in evaluating and integrating the strategic plans of the Business Units;
- *Internal Auditing*: co-ordinates audit and risk control activities for the Group;

The Corporate Functions are responsible for directing, co-ordinating and controlling the Group. Such functions include:

- *Finance and Control*: guides, co-ordinates and controls the economic and financial activities and performance of the Group; it also co-ordinates the administrative service center and the real estate and services Business Unit;
- *Human Resources*: guides, co-ordinates and controls labor relations and personnel development activities of the Group and manages the strategic and corporate personnel;
- *Corporate and Legal Affairs*: supports senior management on legal and company matters and co-ordinates such activities within the Group;
- *Public and Regulatory Affairs*: manages and fosters the relations between the Group and national and international institutions (including in particular the National Regulatory Agency and the Antitrust Authority); and
- *Corporate Communication and Image*: defines and develops communication and image strategies and manages investor relations for the Group.

As of the beginning of 2001, the Group divided its businesses into seven Business Units. See "— Recent Developments—Group Results for First Quarter ended March 31, 2001" for a description of the Business Units.

Telecommunications Services

The table below sets forth gross operating revenues from telecommunications services for the years indicated in accordance with Telecom Italia's segment reporting prior to the reorganization into seven Business Units at the beginning of 2001.

	1998	1999	2000
Fixed line services Italy	36,292	35,856	33,723
Mobile services Italy	11,904	14,425	15,352
Satellite services	739	619	659
International telecommunications services	1,520	3,253	7,615

See "Recent Developments — Group Results for First Quarter Ended March 31, 2001" for a description of the Group's new business segments and "Item 5. Operating and Financial Review and Prospects."

Wireline Telecommunications Services Italy

Wireline telecommunications services are operated directly by the Company. This sector accounted for gross operating revenues of Lit. 33,723 billion in 2000, Lit. 35,856 billion in 1999 and Lit. 36,292 billion in 1998.

Subscribers. The table below sets forth, for the periods indicated, certain subscriber data for fixed telecommunications services.

	As of December 31,				
	1996	1997	1998	1999	2000
Subscriber fixed lines at period-end (thousands)(1)	25,259	25,698	25,986	26,502	27,153
Subscriber fixed line growth (%)(2)	1.7	1.7	1.1	2.0	2.5
Subscriber fixed lines per full-time equivalent employee at period-end(3)	298	317	332	354	409
ISDN equivalent lines at period-end (thousands)(4)	341	897	1,735	3,049	4,584

(1) Data include multiple lines for ISDN and excludes 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 for 1997, 1998, 1999 and 2000 are based on employees of the Company.

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

At December 31, 2000, Telecom Italia had approximately 27.2 million fixed subscriber lines, including approximately 19.3 million residential lines (including multiple lines for ISDN), approximately 7.5 million business lines (including multiple lines for ISDN), and approximately 294,000 public telephones lines (including ISDN equivalent lines). Italy has 47.1 subscriber lines per 100 inhabitants.

At December 31, 2000, Telecom Italia had approximately 4,584,000 ISDN equivalent lines with approximately 3,860,000 equivalent basic rate ISDN lines and approximately 724,000 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, 2000, Telecom Italia had approximately 115,000 broadband points of access with approximately 83,000 ASDL wholesale points of access and 32,000 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, 2000, 78.8% (an increase of 3.9% compared to 1999) 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 1 public telephone per square kilometer and approximately 5 public telephones for every 1000 inhabitants. As of the second half of the year, ISDN technology was introduced to more than 15% of public telephones in order to support the launch of innovative services (45,364 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 fixed telecommunications services.

	Year ended December 31,				
	1996	1997	1998	1999	2000
Average minutes of use per fixed line subscriber during period(1)	4,191	4,270	4,259	4,313	4,753
Of which:					
Local traffic during period (in average minutes)(2)	2,557	2,607	2,628	2,782	3,234
Long distance traffic during period (domestic and international) (in average minutes)	1,634	1,663	1,631	1,531	1,519

(1) Data include domestic fixed outgoing traffic and traffic from special services, such as audio text and operator assisted services.

(2) Data does not include district traffic.

Domestic Fees and Tariffs. Pursuant to Order 85/98 issued by the National Regulatory Agency on December 22, 1998, and Order 101/99 issued on June 25, 1999, on November 1, 1999 Telecom Italia introduced per second billing, with an initial fixed charge (the “call set up”). The price per call set up is Lit. 100 for local calls, Lit. 127 for long distance calls (fixed to mobile and fixed to fixed) and Lit. 500 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. The cost of local calls and same area code calls is distance-dependent. For local calls, there are price rebates on the standard pricing after 15 minutes. For domestic long distance calls, as of December 1, 1998, there are two tariffs according to the time of day and three tariff areas. 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.

The current tariff packages include targeted discount and customized programs, including the following tariff packages which were introduced during 2000 to replace old packages:

- 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”.

- In June 2000, we introduced “Teleconomy”, which consists of three flat fee programs, “24", “24 Aziende” and “No Stop”, in which either local and long-distance calls have a single price or, with “No Stop”, unlimited local and long distance calls may be made. In November 2000, “Teleconomy ADSL” was launched, which provides a fast internet connection also 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.

In addition to business tariff packages targeted at the corporate customer, Telecom Italia introduced a number of new programs designed to enhance the management and development of telecommunications systems, connectivity and security ("Business One", "Full Business Company", "Full Business Security" and "Dataw@n").

Pursuant to Order 10/99 issued by the National Regulatory Agency on March, 1999, and Order 338/99 of December, 1999, the charges for fixed to mobile calls from both Residential and Business users, were reduced by 12% and 29%, respectively. On January 12, 2000, the National Regulatory Agency approved the proposal of Telecom Italia relating to the charges for fixed to mobile calls.

Tariff Rebalancing

Telecom Italia commenced rebalancing its tariffs in 1991 and made various adjustments during the period up to 1997. In March 1997, the Ministry of Communications approved a progressive reduction in tariffs to be phased in by March 1, 1998. As a result of these adjustments the bimonthly subscription fee for residential and business customers increased in the aggregate by an average of approximately 20% and domestic long distance call charges were reduced by an average of approximately 11.7% as compared to the fee and tariff structure in effect prior to March 1, 1997. Local call charges were reduced by an average of approximately 3.0% by the elimination of the higher tariff for local calls with effect from March 1997. In March 1998, residential bimonthly subscription fees increased by 6.5%.

Since December 1998, the National Regulatory Agency has been responsible for tariff regulation. Effective January 6, 1999, it authorized reductions in long distance and international tariffs and also authorized increases in the bimonthly subscription fees which became effective on March 1, 1999. Residential bimonthly subscription fees increased by 3% while business bimonthly subscription fees increased by 4%; domestic long distance tariffs decreased by 6% and international long distance tariffs fell by 10%.

Additional tariff reductions, which became effective on August 1, 1999, for long distance calls (a decrease of 5.0%) and international calls (a decrease of 5.5%) were approved by the National Regulatory Agency in June 1999. At the same time, increases in bimonthly subscription fees (an increase of 7.1%) became effective on November 1, 1999. The same Order introduced a new tariff for District calls, which are calls between local areas within the same "area code". These calls were charged until October 31, 1999 as long distance calls and currently have the same tariffs as local calls. Local calls are calls made within the local areas of the districts. The new tariff resulted in a decrease for these charges of about 58%.

On July 28, 1999, the National Regulatory Agency issued Order 171/99 which introduced the price cap mechanism 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. In particular, a general price-cap was established for the basket of the public voice telephone service, equal to the RPI minus 4.5 percentage points, and specific sub-price cap for a basket of residential services (the RPI minus 2.5 percentage points), for installation fees and basic charges (the RPI plus 1 percentage point) and local telephone services (the RPI).

As of August 1, 2000 the basic monthly residential subscription charge was increased by 3.8% (from Lit. 18,000 to Lit. 18,700). On December 28, 2000 there was an additional 10% reduction of inter-district tariffs and a reduction of international prices. (See "International Tariff—Tariff Rebalancing"). On February 1, 2001, pursuant to resolution 847/00 of the National Regulatory Agency, which addressed suggestions of the European Union for the Italian Government, the basic monthly residential subscription charge was increased by 6% and 2.3% for residential and business customers, respectively, and charges for district and long distance calls were reduced by 24.4% and 8% (due to the introduction of weekend tariff), respectively. See “Regulation — Tariff and Pricing Policy — Pricing Policy and Telecom Italia’s Tariffs”.

Following the EU Commission infringement procedure against the Republic of Italy concerning the rebalancing of voice telephony tariffs, including subscription fees, installation fees, and charges for local, national and international calls, on December 11, 2000, the National Regulatory Agency issued an order revising the price cap formulas in effect for rental and installation fees, and charges for local, national and international calls (Resolution 847/00). 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(1)	-4.5%
Sub-price cap on overall expenditure of residential users	RPI	-2.5%
Sub-price on installation fees and monthly rentals	RPI	+6%
Sub-price cap on local call charges	RPI	+0%

(1) RPI = Retail Price Index

The change compared to the previous price cap formulas is 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 resulted in:

- an increase of up to 8.5% in Telecom Italia’s access service charges such as monthly subscription fees; and

- reductions of 9.8% in Telecom Italia’s domestic and international traffic charges, (an increase of 2.5% in RPI and a reduction of 2% in general price cap).

In October 2001, the National Regulatory Agency is expected to review the status of the tariff rebalancing process and the possible need for new adjustments to the price caps.

Please see also “Item 4. Information on the Company—Regulation—Tariff and Pricing Policy—Pricing Policy and Telecom Italia’s Tariffs—Tariff Rebalancing”.

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 1996.

	Year ended December 31,					Percentage change since
	1996	1997	1998	1999	2000	1996(1)
			(Lit.)			(%)
Connection fee	200,000	200,000	200,000	200,000	200,000	-
Bimonthly subscription fee: (2)						
Residential subscribers	26,100	30,600	32,600	36,000	37,400	+43.3
Business Subscribers	45,400	50,800	50,800	52,800	52,800	+16.3
Basic ISDN connection fee	400,000	200,000	200,000	200,000	200,000	-50.0
Basic ISDN bimonthly subscription fee:						
Residential subscribers	100,000	64,000	64,000	64,000	64,000	-36.0
Business Subscribers	100,000	100,000	100,000	100,000	100,000	-
Three minute local call:						
Standard	180	180	180	192	192	+6.7
Higher(3)	208	180	180	192	192	-7.7
Three minute call in the same 'District' at higher rate(4)(5)				254	254	-
Three minute domestic long distance call at higher rate(6):						
Region 1	528	432	432	432	432	-18.2
Region 2	780	699	699	699	699	-10.4
Region 3	1,190	1,143	1,143	924	787	-33.9
Region 4(7)	1,330	1,143	1,143	924	787	-40.8

(1) Data are not adjusted for inflation.

(2) In February 2001, the residential and business subscription fees increased to Lit. 39,600 and Lit. 54,000, respectively.

(3) 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 3 minute call, while leaving unchanged the overall spending of the customers.

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

(5) In February 2001, district rates for three minutes calls decreased by 24.4%.

(6) In February 2001, the week-end flat tariff (Lit. 277 for three minutes call) was introduced.

(7) 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				
	1996	**1997**	**1998**	**1999**	**2000**
Total outgoing traffic (millions of minutes)	2,028	2,209	2,339	2,390	2,706
Growth in outgoing traffic (%)(1)	10.28	8.93	5.89	2.18	13.2
Total incoming traffic (millions of minutes)	2,349	2,619	2,950	3,419	3,415
Growth in incoming traffic (%)(1)	13.53	11.49	12.64	15.90	-0.1

(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 1996 to 2000 has resulted mainly from macroeconomic factors such as growth in foreign demand and import/export activities, immigrants and new subscribers. 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 2000.

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.

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 1995.

	As of December, 31					Percentage change since
	1996	**1997**	**1998**	**1999(1)**	**2000**	**1996(2)**
			(Lit.)			(%)
Germany, France	2,760	2,760	2,760	1,990	1,700	-38.4
United Kingdom	2,760	2,230	2,230	1,990	1,700	-38.4
Spain	2,760	2,760	2,760	1,990	1,700	-38.4
Russia	4,040	4,040	4,040	4,040	3,200	-20.8
Canada and United States	3,230	2,740	2,740	1,990	1,700	-47.4
Australia	8,300	6,380	6,380	5,110	4,700	-43.4
Japan	8,300	6,380	6,380	5,110	4,700	-43.4
Brazil	10,780	8,300	8,300	6,370	5,900	-45.3
Chile	10,780	10,550	10,550	10,550	9,500	-11.9

(1) Rates became effective on November 1, 1999

(2) 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 2000 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 the charges for all western European countries.

In addition to permanent price reductions, during 1998 and 1999, Telecom Italia launched

- two new discount tariff packages targeted at both residential and business customers, which included discounts for international traffic ranging from 10% to 40% (based on the monthly telephone bill of the customer),

- two temporary discount campaigns targeted at residential customers, and

- two new pre-paid international calling cards, one of which was targeted at the largest ethnic communities in Italy and offered competitive tariffs to 18 destinations and the other which was targeted at business travelers to European and North American destinations.

Telecom Italia believes that further adjustments and greater pricing flexibility will be required for it to be competitive in the provision of these services in the future.

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 1999 and 2000, gross operating revenues from leased lines amounted to Lit. 2,709 billion and Lit 3,084 billion, respectively, an increase of 13.8%. In 1999 and in 2000 the data gathering system for leased lines was modified to include exclusively connectivity charges and not service charges. Information on this basis is not available for 1998. Leased line gross operating revenues also include revenues from the leasing of lines to 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. During the last five years, Telecom Italia has experienced significant growth in digital leased lines due to the growth of lines leased to business customers and to other telecommunications operators. As of December 31, 2000, there were approximately 422,700 (in points of entry of data network) lines leased to business customers (including direct leased lines for voice telephony), of which 231,000 related to data transmission. In 2000, there were approximately 200,000 digital leased lines. In 2000, new offers and the evolution towards IP protocol and XDSL technology resulted in a concentration of points of entry on the data network.

In addition, as of December 31, 2000, there were approximately 25,820 digital leased lines related to back-bone networks and approximately 20,900, digital lines for interconnection with the Telecom Italia network leased to other domestic telecommunications operators.

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 “Item 4. Information on the Company — Regulation — The Telecommunications Regulations and Implementing Regulations”.

Telecom Italia commenced rebalancing its domestic leased line tariffs in 1991. Effective October 1, 1996, tariffs for domestic leased lines, both digital and analog, were reduced by an average of 13%. The tariff adjustments announced in March 1997, which became effective for leased lines in March and July 1997, reduced tariffs for domestic leased lines, both digital and analog, by an average of a further 10.7%. See “Regulation — Tariff and Pricing Policy — Pricing Policy and Telecom Italia’s Tariffs”. In 1998, Telecom Italia announced additional tariff reductions for digital leased lines, both high speed (greater than 2 Mbit/s) and low speed (equal to or lower than 2 Mbit/s) digital leased lines. These tariff adjustments became effective on October 31, 1998 for high speed digital leased lines and January 1, 1999 for low speed digital leased lines and reduced tariffs by an average of a further 15.9%. In November 2000 there was another average reduction of 23.7% for digital leased lines.

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 — Interconnection.” Telecom Italia will submit in July 2001 to the National Regulatory Agency its interconnection rate for 2001 which will be subject to approval of the National Regulatory Agency. Telecom Italia’s catalogue, revised on October 23, 2000, quotes interconnection rates at a lower rate than those in the previous catalogue (a reduction of 16.5% for local service, and a reduction of 10% for single transit). Telecom Italia has continued to promote the development of internet traffic by cutting interconnection rates. The interconnection rates for local and single transit have decreased by 4.5% and 17.7%, respectively, in comparison with voice rates included in the proposed Reference Interconnection Offer - RIO (catalogue) for 2001.

Telecom Italia has offered services by which customers are able to choose to route calls (both local and long distance) through either Telecom Italia or one of its competitors (carrier pre-selection). Such services have been available, on a continuing basis, since mid 2000, and on a call by call basis (carrier selection) since mid 1998. In addition, Telecom Italia has added new services to its interconnection rate catalogue for 2000, including, in particular dial up services using non geographical access codes for internet access.

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.

2000 was characterized by a strong increase of the broadband market. In less than eight months more than 115,000 ADSL, HDSL and fiber optic technology points of access have been sold to the retail and the wholesale market. 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, a service bundled with voice services, launched in November 2000.

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.

Fixed Network

Since 1988, Telecom Italia has installed high levels of fiber optics, 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.

Telecom Italia has been sensitive to changes in demand, leading to a need to improve its network, to raise standards of performance from the point of view of quality and reliability, so that it can offer its customers new services based on higher technological infrastructure and control system standards. With this in mind it has been implementing plans to develop technology in the area of multiplexing and switching, and to introduce new operation systems; in particular, it has improved levels of overall availability by taking action both in the area of the SDH transmission network and in the area of service and duplication exchanges of the areas that have not yet been appropriately sized. Telecom Italia is planning to develop a system to monitor and verify data network services, with the aim of processing the performance data of individual components and to produce reports on the network as a whole and in terms of its customers, with the option of offering customers the tools to verify for themselves the levels of service offered. See "— Telecommunications Services".

Domestic Network

Fixed Network. Telecom Italia's domestic fixed network includes 66 transit switches and 653 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.

During 2000, Telecom Italia set up interconnections with the networks of 30 additional operators, in addition to the 23 recorded in the prior two years. During the year, the following contracts were also signed or renewed:

- 25 new interconnection agreements (adding to the 40 interconnection agreements previously agreed, including agreements with Infostrada and Wind for carrier selection between districts already in effect);
- 28 additional "reverse" agreements, terminating calls on the network of another operator, for a total of 44; and
- 20 agreements to supply direct connections between the networks of other operators for a total of 30.

In addition, Telecom Italia entered into the following additional agreements in 2000:

- 8 agreements to supply high-speed access services using ADSL technology;
- 40 carrier preselection contracts, 40 district carrier selection agreements, 19 number portability agreements and 9 housing framework agreements for interconnection;
- 16 contracts for testing the local loop unbundling service on the local network and two contracts to supply the local loop unbundling service to the local network; and
- an agreement with TELE+ to carry signals relating to multimedia broadcasting services, similar to an agreement in place with Stream.

In 2000, the necessary technical preparations were made to launch the SMS service; for the activation of the "400" call return service in about 75% of the Italian territory; for the services available with the "Carta Unica" prepaid card, which can be used from public and private terminals on the fixed network, in Italy and abroad; for the

NetCard /Business, the evolution of the virtual private network service, to which the phone card service has been added with charges being made to a single account; for the personal number service with access through TIM; and, finally, to make new games available through the telephone, such as LottoTel and Totobingol.

Digitalization and ISDN. At December 31, 2000, 99.7% 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 fiber optics 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 2000. 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; from 2000, in order to reduce the number of fibers, DWDM systems will be used capable of multiplying 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. During 2000, work was completed on the first stage of the 7 backbone rings which will connect the 16 national transit junctions; 10 rings linking the backbone level with the regional level and 8 rings linking up with the international network.

During the second half of 2000, testing was also completed on a high capacity optic fiber carrier network, which functions with DWDM and OADM (Optical Add Drop Multiplexer) equipment, and is able to carry various signals and to carry out operations such as routing and protecting flows entirely within the optic fiber domain. Experiments have begun involving a high-performance IP network, based on an architecture involving a carrier infrastructure relying on DWDM connections nationwide and optical ring networks in cities on a local level realized on OADM equipment. The cities involved in the project are Milan, Rome and Turin. In the SDH network, testing was started on new equipment which offers the option of extending the functionality of the synchronous network onto copper lines to the customers' premises. During the year, the number of connections made on the network (about 180,000) almost tripled.

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. In this context, experiments with CSELT continued on the PEGASO project (Project for the Evolution of the Operation and Architectures of Optical Networks and Systems), which has the aim of learning more about optical networking, and the transport of IP and ATM flows on optical networks.

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. Atmosfera gives the ATM native services with access rate from 2 Mbit/s up to 155 Mbit/s, in 27 POP (Point of Presence) and acts as backbone also for the IP network. PAN network provides frame relay services (with access rate up to 2 Mbit/s) in 130 POP and collects IP customers at the edge.

Fiber Optic Cables. At December 31, 2000, Telecom Italia had installed approximately 3.1 million kilometers of optical fiber, of which approximately 2.6 million kilometers were installed on long distance fixed lines. Fiber optic 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 fiber optics in its local access network.

In the second half of 2000, a project was also drawn up to create an optic fiber ring between Milan and Palermo (I-Bone), which will involve the installation of approximately 4,200 km 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, 2000, 561,000 "direct digital line" access points and 166,000 "direct analog line" access points had been installed.

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 fiber optic cables to many countries. During 2000, major digital submarine links were installed in the Atlantic area. In order to satisfy the demand for new services (such as internet and multi-media 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 Atlantis 2 system and the upgrade of Colombus III; and
- in the West and South African regions, with the SAT 3 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 multiserve 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 multiserve 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 optical fiber network (PEB, Pan European Backbone) is laid in the main industrialized European countries: Italy, France, Spain, U.K., Holland, Belgium, Germany, Switzerland, Austria and is 10,600 km. long.

The Mediterranean Nautilus (MEN) owned by Mediterranean Nautilus, a company controlled by Telecom Italia, is building a new submarine optical ring. It is 7,000 km long and links the main markets of the Southern Mediterranean area: Italy, Greece, Turkey, Israel and Egypt.

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 fibre 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 1 Tbit/s, will link the most important cities of South America to Central and North America.

In 2000, Telecom Italia further rationalized its international fixed network and enhanced international transmission capacity. At December 31, 2000 there were 197,000 international circuit links, including about 4,000 via satellite and 116,331 via cable. The number of exchanges utilized in the international network has been reduced from eight to seven. The digitalization of the international network exceeded 98.0% in December 2000.

In the aggregate, Telecom Italia has access to more than 350,000 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 89.7% of faults on main lines within 48 hours. The effectiveness rate (defined as the number of successfully completed calls, not including those calls not completed due to an engaged line, a party not answering or a calling party's behavior, divided by the total number of calls) of the local fixed network has steadily increased from 98.2% in 1993 to 99.6% in 2000. Similarly, the effectiveness rate of the long distance fixed network increased from 95.4% in 1993 to 99.1% in 2000.

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

In 1999 and 2000, 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, 2000, the broadband network program extended to 58 cities, passing approximately 526,000 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 applications (of which 70,000 are customers of Stream). 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.

In its place, Telecom Italia began introducing ADSL systems over copper pairs in 1998 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. The experiments took place in the second half of 2000, in order to permit installation in new or re-structured offices from 2001.

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 the second half of the year, commercial services with access in ADSL technology for business customers and ISPs (Internet Service Providers) were extended to 25 cities. The commercial services for business customers include the use of ADSL technology in urban areas to supply access to the "RING" services (IP, Frame Relay and ATM) 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 2000, the "local exchange areas" covered by ADSL technology numbered 644, covering 110 local areas; in 2001, 800 local areas and 1500 local exchange areas will be served.

In 1999, both high-speed access on copper pairs using HDSL technology with ATM protocols and access using optical fiber with SDH connections were made available, making it possible to exploit data services locally and to access the long-distance services of the Telecom Italia networks. The innovative feature of this offer lies in the availability of fast access on copper connections and in the possibility of using RING services with tariffs matched to consumption, in local, national and long-distance scenarios. During the second half of the year, the technical verifications for opening IP services for business customers with this type of tariff system were successfully concluded. This functional advance, which is significant from a technological point of view, places the company on the leading edge in worldwide terms. Due to this new system, customers only pay for the traffic they generate on IP networks, subdivided into local, national and “Big Internet” traffic, up to the maximum speed which subscribed access to the service exchanges of the Telecom Italia network allows. During 2000, tariffs matched to consumption were introduced to the ATM and Frame Relay networks in the same cities for IP consumption services.

The evolution of new ways of offering Internet access includes the introduction of different levels of quality for both the general telephone network gates reserved for the Service Provider, and broad band access to the national and international IP backbone. Technical assessments were carried out in the first half of 2000. During the same period, a technical analysis was scheduled for the opening of IP “multicast” services on a national scale, which, initially, will be directed towards ISPs who intend to extend the offering of their services to residential and SOHO customers with audio/video and multimedia content, distributed by broadcasting mode on IP networks from their own service centers. The technical capabilities of these services will permit nationwide access from the switched networks, as well as access from ADSL networks, which is limited to the cities covered by the service.

Within the framework of developing the network and services, various experimental activities have been planned, the most important of which are as follows:

- ADSL terminations of networks for various network configurations for the customer, and ADSL access for ATM services and IPs for business customers;
- integrated messaging and voice and fax services on IP for residential and SOHO customers;
- services with the use of integrated ATM/IP technologies, as well as intelligent systems on IP networks capable of tailoring the offering according to the customer base or ISP;
- hi-tech tariff solutions, no longer based on consumption (volume or time), but on the basis of the content or application requested by the customer.

Mobile Telecommunications Services

Among the large mobile telecommunications operators in Europe at the end of 2000 TIM has the largest number of customers 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. Customer growth was 54% in 1998, 30% in 1999 and 17% in 2000. Gross operating revenues from TIM totaled Lit. 11,904 billion, Lit. 14,425 billion and Lit. 15,352 billion in 1998, 1999 and 2000, respectively.

Holdings of International Operations

As a result of a corporate reorganization completed at the end of 2000, TIM acquired 100% of SMH, the international holding company of the Group holding substantially all of the Group’s wireless investments outside of Italy. SMH is now managed by TIM and the international results will be fully consolidated with TIM’s results beginning January 1, 2001. At December 31, 2000, the overall number of TIM customers calculated on an equity basis, in Italy and internationally was approximately 27.3 million. There are approximately an additional 1 million equity mobile customers that are part of the Telecom Italia group.

The following tables list the countries in which TIM (through SMH) currently has operations, the ownership interest in each operator and the number of subscribers for each operator.

Controlled operations

Country	Operator	Percentage interest held by SMH(1)	Total Wireless customers per operator at December 31, 2000
			(in millions)
Europe			
Greece	Stet Hellas	58.14	1.6
Latin America			
Brazil	Maxitel	90.0 (2)(3)	0.9
	Tele Nordeste Celular	51.79 (2)(3)	1.5
	Tele Celular Sul	51.79 (2)(3)	1.4
Peru	TIM Peru	100 (4)	—
Venezuela	Digitel	56.56 (5)	0.2

Minority interests

Country	Operator	Percentage interest of SMH(1)	Total Wireless customers per operator at December 31, 2000
			(in millions)
Europe			
Austria	Mobilkom Austria	25.00	2.8
Czech Republic	Radiomovil	5.88	1.9
France	Bouygues Decaux Telecom	19.61	5.2
Spain	Auna	7.24	3.7(6)
Turkey(5)	IS TIM	49 (5)	(7)

(1) For more detailed information regarding the Group's international mobile operations see "International Telecommunications Services."

(2) Ownership of common shares.

(3) Held through BITEL Participaçoes S.A., a Brazilian subsidiary of SMH.

(4) Operations started January 25, 2001.

(5) Held through TIM International B.V., a wholly owned subsidiary of TIM.

(6) The amount refers to Retevision Movil customers (the wireless company of AUNA).

(7) Operations started March 21, 2001.

Services. 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. Roaming agreements have been reached with 218 operators in 145 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 "— Network — 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,			
	1997	1998	1999	2000
		(%)		
TIM Italian geographic coverage				
TACS	79	81	83	83
GSM	76	83	89	92
TIM Italian population coverage				
TACS	97	98	98	98
GSM	97	98	99	100

Customers. The penetration of mobile telecommunications service in Italy is above the Western European average at approximately 73 customers per 100 inhabitants and growth rates have been substantially higher than the European average. This compares to a penetration rate of 53 customers per 100 at the end of 1999. The increase is due in part to the entry of a fourth operator in May 2000. 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 2000, TIM added 24.8% of the net additional GSM customers, with 3.8 million net additions compared to 4.5 million for Omnitel and the remaining 4.4 million attributable to the third and fourth operator. At December 31, 2000, the number of customers for TIM's TACS and GSM mobile service was approximately 21,601,000 (of which 19,156,000 were GSM customers, consisting of 2,485,000 GSM subscribers and 16,671,000 GSM Prepaid Customers). As of April, 2001, TIM's customer base increased by a further 2.6%.

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

	Year ended December 31,				
	1996	1997	1998	1999	2000
			(number of customers)		
Customers at period end(1)	5,700,300	9,278,000	14,299,000	18,527,000	21,601,000
TACS subscribers	3,787,800	3,211,000	1,563,000	832,000	495,000
TACS prepaid customers	—	183,000	2,001,000	2,344,000	1,950,000
GSM subscribers(2)	1,343,000	2,056,000	2,453,000	2,442,000	2,485,000
GSM TIM Card	569,500	3,828,000	8,282,000	12,909,000	16,671,000
	(%)				
Customer growth	47.5	62.8	54.1	29.6	16.6
Churn(3)	14.1	18.0	16.8	12.7	15.7
TIM penetration(4)	10.0	16.3	25.1	32.5	37.5
Cellular market penetration(5)	11.2	20.6	35.9	53.1	73.3
			(Lit.)		
Average revenue per customer per month(6)	121,000	97,000	77,600	65,500	59,200

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

The significant growth in TIM's mobile customers 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 86.2% of TIM's customers at December 31, 2000 used the prepaid card.

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 Lit.4,680 billion for its license, with approximately Lit.4,000 billion having been paid in December 2000. The remaining Lit.680 billion will be payable over a three year period. The licenses are valid for 15 years starting January 1, 2002.

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

	Year ended December 31,				
	1996	1997	1998	1999	2000
	(in millions of minutes)				
Total outgoing traffic per month	421.8	542.8	838.7	1,218.6	1,568.8
Total incoming and outgoing traffic per month	772.9 (1)	1,016.8 (2)	1,472.6 (3)	1,989.3 (4)	2,479.1 (5)
	(% of total)				
Of which:					
TACS(6)	80.0	56.3	33.3	19.5	10.3
GSM(6)	20.0	43.7	66.7	80.5	89.7

(1) Includes domestic mobile incoming and outgoing traffic (97.3% of total mobile traffic in 1996 compared to 97.4% in the period from July 14, 1995 to December 31, 1995), international traffic (1.6% in 1996 compared to 1.2% in the period from July 14, 1995 to December 31, 1995) and roaming traffic (GSM only) (1.1% in 1996 compared to 1.4% in the period from July 14, 1995 to December 31, 1995). This data includes fixed outgoing traffic to the mobile network.

(2) 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). This data includes fixed outgoing traffic to the mobile network.

(3) 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). This data includes fixed outgoing traffic to the mobile network.

(4) 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). This data includes fixed outgoing traffic to the mobile network.

(5) 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). This data includes 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 one-time 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 Lit. 50,000 for the GSM TIM Card and TACS prepaid service and are required to pay a fee of Lit. 10,000 to the dealer for 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 2000, approximately 83.5% of revenues from TIM mobile services (net of access charge) were derived from traffic charges, 8.8% from subscription and connection fees, 7.7% from sales and rental of equipment and 6.2% were miscellaneous revenues.

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 set-up charge of Lit. 200 (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 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 Lit. 7,200 (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 2000, in the consumer segment, TIM introduced a number of new tariff options and services including:

- promotion of alternative ways of recharging prepaid cards, especially using Bancomat cards, with free SMS or traffic offers; and

- implementing rate plans to encourage customers to join without activation charges or with free traffic offers, such as, for the prepaid market, the “Duetto” formula which provided an option of combining it with other rates, enabling users to call a TIM number at Lit. 90 (+ VAT) per minute.

In addition, the Short Message Service (SMS) was also extended to TACS, while users who had subscribed for at least four years were rewarded with discounts on traffic and the Long TIM rate was extended to all users to further develop the service. Promotional campaigns were also launched in the summer and at Christmas.

For business customers (a segment in which TIM leads the market with a share of 65%), a special trademark and customer care service was launched on a dedicated website. For small and medium-size companies, a market which TIM is targeting, offerings such as the “2-4" plan (for companies which hold from 2 to 4 TACS or GSM subscriptions, with a particularly advantageous basic rate and the possibility of customized services) and the “Mix” plan, which charges the same rate for outgoing calls to the TIM network or the Telecom Italia wireline network, were introduced. New features were added to business tariffs and packages targeted at medium size companies.

Value added services. In 2000, TIM enhanced its range of value-added services, combining it under the new i-TIM trademark. This includes, in an integrated solution, WAP, SIM ToolKit technology, voice information and UNI.TIM applications (a universal number which makes it possible to operate voice, fax, e-mail and surfing the Internet in an integrated manner). The i-TIM service also allows access to the Internet directly in a fast, simple way.

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 the General Packet Radio Service (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.

On January 18, 2001, TIM announced that it had entered into a joint venture with KPN Mobil N.V. and NTT DoCoMo, Inc. to provide mobile internet services across Europe. Initially, the services which are expected to include gaming, exchange of messages and images, and certain internet based transactions, will be introduced in Italy, Germany, The Netherlands and Belgium (estimated total market reach: approximately 165 million customers). Other countries will be added elsewhere in Europe through affiliates of the parties, commercial service delivery contracts with other operators and through mobile virtual network operators. The handsets to be used in connection with these services will be combined i-mode/WAP handsets, which are expected to be available at the end of 2001 at the earliest. TIM expects that these services will be rolled out in Italy late in 2001.

On January 29, 2001, TIM signed a protocol agreement with NTT DoCoMo and Sony Computer Entertainment Inc. to jointly develop a mobile Internet service. One of the potential applications made possible by this agreement is access to PlayStation videogames.

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 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, 2000, there were 1,752 dealers, with 4,837 sales points (including 114 Telecom Italia outlets marketing TIM products and 93 shops directly owned by TIM), a decrease of 201 over 2000. Such decrease is due to a reorganization of the distribution network. 5,804 TIM employees (about 60% of its total workforce) were involved in marketing and customer service activities at December 31, 2000.

TIM connects approximately 95.7% of its customers through its independent dealer network and approximately 4.3% 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.

International Strategy. TIM is consolidating its role as a global player. TIM is present in Europe, the Mediterranean Basin, and Latin America. In December 2000 TIM had 19.4 million lines attributable to customers abroad, corresponding to 5.7 million equity customers. 78.7% of TIM's international lines are European mobile lines while 21.3% are Latin American mobile lines. See "International Telecommunications Services".

In Europe, excluding Italy, affiliates of TIM were awarded two UMTS licenses; one in Spain, through the subsidiary Amena at a cost of Lit. 255.6 billion, and another in Austria with Mobilkom at a cost of Lit. 332 billion. "In-Europe", TIM's pan-European tariff, was introduced in 2000. This offer will combine the preferential roaming agreements among TIM, it's foreign subsidiaries and other European partners and will allow TIM clients to roam in 30 countries using the same tariff. See "International Telecommunications Services".

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 Amena mobile business (Spain), the recent commercial launches of TIM Peru (Peru) and IS TIM (Turkey). 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, Peru 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 towards value added services (VAS). See "International Telecommunications Services".

On February 13, 2001 TIM's subsidiaries acquired PCS licenses in Brazil in the regions of Sao 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".

Cellular Network. TIM's TACS network consists of 2,706 radio base stations and 85,998 radio channels. TIM has reduced the level of investment in its TACS network as the number of TACS customers has leveled off. TIM's GSM network consists of 8,935 radio base stations and 546,512 radio channels (an increase of 22% over 1999). Management 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 "— Telecommunications Services — Mobile Telecommunications Services — Services" and "Item 5. Operating and Financial Review and Prospects — Liquidity and Capital Resources — Capital Expenditures".

Satellite Systems and Services.

In this sector, Telecom Italia Group operates through Telespazio and its subsidiaries. The satellite sector accounted for gross operating revenues of Lit. 659 billion in 2000, Lit. 619 billion in 1999 and Lit. 739 billion in 1998.

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. Revenues from satellite systems and services for 2000 were Lit. 634 billion, of which Lit. 150 billion were intra-Group.

Telespazio's principal activities include: (i) telecommunications — marketing turn-key systems (ground stations, VSAT systems, overlay networks) and services; (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. Together with the U.S. companies Liberty Media, Lockheed Martin Global Telecommunications and TRW, a global technology, manufacturing and service company, Telespazio is implementing the Astrolink Broadband Communication System which is intended to support high speed Internet access and broad band interactive multimedia services. According to the current commercial agreements such high speed access and services are expected to be available in 2003. Telespazio is also 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 co-operation 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.

International Telecommunications Services

The international telecommunications sector accounted for consolidated gross operating revenues of Lit. 7,615 billion in 2000, Lit. 3,253 billion in 1999 and Lit. 1,520 billion in 1998. These gross operating revenues include international mobile telecommunications services which will be consolidated with TIM's results beginning January 1, 2001.

The significant increase in operating revenues in 2000 is due to the first time proportional consolidation of the Nortel Inversora group. The significant increase in operating revenues in 1999 was primarily due to the first time consolidation of the two Brazilian companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes, in which the Group increased its ownership to over 51% of voting rights during 1999.

Telecom Italia owns TMI, which offers advanced telecommunication services to multinational business customers in Asia, Europe and America such as point to point digital connectivity, X25 and Frame Relay services, IP services, international VPN services, messaging services and outsourcing services. At December 31, 2000 TMI was active in 45 countries and had more than 94 installed POP (Points Of Presence).

International Investments

In light of the increasing liberalization of the telecommunications market, Telecom Italia has pursued a strategy of progressive internationalization of its operations aimed at achieving a stronger competitive position and balancing the loss of market share in its domestic market.

The Group's international strategy currently has the following objectives :

- to consolidate the Group's international presence in the two strategic markets: Europe, primarily Southern Europe, and Latin America, and to expand selectively in the Mediterranean Basin;
- to develop its international investments in high-growth market segments, such as wireless, data and Internet;
- 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 rationalize the existing international portfolio 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.

To take advantage of the expected technological and market developments in the mobile and data/IP services, the Group provides a full range of competitive international communications services able to meet the evolving needs of its business customers in Italy and abroad.

Regional Investments

In 2000 in order to rationalize the structure of its international holdings and ensure a clearer identification of management's responsibility, Telecom Italia reorganized the holding structure of its international operations. In late December, 2000, Telecom Italia completed the corporate reorganization. As a result of the reorganization, Telecom Italia now owns 100% of SIN, the primary vehicle through which the Telecom Italia group holds its international wireline investments (and certain integrated mobile/fixed line investments) and TIM owns 100% of SMH, the primary vehicle for international wireless investments.

In the following discussion the Group's main international holdings are subdivided 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. International holdings are further broken down considering the new holding structure based on investments held through SIN or SMH. The total consolidated value of holdings in affiliated companies as of December 31, 2000, based on the book value of such holdings, was approximately 69% in Europe and 30% in Latin America.

Europe

In Europe the Group has pursued an expansion strategy by establishing a strong presence in Europe, primarily Southern Europe, through acquisition of interests in both established and alternative operators and by acquiring wireless licenses.

The international strategy objectives in this region aim at maximizing the value of the existing investments in Spain, France, Austria, Greece and Turkey and to leverage the Group's existing presence to achieve a European footprint.

The Group considers a selective expansion in the mobile and data/IP market.

Europe, Consolidated Holdings

Companies Controlled by SIN

France

9 Télécom Reseau S.A. (“9Télécom”) 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. The holding in the group rose during 2000 to 93.99%

In November 2000 Telecom Italia, through 9Télécom completed the acquisition of 95.5% of Jet Multimedia S.A., the French hosting services company listed on the “Nouveau Marché” of Paris. Jet Multimedia is a leading supplier of value added services for business customers and in the development online applications using the Internet, Audiotel and Minitel platforms. Total cash consideration was euro 810.65 million.

In November 2000, 9Télécom concluded an alliance 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. This agreement provides for a strategic cooperation on Internet related activities and the acquisition of the free ISP Mageos S.A.. Mageos S.A. has a customer base of approximately 500,000.

In 2000, 9Télécom acquired 520,000 new customers (reaching 750,000 customers compared to 230,000 at the end of 1999). In addition, it acquired about 70,000 new Internet customers (for a total of 130,000 or +117% compared to the end of 1999).

9Télécom recorded operating revenues of French francs 628 million (Lit. 185 billion), five times the figure of 1999 of French francs 120 million (Lit. 35 billion). The deterioration of the operating result, which showed an operating loss of French francs 1,153 million (Lit. 339 billion) compared to an operating loss of French francs 1,024 million (Lit. 302 billion) in 1999 and the loss of French francs 1,165 million (Lit. 343 billion) compared to a loss of French francs 1,018 million (Lit. 300 billion) in 1999 were again due to the start-up phase of most of 9Telecom’s activities.

Republic of San Marino

The Group owns a majority stake (70%) in Intelcom San Marino, a telecommunications operator, which offers international voice telephony services, 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. As of December 31, 2000, Intelcom San Marino had 3,500 Internet customers and 6,300 mobile customers, revenues were equal to Lit. 111 billion, an increase of 147% compared with 1999, and net income was Lit. 4 billion, an increase of 32% compared with 1999.

The Netherlands

BBNed is a company established in July, 2000 by Telecom Italia. Telecom Italia, through SIN, owns 100% of BBNed. 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.

In 2000 BBNed had an operating and a net loss of respectively euro 1.7 million and euro 1.6 million.

Companies Controlled by SMH

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. At December 2000, STET Hellas had approximately 1.6 million customers. In 2000, operating revenues were Lit. 1,019 billion (against Lit. 900 billion in 1999), operating income was Lit. 148 billion in 2000 (an increase of 2.2% compared to 1999) and net income was Lit. 52 billion (against Lit. 15 billion in 1999). Net income was adversely affected by the cost of interconnections with the fixed operators which tripled 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 SMH was reduced from 74.8% to 58.1%. In February 2001, a stake of 1.14% was acquired by SMH. The Group's stake in STET Hellas increased to 59.3%.

Latin America, Consolidated Holdings

Companies controlled by SIN

Argentina

The Group and the France Telecom group, each have a 50% interest in, and together share control of, Nortel Inversora S.A. ("Nortel Inversora"). The current interest of the Group is the result of an initial share of 32.5% acquired in 1990 for approximately US$ 33 million and an additional share of 17.5% acquired in August 1999 for approximately US$ 265 million. Nortel Inversora 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 and mobile telecommunications operations, international services, data transmission services, value added services and directories publishing. Since October 1999, the Argentinian 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 US$ 327 million. Telecom Argentina is currently undergoing a reorganization of its subsidiaries. In 1999, its international long distance services were transferred to Telecom Argentina Matriz, a holding company. In September 2000 Telecom Argentina completed the reorganization of its subsidiary, Telecom Soluciones Assets. The data business of Telecom Soluciones Assets converged in Telecom Argentina Matriz and the internet segment in a newly formed company named Telecom Internet. At the end of 2000, Telecom Argentina had accumulated 3.5 million fixed network subscribers corresponding to a market share of 45% (an increase of 12% compared to 1999). Its subsidiary Telecom Personal, a subsidiary of Telecom Argentina and a leading company in the wireless segment, accumulated more than 2 million mobile customers (57% with prepaid cards), with a market share of 32%. In the Internet sector, there were approximately 250,000 subscribers, with a market share of 20% and a growth of 146% compared to the end of 1999.

In 2000, the Nortel Inversora group, through Telecom Argentina, recorded consolidated operating revenues of Argentine pesos 3,362 million (Lit. 7,068 billion), an increase of 2.5% compared to 1999. The increase can largely be attributed to the positive performance of mobile telephone services (an increase of 14% compared to 1999) and the data business (up 28% compared to 1999). The operating income was Argentine pesos 691 million (Lit. 1,454 billion); the net result attributable to Telecom was Argentine pesos 143 million (Lit. 301 billion).

Bolivia

In November 1995, SIN 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 establish that until November 2001, when liberalization of the market is expected to begin, fixed, mobile and long distance telecommunication services will be provided by Entel Bolivia under a monopoly system. Entel Bolivia has reinforced its position by becoming an integrated carrier. In 2000, it reached 262,000 mobile customers and 18,500 internet clients and 33,000 connections through direct lines, representing increases of 81%, 68% and 19%, respectively, compared to 1999. Entel Bolivia had operating revenues of approximately Lit. 446 billion (in line with those of 1999, due to the recession in the country), operating income of Lit. 45 billion (a decrease of 22% compared with 1999) and net income of Lit. 74 billion in 2000 (a decrease of 3% compared with 1999).

Chile

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 the Chilquinta Group and the Matte Group. The overall cost of the acquisition was US$905 million. The acquisition was completed in March 2001. Entel 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 is the second largest wireless telecommunications operator with nationwide coverage. Entel Chile, through Entel Telefonia Personal, has reached 1.3 million customers (an increase of 94% compared to 1999). Internet traffic increased by 96% in 2000. 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 had consolidated operating revenues of approximately Lit. 2,076 billion (an increase of 39% compared with 1999, due to increases of 86% in mobile and 55% in long distance traffic) and consolidated net income Lit. 12 billion in 2000. (In 1999 net income was Lit. 112 billion, which included a one time gain of Lit. 144 billion relating to the assignment of a mobile license to Bell South). Entel Chile is fully consolidated beginning in the first quarter of 2001.

Companies controlled by SMH

Brazil

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 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.

Maxitel reported operating revenues of Brazilian reais 484 million (Lit. 557 billion), a marked increase (+64.9%) compared to 1999, as a result of an increase in traffic and sales of terminals. The operating result showed a loss of Brazilian reais 125 million (-Lit. 144 billion), primarily due to higher amortization and depreciation charges. The net result, which showed a loss of Brazilian reais 641 million (-Lit. 737 billion) compared to a loss of Brazilian reais 295 million in 1999, 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 2000, in a market characterized by a level of penetration of 9%, Tele Nordeste had more than 1.5 million customers (an increase of 27% compared to 1999), corresponding to a market share of 65%.

During 2000, Tele Nordeste considerably extended its range of services for the consumer and business segments, in preparation for the launch of a WAP service and its own virtual network.

In 2000, Tele Nordeste reported operating revenues of Brazilian reais 890 million (Lit. 1,024 billion),an increase of 26.2% compared to the end of 1999; operating income of Brazilian reais 199 million (Lit. 229 billion), an increase of 64% compared to 1999; and consolidated net income of Brazilian reais 25 million (Lit. 29 billion), an increase of 164.5% compared to 1999.

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 2000, Tele Celular Sul had 1.4 million customers (an increase of 37% compared to 1999); an overall market share of 75% and an incremental market share of 57%. The prepaid service reached 47% of the customer base of 659,000.

Tele Celular Sul reported operating revenues of Brazilian reais 750 million (Lit. 863 billion), an increase of 4.7% compared to 1999; operating income of Brazilian reais 125 million (Lit. 144 billion), an increase of 13.4% compared to 1999; and net income of Brazilian reais 14 million (Lit. 16 billion), 59.4% less than in 1999, due to higher amortization, depreciation and financial expenses incurred by the company during the year.

Acquisition of additional mobile licenses in Brazil. On February 13, 2001, TIM successfully bid for two additional PCS licenses to provide wireless services in Brazil. The bids, made through wholly owned subsidiaries Blucel S.A. and Starcell S.A., were awarded Band D Licenses covering (a) the nine-state region stretching from the far south of Brazil up its western border to the Amazon and (b) the region covering Sao Paolo, Brazil's wealthiest and most populous state. TIM has agreed to pay Brazilian reais 1.54 billion (at the March 31, 2001 exchange rate, Lit. 1,567 billion) for the two licenses although the amount due will be reduced by approximately US$100 million due to TIM's entitlement to certain discounts. The discounts refer to the return of license frequencies owned by other TIM companies which overlap with the new licenses awarded. TIM made payments of Brazilian reais 770 million (at the March 31, 2001 exchange rate, Lit. 783 billion) on March 12, 2001, the date of the authorization and will make the remaining payments in the following twelve months.

On March 13, 2001, Unicel S.A., a wholly-owned subsidiary of TIM, was awarded a Band E licence for Region One in Brazil, including the Rio de Janeiro state and the northern part of the country. TIM will pay Brazilian reais 520 million (approximately Lit. 535 billion) for the licence, consisting of an initial payment of Brazilian reais 495 million (approximately Lit. 509 billion), expected on the date of the authorization, and payments of the remaining amount to be made in the following twelve months. Since obtaining these licences, TIM has extended its cellular network to cover the entire country, becoming the first nationwide cellular operator in Brazil. The operation of the PCS licenses is subject to the achievement of certain milestones by Brazil Telecom.

Peru

In March, 2000 TIM Perù was awarded the third mobile PCS license in the country at a cost of US$ 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 Peru to request licenses for supplementary services, including basic and long-distance telephone services. In 2000, TIM Perù had a loss of Lit. 36 billion due to start-up costs. TIM Peru commenced providing service in January 25, 2001.

The Group has elected to use GSM technology for its mobile services in Peru consistent with the development a Latin American platform and GSM roaming worldwide. Commercial operations commenced in January 2001.

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 GSM license in 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.

Europe, Operations Accounted for Using the Equity Method

Investments held by SIN

Austria

In December 1998 SIN 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 15, 2001 the Group's shareholding in Telekom Austria is 29.78%. Telecom Italia is providing Telekom Austria with senior management and support.

In 2000, due to continuing competitive pressures, Telekom Austria continued to lose market share. In response Telekom Austria accelerated the launch of its new services portfolio (i.e. ADSL, ISDN) and strengthened its Internet offer by acquiring 100% of Czech on Line, the Czech Republic's leading Internet Service Provider, for the sum of Lit.455 billion, and setting up the company Jet2Web Internet Services in Austria, which will offer integrated broadband access and Internet services (portal, services and content). In an effort to reduce costs, at the end of 2000, Telekom Austria Personnel Management, a wholly owned subsidiary of Telekom Austria, was formed. Telekom Austria Personnel Management's goal is to reduce the level of governmental employment, primarily through outsourcing and early retirement incentives. The workforce at Telekom Austria was reduced by 7% in 2000.

At the end of 2000, Telekom Austria market shares amounted to 71% in terms of traffic (-18% compared to 1999) and 94% in terms of the number of lines, equal to almost 3.8 million (96% in 1999). Internet customers numbered 388,000 (with a market share of 25%) and Telekom Austria remained the leading provider to the residential segment.

In 2000, Telekom Austria reported operating revenues of Austrian schillings 35.7 billion (Lit. 5,020 billion), slightly less than that in 1999 of Austrian schillings 38.2 billion (Lit. 5,381 billion). The operating result showed an operating loss of Austrian schillings 1.9 billion (-Lit. 276 billion), compared to an operating income in 1999 of Austrian schillings 3.8 billion (Lit. 534 billion). This difference is due particularly to the higher costs of marketing and interconnection. The writedown of the investment in Libro AG and the extraordinary expenses of Austrian schillings 3.5 billion (Lit. 493 billion) deriving from early retirement incentives generated a loss of Austrian schillings 6.3 billion (Lit. 881 billion), compared to a profit in 1999 of Austrian schillings 2.8 billion (Lit. 395 billion).

Spain

The Group's investments in Spain date back to 1997 and include six companies: Netco Redes, Retevisión, Euskaltel, Madritel, CTC — Cable i Televisión de Cataluña (which will operate 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.

In August 1997, Endesa, Union Electrica Fenosa and the Group acquired a 70% stake in Retevisión, the former State owned company which owns a Spanish national radio and television broadcast network and was awarded a license to operate as Spain's second telecommunications operator in competition with Telefonica de España SA. In April 1999, the Group, Endesa, Union Electrica Fenosa and a group of Spanish banks acquired the remaining 30% stake held by the Spanish Government. As a result, the Group's stake in Retevisión was 28.67%.

During 1999 the three partners agreed to undertake a rationalization process which resulted in the creation of the holding company AUNA, which was established during 2000. Telekom Italia's stake, as of December 31, 2000, in AUNA was 30% (22.76% held through SIN and 7.24% held through SMH). 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; 98.16% (cable television company);
- EresMas Interactiva: 99.32% (internet company);
- Quiero TV: 49% (television company);
- Hispasat: 30.32% (satellite communication company);
- Aragon del Cable: 100% (cable television company); and
- Cable Telca: 100% (cable television company).

Retevision I ended 2000 with more than 1,950,000 customers, corresponding to 2,766,000 indirect access lines and 62,000 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 2000, it had 1,420,000 customers, confirming its position as the second largest operator in the Spanish market of Internet Service Providers and portals, with 664 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, 2000 Amena had more than 3.7 million lines (an increase of 267% compared to the end of 1999), and a market share of 15% of the total market. During 2000 it increased its market share adding 29% 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 Lit. 255 billion. 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.

The company reported operating revenues of Spanish pesetas 139 billion (Lit. 1,618 billion), showing a significant increase (an increase of 372%) compared to the end of 1999, as a result of the commercial success achieved during the year. However, the expansion of the clientele led to a considerable increase in operating costs, and reflected negatively on the operating result, which showed an operating loss of Spanish pesetas 113 billion (-Lit. 1,317 billion), and on the result for the year, which was a loss of Spanish pesetas 81 billion (-Lit. 938 billion).

CTC — Cable i Televisión de Cataluña, which operates under the commercial brand of Menta, in August 1997, was awarded a license to provide CATV and basic telecommunication services in the Cataluña region. The company launched its services in late 1999 and is currently upgrading its commercial offer, extending the range of services offered: fixed telephony, CATV, Internet with broadband access, data transmission. In 2000, CTC had total revenues of Lit. 9.2 billion (against Lit. 1.5 billion in 1999) and net loss of Lit. 65.9 billion, due to CTC's start-up phase.

Madritel launched its CATV and telephone service in September 1999 in the Madrid Area. In May 2000, Madritel, with CTC and nine other cable carriers, established Estreno Digital for the purpose of acquiring pay-tv content at advantageous conditions. Moreover, Madritel includes, among its services, fixed telephony, CATV, internet with broad band access and data transmission. In 2000, Madritel had 33,000 customers with 59,000 executed contracts (against about 6,000 and 13,000 in 1999, respectively). In 2000, Madritel had total operating revenues of Lit. 33 billion and a net loss of Lit. 111 billion, due to Madritel's start-up phase.

In 2000, AUNA reported operating revenues of Spanish pesetas 97.4 billion (Lit. 1,133 billion), an increase of Spanish pesetas 6.0 billion compared to Spanish pesetas 91.4 billion (Lit. 1,064 billion) in 1999; the operating result was an operating loss of Spanish pesetas 42.9 billion (Lit. 500 billion) compared to an operating loss of Spanish pesetas 10.4 billion (Lit. 121 billion) in 1999; there was a loss for the year of Spanish pesetas 53.3 billion (Lit. 623 billion); in 1999, the company reported a loss of Spanish pesetas 19.1 billion (Lit. 221 billion).

The following two companies 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 2000 Euskaltel had reached 280,000 customers through carrier selection and, through a co-operation agreement with Retevision Movil, it became an integrated fixed-mobile operator. In 2000 Euskaltel had total operating revenues of Lit. 164 billion, an operating loss of Lit. 125 billion and a net loss of Lit 96 billion.

In August 1997, SIN acquired a 30% stake in Netco Redes SA for approximately Lit. 319 billion. In 2000, Netco Redes had operating revenues of Lit. 40 billion and a net result of Lit. 10 billion 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

The Telecom Italia Group owns a 29% stake in Telekom Srjbija, the Serbian national fixed telecommunications and second largest mobile operator.

At December 31, 2000, Telekom Srjbija had 2,220,000 subscribers to the fixed network (compared to 2,121,000 at the end of 1999) and 432,000 customers of the mobile network (compared to 99,000 at the end of 1999).

No official evaluation of the extent of the damage resulting form 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 2000, Telekom Srjbija, according to the draft financial statements of Telecom Srjbija, reported operating revenues of Serbian dinars 17,610 million (Lit. 581 billion based on an exchange rate of 30 Serbian dinars to the German mark), compared to Serbian dinars 8,640 million (Lit. 1,424 billion based on an exchange rate of 6 Serbian dinars to the German mark) in 1999. Gross operating profit was Serbian dinars 7,335 million (Lit. 242 billion), compared to Serbian dinars 3,408 million (Lit. 562 billion) in 1999. Telekom Srjbija reported a loss for the year of Serbian dinars, 2,970 million (-Lit. 98 billion), compared to a profit in 1999 of Serbian dinars 1,050 million (Lit. 173 billion). The loss can be attributed to the devaluation of the Serbian dinar against the German mark. See "Item 8. Legal Proceedings."

Investments held by SMH

Austria

SMH holds a 25% (plus one share) stake in Mobilkom Austria, the remaining 75% is held by Telekom Austria. The Group has a 29.78% (plus one share) stake in Telekom Austria. See: "Europe—Operations Accounted for using the Equity Method—Investments held by SIN-Austria".

SMH's interest in Mobilkom Austria was acquired in July 1997. TIM is providing Mobilkom Austria with senior management and support. In 2000, partly as a result of the entry, in May 2000 of the fourth operator, the penetration rate reached 74.5%, corresponding to more than 6 million lines, which high penetration slowed overall growth rates. Mobilkom Austria retained its leadership position with 2.8 million lines (an increase of 24% compared to the end of 1999) and a market share of 45%.

During 2000, Mobilkom Austria reported operating revenues of Austrian schillings 18 billion (Lit. 2,554 billion), 10% compared to 1999; the operating result was Austrian schillings 2.8 billion (Lit. 389 billion); and net income was Austrian schillings 1.8 billion (Lit. 258 billion). In November 2000, Mobilkom Austria was awarded one of the six UMTS licenses auctioned by the Austrian government; the cost of the license was Lit. 332 billion. Net income was affected by high financial expenses attributable to the acquisition of the UMTS license and investments in GPRS.

Czech Republic

The Group holds a 12% interest in a company which owns a 49% interest in Radiomobil, a mobile telecommunications operator, which in March 1996 won a GSM license in the Czech Republic. As of December 31, 2000, the penetration rate in the Czech Republic had reached 38% and Radiomobil had approximately 1.8 million customers. Radiomobil had operating revenues of Lit. 966 billion (an increase of 65% compared to 1999) and net income of Lit. 93 billion (an increase of 33%) in 2000.

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 2000 the company reported operating revenues of French francs 12.8 billion (Lit. 3,783 billion), an increase of 62% compared to 1999 on account of the increase in the customer base. This was accompanied by a reduction in industrial and commercial costs, with significant repercussions on the operating result, which showed an operating loss of French francs 1.2 billion (Lit. 364 billion) a decrease of 57% compared to 1999. The net result, which showed a loss of French francs 2.2 million (Lit. 655 billion), is however an improvement of 37% compared to 1999.

The company recently decided not to participate in the award of UMTS licenses in France owing to the high cost reached during the bidding (euro 4.95 billion (Lit 9,585 billion)). However, the French government, which only awarded two of the four available licenses, is evaluating the possibility of starting another auction for the frequencies that have not yet been assigned.

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 May 2001, there were over 130,000 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 US$ 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, TIM and Is Bank formed the company Is TIM, which launched the activities for the start-up of mobile telecommunications services. According to the agreements with its local partner, TIM will be responsible for the technical and commercial operation of the enterprise.

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%).

Ukraine

SMH, through U-Mobile, has 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 worsening economic and competitive conditions, TIM decided to divest in the Ukraine.

Latin America, Operations Accounted for using the Equity Method

Investments held by SIN

Brazil

Brasil Telecom Participacoes ("BTP", the new name of Tele Centro Sul Participacoes owned through Solpart in which SIN has a 38% stake) operates in the wireline telephone sector. Within the frame work of a corporate restructuring process begun in 1999, during 2000, ten operative wireline companies, including Companhia Riograndense de Telecomunicacoes ("CRT"), merged and acquired in 2000, for US$ 800 million, Tele Brazil Sul. After these transactions, at the end of 2000, BTP holds 65.47% of the total share capital of Brasil Telecom (97.97% of ordinary shares and 39.34% of preferred shares).

The investments made during the year had the aim of strengthening the transmission and switching structures and completing the digitalization of the exchanges. At the end of 2000, there were 7.2 million lines in service (of which about 2 million were newly installed). In addition, during the year, the technological platform to support the broadband Internet services became available.

The consolidated financial statements showed operating revenues of Brazilian reais 4,732 million (Lit. 5,444 billion) an increase of 48% compared to 1999; operating income was Brazilian reais 869 million (Lit. 999 billion); the consolidated profit was Brazilian reais 342 million (Lit. 393 billion), an increase of 21% compared to the prior year.

Cuba

In 1995, STET International Netherlands acquired an indirect participation of 12.25% in Empresa Nacional de Telecomunicaciones de Cuba S.A. ("ETEC S.A."), the operator for national and international wire telecommunications services in Cuba, by purchasing, for approximately Lit. 500 billion, 25% of the Mexican company CITEL S.A. de C.V., which owned 49% of ETEC S.A. In February 1997, SIN transformed its indirect interest in ETEC S.A. into a direct investment and increased such interest to 29.29%. The acquisition price for such further stake (17.04%) in ETEC S.A. amounted to US$ 305 million. In order to realize the objectives of its license, ETEC S.A. has increased the number of lines from 424,000 in 1999 to 484,000 in 2000 and the digitalization rate from 40% in 1999 to 53% in 2000. The data network was also improved in 2000 with net ATM/Frame Relay technology. In 2000 ETEC S.A. had operating revenues of US$ 293 million compared with $249 million in 1999. Net income was US$ 160 million compared with US$ 144 million in 1999.

On December 15, 2000, connections with the United States were interrupted because of a failure on the part of the U.S. operators to impose taxes on calls between the US and Cuba. In order to minimize the negative effects of such failure, ETEC S.A. has entered into transit agreements and connections with other carriers.

Other Investments

China

In July 1996, STET International formed a joint venture with a local partner for the construction in the Jilin province of a network for GSM mobile services. The Group's total investment to date in China has been approximately US$ 21 million. Following the decision of the local authorities concerning the legitimacy of foreign investments in telecommunications operations, both joint ventures undertook negotiations with the Chinese partner to terminate their participation to their projects. It is expected that following such termination Telecom Italia Group will be able to substantially recover its investments in China.

Greece

On December 3, 2000, through Mediterranean Nautilus S.A., Telecom Italia concluded a strategic partnership with the operator Forthnet, acquiring a 5% stake at the cost of approximately euro 9 million. On December 4, through a subsidiary Mediterranean Broadband Access, Telecom Italia and Forthnet were awarded a "Fixed Wireless Access" license for the sum of euro 8.5 million.

India

In September 2000, Telecom Italia sold all of its investments in companies belonging to the Bharti group: 20% in the holding company Bharti Tele-Ventures, 30.2% in Bharti Telenet (a fixed network operator in the region of Madhya Pradesh) and 2% in Bharti Cellular (a mobile GSM operator in Delhi).

The investment holdings in Bharti Cellular and Bharti Telenet were first sold to Bharti Tele-Ventures, which, in turn, were transferred to the Singapore Telecom group, which is establishing an alliance with Bharti. The deal was concluded for an overall expenditure of US$ 121 million.

Israel

Golden Netherlands (39.06% owned by Telecom Italia and 60.94% owned by SIN) owns 26.4% of Golden Lines International Communications Services Ltd., a company formed with local partners and Southwestern Bell of the United States, which was awarded on November 6, 1996 one of two international telecommunications services licenses put up for tender by the government of Israel. Golden Lines commenced services in July 1997. In December 1999, Golden Lines achieved about 26 % market share; operating revenues for 1999 amounted to Lit. 220 billion and net loss was Lit. 35 billion. In 2000 Golden Lines had operating revenues of Lit. 284 billion (an increase of 13% compared to 1999) and a net loss of Lit. 28.5 billion (a 30% improvement compared with 1999).

Iridium

Commercial and financial difficulties forced Iridium to file for Chapter 11 bankruptcy protection on August 13, 1999. Although significant efforts were made by Iridium investors to support the reorganization and continue operating the business, these efforts were not successful. On March 17, 2000, Iridium announced that it would terminate the provision of commercial service and that it would begin the process of liquidating its assets. The Iridium satellite system has been maintained to allow subscribers in remote locations to obtain alternative communications, while the deorbiting plan is being finalized. Iridium Italia (30% Telecom Italia, 35% TIM, 35% Telespazio) has set a plan of operations in order to complete the winding down of its operation by the year end 2000. Iridium was liquidated on March 19, 2001. The investment in this venture was written off in the 1999 financial statements.

Internet and Media

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. See “Significant Developments during 2000 - Completion of SEAT - TIN.IT Transaction”.

SEAT’s predecessor, Otto S.p.A., was incorporated as a Societá per Azioni on July 29, 1997. In November 1997, through a wholly-owned subsidiary, Otto S.p.A. acquired a controlling interest in SEAT, a Societá per Azioni the majority of whose shares had been held by the Italian Treasury. In September 1998, SEAT S.p.A. was merged upward into Otto S.p.A.’s wholly-owned subsidiary and the merged company changed its name to SEAT Pagine Gialle S.p.A. In December 1999, SEAT was merged into Otto S.p.A., with the merged company retaining the name of SEAT Pagine Gialle S.p.A. In November 2000, Tin.it was merged into SEAT in exchange for SEAT shares.

Business

SEAT’s business activities are organized in five segments: telephone directories, Internet, distribution of office products and services, professional publishing and business information. In telephone directories, SEAT is the principal seller in Italy of advertising in the Yellow Pages (*Pagine Gialle*) and the principal publisher of the Yellow Pages and the White Pages (*Elenchi Telefonici*) 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. In Internet services, SEAT is a leading Internet services provider in Italy and operates Italy’s most frequently visited portal and an integrated business-to-business platform. Through Gruppo Buffetti, SEAT is also a leading distributor of office products and business solutions in Italy.

SEAT’s products and services are organized in the following business segments:

- telephone directory publishing;
- Internet services;
- distribution of office products and services;
- business information services; and
- professional publishing.

Directory Publishing

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 business-to-business Yellow Page directories (*Pagine Gialle Lavoro*), business-to-home Yellow Page directories (*Pagine Gialle Casa*) and the White Pages (*Elenci 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*) publishes city maps and information about local public services (*Tutto Città*) to be inserted into certain editions of the Yellow Pages, as well as a directory of facsimile numbers in Italy (*Telefax*).

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*;
- Euro Directory, which publishes Yellow and White Pages telephone directories in Luxembourg; and
- Telegate, the second largest operator of directory assistance services and vocal portal services in Germany, with operations in Italy, Spain and the United States.

Internet Services.

SEAT offers a full range of Internet services, comprising:

- 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, 2000, Tin.it's subscriber base amounted to approximately 4 million registered users and 1.7 million active users (defined as users who connect to the Internet at least once every 45 days).

Million users	2000	1999
Registered users	4.0	2.0
Active users	1.7	1.1

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

Virgilio is a leading Italian portal, with approximately 744 million web page views in the first quarter of 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 2000, *Virgilio* concentrated primarily on developing new contents and services for its site, including *Virgilio* Sport, the MP3 and video section, the game room, beauty section, *Disney Blast* (on-line entertainment service for children and families, available in Italian only on *Virgilio* in accordance with a contract with Disney) and the agreement with ZD Net Italia. *Virgilio* acts as a traffic and visibility aggregator for its advertisers, clients and partners on the Internet where the portal is a real distribution platform to be used to reach Italian consumers.

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. During 2000, Active Advertising sold approximately 271 million impressions (excluding *Virgilio*'s impressions), compared to 45 million in 1999, and the number of its advertisers exceeded 500, compared to 242 in 1999.

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 Services/Business Services. 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 it also offers direct marketing and database services.

Recent Events

Recent Acquisitions

TeleMonte Carlo. In August 2000, SEAT agreed to purchase Cecchi Gori Communications S.p.A. , the owner of the TeleMonteCarlo television network ("TMC"), for an aggregate amount of Lit 1,000 billion from Cecchi Gori Media Holding S.r.l and its parent company, the Cecchi Gori Group FIN.MA.VI S.p.A. TMC is the third largest TV network in Italy. The transaction was the subject of litigation in the Italian Administrative and Civil Courts. See "Item 8. Legal proceedings—Acquisition of TeleMonte Carlo".

At December 31, 2000, SEAT owned a 25% interest in Cecchi Gori Communications and had already contributed Lit. 250 billion to TMC in the form of a capital increase and begun the integration of new management. The remaining consideration was to be paid through the issuance by SEAT of up to 109,867,484 ordinary shares in exchange for Cecchi Gori Communications ordinary shares.

On April 27, 2001, the ordinary and extraordinary shareholders' meeting of Cecchi Gori Communications approved the company's annual report and resolved to increase its capital in order to cover its losses for the fiscal year 2000. SEAT subscribed to the portion of the capital increase necessary to maintain its 25% interest by paying Lit. 41 billion and also advanced Lit. 125 billion for Cecchi Gori Media Holdings' 75% portion. As of June 5, 2001, the prescribed deadline for subscribing to the capital increase, Cecchi Gori Media Holding Group had failed to make a payment with respect to its share or provide notification of its intent to do so. Accordingly, its shares in Cecchi Gori Communications have been cancelled under Italian law and SEAT owns 100% of the share capital of Cecchi Gori Communications.

Consodata. On February 9, 2001, SEAT completed the acquisition of a 54.5% stake in Consodata S.A. ("Consodata"), a French company listed on Paris's Nouveau Marché. Consodata operates in the information marketing sector. The acquisition was completed through the issuance by SEAT of 63,789,104of its ordinary shares in exchange for Consodata shares held by certain funds and management and the contribution by SEAT to Consodata of its 100% in *GialloData*, a business information company. Based on SEAT's share price on February 9, 2001, the value of the consideration paid was €130 million which represents the value of the acquired shares and of the contribution in kind. On May 28, 2001, SEAT launched a public exchange offer (16 SEAT shares for each Consodata share) for the remainder of the Consodata share capital it does not currently own. The offer started on May 30, 2001, and will expire on July 4, 2001.

Net Creations. On December 22, 2000, SEAT and Sogerim entered into a definitive merger agreement with NetCreations, Inc. ("NetCreations") pursuant to which, through a merger of NetCreations into a special purpose vehicle wholly owned by Sogerim, Sogerim acquired all of NetCreation's outstanding stock for US$ 7.00 per share in cash, representing a total acquisition price of approximately US$ 109 million. The merger was consummated on February 15, 2001. NetCreations is the U.S. leader in Opt-In® e-mail marketing services.

NetCreations specializes in e-mail data collection, database management and e-mail marketing services. At year end 2000, its database contained over 22 million double Opt-In® e-mail addresses — addresses of consumers who have identified and confirmed areas of special interest to them — a database that is growing by approximately 80,000 names a day. NetCreations has partnerships with over 380 Web sites and provides direct e-mail marketing services to over 2,000 clients. In 2000, NetCreations had operating revenues of Lit. 122 billion (€63 million).

The acquisition was financed through a sale of SEAT shares. Sogerim borrowed SEAT ordinary shares from a subsidiary of Telecom Italia and sold them in the market resulting in net cash proceeds to finance the merger consideration. SEAT shares were issued to Sogerim when Sogerim contributed NetCreations to SEAT. The contribution of NetCreations to SEAT was completed in June 2001.

Eniro. On April 22, 2001 the SEAT board of directors resolved to launch a public offer to the shareholders and warrantholders of Eniro to sell their shares and warrants issued by Eniro, respectively, to SEAT. The offer was announced on April 23, 2001 with an acceptance period between May 18 and June 12, 2001.

SEAT offered Eniro's shareholders 12.25 new SEAT shares, for each of their Eniro shares tendered. Additionally, all registered holders of Eniro shares, who on April 20, 2001 (directly or through a nominee registered in the Swedish clearing system of VPS) were registered holders of Eniro shares, were offered the opportunity to sell to SEAT a maximum of 1,000 Eniro shares per shareholder for an aggregate of SEK 250 million. SEAT offered the holders of warrants issued by Eniro SEK 63.80 in cash for each Eniro warrant tendered.

The offer is conditional, among other things, upon SEAT receiving acceptances in respect of at least 50.1% of the total number of outstanding Eniro Shares at the end of the acceptance period.

On May 3, 2001, Telia, Eniro's largest shareholder with a 47.5% stake, announced its intention not to tender its shares. Following such announcement SEAT declared that its offer remained valid and reserved the right to modify certain terms of the offer. On June 26, 2001 SEAT's board announced that it would not waive the 50.1% minimum acceptance condition of the offer. On June 27, 2001 the extraordinary general meeting of SEAT shareholders approved a capital increase of a maximum of 2,008,052,916 new ordinary shares corresponding to the total maximum number of shares to be issued according to the offer and announced the extension of the acceptance period until July 27, 2001.

Globo.com

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 has acquired 30% of the voting and total capital of Globo.com for US$ 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 special focus on its technological aspects. Telecom Italia and Globo Organizacoes are exploring further joint initiatives on the Internet field.

IT Software and Services

The IT software and services segment includes the Finsiel Group, Netsiel and Telesoft, a company held by Telecom Italia (60%) and Finsiel (40%) and Sodalia S.p.A. ("Sodalia"), which is 100% owned by the Company. Finsiel is held 77.92% by Telecom Italia, 14.38% by the Bank of Italy and 7.70% by other shareholders.

On April 10, 2000, Telecom Italia created a new Business Unit called Information Technology Services, grouping together all the IT companies belonging to the Group: Finsiel, Netsiel, Telesoft and Sodalia, together with Telecom Italia's IT Department. Responsibility for the IT services has been assigned to Gilberto Ricci, who is also Chairman and CEO of Finsiel and Chairman of Sogei. The creation of the IT Services as reorganized represents the development of a project to create strategic value within the Group's information technology business. The IT Services goal is to integrate Telecom Italia's network services offer with application solutions, to develop a competitive offer for IT professional services in traditional and newer market segments and, to assure innovation, development and effective management of Telecom Italia's internal information system.

The main aims of this reorganization are to fully concentrate the sector activities on the product/customer/market, make better use of specific professional skills and improve production efficiency. The Business Unit is expected to diversify into the following areas: "Telecommunication Services", specialized in applications consultancy and in system integration services for the telecommunications market; "Operational Services", devoted to managing computer infrastructures; "Market", geared to the segments of finance, industry and the central Public Administration; "Web Professional Services", with the aim of playing a leading role in the offering of professional services and innovative web-related solutions; "Regional Services", devoted to the local Public Administration; "Consulting", specialized in executive consultancy; and "Tax Services", devoted to support activities for the tax-records office and the Ministry of Finance.

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, playing an advisory role in the key areas of administrative decentralization, taxation and healthcare systems.

SOGEI, 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 online 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.

In 2000, the Finsiel Group contributed operating revenues of Lit. 2,259 billion, operating income of Lit. 207 billion and net income of Lit. 152 billion (Lit. 132 billion attributable to Telecom Italia and Lit. 20 billion to minority shareholders).

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 whole OSS and BSS range of applications, a wide range of solutions combining internal assets and best of breed packages and a consolidated presence in the international telecommunication market.

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. Sodalia is recognized in the world of telecommunications where it is known as an innovative "Software Factory".

Manufacturing

As part of its non-core asset disposal plan, on December 6, 2000, Telecom Italia sold 80.1% of Italtel to a group of investors led by Clayton Dublier & Rice and Cisco Systems. See "Non-Core Assets Disposal Program". Italtel's financial results are included in Telecom Italia's consolidated results only through September 30, 2000.

Italtel S.p.A. is the main Italian manufacturer of telecommunications equipment and had been jointly owned by Siemens and Telecom Italia. In 1999 Telecom Italia and Siemens decided to terminate the joint venture by splitting the company in two parts. As a consequence of this decision, in December 1999 Italtel sold to Siemens Beteiligungsverwaltung 100% of Siemens Information and Communication Networks S.p.A., the company which assumed (since November 1, 1999) the activities relating to mobile networks and transmission systems equipment. At the same time Telecom Italia acquired control of 100% of the remaining businesses in Italtel. Italtel currently focuses its activities on fixed networks, voice, data and image systems equipment.

Installation

SIRTI is a major international company operating in several countries in the field of telecommunications engineering and networks installation, including provision of turnkey solutions for high voltage power supply networks and systems for special applications.

In November 2000, Telecom Italia accepted the tender offer launched by Wiretel on October 4, 2000 for 100% of the share capital of Sirti. Telecom Italia tendered all the Sirti shares it owned (49.1% of Sirti's share capital) for Lit. 2,910 per share, a total consideration of euro 162 million. Sirti's financial results are included in Telecom Italia's consolidated results only through September 30, 2000. See "Significant Developments During 2000—Non-core Assets Disposal Program".

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 "— 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 Lit. 130 billion. 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 Lit. 240 billion.

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 Lit. 380 billion.

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.

At the end of 2000, Stream had 670,000 customers, compared to 385,000 at the end of 1999. Operating revenues were Lit. 274 billion (+238% compared to 1999). The expenses incurred for the acquisition of content, sales assistance and extension of the technical infrastructures led to a deterioration in the results for 2000. In 2000, Stream's net loss was Lit. 687 billion, Lit. 229 billion (+50%) more than in 1999.

Telecom Italia has recently stated its intention to exit Stream by the end of the current year.

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; 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 contributed operating revenues of Lit. 276 billion in 2000.

Research and Development

The Group spent Lit. 730 billion, Lit. 640 billion and Lit. 520 billion on research and development in 1998, 1999 and 2000, respectively. The Group also receives grants from research and development nationale 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 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 TI Lab, the corporate research center of the Group. TI Lab performs both strategic research and research specifically requested by Group Companies.

TI Lab accounts for about 56% of the Group total research and development expenditure.

TI Lab was established in March 2001 to combine Telecom Italia's venture capital and innovation Business Unit, the CSELT research laboratories in Turin, the Future Centre in Venice, the Consumer Lab in Rome. The Technology Observatory in San Francisco collaborates, on an exclusive basis, with TI Lab. 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.

Competition

Domestic Fixed and International Telecommunications Services

Pursuant to the Telecommunications Regulations, fixed public voice telephony services and the operation of the fixed 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 public voice telephony services, which consist of local, long distance and international telecommunications services, in Italy. In addition to fixed 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 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.

In 2000, TIM 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 may cause TIM to grow more slowly in the future. Although the entry of the fourth operator further increased penetration in the Italian market to 73.3% or approximately 42.2 million customers, TIM's overall subscriber growth was only 17% in 2000 (compared to 30% in 1999) and its overall market share declined to 51% in 2000 from 61% in 1999.

On April 2001, 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 was approximately 20. See "Regulation".

Telecom Italia is now facing increasing competition in international and domestic telecommunications services from, among others, Infostrada (now fully controlled by Omnistrada, a holding fully controlled by Mannesmann), Albacom (a joint venture among British Telecommunications, Banca Nazionale del Lavoro, ENI and Mediaset) and Wind (a joint venture between Deutsche Telekom, ENEL, the Italian electrical utility company and France Telecom), TISCALI (national competitor: 90% Renato Soru, 10 KIWI Venture Capital), and Tele2 (Italian branch of the Socièté Europeenne 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 Framework Law (effective November 14, 1995), the Maccanico Law (effective August 1, 1997), the Telecommunications Regulations (effective October 7, 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 2000 as additional steps were taken regarding tariff rebalancing, interconnection charges and the initial signing of contracts to permit the unbundling of the local loop. See "Regulation."

Although management believes that it took steps to prepare for increased competition, including the provision of fixed public voice telephony services, as management expected it has lost fixed telephony services market share, in particular, with respect to domestic fixed long distance traffic (including fixed to mobile traffic) and outgoing fixed international traffic. In 2000, 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 network. Telecom Italia expects to maintain its subscriber lines volume for 2001, because the unbundling of the local loop is not expected to have a significant impact before the end of 2001. For 2001 competition will be on both carrier selection and on carrier pre selection and in the second half of the year in unbundling of the local loop.

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 rapidly in Italy in 2000. By December 31, 2000, the number of cellular phone lines reached 42.2 million, corresponding to a penetration rate of around 73.3% 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. Competition for mobile telecommunication services grew stronger in 2000. WIND, which introduced its services in March 1999 obtained a market share of 11.7% and the fourth Italian operator, which began commercial operations in May 2000, reached a market share of 1.9% at December 31, 2000.

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 was the designation of TIM and Omnitel as providers with considerable market strength in terms of cellular service, interconnection, and the definition of new pricing scheduled for fixed-to-mobile communications.

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 Tin.it 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 to execute 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 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 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.

In addition to implementing the Framework Law and allowing the National Regulatory Agency to commence operations, the Maccanico Law contains provisions relating to broadcasting activities, under which Telecom Italia has been permitted to apply for a license to broadcast television programs since January 1, 1998, by satellite, cable and encrypted terrestrial frequencies. See "— The National Regulatory Agency and the Maccanico Law".

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, 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".

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:

- Law No. 58 of January 29, 1992 ("Law 58"), and implementing regulations;
- the Ministry of Communications decrees principally promulgated with respect to tariffs;
- Regulation No. 197 of May 8, 1997 concerning telephone service and subscriptions contracts;
- 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");
- the Ministry of Communications Decree of November 25, 1997, defining new local areas relevant to the application of tariffs, which partially modified the NT Plan;
- the Law Decree No. 455 of December 12, 1997, approved with modification by the Parliament through the Law No. 29 of February 2, 1998, concerning the allocation of frequencies and the testing of DCS 1800 services ("DCS 1800 Decree");
- the Ministry Decree of February 5, 1998 on the individual licenses and general authorization fees to be paid by telecommunications operators;
- the Ministry of Communications Decree of March 10, 1998 on costs and financings of Universal Service ("Universal Service Decree");
- the Ministry of Communications Decree of April 23, 1998, published on June 10, 1998, pertaining to the interconnection agreements ("Interconnection Agreements Decree");
- President Republic Decree 77/2001 of January 11, 2001, pertaining to transposition of Directive 97/51/Ce and 98/10/Ce; and

- Law 66/2001 of March 20, 2001, pertaining to broadcasting and licenses.

Certain Orders of the National Regulatory Agency issued since its formation:

- the Order of March 22, 1999, No. 20 pertaining to the revision of maximum number of DCS licenses;
- the Order of June 9, 1999, No. 69 pertaining to measures for effective competition in the mobile market;
- the Order of June 25, 1999, 101/99, pertaining to the voice telephony calls economic offer;
- the Order of July 28, 1999, No. 170 pertaining to the modification of billing system from pulse metering to per second billing;
- the Order of July 28, 1999, No. 171 pertaining to the introduction of Price Cap method;
- the Order of August 4, 1999, 2/CIR/99 pertaining to the establishment of universal service obligation Fund for 1998;
- the Order of September 7, 1999, No. 197 pertaining to the significant market power operators;
- the Order of October 20, 1999, No. 274 pertaining to the regulation of volume discount schemes under the price cap method;
- the Order of December 6, 1999, No. 338 pertaining to the interconnection between fixed and mobile networks;
- the Order of December 7, 1999, 3/CIR pertaining to the provisioning scheme for carrier pre-selection;
- the Order of December 7, 1999, 4/CIR pertaining to the provisioning scheme for service provider portability;
- the Order of December 21, 1999, No. 407 pertaining to the temporary authorization to Telecom Italia for the commercialization of high speed Internet access based on ADSL technology;
- the Order of December 22, 1999, No. 410 pertaining to the framework for UMTS licensing;
- the Order of February 22, 2000, 3/CIR pertaining to the modification of the Carrier pre selection offer;
- the Order of March 16, 2000, 2/CIR pertaining to the implementation of local loop unbundling and;
- the Order of April 5, 2000, 217/00/CONS pertaining to the modification of the condition of commercialization of high speed internet access based on ADSL technology;
- the Order 4/00/CIR of May 9, 2000, introducing obligations in the provision of the Carrier Pre-Selection;
- the Order 310/00/CONS, issued on May 24, 2000 regarding the charges from public payphones;
- the Order of June 1, 2000, 314/00/CONS, regarding low income users;
- the Order of June 8, 2000, 6/00/CIR, regarding new numbering plan;
- the Order of July 19, 2000, 467/00/CONS, regarding the general authorization regime;

- the Order of August 1, 2000, 7/00/CIR, regarding number portability provisioning;
- the Order of August 1, 2000 8/00/CIR, regarding contribution to universal service fund year 1999;
- the Order of October 18, 2000, 9/00/CIR, regarding carrier preselection provisioning;
- the Order of October 18, 2000, 10/00/CIR, regarding evaluation of Telecom Italia's 2000 RIO;
- the Order of October 31, 2000, 711/00/CONS, regarding Telecom Italia's leased lines offer;
- the Order of November 14, 2000, 11/00/CIR, regarding extension to 11 digits of numbering plan;
- the Order of November 22, 2000, 822/00/CONS, regarding wireless local loop licenses;
- the Order of December 6, 2000, 13/00/CIR, regarding evaluation of Telecom Italia 2000 local loop unbundling (technical and provisional aspects);
- the Order of December 11, 2000, 847,00/CONS, regarding revision of price cap value;
- the Order of December 21, 2000, 14/00/CIR, regarding evaluation of Telecom Italia 2000 local loop unbundling (economical aspects);
- the Order of December 21, 2000, 15/00/CIR, regarding Telecom Italia's permanent virtual circuit offer; and
- the Order of February 22, 2001, 4/01/CIR, regarding evaluation of Telecom Italia's permanent virtual circuit offer.

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

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

- authorizations and licensing;

- universal service obligations;

- access deficit contributions;

- 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

In accordance with Law 66/2001, since January 2001 the Ministry of Communications has regained its power relating to the granting of 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 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.

In accordance with Order 820/00/CONS 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 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 and may be expanded over time to include other services due to technological advances and market developments. 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 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 and, if such costs represent an unfair burden on the supplier, the telecommunications operators running public telecommunications networks, providing fixed public voice telephony service or mobile and personal communications services are required to contribute to a fund, instituted by the Universal Service Decree and managed by the Ministry of Communications, to cover such costs. Telecom Italia must keep separate accounts in order to calculate the net cost of the provision of the universal service and is required to submit yearly (within March 31 of each year) the evaluation of the net cost, to the National Regulatory Agency. The National Regulatory Agency determines if the net cost represents an unfair burden on Telecom Italia and, in this case, appoints an independent Advisor to audit the cost evaluation. Within 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 by August 15 of such year. Telecom Italia, as the operator required to provide the universal service receives payment from the Ministry of Communications on September 15 of that 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 cost. 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 Lit. 120.8 billion. The operators obliged to contribute to finance such net cost are: (a) Telecom Italia (57.1%); (b) TIM (28.1%); (c) Omnitel (13.8%) and (d) Infostrada (1%).

In January 2000, the National Regulatory Agency started a proceeding regarding the treatment of low income and disabled customers aimed at defining specific reductions of the monthly rental fee for voice telephony services. The National Regulatory Agency proposal, issued on June, 2000, defines the guidelines to grant users access to the benefits. To date the procedures to identify targeted customers remains to be defined.

On March 31, 2001, Telecom Italia filed the evaluation of the net cost for the year 2000. The decision on whether such net costs are an unfair burden on Telecom Italia by the National Regulatory Agency is pending.

According to article 5 of the Order 8/00/CIR, on January 31, 2001 Telecom Italia filed detailed information regarding the net cost of universal service requested by the National Regulatory Agency to open a public consultation aimed at determining the guidelines for the competitive provision of the universal service.

Access Deficit Contributions

In principle, the Telecommunications Regulations provide that Telecom Italia is allowed to recover the cost of installing and operating the local access network not covered by the rental fees and the connection charges (the "Access Deficit") through additional charges to the interconnection charges paid by the other Operators (the "Access Deficit Contributions") until December 31, 1999.

In accordance with applicable regulations Telecom Italia filed with the National Regulatory Agency the computation elements (audited by an independent Advisor appointed by the Agency itself) for the year 1997. The certified amount related to the Network Access Deficit was Lit. 4,470 billion. The National Regulatory Agency on June 26, 1999, with Order 101/99 decided not to apply the mechanism for financing the Access Deficit Contribution.

The European Commission opened an infringement procedure against Italy on the basis of an allegedly incomplete implementation of tariff rebalancing, which did not result in an effective competitive market. On

December 21, 2000 the European Commission suspended the infringement proceedings against Italy following the decision of the National Regulatory Agency to authorize Telecom Italia to increase its subscription charges in 2001 by a percentage equal to RPI +6%, (Order 847/00/CONS which modifies the sub-cap for rental charges), in order to bring them closer into line with access network costs. This allowed Telecom Italia to increase the monthly rentals by 4.4% from February 1, 2001. The full tariff rebalancing is expected to be completed within July 1, 2002. See "— Tariff and Pricing Policy").

Special Status of Operators Having Significant Market Power

Under the Telecommunications Regulations, telecommunications operators operating fixed 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 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 — 1999 Review — Working Document on a Common Regulatory Framework."

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.

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 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 Interconnection Agreement 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 others, non discriminatory 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 24, 1998, Telecom Italia submitted a new cost based RIO , in accordance with the Telecommunications Regulations and EU Directive 97/33. Subsequently, the National Regulatory Agency issued Order 1/CIR/98, calling for (i) interconnection prices consistent with the thresholds fixed by the Recommendation above, and (ii) the widening of the interconnection services to be offered. As a result, on December 31, 1998, Telecom Italia published a new RIO, consistent with the new order of the National Regulatory Agency.

On June 25, 1999 the National Regulatory Agency issued the extension of carrier selection to calls within the same national destination code with the exception of local calls for which the carrier selection started January 1, 2000. For this data, therefore, the carrier selection will apply to all types of calls. In the same Order the National Regulatory Agency required verification of the cost and the price of leased lines, both for interconnection and the end users market and to produce an accounting separation for short distance (local), national, international and for interconnection leased lines. The verification is still in progress.

On July 15, 1999, Telecom Italia submitted a new cost based 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 inter-connection prices. 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.

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; fiber optics; 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 fiber optics 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).

After an experimental phase, LLU is now in operation: Telecom Italia is implementing exchanges for co-locations (ongoing activities for 500 sites as required by the National Regulatory Agency). As of May 2001, the number of contracts signed was 12.

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.

Numbering

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

Number Portability ("NP")

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 has been introduced since February 2000, 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 start consistently with unbundling of the local loop.

Number portability for mobile services, which should have been introduced beginning July 1, 1999, is expected to be introduced between April 30, 2002 and June 30, 2002.

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. Starting from May 2000 in Milan, June 2000 in Rome and July 2000 in other local areas, 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 19th January 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 and 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 25th November 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 (2.7% for 2000, 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. To date, the GSM concessions have not been modified and they remain in force, to the extent they have not been superseded by relevant domestic and EU regulations.

Licensed Operators

In May 2001, 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 208.

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 has been granted both a mobile and a fixed license at the beginning of its activities. 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 Lit. 4,680 billion for its license, with approximately Lit. 4,000 billion having been paid in December 2000. The remaining Lit. 680 billion will be payable over a three year period. 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. Until May 1997, analog tariffs were approved by the Ministry of Communications following proposals from TIM. 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).

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.

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 has 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 provides 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.

In October 2001, the National Regulatory Agency is expected to review the status of the tariff rebalancing process and the possible need for new adjustments to the price caps.

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 will be important to Telecom Italia's competitive position.

Pricing Policy and Telecom Italia's Tariffs

Tariff Rebalancing. The Ministry of Communications recognizes the need to attain a more balanced pricing structure. Telecom Italia, which commenced rebalancing in 1991 with further adjustments to its tariff structure approved by the Ministry of Communications in 1993, 1994, 1996, 1997 and 1998, and by the National Regulatory Agency in 1999 and 2000, has progressively rebalanced its 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 1:4 for reduced rate calls and 1:6 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% and 4.5% in 1996, 1997 , 1998, 1999 and 2000, respectively, compared to inflation rates as set forth in the table below.

	Year ended December 31					
	1995	**1996**	**1997**	**1998**	**1999**	**2000**
			(%)			
Inflation Rate	5.4	3.9	1.7	1.8	1.7	2.5

This rebalancing has been accompanied by a simplification of the tariff structure which has reduced the number of tariff schemes and aims to clarify 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 has been 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 UK, 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) on tariff rebalancing. 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 and whose 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%)

Moreover, Telecom Italia has announced the following changes:

- from July 1, 2001:

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

    - decrease in long distance prices (- 10.6%)

On January 12, 1999, the National Regulatory Agency stated that Telecom Italia is responsible for fixing fixed-to-mobile calls 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 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.

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.

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 (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 . When initially issued, EU Directive 90/388 did not apply to radio mobile services or to satellite services. As discussed below, subsequent amendments to EU Directive 90/388 extended its terms to cover such services. 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 Commission intends to adopt the Directive after having heard the comments of all interested parties.

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.

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 only be limited 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. State of Play and the Way forward.

In March 2001, the Commission published a Communication concerning the introduction of Third generation Mobile Communications in the European Union. The Communications 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.

Electromagnetic fields

In July 1999, the Council adopted a recommendation on the limitation of exposure of the general public to electromagnetic fields O Hzr-300 GHZ. 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.

Terminal Equipment

EU Directive 88/301 (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 ONP Directives

The EU directive relating to 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 concern the supply and the use of the network, technical characteristics and tariff principles. 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, replaced 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 and licenses (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 pricing of 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.

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

The Commission has 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. These studies started in the first half of 1999 and were expected to be completed by the end of 1999.

The following five European Commission draft proposals for new directives, called "Working Documents" (the Working Document is a transitory draft proposal presented by the Commission before the public consultation period ended on May 19, 2000; the formal draft directive proposals were adopted by the Commission in July 2000).

- a common regulatory framework for electronic communications networks and services;
- the authorization of electronic communications networks and services;
- access to, and interconnection of, electronic communications networks and associated facilities;
- universal service and users' rights relating to electronic communications networks and services; and
- the processing of personal data and the protection of privacy in the electronic communications sector.

In Spring 2001, the first lecture of both the European Parliament and the Council was completed. The procedure is expected to end by the end of 2002, and should be implemented at national level by 2003.

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

In the proposal, 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. On the basis of art. 14 of the proposed Directive on a Common Framework for Electronic Communications Network and services, 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 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 as defined in art. 13 of the proposed Directive. Operators having significant market power may be subject to obligations under other Directives in the regulatory package. Adoption of definitive version of the Guidelines would take place when the Framework directive is finally adopted. The Guidelines will be updated if necessary.

Draft Directive on Authorizations. The Working Document on authorizations 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.

Any notification should contain no more than the following elements:

- a declaration of the intention to start operation;
- the coordinates of the undertaking;
- 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.

Draft Directive on Access and Interconnection. The draft proposal for a directive on access to, and use of, electronic communications networks and associated facilities 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 proposal, national regulatory agencies would 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 proposal.

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 would 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 would 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 would 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.

Draft Directive on Universal Service. A new universal service directive is proposed to replace the existing directive on voice telephony and universal services. The draft proposal also contains rules on number portability, carrier selection and carrier pre-selection which are currently in the Interconnection Directive. The draft proposal 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 would remain in place, at least for the time being. The principal changes proposed 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.

It is also proposed to extend the requirement for number portability to mobile operators.

As a mandatory service, Member States would be required to ensure that all schools have access to Internet at transparent and cost oriented tariffs, with NRAs 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 on going.

Leased Lines Pricing

In the context of the growing debate on prices for leased lines in the EU, the Commission has 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 nationale 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, NRAs 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 the Local Loop Unbundling (LLU) distinct from the proposal for a Directive on Interconnection and Access.

The proposed Regulation 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. The Regulation 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 NRAs determines 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.

Proposal for a decision on a 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 proposal seeks to complement, rather than to replace, the spectrum management activities of ITU/WRC and CEPT and of the member States.

In November 1999, the Commission published a Communication from the Commission to the European Parliament, the Council, the Economic and Social Committee and Committee of regions on the "Development of the Market for Digital Television in the EU", Report in the context of Directive 65/47/EC on the use of standards for the transmission of television signals.

Commission revised notice on the provision of voice services over the Internet (December 20, 2000)

On January 10, 1998 the Commission published a notice on the status of voice communications on Internet under Community law and, in particular, pursuant to Directive 90/388/EEC. This notice was a supplement to the Commission communication of 20 October 1995 to the European Parliament and the Council on the status and implementation of Directive 90/388/EEC on competition in the markets for telecommunications services.

On December 22, 2000, the Commission published the communication on status of voice on the Internet under Community law, as a supplement to the above-mentioned communication. After public consultation, the Commission concluded that under the current legal framework provided by the Services Directive, no substantial changes are needed to the 1998 notice.

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 justified. 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 EU 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 aim 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. The adoption by the Council is expected by the middle of 2001.

Moreover, the EU Commission proposed in November 2000 a proposal for a Directive on the harmonization of the rules of invoicing for VAT purposes. This proposal amends the existing provision on VAT invoices contained in the VI VAT directive to take account of electronic commerce. The adoption is expected by the end of 2001.

Legal aspects of electronic commerce

In June 2000 the Council and the European Parliament adopted Directive 2000/31/EC on certain legal aspects of electronic commerce in the internal market. The directive seeks to clarify some legal concepts and harmonize certain subject matters in order to enable information society services to fully benefit from the free movement of services within the internal market. The deadline for member states for implementing the directive is January 17, 2002.

On February 9, 2001 the Commission published a Communication on electronic commerce and financial services. The communication makes proposals on how to establish an integrated European market in financial services by 2005 by harmonizing contractual and non contractual rules, encouraging consumer confidence in cross border redress and internet payments and increasing the monitoring of cross border financial services.

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 EP vote in Plenary is expected in July or September 2001.

Copyrights

In April 2001, the Council adopted the Directive on copyright and related rights in the Information Society. The deadline for implementation of the Directive in the member States is within 18 months from the publication in the Official Journal. The directive deals both legal and technical aspects.

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.

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 Lit. 730 billion or the turnover of the company being acquired is, in Italy, higher than Lit. 73 billion, 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 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.

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.

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 ("Regulation implementing Articles 81 and 82 of the Treaty"), 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; the strengthening of Commission's investigation powers.

Under Regulation 17/62 (regulation implementing articles 81 and 82), 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.

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.

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.

DECT (Digital Enhanced Cordless Telecommunications): A radio technology, using a frequency of 1900 MHZ, for access to a private or public telecommunications network enabling subscribers in urban areas to utilize cordless equipment, with the same telephone number as their fixed line telephone, both inside and, within a limited range, outside their home.

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.

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 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, 2000, the Group owned approximately 8000 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 Turin in a building which it rents from a subsidiary 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, 2000, telecommunications installations, including local and domestic long distance networks and radio transmission equipment represented approximately 77% of the fixed assets of the Group. Land and buildings represented 13%, plant under construction, advances to suppliers and stock for fixed assets represented 6%, and furniture, office equipment and other equipment, technical installations and machinery comprised the remaining 4%.

As of December 31, 2000, the total amount of liens and mortgages on real property owned by the Group was Lit. 402 billion. Such liens and mortgages 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. On November 23, 2000, Telecom Italia announced that it had 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. Pursuant to the agreement with Beni Stabili and Lehman Brothers, Telecom Italia sold to its two partners 60% of IM.SER S.p.A., a joint stock company formed by Telecom Italia to hold a portion of its real estate assets. As a result Beni Stabili acquired a 45% interest of IM.SER and Lehman Brothers acquired 15%. On May 16, 2001 Beni Stabili exercised an option to buy the Lehman Brothers' stake in IM.SER. Currently Beni Stabili has a 60% stake in IM.SER and Telecom Italia, a 40% stake.

The real estate portfolio held by IM.SER consisted of 581 properties, totaling 3.7 million square meters, divided into:

- 386 properties ("Real Estate Investment Portfolio"), totaling approximately 2.4 million square meters, located throughout Italy, mainly in the regions of Lombardia (20%), Lazio (14%) and Piemonte (11%). All the properties, including buildings that contain telecommunications equipment, will be leased to Telecom Italia under-long term lease contracts (21 plus 6 years) at market rates; and

- 195 properties ("Real Estate Trading Portfolio"), totaling approximately 1.3 million square meters, located throughout Italy, mainly in the regions of Lazio (19%), Lombardia (16%), Campania (8%) and Piemonte (8%). 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. Such early termination clauses will allow Telecom Italia to vacate approximately 1,000 properties in the next five years.

As a result of the transaction, Telecom Italia received approximately Lit. 5,228 billion in cash.

In May 2001, IM.SER contributed its Real Estate Trading Portfolio to Telemaco, a newly formed company. Following such contribution, IM.SER distributed the shares of Telemaco, to its shareholders. The shareholders of Telemaco are Beni Stabili with a 45% stake, Telecom Italia with a 40% stake and Lehman Brothers with a 15% stake.

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.

Background

Market Developments

Dimensions and dynamics of the Italian market for telecommunications services. In 2000, the Italian telecommunications market grew by 13.4%, with revenues of more than Lit. 61,000 billion (source: Dataquest). 47% of the total market was attributable to fixed line telephone services, 40.6% to wireless telephone services and 12.4% to the data transmission/Internet segment.

The greatest contributor to the increase was wireless services, with an increase in the number of subscribers of 38.4% and a rise in revenues of 25.4%. With over 42 million subscribers at the end of 2000, Italy is the second largest market in Europe (behind Germany with over 47 million subscribers); although the level of penetration (calculated as the number of customers of mobile telephone services to population) reached 73.3% and is the highest together with Finland. During 2000, the number of mobile telephones continued to grow faster then the number of fixed telephones, with wireless connections now representing 60.3% of total connections.

The Internet market increased from 8.2 million subscribers at the end of 1999 to 14.1 million at the end of 2000 (an increase of 72%). Despite the considerable increase generated by free access and specific commercial offers (such as "E vai!" promoted by Tin.it), the level of penetration (25%) remains below the European average, with room for growth. Average annual growth rates in Italy are forecasted to be 27% compared to 22% for the rest of Western Europe.

Competitive pressure in the Italian market continued during 2000, as evidenced by the following:

- issue of licenses for fixed networks and voice telephony service, which rose from 89 at the end of 1999, to 151 at the end of 2000;
- awarding of the fourth license to operate a mobile telephone network in July 1999 which operator began commercial operations in May 2000;
- 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, WAP 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.

Market and structural changes in the telecommunications sector. In 2000 and in the first few months of 2001, the telecommunications sector was characterized by the following notable developments:

- further increase in competitive pressure on national fixed phone services markets, resulting in further losses of market shares by the main operator (Telecom Italia);
- the continuation of the trend of "grouping" mobile operators (Vodafone/Mannesmann, France Telecom/Orange, Deutsche Telekom/Voicestream); currently, the European mobile market is dominated (66%) by 6 large operators;
- the start of radical restructuring on the part of former monopoly operators, geared toward rationalizing activities by creating Business Unit and then listing them on the stock exchange;
- the resumption of investments to develop broadband infrastructures, the migration towards networks of the new generation, the acquisition of UMTS licenses and network development with the aim of seizing opportunities offered by the growth of Internet and data traffic;
- the acceleration of broadband access network offerings, particularly using ADSL technology;
- the development of value-added services offerings on the part of mobile operators and the start of wireless portals (WAP);
- the large number of new operators of the Internet/Application Service Provider type, and new portals;
- significant debt levels of telecommunication operators largely incurred to fund UMTS licenses; and
- weak market conditions for asset sales and significantly lower valuations for telecommunication assets.

Competition

Domestic competition has been introduced in all of the Group's businesses, including the provision of fixed line and mobile voice telecommunications services and the operation of networks to support the provision of such services which has been fully liberalized and opened to competition since January 1, 1998. The proportion of the Group's gross revenues from telecommunications services that are open to competition (including competition from by-pass and call-back service providers for international traffic) has been 100% since 1998. See "Item 4. Information on the Company—Business—Strategy" and "Business—Competition".

Although 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 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, 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, (iv) continued focus on customer service, quality and marketing initiatives, including the introduction of innovative tariff packages targeted at specific segments of the market and (v) growth of the Italian economy. However, 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 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.

In the domestic fixed line 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.

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 to decrease by 10% although the total market has grown with a penetration rate of 73.3% at the end of 2000.

Sale of Non-Core Assets and Cost Reduction Plan

In September 1999 the Telecom Italia Board of Directors approved the guidelines for a restructuring plan of certain group assets. 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. The operating results for Sirti and Italtel have been included in the Group's consolidated results of operations through September 30, 2000.

These sales did generate approximately Lit. 8,545 billion in cash used to reduce the level of indebtedness incurred as a result of various acquisition and other investment activities during 2000. See "Liquidity and Capital Resources."

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 8,000, including approximately 9,500 permanent reductions in the fixed line business and approximately 18,000 due to dispositions (offset in part by acquisitions and change in scope of consolidation).

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 2000 continued to be characterized by an intensive implementation process in order to complete the liberalization. Throughout 2000 there were extensive negotiations with the National Regulatory Agency regarding conversion of Telecom Italia's Public Concessions into Licenses and local loop unbundling as well as certain other continuing changes in the regulatory environment. See Part 1 - "Item 4. Information on the Company — Business — Competition" and "Business — Regulation".

Public Concessions

Pursuant to an order of the National Regulatory Agency notified to Telecom Italia on January 19, 2001, certain of the Public Concessions under which Telecom Italia had been operating were converted into licenses ("Licenses"). The general effect of the new Licenses is to reduce certain public service obligations and regulatory constraints that were previously applicable to Telecom Italia. Public Concessions applicable to TIM are currently in the process of conversion into licenses. The conversion had no impact on the Group's operations in 2000. See Part I — "Item 4. Information on the Company — Business—Regulation."

Local Loop Unbundling

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.

Although local loop unbundling is expected to increase competition for the provision of certain services, the effect of local loop unbundling is not expected to have a significant impact in 2001.

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 and 2000. Further tariff adjustments were approved by the National Regulatory Agency and implemented effective February 1, 2001. 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.

The overall effect on customers' total telephone bills of the tariff adjustments implemented during 1997, 1998, 1999 and 2000 are estimated as follows:

- Lit. 600 billion (a decrease of 3%) in 1997;
- Lit. 300 billion (a decrease of 1.6%) in 1998;
- Lit. 800 billion (a decrease of 4.1%) in 1999; and
- Lit. 860 billion (a decrease of 4.5%) in 2000.

These estimates are not cumulative and are based on certain average consumption patterns (namely consumption baskets 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.

For the year 2000, the first year of real application of the price-cap mechanism, the effective reduction in revenues was approximately Lit. 490 billion (a decrease of 2.8%).

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 is 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 provides 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 price-cap mechanism is expected to result in, assuming the same volume of traffic as in 2000, lower revenues for residential and business users of approximately Lit. 320 billion in 2001.

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—Telecommunications Services—Domestic Telecommunications Services—Tariff Rebalancing", "—International Telecommunications Services—Tariff Rebalancing" and —"Regulation—Tariff and Pricing Policy—Pricing Policy and Telecom Italia's Tariffs".

Globalization

Increasing globalization and liberalization of the telecommunications industry and telecommunications markets have created new opportunities for the Group to expand outside Italy. Globalization of the telecommunications industry is also subjecting the Group to competition in Italy and elsewhere from international telecommunications operators and competing global alliances.

Results of Operations

General

Due to the reorganization implemented in 1999 (See "Item 4. Information on the Company—Business—Overview of the Group's Operating Revenues by Major Business Area"), the Group's operating revenues have been generated principally from five separate but related business areas during 2000: (i) fixed line services in Italy; (ii) mobile services in Italy; (iii) satellite services; (iv) international telecommunications services; (v) and IT software and services. Through September 30, 2000, and in prior years Telecom Italia also generated revenues from manufacturing (Italtel) and installation (Sirti) activities. During 2000 Telecom Italia disposed of its manufacturing and installation activities effective as of September 30, 2000.

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 is fully consolidated for balance sheet purposes at December 31, 2000, SEAT's results of operations are not included in the Group's income statement for purposes of Italian GAAP. As a result, beginning in 2001 the impact of the SEAT acquisition will effect comparative period results of operations. See "Item 8. Financial Information — US GAAP Unaudited Pro Forma Condensed Consolidated Statement of Income for the Year Ended December 31, 2000" for a presentation of the pro forma effect of the acquisition of SEAT/Tin.it merger on the U.S. GAAP historical operating results of Telecom Italia for the year ended December 31, 2000 as if such transaction had occurred on January 1, 2000.

For 2000, under Italian GAAP, SEAT reported operating revenues of euro 1,333 million, gross operating profit of euro 408 million and a net loss after minority interest of euro 0.9 million. See also the discussion under "Consolidated Financial Statements as of and for the Year Ended December 31, 2000 — Reconciliation of Italian GAAP to US GAAP" for a discussion of certain US GAAP adjustments associated with the SEAT/Tin.it transaction which had a material impact on the US GAAP net income and stockholders equity of Telecom Italia in 2000.

Late 2000 marked the start of the transformation of the Telecom Italia Group announced in conjunction with the take-over by Olivetti. The transformation has been 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 and, above all, the reorganization of the seven autonomous Business Units from the standpoint of management, objectives, strategies and operational leverage. Beginning with 2001 the Group is reporting its results on the basis of these new segments. The discussion which follows is based on the Group's segments as they were managed and operated through 2000. For a discussion of the new business segments see "Item 4. Information on the Company—Business—Recent Developments—Telecom Italia Group Results for the First Quarter Ended March 31, 2001."

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 2000 also include the associated companies Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group) and Viasat and its subsidiary Viasat Assistance (Viasat group). Nortel Inversora group and Viasat group have been proportionately consolidated on a line-by-line basis, in accordance with Italian Law 127/1991, Article 37. Prior to this year the Nortel Inversora group was accounted for on the equity method. 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 interest income or interest expense. See Notes 21 and 22 of Notes to the Consolidated Financial Statements included elsewhere herein.

The SEAT Group, Jet Multimedia group, Mageos, Corporacion Digitel and Maxitel group, acquired in the last part of fiscal 2000, are included within the scope of consolidation only for balance sheet purposes as of December 31, 2000 and the Sirti group and Italtel group, disposed of during the last part of the fiscal 2000, are consolidated only in the statement of income for the period from January 1, 2000 to September 30, 2000.

The following table sets forth the Group's statement of income for the years ended December 31, 1998, 1999 and 2000.

	Year ended December 31,			
	1998		1999	2000(2)
	(in billions of Lit.)			
Operating revenues	48,507	(1)	52,481	55,979
Other income	1,085		998	826
Total revenues	49,592	(1)	53,479	56,805
Cost of materials	4,535		4,795	4,373
Salaries and social security contributions	9,665		9,636	9,729
Depreciation and amortization	10,480		10,338	10,933
Other external charges	17,552	(1)	18,561	20,893
Changes in inventories	262		(251)	(537)
Capitalized internal construction costs	(2,088)		(2,056)	(1,765)
Total operating expenses	40,406	(1)	41,023	43,626
Operating income	9,186	(1)	12,456	13,179
Interest income	1,579		1,073	1,636
Interest expense	(1,681)		(2,837)	(4,779)
Other income and expense, net	133	(1)	(981)	(415)
Income before income taxes	9,217		9,711	9,621
Income taxes	(3,965)		(5,046)	(3,912)
Net income	5,252		4,665	5,709
Minority interest	(1,422)		(1,301)	(1,782)
Net income, after minority Interest	3,830		3,364	3,927

(1) Beginning in 1999 Telecom Italia changed the way in which it accounts 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 and other external charges have been increased by the same amount: Lit. 3,042 billion in 1998. This accounting change has had no impact on reported net income for 1998. In 1998, the item "other external charges" also takes into account additional expenses (Lit. 19 billion) included in "other income and expense, net" in Telecom Italia's 1998 consolidated financial statements.

(2) Beginning January 1, 2000, under Italian GAAP the Nortel Inversora group has been consolidated using the proportional method. Prior to this year the Nortel Inversora group was accounted for on the equity method.

Revenues

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services. Since 1999 domestic telecommunications services are segmented as follows: fixed line services managed by Telecom Italia, mobile services conducted by TIM and satellite services provided by Telespazio.

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, SIN and SMH. In late December 2000, Telecom Italia completed the reorganization of its international activities. As a result of the reorganization, Telecom Italia now owns 100% of SIN, the primary vehicle through which the Telecom Italia Group holds its international wireline investments and TIM owns 100% of SMH, the primary vehicle for international wireless investments. The reorganization has no significant impact on the consolidated financial results of the Group although it increased goodwill by approximately Lit. 400 billion.

The Group now has a significant presence in the internet media market through SEAT. For purposes of Italian GAAP the results of this segment will only be included in the consolidated statement of income beginning in 2001.

The Group is also present in information technology software and services provided by the companies FINSIEL, Netsiel, Telesoft and Sodalia. As of 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. The companies mentioned, together with the Information Technology function of Telecom Italia, make up the "Information Technology Services" Business Unit. In 2001, their activities will come under the control of Telecom Italia Information Technology, a company 100% owned by Telecom Italia, set up in the second half of 2000 with the aim of ensuring the coordination of the information technology activities distributed throughout the various companies.

The Group sold its manufacturing activities conducted by Italtel and the installation activities conducted by Sirti during 2000 although the results for Italtel and Sirti are included in the Group's consolidated results through September 30, 2000.

The composition of the Group's business segments has changed beginning in 2001. For a discussion of these new segments see "Item 4. Information on the Company—Business—Recent Developments—Telecom Italia Group Results for the First Quarter Ended March 31, 2001."

The table below sets forth the gross operating and consolidated operating revenues of each major business area and the other activities of the Group for the last three years and the percentage contribution of such business area to the Group's consolidated operating revenues:

	Year ended December 31,								
	1998(1)			1999(1)			2000(2)		
	Gross Operating Revenues (3)(4)	Consolidated Operating Revenues (4)(5)	% Consolidated Operating Revenues	Gross Operating Revenues (3)	Consolidated Operating Revenues (5)	% Consolidated Operating Revenues	Gross Operating Revenues (3)	Consolidated Operating Revenues (5)	% of Consolidated Operating Revenues
	(in billions of Lit., except percentages)								
Fixed line services Italy	36,292	31,080	64.1	35,856	30,953	59.0	33,723	29,419	52.6
Mobile services Italy . .	11,904	11,094	22.9	14,425	13,722	26.1	15,352	14,701	26.3
Satellite services	739	534	1.1	619	443	0.8	659	509	0.9
International telecommunications services	1,520	1,273	2.6	3,253	3,069	5.8	7,615	7,435	13.3
IT software and services	2,566	1,916	3.9	3,074	2,127	4.1	3,137	2,164	3.8
Manufacturing (6)	1,975	1,041	2.1	1,776	959	1.8	1,221	385	0.7
Installation (7)	2,165	1,220	2.5	1,501	837	1.6	1,165	772	1.4
Other activities	1,019	349	0.8	1,154	371	0.8	1,307	594	1.0
Total operating revenues	58,180	48,507	100.0	61,658	52,481	100.0	64,179	55,979	100.0

(1) 1998 and 1999 gross operating revenues and consolidated operating revenues of each major business area and other activities of the Group are restated and presented consistent with the presentation of 2000 gross operating revenues and consolidated operating revenues.

(2) Beginning January 1, 2000, under Italian GAAP the Nortel Inversora group has been consolidated using the proportional method. Prior to this year the Nortel Inversora group was accounted for on the equity method.

(3) 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).

(4) Beginning in 1999 Telecom Italia changed the way in which it accounts for revenues from telecommunications services, calculating such revenues gross of interconnection and service charges payable to other operators and service providers. As a result, the gross operating and consolidated operating revenues for the year ended December 31, 1998 have been reclassified. Due to this change, operating revenues from fixed line services Italy and other external changes have been increased by the same amount: Lit. 3,042 billion 1998. This accounting change had no impact on reported net income for 1998.

(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 results of operations for Italtel for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group. The figures are not directly comparable, therefore, 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. Until 1998 Italtel Group was proportionately consolidated at 50%.

(7) In December 2000, Telecom Italia disposed of its interest in Sirti. Only the results of operations for the first nine months of 2000 have been included in the 2000 consolidated financial statements of the Telecom Italia Group. Therefore, the figures are not directly comparable to those of previous years.

The following table sets forth, for the periods indicated, certain selected statistical data of Telecom Italia and TIM.

	Year ended December 31,		
	1998	1999	2000
Subscription and Customers:			
Subscriber fixed lines at period-end (thousands)(1)	25,986	26,502	27,153
Subscriber fixed line growth (%)	1.1	2.0	2.5
Subscriber fixed lines per full-time equivalent employee at period-end(2)	332	354	409
ISDN equivalent lines at period-end (thousands)(3)	1,735	3,049	4,584
Mobile customers at period-end (thousands)(4)	14,299	18,527	21,601
Mobile customers growth per annum (%)	54.1	29.6	16.6
Average revenue per mobile customer per month (Lit.)(5)	77,600	67,600	59,100
Cellular penetration at period-end (TIM customers per 100 inhabitants)(%)	25.0	32.5	37.5
Cellular market penetration at period-end (customers for the entire market per 100 inhabitants) (%)	36.0	53.1	73.3
Internet subscribers (6) (thousands)	396	1,990	3,997
Traffic:			
Average minutes of use per fixed line subscriber during period(7)	4,259	4,313	4,753
Of which:			
Local traffic during period (in average minutes) (8)	2,628	2,782	3,234
Long distance traffic during period (domestic and international) (in average minutes)	1,631	1,531	1,519
Growth in international incoming and outgoing traffic in minutes (9)	9.5	9.8	5.4
Total mobile outgoing traffic per month (in millions of minutes)	839	1,219	1,569

(1) Data includes multiple lines for ISDN and excludes internal lines.

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

(3) Data excludes internal lines.

(4) TIM only.

(5) Including Prepaid Customers' revenues and excluding equipment sales.

(6) Tin.it only.

(7) Includes total fixed outgoing traffic (including international outgoing traffic and fixed outgoing traffic to the mobile networks).

(8) Not including district traffic.

(9) 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.

Year ended December 31, 2000 compared with Year ended December 31, 1999.

Consolidated Operating Revenues

The Group's consolidated operating revenues grew by 6.7% in 2000 compared to 1999. The growth in consolidated operating revenues was primarily attributable to a 142% increase in revenues from international telecommunications services (from Lit. 3,069 billion in 1999 to Lit. 7,435 billion in 2000) substantially all of which increase is due to the first time proportional consolidation of Nortel Inversora group. The Group's consolidated operating revenues also benefitted from a 7.1% increase in mobile services revenues in Italy. These increases more than offset the decrease in revenues from fixed line services in Italy which declined by 5.0% as well as the decline in revenues from manufacturing and installation companies which were sold during 2000.

Telecommunications Services Revenues

The table below sets forth, for the periods indicated, gross operating revenues from telecommunications services.

	Year ended December 31,	
	1999	2000
	(in billions of Lit.)	
Fixed line services Italy	35,856	33,723
Mobile services Italy	14,425	15,352
International telecommunications services	3,253	7,615
Satellite services	619	659

Fixed Line Services Revenues Italy

Revenues from fixed line services in Italy consists mainly of revenues from domestic and international traffic. Gross operating revenues from fixed line telecommunications services decreased by 5.9% 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 27.3%. 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 Lit. 71 per minute in 2000 compared to Lit. 111 per minute in 1999, a 35.8% decrease which translates into a revenue loss of approximately Lit. 5,006 billion. Other income includes sales revenues (Lit. 687 billion), telephone cards (Lit. 166 billion), and other less important revenues. Sales revenues, down by Lit. 333 billion (a decrease of 32.7%) 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 (3,048,900 lines at the end of 1999 and 4,583,500 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). Telecom Italia expects internet-related revenues will 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 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 has 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 over 2.2 million customers by the end of 2000, and 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 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 24.1 % 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 Lit. 29,419 billion in 2000 and Lit. 30,953 billion in 1999.

Mobile Services Revenues Italy

Gross operating revenues from mobile services in Italy increased by 6.4% in 2000 compared to 1999. This increase is attributable principally to the strong performance of TIM, despite increasing competition with increasing levels of revenues attributable to value added services.

Mobile telecommunications customers increased to 21,601,000 customers at December 31, 2000, a 17% increase compared to December 31, 1999. TIM's GSM customer base increased by 24.8% in 2000, to 19,156,000 customers at December 31, 2000, while TIM's TACS customer base decreased by 23.0% in 2000, to 2,445,000 customers at December 31, 2000 in each case compared to December 31, 1999. Approximately 89% of TIM's customer lines are now GSM lines. The continuing significant growth in GSM customers 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 users by December 31, 2000 compared to 12,909,000 users 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 is 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.

Mobile traffic volumes increased by 24.6% in terms of minutes and mobile traffic revenues increased by 9.8% in 2000 (Lit. 12,820 billion) compared to 1999 (Lit. 11,672 billion). 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 customer (which includes traffic revenues and subscription fees) decreased from approximately Lit. 67,600 in 1999 to Lit. 59,200 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.

Revenues from equipment sales decreased by 13.0% in 2000 (Lit. 1,180 billion) compared to 1999 (Lit. 1,357 billion). The mobile subscription fees decreased by 29.6% in 2000 (Lit. 288 billion) compared to 1999 (Lit. 409 billion) due to the continuing sharp expansion in the prepaid service customer base, where no subscription fees are paid.

Revenues from value added services (VAS) (Lit. 658 billion 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. These trends are expected to continue in 2001. 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 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. This rate is expected to continue to rise as a result of increasing competition.

Consolidated operating revenues were Lit. 14,701 billion in 2000 and Lit. 13,722 billion in 1999.

International Telecommunications Services Revenues

Gross operating revenues from international telecommunications services increased by 134.1% in 2000 compared to 1999 (plus 25.5% on a comparable consolidation basis), benefitting mainly from the first time proportional consolidation of Nortel Inversora Group and the growth of mobile services.

Revenues from the Nortel Inversora Group, through Telecom Argentina, were Lit. 7,068 billion in 2000 (Lit 3,534 billion of which are proportionately consolidated with the Group's results). The 2000 revenues represented an increase of 2.5% over 1999 (in 1999 the Nortel Inversora Group was accounted for on an equity basis). The increase is largely attributable to the contribution of mobile telephone services (plus 14% in 2000 compared to 1999) and data services (plus 28% in 2000 compared to 1999). At the end of 2000 Telecom Argentina had accumulated 3.5 million fixed line subscribers (approximately a 45% market share) and approximately 2 million mobile customers (a market share of around 32%).

Increased revenues from the Group's investments in Brazil also contributed to the increase in international telecommunications revenues. Tele Nordeste Celular Participacoes, first consolidated in 1999, had revenues of Lit. 1,024 billion 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 in customers. Tele Celular Sul Participacoes, also first consolidated in 1999, recorded revenues of Lit. 863 billion, a 4.7% increase over 1999 in Brazilian reias.

Revenues from Entel Bolivia increased by 8.3% in 2000 to Lit. 446 billion compared to Lit. 412 billion in 1999.

Revenues from STET Hellas amounted to approximately Lit. 1,019 billion in 2000, representing an increase of 17% over 1999 (based on local currency). This growth reflected 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.

Revenues from TMI decreased by 12% in 2000 to Lit. 264 billion, compared to Lit. 300 billion in 1999, brought about by the launch of the new commercial strategy. In 2000, revenues from 9Télécom Reseau amounted to Lit. 185 billion (five times the figures of 1999 in French francs) and Intelcom San Marino had revenues of Lit. 111 billion, with an increase of 147% compared to 1999 (Lit. 45 billion).

At the beginning of 2001 Telecom Italia acquired control of Entel Chile which will be fully consolidated from first quarter 2001.

Consolidated operating revenues were Lit. 7,435 billion in 2000 and Lit. 3,069 billion in 1999.

Satellite Services Revenues

Gross operating revenues from satellite services increased by 6.5% (Lit. 659 billion) in 2000 compared to 1999 (Lit. 619 billion). Revenues from Viasat have been reclassified to "other activities" for 2000 and 1999 as the company was taken over by SEAT as part of the SEAT-Tin.it transaction. This increase is principally due to the results of the Telespazio group which recorded increased results in its "space systems and services" business unit due to the positive impact of the Artemis and Sax projects. The "Media & Communications" business unit, though operating in a mature competitive market, achieved results substantially consistent to 1999. Increased revenues from the television sector offset the negative impact of price declines on telecommunications revenues.

Consolidated operating revenues were Lit. 509 billion in 2000 and Lit. 443 billion in 1999.

IT Software and Services Revenues

The table below sets forth, for the periods indicated, gross operating revenues from the IT software and services segment.

	Year ended December 31,	
	1999	2000
	(in billions of Lit.)	
IT Software and Services gross operating revenues	3,074	3,137

Gross operating revenues from this segment increased by 2.0% from Lit. 3,074 billion in 1999 to Lit. 3,137 billion in 2000. Gross operating revenues grew due to a 2.5% increase in revenues from the FINSIEL Group (Lit. 2,259 billion in 2000 compared to Lit. 2,204 billion in 1999) and to a 6.6% increase in revenues from Telesoft (Lit. 808 billion in 2000 compared to Lit. 758 billion in 1999), which develops software applications for telecommunications services. 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 is also attributable to new activities such as development and system integration services, enterprise resources planning projects, e-business and training on-line services. Gross operating revenues from Telesoft increased due to the development of Group activities and international markets where the Group is already operating (Spain, Latin America and Greece).

Consolidated operating revenues were Lit. 2,164 billion in 2000 and Lit. 2,127 billion in 1999.

Manufacturing and Installation Revenues

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 are 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).

	Year ended December 31,	
	1999	2000
	(in billions of Lit.)	
Manufacturing gross operating revenues	3,114	1,221
Installation gross operating revenues	1,501	1,165

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 Lit. 1,221 billion in 2000 compared to Lit. 1,776 billion in 1999). Revenues for the first nine months of 2000 were Lit. 1,221 billion, due in part to the significant contribution of activities conducted on foreign markets.

Consolidated operating revenues for the manufacturing and installation businesses were Lit. 1,157 billion in 2000 and Lit. 1,796 billion in 1999.

Operating Expenses

The table below sets forth, for the periods indicated, Telecom Italia's total operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31,			
	1999		2000	
	(in billions of Lit., except percentages)			
Cost of materials	4,795	9.1%	4,373	7.8%
Other external charges	18,561	35.4%	20,893	37.3%
Personnel costs (salaries and social security contributions)	9,636	18.4%	9,729	17.4%
Changes in inventories	(251)	(0.5)%	(537)	(0.9)%
Capitalized internal construction costs	(2,056)	(3.9)%	(1,765)	(3.2)%
Depreciation and amortization	10,338	19.7%	10,933	19.5%
Total operating expenses	41,023	78.2%	43,626	77.9%

The Group's operating expenses increased by 6.3% in 2000 compared to 1999 due to the changes in the scope of consolidation (mainly the Nortel Inversora group) and the expansion of mobile telecommunications services, partially offset by cost containment programs in the fixed line business where costs were reduced. The increase in operating expenses, mainly due to the expansion of the Group's activities, was also reflected in the Lit. 1,963 billion 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 77.9% and 78.2% in 2000 and 1999, respectively. The decrease in operating expenses as a percentage of gross operating revenues is due primarily to the reduction of costs at Telecom Italia only partially offset by the change in scope of consolidation to include the Nortel Inversora Group and the higher costs in the mobile telecommunications services associated with the increase of the related activities.

Cost of Materials

Cost of materials decreased by 8.8% 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. Such decrease was partly offset by the inclusion in the scope of consolidation of Nortel Inversora.

Other External Charges

The table below sets forth, for the periods indicated, Telecom Italia's other external charges broken down by major components.

	Year ended December 31,	
	1999	2000
	(in billions of Lit.)	
Costs of external services rendered	14,289	16,252
Write-downs of fixed assets and intangibles	142	93
Provision for bad debts	702	924
Rent and lease payments	1,363	1,546
TLC license fee	1,174	1,107
Provision for risk	155	231
Other provisions and operating charges	736	740
Other external charges	18,561	20,893

Other external charges increased by Lit. 2,332 billion in 2000 compared to 1999. These charges relate primarily to the telecommunications services segments and 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 13.7% in 2000 compared to 1999 mainly due to the inclusion of the Nortel Inversora 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 34.5% 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 13.4% in 2000 compared to 1999, mainly due to the inclusion of the Nortel Inversora Group in the scope of consolidation. Also, these costs more often arise out of mobile telecommunications services and increased with the expansion of TIM's activities.

- TLC license fee, which are principally payable to the Italian Government and are proportional to revenues, decreased by 5.7% 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 (Lit. 101 billion) and taxes other than income taxes (Lit. 270 billion), increased by 0.5% in 2000 compared to 1999.

Personnel Costs

Personnel costs (salaries and social security contributions) increased by 1.0% in 2000 compared to 1999, although, as a percentage of the Group's operating revenues, personnel costs declined to 17.4% in 2000 compared to 18.4% in 1999. Overall personnel costs increased following the changes in the scope of consolidation (Nortel Inversora group: an increase of Lit. 541 billion; Sirti group and Italtel group: a decrease of Lit. 367 billion) offset by the lower costs of Telecom Italia (a decrease of Lit. 186 billion) 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. At December 31, 2000, employees of the Group numbered 114,669 (122,662 at December 31, 1999), a decrease of 7,993 owing to personnel turnover and the effect of the change in the scope of consolidation. In particular, 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 10,316 units in international telecommunications, mainly for the Nortel Inversora group (an increase of 7,498) and Maxitel (an increase of 1,229), and the inclusion of the SEAT group (an increase of 7,515).

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 the Italy's telecommunications services of the Group. At December 31, 2000, Telecom Italia's potential range of liability for principal contribution was estimated to be between Lit. 1,900 billion and Lit. 2,500 billion (Lit. 509 billion 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. 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 by 14.2% 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 the Italtel Group.

Gross Operating Profit

The table below sets forth, for the periods indicated, the Group's 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")) by major business area and other activities and gross operating margin (gross operating profit as a percentage of operating revenues).

	Year ended December 31,			
	1999		2000	
	(in billions of Lit., except percentages)			
Fixed line services Italy	15,434	29.4%	14,552	26.0%
Mobile services Italy	6,734	12.8%	7,445	13.3%
Satellite services	91	0.2%	98	0.2%
International telecommunications services	635	1.2%	2,741	4.9%
IT software and services	405	0.8%	388	0.7%
Manufacturing	23	–	38	-
Installation	123	0.2%	107	0.2%
Other activities	501	1.0%	206	0.4%
	23,946	45.6%	25,575	45.7%
Consolidation adjustments	(273)	(0.5)%	(175)	(0.3)%
Total Gross Operating Profit	23,673	45.1%	25,400	45.4%

Gross Operating Profit increased by 7.3% in 2000 compared to 1999 (an increase of 1.5% on a comparable consolidation basis) and gross operating margin increased to 45.4% in 2000 from 45.1% in 1999. The overall increase in Gross Operating Profit was primarily attributable to the changes in consolidation to include the Nortel Inversora group and improved Gross Operating Profit from mobile telecommunications. The gross operating profit for the mobile services Italy increased because of continued revenue growth (an increase of 6.4%), improved mix of traffic and significant cost cutting. The improved mix of traffic is largely due to the increase in on-net traffic (i.e. calls made from TIM mobile phones to other TIM mobile phones), which rose to 30% of total traffic from 26% in 1999. Such traffic is not subject to interconnection fees and is therefore higher margin business. Increased efficiencies were achieved through generalized operating cost cutting and reduced network costs, the latter largely as a result of the introduction of half-rate codes. Such introduction greatly increased the operating capacity of the mobile network. These increases were partially offset by a decline in fixed line services in Italy, the Group's largest segment. The decline in Gross Operating Profit in the fixed line segment was principally attributable to the decrease in revenues due to increasing competition and competitive pressures leading to lower prices. The decline in revenues in the fixed line segment was only partially offset by reduced operating costs reflecting actions taken by the Group to contain costs in a highly competitive environment.

Depreciation and Amortization

Depreciation and amortization which is calculated on a straight line basis over the estimated useful lives of the assets, increased by 5.8% in 2000 compared to 1999. Depreciation of fixed assets increased by Lit. 316 billion or 3.8% to Lit. 8,741 billion in 2000 compared to Lit. 8,425 billion in 1999. The increase in depreciation of fixed assets was principally attributable to the change in scope of consolidation to include the Nortel Inversora group (an increase in depreciation of Lit. 740 billion) and higher levels of depreciation at TIM. These increases were only partially offset by a decrease in the depreciation charge of Telecom Italia (a decrease of Lit. 474 billion) 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. Amortization of intangible assets increased by Lit. 279 billion or 14.6%, from Lit. 1,913 billion in 1999 to Lit. 2,192 billion in 2000. This change is due to higher amortization at TIM (an increase of Lit. 102 billion compared to 1999), mainly as a result of the amortization of new investments in software, and the inclusion of the Nortel Inversora group in the scope of consolidation.

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 (Lit. 1,975 billion as of December 31, 1999 and Lit. 19,942 billion as of December 31, 2000). As a result, amortization of intangible assets in future periods is expected to be significantly higher than in recent historical periods. See "Item 4. Information on the Company — Business — Recent Developments — Telecom Italia Group Results for the First Quarter Ended March 31, 2001."

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
	(in billions of Lit.)	
Operating income	12,456	13,179

Operating income for the Group increased by 5.8% in 2000 compared to 1999 (+1.2% on a comparable consolidation basis). The increase in operating income is mainly attributable to the Nortel Inversora group (Lit. 726 billion) and the improved results of TIM (operating income increased by Lit. 423 billion), partly offset by the lower operating income of Telecom Italia (a decrease of Lit. 110 billion). As a percentage of operating revenues, operating income decreased in 2000 to 23.5% from 23.7% in 1999.

Interest Income, Interest 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
	(in billions of Lit.)	
Interest income	1,073	1,636
Interest expense	(2,837)	(4,779)
Other income and expense, net	(981)	(415)
Total financial expense, net and other income and expense, net	(2,745)	(3,558)

Total financial expense, net and other income and expense, net increased from a net expense of Lit. 2,745 billion in 1999 to a net expense of Lit. 3,558 billion in 2001, a 29.6% increase. Interest expense (which includes interest expense on financial indebtedness and income or loss from equity investments) increased by 68.4% . The increase is attributable to two principal factors:

- higher average borrowings outstanding during 2001 to finance the acquisition of SEAT as well as the inclusion of the Nortel Inversora Group in the scope of consolidation which resulted in an increase in interest expense increasing by Lit. 809 billion (Lit. 906 billion in 1999 and Lit. 1,715 billion in 2000). Interest expense on financial indebtedness is expected to increase in 2001 as overall levels of indebtedness remain relatively constant or increase slightly but short-term indebtedness is replaced with long term debt with higher average interest costs. See "— Liquidity and Capital Resources."

- higher levels of equity losses of investments in unconsolidated subsidiaries, affiliated and other companies (Lit. 1,984 billion in 2000 compared to Lit. 1,095 billion in 1999) 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 (Lit. 877 billion in 2000 and Lit. 356 billion in 1999). The increase in 2000 is attributable to the acquisition of SEAT (amortization of Lit. 423 billion) which was treated as an equity investment during 2000 and the acquisition of the Group's stake in Globo.com (amortization of Lit.

117 billion). Beginning in 2001, with full consolidation of the SEAT Group, amortization of goodwill from this investment will be included in depreciation and amortization and not in this line item. In addition, the increase is due to the losses incurred by the Maxitel group (Lit. 433 billion), Stream (Lit. 392 billion), Auna (Lit. 340 billion) and Telekom Austria (Lit. 101 billion).

Other income and expense, net decreased from a net expense of Lit. 981 billion in 1999 to a net expense of Lit. 415 billion in 2000. In 2000 such balance, among other things, includes gains on the disposal of investments, fixed assets and business segments (Lit. 2,219 billion). These gains offset the following:

- provision made by TIM to reserve for technological risk (Lit. 775 billion)
- the expenses and the provisions connected to the transactions for the disposal of investment holdings and the real estate portfolio (Lit. 349 billion)
- restructuring costs (Lit. 953 billion) principally related to Telecom Italia's costs for the corporate reorganization plan
- the social security charges (Lit. 297 billion) pursuant to Law No. 58/92 to guarantee uniform status under the former Fondo Previdenza Telefonici (FPT)
- the extraordinary annual contribution to INPS (Lit. 150 billion) to meet the higher financial requirements covered by the rules of the Fondo Previdenza Telefonici (FPT).

Income Taxes

Income taxes were Lit. 3,912 billion in 2000 compared to Lit 5,046 billion in 1999. The statutory income tax rate for 2000 and 1999 was 41.25%. Tax as a percentage of income before income taxes was 40.7% in 2000 and 52% 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 22.4% in 2000 compared to 1999. The increase was principally attributable to the increase in operating income and the significantly lower overall tax provision offset in part by an increase in financial expenses, net. Net income after minority interest was Lit. 3,927 billion in 2000 compared to Lit. 3,364 billion in 1999 a 16.7% increase. Minority interest increased from Lit. 1,301 billion in 1999 to Lit. 1,782 billion in 2000 mainly due to higher levels of profit at TIM.

Historical Year ended December 31, 1999 compared with Historical Year ended December 31, 1998.

Consolidated Operating Revenues

The Group's consolidated operating revenues grew by 8.2% in 1999 compared to 1998. The growth in consolidated operating revenues was primarily attributable to a 23.7% increase in revenues from mobile services in Italy, the first time consolidation of Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes (two Brazilian mobile telecommunications companies of which Telecom Italia acquired a controlling interest in 1999) and the increase in revenues from the Group's IT software and services segment, offset in part by the decrease in revenues from the fixed line services in Italy and the manufacturing and installation businesses.

Telecommunications Services Revenues

The table below sets forth, for the periods indicated, gross operating revenues from telecommunications services.

	Year Ended December 31,	
	1998	1999
Fixed line services Italy	36,292	35,856
Mobile services Italy	11,904	14,425
International telecommunications services	1,520	3,253
Satellite services	739	619

Fixed Line Services Revenues Italy

Revenues from fixed line services in Italy consists mainly of revenues from domestic and international traffic. Gross operating revenues from fixed line telecommunications services decreased by 1.2% in 1999 compared to 1998. This decrease resulted principally from a decline of 6.4% in revenues from traffic, in spite of an increase of 11.6% in terms of minutes. Although usage increased the tariff changes of January 6, 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 (+7.6% due to tariff increases, ISDN and connection with other carriers) and other income. Other income includes sales revenues (Lit. +57 billion), telephone cards (Lit. +59 billion), and other less important revenues. Revenues from interconnection access charges from the new fixed network carriers were Lit. 708 billion (Lit. 44 billion in 1998). Sales revenues, up by Lit. 57 billion (+6.0%) compared to 1998, mainly arise from sales of telephone and telematic products (special internal systems, facsimile machines, data transmission equipment and accessories).

The number of fixed line subscribers in Italy rose by 2% to approximately 26.5 million at December 31, 1999 representing a telecommunications density (fixed line subscribers to total population of Italy) of 46.1% at December 31, 1999, compared to 45.1% at December 31, 1998. The increase is mainly attributable to the increase in ISDN lines (1,753,300 lines at the end of 1998 and 3,049,000 lines at the end of 1999) which make up about 40% of total lines held by business customers.

The average minutes of use per fixed line subscriber increased 1.28% during 1999 due to the growth of Internet traffic (included in local traffic). Telecom Italia expects internet-related revenues will 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 entry of new competitors which have begun to take market share from Telecom Italia.

Gross operating revenues from international traffic decrease by 5.3% in 1999 compared to 1998 despite a 15.4% increase in total international traffic volume, to 6,667 million minutes in 1999 from 5,777 million minutes in 1998 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 Lit. 30,953 billion in 1999 and Lit. 31,080 billion in 1998.

Mobile Services Revenues Italy

Gross operating revenues from mobile services in Italy increased by 21.2% in 1999 compared to 1998. This increase is attributable principally to the strong performance of TIM, despite increasing competition.

Mobile telecommunications customers increased to 18,527,000 customers at December 31, 1999, a 29.6% increase compared to December 31, 1998. TIM's GSM customer base increased by 43% in 1999, to 15,351,000 customers at December 31, 1999, while TIM's TACS customer base decreased by 10.9% in 1999, to 3,176,000 customers at December 31, 1999 in each case compared to December 31, 1998. The continuing significant growth in

GSM customers was attributable principally to the continuing rapid growth of the GSM TIM Card (a prepaid rechargeable GSM card) launched in October 1996, which had 12,909,000 users by December 31, 1999 compared to 8,282,000 users at December 31, 1998.

At December 31, 1999, TIM had a market share in Italy of approximately 61% (including TACS and GSM) compared to 70% at December 31, 1998, and a market share of approximately 57% for GSM only compared to 64% in 1998. The market share decrease is due to increased competition and the commencement of services by the third mobile operator (Wind) in March 1999. Although TIM in 1999 remained the market leader in net new acquisitions (+43%). The aggregate number of customers at December 31, 1999 for TIM's analog and GSM services represented a penetration rate of 32.5% compared to 25.1% at December 31, 1998.

Average monthly revenue per mobile customer (which includes traffic revenues and subscription fees) decreased from approximately Lit. 77,600 in 1998 to Lit. 67,600 in 1999, as low-usage customers, principally non-business customers and GSM and TACS TIM Cardholders, grew further in 1999, making up almost 82.3% of the customer base. 100% of TIM's net new additions for its GSM service came from Prepaid Customers. Traffic revenues however, increased in 1999 compared to 1998.

Mobile traffic revenues increased by 27.2% in 1999 (Lit. 11,672 billion) compared to 1998 (Lit. 9,178 billion). Revenues from equipment sales also increased (9.2%). The mobile subscription fees decreased by 51.5% in 1999 (Lit. 409 billion) compared to 1998 (Lit. 843 billion) due to the sharp expansion in the prepaid service customer base, where no subscription fees are paid.

Consolidated operating revenues were Lit. 13,722 billion in 1999 and Lit. 11,094 billion in 1998.

International Telecommunications Services Revenues

Gross operating revenues from international telecommunications services increased by 114.0% in 1999 compared to 1998, benefitting mainly from the first time consolidation of the two Brazilian mobile companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes and the continued growth of STET Hellas, the Group's GSM mobile operator in Greece. Revenues from Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes amounted to Lit. 722 billion and Lit. 711 billion, respectively.

Revenues from STET Hellas amounted to approximately Lit. 900 billion in 1999, representing an increase of 27.3% over 1998. This increase reflected an increase of 72% 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. Revenues from Entel Bolivia decreased by 0.5% in 1999 to Lit. 412 billion compared to Lit. 414 billion in 1998 (taking into account inflation adjustments). Revenues from TMI decreased by 18% in 1999 to Lit. 300 billion, compared to Lit. 366 billion in 1998, principally due to directing commercial operations to more profitable segments.

Consolidated operating revenues were Lit. 3,069 billion in 1999 and Lit. 1,273 billion in 1998.

Satellite Services Revenues

Gross operating revenues from satellite services decreased by 16.2% in 1999 compared to 1998. This decrease is principally due to the results of Telespazio. With reference to this company, value of standard production, including contract work in process (Lit. 680 billion compared to Lit. 623 billion in 1998, +9.1%), already takes into account the first orders for the Astrolink system.

Consolidated operating revenues were Lit. 443 billion in 1999 and Lit. 534 billion in 1998.

IT Software and Services Revenues

The table below sets forth, for the periods indicated, gross operating revenues from the IT software and services segment. Due to the above mentioned reorganization of the Group, the IT software and services segment in 1999 consisted of the operations of FINSIEL, Telesoft and Sodalia; while in 1998 this sector also included Saritel. Due to this fact the 1998 gross operating revenues have been restated to exclude Saritel.

	Year ended December 31,	
	1998	**1999**
	(in billions of Lit.)	
IT software and services gross operating revenues	2,566	3,074

Gross operating revenues from this segment increased by 19.8 % in 1999 compared to 1998. Gross operating revenues grew due to a 9.5% increase in revenues from the FINSIEL Group (Lit. 2,204 billion in 1999 compared to Lit. 2,012 billion in 1998) and to a 44.7% increase in revenues from Telesoft (Lit. 758 billion in 1999 compared to Lit. 524 billion in 1998), which develops software applications for telecommunications services. Gross operating revenues from the FINSIEL Group increased due to an increase in activities in the telecommunications, travel and transportation and banking sectors as well as the expansion in the local government market. Gross operating revenues from Telesoft increased due to the development of Group activities and international markets where the Group is already operating (Spain and Latin America).

Consolidated operating revenues were Lit. 2,127 billion in 1999 and Lit. 1,916 billion in 1998.

Manufacturing Revenues

The table below sets forth for the periods indicated, gross operating revenues of Italtel (proportionately consolidated in 1998; in 1999 the Italtel's results of operations are 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).

	Year ended December 31,	
	1998	**1999**
	(in billions of Lit.)	
Manufacturing gross operating revenues	3,950	3,114

Gross operating revenues of Italtel fell by 21.2% in 1999 compared to 1998 (Telecom Italia's share was Lit. 1,776 billion in 1999 compared to Lit. 1,975 billion in 1998).

Gross operating revenues at December 31, 1999 include ten months of revenues related to the activities assumed by Siemens (radiomobile networks and transmission system equipment) and 12 months of revenues related to the activities which remained in Italtel (fixed networks), after the reorganization agreed with the German partner. Consequently, although comparisons going forward will not be comparable, 1999 and 1998 remain comparable. Gross operating revenues in 1999 were Lit. 3,114 billion. Sales in foreign markets were Lit. 1,481 billion. Gross operating revenues in the 1999 pro forma financial statement (containing only fixed network sales) were Lit. 1,420 billion.

Consolidated operating revenues were Lit. 959 billion in 1999 compared to Lit. 1,041 billion in 1998.

Installation Revenues

The table below sets forth, for the periods indicated, gross operating revenues from the installation segment.

	Year ended December 31,	
	1998	1999
	(in billions of Lit.)	
Installation gross operating revenues	2,165	1,501

Gross operating revenues from the installation segment decreased by 30.7% in 1999 compared to 1998, with the Italian domestic market representing 57% and 60.6% of installation gross operating revenues, respectively (Lit. 856 billion in 1999 compared to Lit. 1,312 billion in 1998). SIRTI's sales suffered mainly from the reduction in the investment plans of Telecom Italia, SIRTI's principal customer, particularly in the multimedia segment (owing to changes in the technological mix in Telecom Italia's broadband network), partially offset by significant increases in volumes for new telecommunications operators in the domestic market. International installation revenues fell by 24.3% in 1999 (Lit. 645 billion compared to Lit. 852 billion in 1998), owing to the decrease in South America only partially offset by an improvement in Europe. In Latin America , in particular, installation activities have suffered from the Brazilian situation: strong changes in the local telecommunication market (privatization and deregulation) and the persistent economic and financial slump in the country have caused SIRTI's Brazilian gross operating revenues to decrease by 30.9%. In contrast European gross operating revenues have benefitted mainly from the Spanish subsidiary's performance.

Consolidated operating revenues were Lit. 837 billion in 1999 and Lit. 1,220 billion in 1998.

Operating Expenses

The table below sets forth, for the periods indicated, Telecom Italia's total operating expenses by major components and expressed as a percentage of total consolidated operating revenues.

	Year ended December 31,			
	1998		1999	
	(in billion of Lit., except percentages)			
Cost of materials	4,535	9.4%	4,795	9.1%
Other external charges	17,552	36.2%	18,561	35.4%
Personnel costs (salaries and social security contributions)	9,665	19.9%	9,636	18.4%
Changes in inventories	262	0.5%	(251)	(0.5)%
Capitalized internal construction costs	(2,088)	(4.3)%	(2,056)	(3.9)%
Depreciation and amortization	10,480	21.6%	10,338	19.7%
Total operating expenses	40,406	83.3%	41,023	78.2%

The Group's operating expenses increased by 1.5% in 1999 compared to 1998. As a percentage of the Group's operating revenues, such operating expenses represented 78.2% and 83.3% in 1999 and 1998, respectively. The decrease in operating expenses as a percentage of gross operating revenues is due to the growth of consolidated revenues, in particular from mobile and international telecommunications services, which grew at a faster rate than the increase in operating expenses. The increase in operating expenses was mainly due to the expansion of the Group's activities reflected in the Lit. 3,207 billion increase in costs of external services rendered (included in other external charges), as well as an increase of costs of materials partially offset by the decrease in depreciation of fixed assets.

Cost of Materials

Cost of materials increased by 5.7% in 1999 compared to 1998, principally due to the first time consolidation of the two Brazilian mobile companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes.

Other External Charges

The table below sets forth, for the periods indicated, Telecom Italia's other external charges broken down by major components.

	Year ended December 31,	
	1998	1999
	(in billions of Lit.)	
Costs of external services rendered	11,082	14,289
Write-downs of fixed assets and intangibles	1,840	142
Provision for bad debts	705	702
Rent and lease payments	1,285	1,363
Contributions for TLC activities	1,029	1,174
Provision for risk	345	155
Other provisions and operating charges	1,266	736
Other external charges	17,552	18,561

Other external charges increased by Lit. 1,009 billion in 1999 compared to 1998. These charges relate primarily to the telecommunications services segments and include costs of external services rendered, write-downs of fixed assets and intangibles, rent and lease payments, provision for bad debts, contributions for telecommunications activities and other provisions and operating charges.

- costs of external services rendered increased by 28.9% in 1999 compared to 1998 because of the increase of Group's activities.

- write-downs of fixed assets and intangibles decreased by 92.3% in 1999 compared to 1998. The 1998 results reflected significant write-downs taken by Telecom Italia on its DECT and SOCRATE platforms.

- rent and lease payments increased by 6.1% in 1999 compared to 1998, principally as a result of an increase in such costs related to the companies included in mobile and international telecommunications services segments due to the expansion of TIM's activities and the first time consolidation of the two Brazilian mobile companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes, partially offset by the lower costs of fixed line services segment.

- contributions for telecommunications activities, which are principally payable to the Italian Government and are proportional to revenues, increased by 14.1% in 1999 compared to 1998.

Other provisions and operating charges, which consist primarily of losses on disposals and write-offs of fixed assets, and taxes other than income taxes, decreased by 41.9 % in 1999 compared to 1998. During 1999 and 1998 the Group disposed of fixed assets with a gross value of approximately Lit. 4,343 billion and approximately Lit. 6,410 billion, respectively.

Personnel Costs

Personnel costs (salaries and social security contributions) decreased by 0.3% in 1999, compared to 1998 and, as a percentage of the Group's operating revenues, personnel costs declined to 18.4% in 1999 compared to 19.9% in 1998. Overall personnel costs decreased principally due to the lower costs incurred by the fixed line services in Italy and in manufacturing and installation segments, in part offset by the higher personnel costs of TIM and the change in the scope of consolidation (with the entry of the companies Tele Celular Sul Participacoes, Tele Nordeste Celular Participacoes and 9Telecom Reseau and the exclusion of Stream).

Total employees at Telecom Italia declined to 76,113 employees at December 31, 1999 compared to 79,508 employees at December 31, 1998. Total employees for the Group decreased to 122,662 at December 31, 1999 compared to 123,966 at December 31, 1998 principally due to the reduction in Telecom Italia and manufacturing section's personnel, partially offset by the extension of the scope of consolidation and the increase in the mobile telecommunications services and in installation activities personnel.

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 the Italy's telecommunications services of the Group. At December 31, 1999, Telecom Italia's potential range of liability for principal contribution was estimated to be between Lit. 1,800 billion and Lit. 2,400 billion (Lit. 381 billion 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. See "Item 8. 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 by 1.5% in 1999 compared to 1998 principally due to a decrease in capital expenditures spent on products purchased from subsidiaries within the Group.

Gross Operating Profit

The table below sets forth, for the periods indicated, the Group's 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")) by major business area and other activities and gross operating margin (gross operating profit as a percentage of operating revenues).

	Year ended December 31,			
	1998		**1999**	
	(in billions of Lit., except percentages)			
Fixed line services Italy	16,238	33.5%	15,434	29.4%
Mobile services Italy	5,650	11.6%	6,734	12.8%
Satellite services	144	0.3%	91	0.2%
International telecommunications services	209	0.4%	635	1.2%
IT software and services	361	0.8%	405	0.8%
Manufacturing	133	0.3%	23	–
Installation	303	0.6%	123	0.2%
Other activities	188	0.4%	501	1.0%
	23,226	47.9%	23,946	45.6%
Consolidation adjustments	(338)	(0.7)%	(273)	(0.5)%
Total Gross Operating Profit	22,888	47.2%	23,673	45.1%

Gross Operating Profit increased by 3.4% in 1999 compared to 1998 although gross operating margin declined to 45.1% in 1999 from 47.2% in 1998. The overall increase in Gross Operating Profit was primarily attributable to the mobile and international telecommunications segments. In addition, profitability increased in IT software and services segment. These increases were offset by a decline in fixed line services in Italy, the Group's largest segment, satellite services, manufacturing and installation segments. The decline of gross operating margin is mainly attributable to the new way of recording consolidated revenues gross of amounts due to other operators and service providers.

Depreciation and Amortization

Depreciation and amortization which is calculated on a straight line basis over the estimated useful lives of the assets, decreased by 1.4% in 1999 compared to 1998. Depreciation of fixed assets decreased by Lit. 457 billion or 5.1% to Lit. 8,425 billion in 1999 compared to Lit. 8,882 billion in 1998. The decrease in depreciation was principally attributable to a decrease in the depreciation charge by Telecom Italia (-Lit. 711 billion) owing to a lower amount of depreciable assets, the change in the mix of depreciable assets, lower depreciation on the DECT and SOCRATE assets that were written down in the 1998 financial statements and the adjustment of depreciation rates relating to the copper network, whose useful life was extended because of the introduction of ADSL technology, and the switching and transmission installations, whose useful life was reduced because of the increase of the software assets included in such equipment. Such change was partially offset by the depreciation charges for the new companies included in the scope of consolidation. Amortization of intangible assets increased by Lit. 315 billion or 19.7%, from Lit. 1,598 billion in 1998 to Lit. 1,913 billion in 1999. This change is due to higher amortization of Telecom Italia and TIM (an increase of Lit. 58 billion and Lit. 91 billion, respectively, compared to 1998) mainly as a result of the amortization of new investments in software, together with the amortization of goodwill from the acquisitions of the Brazilian companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes (a total of Lit. 131 billion).

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,	
	1998	1999
	(in billions of Lit.)	
Operating income	9,186	12,456

Operating income for the Group increased by 35.6% in 1999 compared to 1998. As a percentage of operating revenues, operating income increased in 1999 by 4.8% to 23.7% from 18.9% in 1998.

Interest Income, Interest 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,	
	1998	1999
	(in billions of Lit.)	
Interest income	1,579	1,073
Interest expense	(1,681)	(2,837)
Other income and expense, net	133	(981)
Total financial expense, net and other income and expense, net	31	(2,745)

Total financial expense, net and other income and expense, net decreased from a net contribution to income of Lit. 31 billion in 1998 to a net expense of Lit. 2,745 billion in 1999, principally due to the Group's share of the income and losses of the unconsolidated companies valued using the equity method and in particular to the write-downs related to the Iridium project, Telekom Srbija and the Astelit Ucraina project and the effects of the negative results reported by the Brazilian affiliated companies Maxitel and Solpart Participacoes. Such companies were affected by the costs arising from the currency devaluation of the Brazilian real and, for Maxitel, by the amortization of the purchase of the mobile telephony license, while for Solpart Participacoes, by the investment in Tele Centro Sul. Furthermore 1998 results included the gains arising from the sales of the Impsat investment and TIM and Stet Hellas shares and cumulative effects of the new accounting treatment of deferred tax assets, which were not replicated in 1999.

Income Taxes

Income taxes were Lit. 5,046 billion in 1999 compared to Lit 3,965 billion in 1998. Tax as a percentage of income before income taxes was 52% in 1999 and 43% in 1998. This increase in tax as a percentage of income before income taxes was primarily due to the non taxable gains realized in 1998 by the Dutch companies STET International Netherlands and STET Mobile Holding on the sale of the Impsat investment and STET Hellas shares, as well as to the extraordinary income arising from the cumulative deferred tax assets from previous years recorded in 1998.

The statutory income tax rate for 1999 and 1998 was 41.25%. Tax as a percentage of income before income taxes was higher than the statutory income tax rate mainly due to value adjustments on financial assets that did not have any effect on the Group's income before income taxes.

Net Income

Net income before minority interest decreased by 11.2% in 1999 compared to 1998. The decrease was principally attributable to the increase in financial expenses, net and other expenses, net as well as the increase of income taxes, partially offset by the increase in operating income. Net income after minority interest was Lit. 3,364 billion in 1999 compared to Lit. 3,830 billion in 1998. Minority interest decreased from Lit. 1,422 billion in 1998 to Lit. 1,301 billion 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,		
	1998	**1999**	**2000**
	(in billions of Lit.)		
Net cash provided by operating activities	18,313	15,382	10,897
Net cash used in investing activities	(17,110)	(11,886)	(30,342)
Net cash provided by (used in) financing activities	(1,023)	(3,754)	20,659
Net increase (decrease) in cash and cash equivalents	180	(258)	1,214
Cash and cash equivalents:			
Beginning of year	1,390	1,570	1,312
End of year	1,570	1,312	2,526

Net Cash Provided by Operating Activities. Net cash provided by operating activities was Lit. 10,897 billion in 2000 compared to Lit. 15,382 billion in 1999 and Lit. 18,313 billion in 1998. 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 (for additional details see Notes 4 and 7 of Notes to the Consolidated Financial Statements included elsewhere herein), only partially offset by the net change in other liabilities and the higher levels of net income, depreciation and amortization and write-offs of fixed and intangible assets and investments. The decrease in 1999 compared with 1998 was mainly due to the lower levels of net income, depreciation and amortization, write-offs of fixed assets, intangibles and investments and the net change in other liabilities.

Net Cash Used in Investing Activities. Net cash used in investing activities was Lit. 30,342 billion in 2000, Lit. 11,886 billion in 1999 and Lit. 17,110 billion in 1998. Investments in fixed assets, which consisted for the most part of telecommunications installations acquired by Telecom Italia and TIM, were Lit. 7,530 billion in 2000, Lit. 7,503 billion in 1999 and Lit. 9,423 billion in 1998. Investments in intangible assets were Lit. 25,402 billion in 2000 compared to Lit. 3,057 billion in 1999 and Lit. 2,236 billion in 1998. The significant increase in 2000 is principally due to the goodwill arising from the acquisition of subsidiaries (Lit. 17,637 billion), 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 (Lit. 4,680 billion). Investments in other long-term (financial) assets were Lit. 5,810 billion in 2000 compared to Lit. 2,517 billion in 1999 and Lit. 7,224 billion in 1998; in 2000 such investments include Lit. 1,686 billion for a 30% stake of GLB Servicos Interativos (Globo.com), Lit. 1,281 billion relating to the Savings Shares bought back by Telecom Italia and Lit. 594 billion 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 proceeds arising from the divestiture plan for the non-core businesses of the Group (Lit. 8,545 billion).

Net Cash Provided by (Used in) Financing Activities. Net cash provided by financing activities was Lit. 20,659 billion in 2000 compared to net cash used in financing activities of Lit. 3,754 billion and Lit. 1,023 billion in 1999 and 1998, respectively. The inflow of cash in 2000 was due to the increases in short-term debt (Lit. 19,055 billion) and in long-term debt (Lit. 2,822 billion) as well as to capital contributions (Lit. 8,082 billion, almost entirely related to the conversion of TIM's savings shares), partly offset by repayments of long-term debt and the dividend payments (Lit. 5,903 billion). 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 (Lit. 2,509 billion) and the dividend payments (Lit. 3,278 billion), partly offset by an increase in short-term debt (Lit. 468 billion) and in long-term debt (Lit. 1,485 billion). The outflow of cash in 1998 was due to the repayments of long-term debt (Lit. 2,891 billion) and the dividend payments (Lit. 1,900 billion), partly offset by an increase in short-term debt (Lit. 1,289 billion) and in long-term debt (Lit. 2,479 billion).

Capital Resources

On a consolidated basis, at December 31, 2000, Telecom Italia's outstanding long-term debt was Lit. 16,010 billion and its short-term debt was Lit. 29,307 billion (including current portion of long-term debt). Interest on such debt totaled Lit. 1,715 billion in 2000. Telecom Italia expects its average overall financial indebtedness in 2001 to be higher than 2000 although it expects financial indebtedness at year end 2001 to be only slightly higher than at year end 2000. 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 2001 compared to 2000.

The Group's short-term debt due to banks was Lit. 22,534 billion at December 31, 2000. As of December 31, 2000, the amount of unutilized short-term bank facilities was Lit. 12,608 billion; Lit. 10,377 billion was related to Telecom Italia. Approximately 86% of these facilities are denominated in Lit. and have varying interest rates.

In addition, at December 31, 2000, the Group had cash and marketable securities in excess of Lit. 7,280 billion. The Group believes that its bank facilities, which are committed through August 2001, together with its portfolio of marketable securities and cash, are sufficient to meet its present working capital needs.

The Group's long-term debt was Lit. 16,010 billion at December 31, 2000, Lit. 10,002 billion at December 31, 1999 and Lit. 10,839 billion at December 31, 1998. The increase in long-term debt from December 31, 1999 to December 31, 2000 was primarily due to the proportional consolidation of Nortel Inversora group from January 1, 2000 and acquisitions made in Latin America. The decline in long-term debt from December 31, 1998 to December 31, 1999 was principally due to the repayment and prepayment of debt.

As of December 31, 2000, approximately 58% of the Group's long-term debt was denominated in Lit., while the remainder was primarily denominated in euro, U.S. dollars, pound Sterling and Brazilian Reais. At December

31, 2000, approximately 55% of the long-term debt carried a floating rate. Approximately 11% of the long-term debt of the Group as of December 31, 2000 has an interest subsidy linked to laws relating to the financing of infrastructure and research.

In the year ended December 31, 2000, the Group incurred new long-term debt and short-term debt of Lit. 2,822 billion and Lit. 19,055 billion, respectively, compared to Lit. 1,485 billion and Lit. 468 billion, respectively, incurred in the year ended December 31, 1999. Such indebtedness was incurred to finance investments and refinance certain other indebtedness which had come due.

Long-term indebtedness of Lit. 3,142 billion, Lit. 12,663 billion and Lit. 3,347 billion is scheduled to become due for repayment during 2001, in the years 2002-2005 and beyond 2005, respectively.

The Group's short-term debt was Lit. 29,307 billion at December 31, 2000, Lit. 9,622 billion at December 31, 1999 and Lit. 9,341 billion at December 31, 1998. The significant increase in short term debt at the end of 2000 is due to the Group utilizing significant amounts of short-term debt to fund its international expansion, to fund the acquisition of SEAT and TIM's UMTS license in Italy, to fund dividends paid to shareholders and capital expenditures during 2000 (to the extent such activities could not be financed from operating cash flow).

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$10 billion global medium term note program (the "Global Note Program") at the end of 2000. The Global Note Program includes a shelf registration statement filed with the U.S. Securities and Exchange Commission permitting it to sell up to US$ 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 euro 8.5 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:

- euro 2.5 billion of 1% exchangeable notes due 2006;
- euro 3 billion of 6.125% fixed rate notes due 2006;
- euro 1 billion of floating rate notes due 2004; and
- euro 2.0 billion of 7% fixed rate notes due 2011.

The Group's debt to equity ratio, calculated as the ratio of long-term debt and current maturities of long-term debt and bank loans, less cash and cash equivalents and marketable securities to total stockholders' equity, was 75% and 41% as of December 31, 2000 and December 31, 1999, 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 revised presentation.

	Year ended December 31,		
	1998	1999	2000
	(in billions of Lit.)		
Fixed assets:			
Fixed line services Italy (1):			
Local and long distance networks	3,219	1,706	1,223
Investment in subscribers' equipment	801	790	692
Exchange equipment	1,521	998	824
Buildings and land	457	219	78
Other fixed assets	506	675	762
	6,504	4,388	3,579
Mobile services Italy (1):			
Radio and transmission equipment	809	734	748
Exchange equipment	476	463	546
Buildings and land	96	39	38
Other fixed assets	307	305	315
	1,688	1,541	1,647
Satellite services	82	56	56
International telecommunications services	513	943	1,961
IT software and services	83	73	71
Manufacturing(2)	75	46	34
Installation(2)	23	58	27
Other activities	455	398	155
Total fixed assets (before net advances to suppliers)	9,423	7,503	7,530
Intangible assets (3)	2,236	3,057	25,402
Total capital expenditures	11,659	10,560	32,932
Financial investments (4)	7,224	2,517	5,810
Total investments	18,883	13,077	38,742

(1) Intercompany capital expenditures are adjusted to eliminate intercompany profit.

(2) In December 2000 Telecom Italia disposed of its interests in Italtel and Sirti, although it retained through Sogerim a 19.9% interest in Italtel. For the year 2000 the data related to the manufacturing and installation businesses refer to the first nine months.

(3) Intangible assets include investments such as software for telecommunications systems, licenses and goodwill arising from the acquisition of subsidiaries.

(4) Financial investments include the Group's investment in international activities.

The increase in capital expenditures in 2000 (Lit. 32,932 billion) compared to 1999 (Lit. 10,560 billion) was almost entirely due to the increase in investment in intangible assets which refers mainly to Telecom Italia and Tim and includes:

- the goodwill of Lit. 17,637 billion 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 (Lit. 4,680 billion) and the PCS 1900 license obtained through Tim Perù (Lit. 381 billion).

The decrease in capital expenditures in 1999 compared to 1998 was primarily due to abandoning the SOCRATE and DECT platform projects and the virtual completion of the switching numbering process and a greater selectivity in network investments. Investments in intangible assets increased from Lit. 2,236 billion in 1998 to Lit. 3,057 billion in 1999 due to the recording goodwill paid for a further stake in the Brazilian companies Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes, which gave the Group control over such companies.

Cash flows from operating activities in 2000 (Lit. 10,897 billion) were lower than capital expenditures in fixed and intangible assets (Lit. 32,932 billion) and total investments (Lit. 38,742 billion).

Cash flows from operating activities in 1999 (Lit. 15,382 billion) exceeded capital expenditures in fixed and intangible assets (Lit. 10,560 billion) and total investments (Lit. 13,077 billion).

Cash flows from operating activities in 1998 (Lit. 18,313 billion) exceeded capital expenditures in fixed and intangible assets (Lit. 11,659 billion) but was lower than total investments (Lit. 18,883 billion).

The expected capital expenditures and financial investments of the Group for year 2001 to 2003 are euro 25 billion. Of such capital expenditures and financial investments, approximately euro 7 billion is expected to be allocated to wireline telecommunications services Italy, approximately euro 10 billion is expected to be allocated to mobile telecommunication services (including financing the build out of the UMTS network), approximately euro 5 billion will be allocated to international telecommunication services and the remaining approximately euro 3 billion is expected to be allocated to the other Business Units.

Research and Development Activities

The Group spent Lit. 730 billion, Lit. 640 billion and Lit. 520 billion on research and development in 1998, 1999 and 2000, 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. Some R&D activities have traditionally been devoted to support the manufacturing sector in an increasingly competitive market over the past several years.

Such activities in support of the manufacturing sector was performed by Italtel which was sold by Telecom Italia.

As a result, R&D expenditures recognized by Italtel and included in the Group's consolidated financial statements during 2000 were limited and will be non-existent going forward.

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 TI Lab), the corporate research center of the Group. CSELT performs both strategic research as well as research specifically requested by Group Companies.

Consolidated Financial Statements as of and for the Year Ended December 31, 2000 — Reconciliation of Italian GAAP to U.S. GAAP

As a result of certain significant transactions which occurred during 2000, in particular

- the acquisition of SEAT, including the SEAT put/call option entered into concurrently therewith;
- the real estate transaction in which Telecom Italia sold a 60% stake in IM.SER S.p.A., a company formed to hold certain of its real estate assets, to third parties; and
- the conversion offers of TIM and SEAT in which savings shares were exchanged for ordinary shares,

there are additional material differences and reconciling items, 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 and stockholders' equity under Italian GAAP. For a complete description of the Group's reconciliation to U.S. GAAP and other required U.S. GAAP disclosures see Notes 26, 27 and 28 of Notes to the Consolidated Financial Statements included elsewhere herein.

Net Income

Under Italian GAAP, net income after minority interest for 2000 was Lit. 3,927 billion and under U.S. GAAP net income, after minority interest, was Lit. 6,819 billion. There are many differences between Italian GAAP and U.S. GAAP which 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. In 2000, the Lit. 2,892 billion 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 Lit. 15,231 billion 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 Lit. 770 billion 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 Lit. 15,424 billion based upon FAS 121, *Accounting for the Impairment of Long Lived Assets* and for *Long Lived Assets to be Disposed of.* Due to the decline in price of SEAT shares at December 31, 2000 and further analysis performed by Telecom Italia, which indicated that the undiscounted cash flow 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 Lit. 31,028 billion, including acquisition goodwill of Lit. 26,787 billion. In addition, the historical financial statements of SEAT already included goodwill of Lit. 5,362 billion. Under Italian GAAP, as a result of the treatment being split between purchase and pooling accounting, Telecom Italia recorded goodwill of Lit. 13,159 billion. 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 Lit. 4,283 billion, increasing net income. Under Italian GAAP this gain was accounted for as an equity movement and had no impact on the income statement.

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 Lit. 788 billion) 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 Lit. 609 billion).

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. In prior years the adjustments have been less significant although they have generally resulted in a lower U.S. GAAP net income compared to net income under Italian GAAP.

Stockholders' Equity

Stockholders' equity under U.S. GAAP in 2000 were Lit. 37,018 billion compared with Lit. 36,443 billion 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 Lit. 126,854 billion compared with Lit. 138,497 billion under U.S. GAAP, a difference of Lit. 11,643 billion. Substantially all of the difference is attributable to the higher levels of goodwill recorded for U.S. GAAP purposes (Lit. 34,991 billion under U.S. GAAP compared to Lit. 19,942 billion under Italian GAAP, an increase of Lit. 15,049 billion), 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 Lit. 4,611 billion being recorded on the balance sheet. This was offset by a reduction in fixed assets of Lit. 5,237 billion attributable to Nortel Inversora Group which is accounted for under U.S. GAAP in accordance with the equity method. The increase in total assets is after giving effect to the impairment charge under U.S. GAAP of Lit. 15,424 billion.

With respect to liabilities, the material impact from the U.S. GAAP adjustments relates to long-term debt. Long-term debt increased from Lit. 16,010 billion under Italian GAAP to Lit. 24,138 billion under U.S. GAAP. The increase in long-term debt is due to the following:

- *SEAT Put/Call Option Financing.* Pursuant to the various transactions relating to the arrangements between Huit II and the Chase Manhattan Group, in which 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 these transactions as the acquisition financing of an equity interest. As a result, U.S. GAAP requires Telecom Italia to record additional long term debt of Lit. 5,780 billion. 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 Lit. 5,212 billion.

- *Nortel Inversora Group*. The increases in long-term debt described above were partially offset by a reduction in long-term debt of Lit. 2,973 billion attributable to Nortel Inversora Group which is accounted for under U.S. GAAP in accordance with the equity method.

The Euro

Since 1997, a company-wide project named Euro has been established to coordinate all of the Company's activities for the conversion to a euro-operating environment. Since 1998 the Company has conducted training and communication in connection with the euro.

In 2000, Euro Project, the organizational department of the Telecom Italia Group assigned the task of supervising and coordinating the changeover to the new currency, continued the actions initiated in 1999, both within and the outside the Group.

In Telecom Italia, the Euro Project outlined the steps to be taken in the final phase:

- upgrading of information systems by the third quarter of 2001;
- definition, creation and tests of contingency plans by December 2001; and
- "Independent Verification & Validation" of the main corporate systems, carried out using suppliers, methods and tools other than those used during the changeover stage so as to identify eventual problems in time to make the necessary corrections.

As part of the Group's ongoing systems updates, the Group has concurrently made the necessary modifications to its existing information, financial and management control systems and software to permit the Group to bill, invoice and report in euros. During the year 2000 the Telecom Italia Group had incurred costs for the introduction of the euro of approximately Lit. 14 billion which have been charged to the statement of income.

Cautionary Statement for Purposes of the "Safe Harbor" Provisions of the United States Private Securities Litigation Reform Act of 1995. The foregoing discussion in "Operations 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 the entry of new competitors, especially global and regional alliances formed by other telecommunications operators, in Telecom Italia's core fixed-line and wireless markets;
- Telecom Italia's ability to continue the introduction of 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;
- 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;
- 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 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;
- the Group's ability to realize the benefits of its investment in UMTS licenses and related capital expenditures;
- 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 Group's ability to realize the benefits of the merger of SEAT and Tin.it; and
- SEAT's ability to implement successfully its internet strategy.

In addition to the factors noted above, the ability of the Company to achieve certain of its objectives described herein assumes the continuing rebalancing of the tariff system in order to reduce subsidization of certain tariff categories by other ones and a satisfactory determination on interconnection fees that takes into account both the obligation to provide universal service and the access deficit.

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

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- Lira/Euro denominated assets and liabilities.

The Finance Department of the Group regularly assesses these risks and has established policies to protect against the adverse effects of these exposures. As a result, the Group does not anticipate any material losses in these areas.

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. In addition, 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 table below sets forth, for the periods indicated, the aggregate principal amount of long-term debt (including current portion) payable in each year through 2005 and thereafter. See Note 28(c) of Notes to Consolidated Financial Statements included elsewhere herein for fair values.

	Repayment							As of
	2001	2002	2003	2004	2005	Thereafter	Total	12/31/1999
	(Billions of Lire)							
Fixed Rate Debt	968	947	626	315	154	964	3,974	4,255
Floating Rate Debt	2,174	3,417	4,670	1,436	1,098	2,383	15,178	8,259
Total	3,142	4,364	5,296	1,751	1,252	3,347	19,152	12,514

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), the average interest rate broken down by type of loan and the fair value of long-term debt.

	Year ended December 31, 2000								Fair Value	Fair Value
	2000	2001	2002	2003	2004	2005	Thereafter	As of 12/31/1999	As of 12/31/1999	As of 12/31/2000
	(Billions of lire, except for percentages)									
Long-Term Fixed Rate Debt	3,006	2,059	1,433	1,118	964	806	477	3,404	3,510	2,935
Average Fixed Rate	8.30%	8.90%	9.10%	9.67%	10.06%	10.73%	12.63%			
Long-Term Floating Rate Debt Swapped into Fixed Rate Debt	2,828	2,512	892	853	234	234	234	2,233	2,177	2,809
Average Swapped into Fixed Rate	5.48%	5.16%	7.20%	7.18%	8.76%	8.76%	8.76%			
Average Total Fixed Rate	6.93%	6.84%	8.37%	8.59%	9.80%	10.29%	11.36%			
Floating Rate Debt	6,547	4,326	3,021	2,322	2,075	1,625	784	4,213	4,132	6,384
Long-Term Floating Rate Debt Swapped into Floating Rate Debt(1)	3,629	2,749	1,004	305	73	2	—	152	152	3,626
Total Long-Term Debt	16,010	11,646	6,350	4,598	3,346	2,667	1,495	10,002	9,971	15,754

(1) In the prior year the Company entered into agreements to swap variable rate long-term debt (at domestic parameters) into Euribor.

Market Risk Policy

The Group's policy regarding market risk consists of the following:

- The Finance Department of the Group determines the maximum level of interest rate and foreign exchange rate risk to which the Group should be exposed.
- 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 Risk Management

The Group uses derivatives mainly for the management of its debt positions, primarily interest rate swaps and interest rate options (to reduce the interest rate exposure on fixed-rate and floating-rate bank loans and bonds) and cross-currency and interest rate swaps ("CIRS") (to convert foreign currency loans – US dollar, pound sterling, Japanese yen and euro – into the functional currencies of the various subsidiaries).

The following tables give a description of the financial derivative contracts outstanding as of December 31, 2000 to hedge medium/long-term debt positions.

(in billions of lire)	Notional amount/ Capital exchanged at 12/31/2000	Market value of derivatives at 12/31/2000 (a)	Market value of underlying debt positions at 12/31/2000 (b)	Market value of debt including related derivatives at 12/31/2000 (c)=(b-a)	Market value of derivatives at 12/31/1999
Interest rate swaps and interest rate options	5,629	46	5,637	5,591	36
Cross-currency and interest rate swaps	2,367	38	2,264	2,226	63

	2001	2002	2003	2004	2005	2006	Total
				(Billions of Lire)			
Interest rate swap: Pay fixed/Receive floating interest rate:							
Notional Amount	125	300	1,100	46	58	—	1,629
Weighted average pay rate	3.80%	4.65%	3.92%	4.25%	4.71%	—	
Weighted average receive rate	4.855%	4.855%	4.855%	4.855%	4.855%(1)	—	

(1) Interest rate corresponds to three month Euribor fixed on December 29, 2000 (no margin is added or subtracted). This rate is indicative only; the same number has been repeated for the following years although the effective floating rates will be fixed at each relevant period, depending on market fluctuations.

	2001	2002	2003	2004	2005	2006	Total
				(Billions of Lire)			
Interest rate swap: Pay floating/Receive floating interest rate:							
Notional Amount					282	314	596
Weighted average pay rate(1)	4.765%	4.765%	4.765%	4.765%	4.765%	4.77%	
Weighted average receive rate(2)	Rendint	Rendint	Rendint	Rendint	Rendint	Rendint	
Notional Amount (Billions of Lire)					87.5	91.8572485	179
Weighted average pay rate(1)	4.778%	4.778%	4.778%	4.778%	4.778%	4.781%	
Weighted average receive rate(3)	Rendibot	Rendibot	Rendibot	Rendibot	Rendibot	Rendibot	
Notional Amount (Billions of Lire)				499.8	200	87.5	787
Weighted average pay rate(1)	4.954%	4.954%	4.954%	4.954%	4.971%	5.05%	
Weighted average receive rate(4)	Rolint	Rolint	Rolint	Rolint	Rolint	Rolint	
Notional Amount (Billions of Lire)				91			91
Weighted average pay rate(1)	5.000%	5.000%	5.000%	5.000%			
Weighted average receive rate(5)	Robot	Robot	Robot	Robot			

(1) Interest rate corresponds to Euribor six month plus the spread applicable to the transaction. Six month Euribor is fixed at December 29, 2000. This rate is indicative only; the same number has been repeated for the following years although the effective rates will be fixed at each relevant period, depending on market fluctuations.

(2) 4.74% as of December 29, 2000 (customary domestic Italian interest rate parameter for medium/long-term debt)

(3) 4.94% as of December 29, 2000 (customary domestic Italian interest rate parameter for medium/long-term debt)

(4) 5.07% as of December 29, 2000 (customary domestic Italian interest rate parameter for medium/long-term debt)

(2) 5.41% as of December 29, 2000 (customary domestic Italian interest rate parameter for medium/long-term debt)

	2001	2002	2003	2004	2005	2006	Total
			(Million of US$)				
Interest rate swap: Pay fixed/Receive floating interest rate:							
Notional Amount	56	22	—	—	—	—	77
Weighted average pay rate	6.086%	6.087%	—	—	—	—	—

	2001	2002	2003	2004	2005	2006	Total
			(Million of US$)				
Weighted average receive rate	6.2736%(1)	6.2788%(1)	—	—	—	—	—
Notional Amount	56	22	120	—	—	—	197
Weighted average pay rate	6.89%	6.89%	6.89%	—	—	—	
Weighted average receive rate	6.5061%(2)	6.5061%(2)	6.5061%(2)	—	—	—	

(1) This interest rate corresponds to six month US$ Libor fixed on December 29, 2000 (6.20375%) plus the weighted applicable margin. This rate is indicative only and has been repeated for the following years, adjusting the margin considering matured amounts; the effective floating rates will be fixed at each relevant period, depending on market fluctuations.

(2) This interest rate correspond corresponds to the three months US$ Libor fixing on December 29, 2000 (6.39875%) plus the applicable margin. Such rate is indicative only and has been repeated for the following years; the effective floating rates will be fixed at each relevant period, depending on market fluctations.

The remaining Lit. 1,936 billion notional amounts not reflected in the foregoing table relates to the hedging of certain outstanding floating and fixed rate debt at SEAT. In connection therewith, SEAT has entered into a number of interest rate swap and collar agreements, which partially modify the interest rate characteristics of such fixed and floating rate debt.

IRS (interest rate swaps) and IRO (interest rate options) involve the exchange of flows of interest calculated on the notional 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.

Generally, the counterparties to derivative contracts are only the best rated banks and financial institutions, and they are continually monitored in order to minimize the risk of non-performance.

The same also applies to CIRS which involve the exchange of capital, in the respective currencies of denomination, in addition to the settlement of periodic interest flows, at maturity.

To determine the market value of the above financial derivatives, Telecom Italia Group uses 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 CIRS also reflect the difference between the foreign exchange rate at the closing of the swap and the market rate as of December 31, 2000. For short-term derivatives contracts (up to one year), the Group uses Libor/Euribor rates, whereas for medium/long term derivatives contracts (more than one year), the Group utilizes the swap rates. The financial debt's market value is estimated on the basis of the present value of the future cash flows. The market value of the cross currency and interest rate swaps depends also on the difference between the reference foreign exchange rate of the trade date and the foreign exchange rate of the valuation date.

Although notional amounts of the derivatives increased in 2000 with respect to 1999, the value of the derivatives has been mitigated by two effects: market interest rates growth, occurred between December 1999 and December 2000, and portfolios residual life reduction.

The Group also enters into derivative contracts to hedge the interest rate risk and foreign currency risk on its investments through its finance vehicle SOFTE. As of December 31, 2000 the Luxembourg subsidiary SOFTE had entered into IRS and CIRS on bonds investments for a notional amount of Lire 526 billion.

Foreign Exchange Rate Risk Management

The Group is exposed to financial risks from movements in currency exchange rates from its international operations and in the course of its ordinary business. To manage these risks, the Group selectively utilizes financial instruments, such as currency swap agreements and options (see table under Interest Rate Risk Management). The Group specifically designates these instruments as hedges of either (i) net investments and related cash flows (including debt) in international subsidiaries; (ii) foreign currency denominated debt of the Group; or (iii) anticipated and firmly committed foreign currency transactions related to the ordinary business of the Group.

The hedging of the foreign exchange exposure on short-term US dollar loans contracted by TIM, is shown in the following table:

(Billions of lire)	Notional amount of Debt	Market value of derivatives at 12/31/2000 (a)	Market value of underlying debt positions at 12/31/2000 (b)	Market value of debt including related derivatives at 12/31/2000 (c)=(b-a)
Zero Cost Collars	908	-56	832	888

The strike EURO/USD rates of the zero cost collar put into place to hedge the notional amount of debt of Lit. 346 billion where 0.80 and 0.8680, and for the notional amount of debt of Lit. 562 billion were 0.84 and 0.9082.

The Group's total indebtedness (both short and long-term indebtedness) denominated in foreign currencies (excluding Euro currencies and the Euro) was Lit. 10,889 billion at December 31, 2000. The Group's total indebtedness denominated in foreign currencies (excluding Euro currencies and the Euro) included U.S. dollar-denominated indebtedness in the amount of Lit. 8,531 billion. See Note 11 of Notes to Consolidated Financial Statements. 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.

See Note 18 to Notes to Consolidated Financial Statements for further details of such derivative and other financial instruments and see Note 3 for the accounting policies applied.

Item 6. DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

Directors

As of June 15, 2001, the members of the Telecom Italia Board of Directors and their respective ages, positions and year of appointment were as follows:

Name	Age	Position	Appointed
Roberto Colaninno	57	Chairman and Chief Executive Officer	1999
Antonio Tesone	77	Honorary Chairman	1999
Sergio Erede	60	Deputy Chairman	1999
Peter A. Cohen	54	Director	1999
Salvatore Donato (1)	50	Director	1999
Guido Ferrarini	50	Director	2001
Paolo Ferro-Luzzi (2)	64	Director	1999
Emilio Gnutti	53	Director	1999
Jeffrey E. Livingston	54	Director	1999(3)
Ettore Lonati	63	Director	2000
Joseph M. Tucci	53	Director	1999
Roberto Ulissi (2)	38	Director	2001
Gérard Worms	64	Director	1999

(1) Designated by the Ministry of Communications.

(2) Appointed by the Treasury.

(3) Reappointed in 1999. Member of Telecom Italia's Board of Directors since 1997.

On April 4, 2001 and May 28, 2001, respectively, directors Angelo Benessia and Domenico Siniscalco resigned from the Board of Directors. They were replaced, on June 12, 2001, by Roberto Ulissi and Guido Ferrarini. Roberto Ulissi was appointed by the Board of Directors and will remain in office until the next shareholders meeting. Guido Ferrarini was appointed by the shareholders meeting and will remain in office for the same term as the other members of the board already in office.

As of June 15, 2001 the Secretary of the Board of Directors was Pierpaolo Cotone

Pursuant to the Privatization Law and the special powers of the State included in the Telecom Italia By-laws, 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.

Pursuant to Articles 10 and 13 of Telecom Italia's By-laws, 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 June 28, 1999 set the number of directors at 13 and this number will not be changed until a new resolution of 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 June 28, 1999 resolved that the current Directors of Telecom Italia will remain in office for a three-year term (from 1999 to the Annual shareholders Meeting called to approve the Telecom Italia financial statements for the year ended December 31, 2001).

If during the term of the Board of Directors one or more directors leaves the Board of Directors 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 a Chief Executive Officer and determine his 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.

In October 2000, the ordinary shareholders approved certain rules regulating shareholders' meetings.

Currently the members of the audit and corporate governance committee are directors Guido Ferrarini, Jeffrey Livingston and Gèrard Worms. Guido Ferrarini, who was appointed to the Board of Directors on June 12, 2001 and is an expert in corporate covernance, will be the chairman of the committee.

Such committee:

(a) evaluates the adequacy of the internal control system;

(b) evaluates the working plan prepared by the those in charge of internal control and receives periodical reports from same;

(c) examines the proposals submitted by the audit firms to obtain appointment as auditors, as well as the audit work plan and the conclusions described in the letter of recommendations;

(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;

(e) carries out additional tasks which it is assigned by the Board of Directors, especially with respect to relations with the independent audit firm.

The audit and corporate governance committee also oversees the observance and periodical updating of the rules for corporate governance and compliance with the code of conduct, if any.

Currently the members of the remuneration committee are the Deputy Chairman, Sergio Erede and director Peter Cohen and Roberto Ulissi. The remuneration committee, on the basis of indications of the Chief Executive Officer, formulates proposals for the Board of Directors regarding compensation for the Chief Executive Officer as well as the criteria for compensation of Telecom Italia's top management.

As a result of recent events, Telecom Italia is currently reviewing, together with McKinsey, the consulting firm, its corporate governance policies, in particular its policies with respect to delegation of authority. In addition, the Company has recently appointed Guido Ferrarini who is an expert in corporate governance, as a director. See "Item 4. Information on the Company—Recent Developments—Summary of Memoranda Released by the Board of Statutory Auditors and By the Board of Directors of Telecom Italia at the Shareholders Meeting of June 12, 2001".

Executive Officers

As of June 15, 2001, 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
Roberto Colaninno	57	Chairman and Chief Executive Officer	1999
Enzo Badalotti	40	Chief Business Unit-International Operations	2000
Stefano Braidotti	56	Internal Auditing	2000
Massimo Brunelli	42	Chief Financial Officer	1999
Andrea Camanzi	52	Public and Regulatory Affairs	1999
Pierpaolo Cotone	49	Corporate and Legal Affairs	2000
Marco De Benedetti	38	Chief Business Unit-Mobile Services and Chief Executive Officer of TIM	1999
Andrea Granelli	40	Chief Business Unit and Chief Executive Officer of TI Lab	2000
Mario Luzzi	34	Strategy	2000
Roberto Maglione	43	Human Resources	2001
Vittorio Meloni	44	Corporate Communication and Image	1999
Vittorio Nola	46	General Secretariat	2000
Lorenzo Pellicioli(1)	50	Chief Business Unit Internet and Media and Chief Executive Officer of SEAT	2000
Salvatore Pinto	43	Chief Business Unit-Satellite Service and Chief Executive Officer of Telespazio	2001
Gilberto Ricci	59	Chief Business Unit-IT Services and Chief Executive Officer of ITTI	2000
Rocco Sabelli	46	Chief Business Unit-Wireline Services	1999

(1) On March 15, 2000, in the context of the SEAT/Tin.it Transaction (see Item 4. Information on the Company—Significant Developments during 2000 - Completion of SEAT/ Tin.it Transaction) Telecom Italia agreed to elect, for three years, Lorenzo Pellicioli as SEAT's Chief Executive Officer, with ordinary and extraordinary executive powers, and to elect directors of SEAT who would allow for the independence of the SEAT management from the Telecom Italia management.

Board of Statutory Auditors

The Draghi Law introduced new provisions regarding the Board of Statutory Auditors, which modified the previous legislation. According to the Draghi Law, the Board of Statutory Auditors verifies the observance of the law and the By-laws 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.

Pursuant to Article 17 of Telecom Italia's By-laws, the Shareholders' Meeting appoints the Board of Statutory Auditors through the "voto di lista" system. According to the Draghi Law if shareholders have to elect three Statutory Auditors, at least one must be elected by minority shareholders; if the shareholders have to elect more than three Statutory Auditors at least two statutory auditors 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.

According to the Bylaws the Board of Statutory Auditors is composed of not less than five and not more than eight auditors, as determined by a resolution of Telecom Italia shareholders; two alternate auditors are also appointed. The Board of Statutory Auditors appoints among its members a Chairman of the Board of Statutory Auditors. See “Item 10. Additional Information — Description of By Laws and Capital Stock — Capital Stock — Voto di Lista”. Statutory auditors cannot be members of more than five Boards of Statutory Auditors of listed companies (excluding Telecom Italia and its subsidiaries). Pursuant to the Privatization Law and the special powers of the State included in Telecom Italia’s By-laws, the Treasury has the right to appoint one statutory auditor of Telecom Italia. Pursuant to the Public Concessions which have now been converted into licenses (see “Item 4. Information on the Company — Regulation — Public Concessions”), each of the Ministry of Communications and the Treasury had the right to designate one statutory auditor of Telecom Italia; the statutory auditor designated by the Treasury was to be appointed Chairman of the Board of Statutory Auditors.

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.

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. The present Telecom Italia Board of Statutory Auditors was appointed on July 3, 2000. Statutory auditors are required to attend Shareholders’ Meetings, Board of Directors meetings and Executive Committee meetings.

As of June 15, 2001, 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.

Name	Position	Appointed
Paolo GERMANI(1)	Chairman	2000
Mario BOIDI(3)	Auditor	2000
Paolo GOLIA	Auditor	2000
Fabrizio QUARTA (2)	Auditor	2000
Gianfranco ZANDA(3)	Auditor	2000
Leonida LIUNI(3)	Alternate Auditor	2000
Enrico BIGNAMI	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.

The financial statements of Telecom Italia are required to be audited by an independent auditing firm whose assignment has to be approved 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. According to Italian law, such appointment is for three years and the Shareholders’ Meeting may not appoint the same external auditors for more than three consecutive three-year terms. The report issued at the end of the audit is defined as an opinion with or without qualification and not a “certification”. PricewaterhouseCoopers (“PwC”) has audited the 2000 financial statements of Telecom Italia. Also, PwC reviewed Telecom Italia’s 2000 six months result with the “limited review” method, in accordance with CONSOB’s regulations.

On June 28, 1999 the Shareholders’ Meeting chose Price Waterhouse S.p.A., now called PricewaterhouseCoopers S.p.A., as the auditors of Telecom Italia’s annual financial statements and the limited audit of Telecom Italia’s half-year report for the years 2000, 2001 and 2002. On June 12, 2001 the Shareholders’ Meeting revoked the audit assignment conferred to PwC for the following reasons:

- as the audit assignment conferred by Telecom Italia’s controlling shareholder, Olivetti, to PwC was due to expire at the close of the 2000 financial year, on July 4, 2000 the Shareholders’ Meeting of Olivetti conferred an audit assignment for the three-year period 2001-2003 to Reconta Ernst & Young S.p.A.(“REY”);

- 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, REY has been selected as the audit firm for the majority of Olivetti group companies.

In accordance with Legislative Decree 58/1998, the assignment previously conferred to PwC was “revoked on just grounds”, 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 on June 12, 2001 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 is selected biographical data of the Directors and the Executive Officers.

Directors

Roberto Colaninno. Roberto Colaninno was born in Mantua, on August 16, 1943. Mr. Colaninno has been Telecom Italia Chairman and Chief Executive Officer since June 1999, Chairman of Telecom Italia Mobile since July 1999 and Chief Executive Officer of Olivetti since September 1996. Mr. Colaninno took the helm of Telecom Italia following the acquisition by Olivetti of the majority of Telecom Italia's share capital. At Olivetti, Mr. Colaninno was a driving force behind the strategic and organizational repositioning of Olivetti. Under his leadership Telecom Italia refocused on core business and divested non-core activities. Mr. Colaninno has strengthened the position of the Group in international markets, particularly in Europe, Latin America and the Mediterranean basin. Mr. Colaninno is also Chairman of Hopa, an industrial and financial holding company that owns more than 50% of voting capital in Bell S.A., the finance company that owns a relative majority of shares in Olivetti. Mr. Colaninno is Deputy Chairman of SEAT. Mr. Colaninno was awarded the “Cavaliere del Lavoro” honor by the President of Italy in June 2000. In May 2001, the University of Lecce presented him with an honorary degree in Business Studies.

Antonio Tesone. Antonio Tesone was born in Ancona on July 20, 1923 and graduated in law from Milan State University in 1947. Mr Tesone has his own legal practice in Milan, providing legal advice in corporate, finance and contract law. He has been Chairman of Olivetti since September 3, 1996, Director and Honorary Chairman of Telecom Italia since June 28, 1999 and Chairman of Olivetti International S.A. since November 1997. Currently Mr. Tesone is also Chairman of Sema S.p.A., Deputy Chairman of Banca di Legnano and a Director of Sogefi (Mantus). He was Chairman of Tecnost until December 31, 2000, when Tecnost merged with Olivetti.

Sergio Erede. Mr. Erede was born in Florence in 1940, received a degree in law with top grades and honors from the University of Milan, and a master of law degree from Harvard Law School in Cambridge MA. Mr. Erede founded “Erede & Associati”, which recently merged with another law firm to create Bonelli Erede Papallardo. Mr. Erede’s practice is mainly concentrated in the corporate and contract sector, with particular emphasis on privatizations, acquisitions, sales, joint ventures, and securities law. Mr. Erede is a member of the Board of Directors of numerous companies, including Marzotto, Editoriale la Repubblica, Parmalat Finanziaria, Editoriale L’Espresso, Interpump Group, Autogrill, Carraro and SEAT. Before devoting himself to his private practice in 1969, he worked at Hale & Dorr in Boston, Sullivan & Cromwell in New York, and at IBM Italia as head of the legal office.

Peter A. Cohen. Mr. Cohen was born in 1946, received his bachelors degree in science from Ohio State University, and a masters degree from Columbia University school of business. Mr. Cohen has been a Director of Olivetti since May 12, 1994. Mr. Cohen has many years of experience in the financial services sector and, at present, is managing the Ramius Capital group, a banking and of financial consulting company in New York. Mr. Cohen is also Vice President and Director of GRC International Inc., a primary supplier of systems to the U.S. Government; Director of Presidential Life Insurance Company, a trustee of Mount Sinai/New York University Hospital; Vice President and Director of Republic New York Corp.; and President and Managing Director of Republic New York Securities. From 1983 to 1990, Mr. Cohen was President and Managing Director of Shearson Lehman Hutton Inc., and was a member of the Board of Directors in major companies, including the New York Stock Exchange, American Express Travel Related Service Company Inc., American Express Company, and Société Générale de Belgique S.A. Mr. Cohen has also been a member of the International Capital Markets Advisory Committee of the New York Federal Reserve Bank.

Salvatore Donato. Mr. Donato was born in Forza D'Agrò (Messina) on November 1, 1950. Mr. Donato received a degree B.A. in business and economics from Yale University. Mr. Donato has been advisor to the Chamber of Commerce of New Haven, Connecticut and of TTR S.p.A and Sole Director of Forza d'Agrò S.r.l. a construction company. Mr. Donato acted as assistant to the Minister of Industry for the establishment of joint ventures between Italian companies and Connecticut companies.

Guido A. Ferrarini. Guido A. Ferrarini was born on August 8, 1950. He received a degree in law with top grades and honors from the University of Genoa, and a master of law degree from Yale Law School. Mr. Ferrarini is professor of financial market law, at the faculty of law, University of Genoa and Director of the Law and Finance center of such faculty. Mr Ferrarini has is honorary professor at the faculty of law of the University College of London and honorary fellow of the Society for Advanced Legal Studies, London. Mr. Ferrarini has published several academic books and articles on corporate governance and finance. Mr. Ferrarini is a member of the Board of Directors of Erg S.p.A. and TIM and a member of several committees and arbitration boards. He participated, amongst other things, in the writing of the Draghi Law and was corporate governance adviser to Borsa Italiana SpA.

Paolo Ferro-luzzi. Mr. Ferro-Luzzi was born in Rome on May 14, 1937. He received a degree in law from "La Sapienza" University of Rome, with top grades and honors. Mr. Ferro-Luzzi is a professor of banking law at the faculty of law, "La Sapienza", University of Rome and an attorney for the Corte di Cassazione. Mr. Ferro-Luzzi is Deputy Chairman and member of the Board of Directors of BNL Vita S.p.A. He is Chairman of B.N.L. Fiduciaria Gestioni S.p.A., BNL Gestioni SGR and Credito Fondiario e Industriale – For Mr. Ferro-Luzzi was a member of the Board of Directors of several companies including the Istituto Nazionale per la Ricostruzione Industriale ("IRI") and Cassa per il Credito alle Imprese Artigiane S.p.A., Banco di Napoli S.p.A and GAN International..

Emilio Gnutti. Emilio Gnutti, was born in Brescia in 1947, and holds a degree in philosophy. He began his professional and entrepreneurial career in 1969 with the foundation of GI-EM, an electric motor company, of which he became Chairman in 1989. Mr. Gnutti has been a member of the Board of Directors of over twenty companies, in the Brescia area operating in several fields. He held executive positions in most of them. Mr. Gnutti is Deputy Chairman and Managing Director of Fingruppo and Hopa, the Società Europea Componenti Elettrici, Markfactor and Colmark. Mr. Gnutti is Managing Director of Molveno Oem and Bresciauno real estate company. He has been a member of the Board of Directors and of the Executive Committee of the Banca Popolare di Brescia, from 1984 to 1992, and Managing Director of Fin-Eco, which he founded in 1979. At present he is the Chairman and Managing Director of G.P. Line, F. Leasing, G.P. Finanziaria, Progettazioni Finanziarie, Immobiliare Delfo, and Chairman of GI-EM, SIT Prealpi, Bitech, S.F. Business Consulting, Emozioni d'Oro, and SIBER. All such companies operate in different fields. He is a member of the Board of Directors of SIBER Sardegna and the Luxembourg finance company G.P.P. International and Steinhauslin Bank of Florence. Mr. Gnutti is an Auditor of Thassos Insurance Brokers, the Dutch finance company Siber BV. He became a member of the Olivetti Board of Directors on December 15, 1998.

Jeffrey E. Livingston. Mr. Livingston received his bachelors degree from the University of Rochester and a law degree from New York University. He is a partner at the law firm Holland & Knight LLP in New York. He was Assistant U.S. Attorney for the Southern District of New York. Mr. Livingston has been a Member of the

Board of Directors of Telecom Italia since October 31, 1997. He is also a member of the Corporate Governance committee.

Ettore Lonati. Mr. Lonati was born in Botticino Sera (Brescia) on June 8, 1938. After a secondary school diploma he started his career at LONATI S.p.A. a family owned business. Mr. Lonati's activities were initially related to business development in non-European markets. Together with other family members he participated actively in developing the Lonati Group into a diversified industrial group operating in the following fields: mecchanics-textile sector, metallurgy, electronics, real estate and finance. Since 1972 Mr. Lonati has held the office of Managing Director of LONATI S.p.A.. He is and has been a member of the Board of Directors of several companies, mainly based in the Brescia area. He also holds the office of Managing Director in various real estate and finance companies controlled by his family.

Joseph M. Tucci. Mr. Tucci holds a bachelor's degree from Manhattan College and a master's degree in Business Administration from Columbia University. He joined EMC Corporation ("EMC") in January 2000 as President and Chief Operating Officer and since January 17, 2001 he has been President and Chief Executive Officer. . Prior to joining EMC, Mr. Tucci was Chairman and Chief Executive Officer of Wang Global and President of the U.S. Information Systems for Unisys Corporation. Mr. Tucci began his career as a systems programmer at RCA Corporation.

Roberto Ulissi. Mr. Ulissi was born in Rome on August 20, 1962. Mr. Ulissi received a degree in law from "La Sapienza" University of Rome with top grades and honors. Mr. Ulissi is the general manager, Head of the Directorate IV of the Ministry of the Treasury, Budget and Economic Planning and Contract professor of Banking Law at the faculty of economics University of Cassino and alternate member of the Board of Auditors of ENEL S.p.A. Mr. Ulissi is and has been a member of several committees and Board of Directors. He has published several studies related to corporate law. He is and has been a member of several commissions and boards involved in corporate and banking law.

Gérard Worms. Mr. Worms is general partner of Rothschild Paris and professor of Business at Ecole Polytechnique of Paris. Mr. Worms graduated as an Engineer from Ecole Polytechnique and Ecole Nationale Supérieure des Mines in Paris. Mr. Worms was Deputy Chief Operating Officer and Chief Executive Officer at Rhône Poulenc, Deputy Chief Executive Officer and Chief Executive Officer at Suez and Chief Operating Officer at Hachette. Mr. Worms is a member of the Board of Directors of Metropole Télévision, Mercapital, Odéo Degrémont, Paris-Orléans, Publicis, SIACI, Francarep, SGIM.

Executive Officers

For the biographical data of Mr. Colaninno see above under "Directors".

Enzo Badalotti. Enzo Badalotti was born in Mantua on September 28,1960. Since April 2001 he has been in charge of the International Operations Business Unit. Mr. Badalotti began his career in 1987 as Controller of Industrial Operations at the CIR Group. In 1994, he joined Omnitel as Planning and Operational Control Manager, a position he held until 1996, when he moved to the Olivetti Group. Until 1999 he held the post of Executive Vice President Operations at Olivetti and from 1997 to 1998 her served as a Board member at Omnitel and Infostrada. From 1998 to 1999 he was in charge of Group Industrial Operations. In 1999, he moved to Telecom Italia, where he served as Head of Operational Planning and Quality prior to assuming his current post. From April 2000 to May 2001 he was Head of the Telecom Italia Satellite Services business unit, and Chief Executive Officer of Telespazio. In May 2001, he became Chairman of Telespazio.

Stefano Braidotti. Stefano Braidotti was born in Rome on February 15, 1945. Since July 1999, Mr. Braidotti has been in charge of the Internal Auditing department, serving directly under the current Chairman and Chief Executive Officer. He was hired by SIP in April 1967 and, in October 1980, became Manager of the Organization and Plans Division. In 1984, Mr Braidotti transferred to the Strategic Planning Division, as head of "Scenarios". In early 1988, he worked with the head of the Strategic Planning Area – Information Systems. In January 1989, he became the assistant to the Chief Executive Officer, Mr. Silvano. From May 1991, Mr Braidotti acted as the assistant to Mr. Pascale, Chairman and, in May 1994, was appointed Managing Director. In September 1994, he transferred to the sector head company, STET, as Central Manager in charge of the technical secretariat of the Chief Executive Officer. In May 1997, with the STET-Telecom Italia merger, Mr Braidotti assumed the responsibility for the Internal Auditing.

Massimo Brunelli. Massimo Brunelli was born in Busto Arsizio, on October 16, 1958. He has been Chief Financial Officer at Telecom Italia since July 1999. Prior to this he held positions as Chief Financial Officer at Enel and Chief Financial Officer at the Olivetti Group. For eight years he worked in the US as Group Vice President and CFO of Elsag Bailey Process Automation, where he oversaw its quotation on the New York Stock Exchange. Mr Brunelli has had a broad range of work experience, most notably at Prometeia, where his responsibilities included advising banks and insurance companies; A. C. Nielsen, where he worked as a market research sector economist; and the Commission of the European Community, where he was responsible for company structure. Mr. Brunelli is currently Chairman of Stream and IMMSI and sits on the boards of TIM, Seat Pagine Gialle, Italtel, Finsiel and Lottomatica. He is Professor of International Finance at LUISS, Rome. He is also President of the ANDAF – National Association of Administration and Financial Managers.

Andrea Camanzi. Andrea Camanzi was born in Alfonsine on February 2, 1949. After a rich and varied career, he was appointed Head of Public and Regulatory Affairs at Telecom Italia in July 1999. From 1975 to 1978, he was a salesman for an Italian food industry trading company operating in Central and Eastern Europe and the Middle East. From 1978 to 1983, he worked as area manager for an industrial engineering and planning concern operating in Central and Eastern Europe. From 1983 to 1989, Mr Camanzi held the post of European Affairs Manager for the *Lega delle Cooperative* (Italian Co-operatives Union). He worked at Olivetti as area manager for Eastern and Central Europe from 1989 to 1993. Thenceforth, he held the position of European Affairs Manager, before receiving a promotion to Head of Legal, Institutional and Regulatory Affairs in 1996, a post he held until 1999, when he moved from Olivetti to Telecom Italia.

Pierpaolo Cotone. Pierpaolo Cotone was born in Rome on August, 14 1951. Since August 2000 he has been in charge of Telecom Italia Corporate and Legal Affairs. He began his career in legal banking, as a manager at the Head Office of Banca Cattolica del Veneto in Vicenza, before moving on to the Banca Nazionale dell’Agricoltura in Rome. Between 1984 and 1995 he was Head of Alitalia Fiscal, Legal & Corporate Affairs, and additionally sat on the Board of Directors. From 1996 to July 2000, he was Manager of Legal, Corporate, Fiscal and Insurance Affairs, and Member of the Board of Directors at Aeroporti di Roma SpA. He has filled a number of positions at IRI Group companies, including, most recently, that of Director of Genoa Airport, Deputy Chairman of ADR Engineering, Deputy Chairman of ADR Handling, and Chairman of ADR International Airport South Africa Ltd. He has also sat on the Board of Airport Invest BV and ACSA Airport Company South Africa. Mr. Cotone holds a research fellowship into commercial and navigational law at the LUISS Guido Carli University of Roma. He’s Secretary to the Board of Directors of Telecom Italia.

Marco De Benedetti. Marco De Benedetti was born in Turin in 1962. On July 2, 1999 he was appointed TIM Chief Executive Officer, and took on his role as a member of the Remuneration Committee. Mr De Benedetti began his career with the marketing department of Procter & Gamble. From 1987 to 1989 he worked in Mergers & Acquisitions for Wasserstein, Perella & Co, a New York merchant bank. He joined Olivetti in 1990 as assistant to the 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.

Andrea Granelli. Andrea Granelli was born in Bergamo on November 13, 1960. In January 2001, he was appointed CEO of Telecom Italia Lab, the Group company responsible for venture capital, incubation, and research and development operations. Mr. Granelli's early career included a period as head of office automation at CESI (Centro Elettrotecnico Sperimentale, ENEL) in 1986. The following year, he took over information technology planning and control at (Montedison Group company) Iniziativa ME.T.A.'s Strategic Management Office. From 1988 to 1989, he worked at Fimedit (a Iniziativa ME.T.A./Gruppo Ferruzzi 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 activities at the company's Italian office. That same year Mr Granelli began working for Video On Line and, in 1996, assumed responsibility 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 Video 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, the division responsible for the commercialization of TIN. In May 1999, he took over responsibility for Telecom Italia Internet management, and was subsequently named Tin.it CEO. In April 2000, Mr Granelli took charge of the Venture Capital and Innovation Business Unit.

Mario Luzzi. Mario Luzzi was born in Rome on May 2, 1967. Since June 2000, he has been Head of Corporate Strategy at the Telecom Italia Group. He began his career in 1990 at Procter & Gamble Italia. By the time he left in 1992, he had risen to Planning Manager at the Health and Beauty Care division. After obtaining an MBA from Columbia Business School, he took up a position at Bain & Co. Italia, where he acted as Head of Media and Multimedia from 1994 to 1999. During this time he worked on the project to reorganize RAI and, in 1999, he became a partner. Between 1999 and 2000, he served as CEO of Fininvest Multimedia, the Group's Internet operations holding company, where his focus was business start-ups. He conceived, launched and developed Jumpy in Italy and Spain; he also managed direct investment activities (GSM Box, Starmedia, etc.), and launched two venture capital firms. Mr Luzzi is currently a Board member of Telecom Italia Information Technology S.p.A., Seat Pagine Gialle S.p.A and Saritel S.p.A.

Roberto Maglione. Roberto Maglione was born in Vercelli on August 20, 1957. Since April 2001, Mr. Maglione has been Head of Human Resources at Telecom Italia Group. Mr. Maglione began his career in economic research management at Olivetti & Co S.p.A. in Ivrea in 1983. He received promotions through the Olivetti Group, and worked in a number of administrative positions. In 1987, he was placed in charge of market analysis and economic and industrial policy; in 1990 he took over the Office for Relations with the European Community. In 1992, he was appointed chief of the New Ventures unit, before taking over responsibility for Research, Projects and Territorial Coverage in 1995. In 1996, he became assistant to CEO Roberto Colaninno. In 1998, Mr Maglione was appointed Director of Human Resources at Olsy, Olivetti solutions. He served as a member of the Top Level Implementation Team for the merger of Olivetti Solutions and Wang and the start-up of Wang Global, as well as Deputy Chairman of Olivetti Ricerca S.C.p.A. That same year he acted as Head of Olivetti Group Personnel and as interim Head of Olivetti Lexikon Personnel. He also served as Chairman of SEVA (Servizi e Soluzioni per l'Amministrazione del Personale). In 1999 Mr Maglione joined the Telecom Italia Group as Head of Personnel for TIM (Telecom Italia Mobile).

Vittorio Meloni. Vittorio Meloni was born in Milan on October 14, 1956. Head of Corporate Communications and Image at Telecom Italia Group since July 1999. Prior to this, from 1996 to July 1999, Head of Olivetti Group Communications and Image. As part of this job, specific responsibilities included handling all communications during the Olivetti - Tecnost takeover campaign. Between 1990 and 1995, Head of Communication at Alfa Romeo; from 1984 to 1989, Communications Manager at IBM. Previous employment includes being a manager at the Lombardy Regional Administration, and Private Secretary to the Vice Presidency and to the council's office for employment. From 1982 to 1985, researcher at the University of Milan History of Political Doctrine unit at the Faculty of Political Science. In May 2001 he joined the Board of Directors of SEAT.

Vittorio Nola. Vittorio Nola was born in Bologna on March 10, 1955. Since April 2000 he has been General Secretary of Telecom Italia and is Assistant to the Chairman and Chief Executive Officer and responsible for the Chairman's Staff. After his first experiences at Seat Company and at IRI in Rome, in 1990 he worked for STET S.p.A. responsible for the Internal Auditing Department at SEAT Division in Turin. In January 1992 he became responsible for the Top Management Division at STET S.p.A. In January 1993 he became responsible for the STET Chairman's Staff and in December 1994 he was appointed the Secretary's Assistant of STET Board of Directors. In February 1997 he was responsible for STET company bodies. In July 1997, after the merger STET Telecom Italia, he became responsible for the company bodies at TELECOM ITALIA S.p.A. In October 1998 he was appointed as assistant of Telecom Italia's Chairman, Prof. Berardino Libonati, and responsible for the relationship with the Managing Shareholders and the relationships between the Board of Auditors and the Company Functions. At the moment he is also member of the Board of Directors of FINSIEL and TRAINET Company.

Lorenzo Pellicioli. Lorenzo Pellicioli was born on July 29, 1951 at Alzano Lombardo, Italy. Since April 2000 he has been in charge of the Telecom Italia Internet/Media business unit. He began his career as a journalist at the *Giornale* in Bergamo, before taking on a job as Director of Programming at Bergamo TV. Between 1978 and 1981, at the time when Italy's first commercial television networks began to develop, he ran the Audiovisual Office at advertising concessionary A. Manzoni & C. From 1981 to 1984 he directly experienced the most significant developments, including rationalization, of the Italian television industry, leading to establishment of the present-day structure, initially as Director of Television for Publikompass (Fiat Group), and subsequently as Director of the Rete4 Channel. In 1984 he moved into publishing, initially as General Advertising Manager and Deputy General Manager of periodicals at Mondadori, before in 1988 becoming Chief Executive Officer of Manzoni & C. S.p.A. In 1990 Mr Pellicioli became Chairman and Chief Executive Officer of Miami-based Costa Cruise Lines, part of the Costa Cruises Group which operates in the North American market (US, Canada and Mexico). Between 1992 and 1997 he was the General Manager of Costa Crociere S.p.A., working out of Genoa. In 1995 he was appointed PDG (Président Directeur Général) of the Compagnie Francaise de Croisières (Costa-Paquet), based at the Costa Cruises offices in Paris. In November 1997 he became Chief Executive Officer of SEAT, the company that publishes the Yellow Pages and Telephone Directories in Italy. SEAT controls a number of companies in the multimedia business, with interests in the Internet and trade publishing, television and business information. In May 2001, he became Chairman of SEAT.

Salvatore Pinto. Salvatore Pinto was born in Torre Annunziata, Italy, on November 27, 1957. Since May 2001 he has been Head of the Telecom Italia Satellite Services Business Unit. Mr. Pinto began his career in 1983 with the STET Group, where he acted as CAE/CAD Project Leader in Milan for the ITALTEL/GTE/TELETTRA consortium. In 1987 he moved on to Italcable, where he was responsible for telecommunications software. That same year he began working for Olivetti, covering a number of managerial positions until 1992. From 1992 to 1993 he worked as Country Sales Manager for TANDEM COMPUTERS. In 1993 he was hired by Pirelli as Sales Manager for Italy, before taking over the position of OEM Worldwide Sales Manager. He returned to TANDEM COMPUTERS in 1994 as Chief Executive Officer. During his time there, he served on the task-force that prepared the Compaq deal, and acted as Chief Executive Officer of Twinsoft, a joint venture between Tandem and Marben Group. In 1996 he was appointed Area Manager for Italy, North Africa and the Middle East for OLIVETTI-OLSY. He also joined the Board of Olivetti Ricerca. In March 1998 he became Chief Executive Officer of OLIVETTI-WANG GLOBAL. In January 1999 he was appointed Chief Executive Officer of the IPM GROUP. Mr Pinto has been Chief Executive Officer of Telespazio since May 2001. Among his other responsibilities, he is a member of the management committee at Anasin.

Gilberto Ricci. Gilberto Ricci was born in Rome, Italy, on January 16, 1942. In April 2000 he was appointed Head of the Telecom Italia IT Services Business Unit, with responsibility for managing the rationalization and extraction of value from Group IT operations. In July 2000 he became Chairman and Chief Executive Officer of I.T. Telecom (Telecom Italia Information Technology S.p.A.). Since beginning his career in 1961, he has worked at Banco di Roma, Olivetti and Olivetti General Electric. From 1969 to 1997 he covered a number of positions, with a variety of responsibilities, at Finsiel Group companies. Between March 1997 and March 2000 he was Chief Executive Officer at SOGEI S.p.A. – Telecom Group. Mr. Ricci's current responsibilities at IT Services Business Unit include that of Chief Executive Officer and Chairman of Finsiel, Chairman of SOGEI S.p.A., Chairman of Netsiel and Chairman of NETIkos S.p.A., I.T. Telecom's web professional company. He also sits on the Board of Lottomatica S.p.A., Banksiel S.p.A., Telesoft S.p.A., WEBEGG S.p.A., Scuola Superiore Reiss Romoli S.p.A.

Rocco Sabelli. Rocco Sabelli was born in Agnone, Italy, on August 12, 1954. Since April 2000 he has been Head of Telecom Italia's Wireline Services Business Unit, which is responsible for the company's fixed wire telephony and corporate Internet operations. Mr Sabelli began his career in 1983 when he joined GEPI as an analyst at the Acquisitions and Partner Research Department. Two years later he was appointed "senior analyst" at ENI Group company AGENI, in 1986 becoming head of the Feasibility Service. In 1990 he was named Chairman of ENI Group finance company NUOVA INDENI S.p.A. In 1992 he was hired by SIP as Head of Lazio Region Management Planning and Control, in the Basic Services Division. Following the merger of Italcable, Iritel, Sirm and Telespazio with SIP, he was assigned responsibility for Planning and Control at the Information Technologies Department of Telecom Italia's head office. In 1995 he moved to TIM as Head of Planning and Operations Control. In May 1997 he was appointed Deputy General Manager at TIM, and from 22 May until July 1999 he held the post of General Manager. In July 1999 he was appointed Head of Telecom Italia Domestic Market operations. Since February 9, 2001 he has also held the positions of Chairman of Atesia and Saritel.

Employees

At December 31, 2000 the Group employed 114,669 persons, a decrease of 7,993 employees compared to122,662 at December 31, 1999. The reduction of 7,993 units is due to personnel turnover and the effect of the change in the scope of consolidation. 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 the agreements, described below, with the labor unions in March and July 2000. In addition, the exclusion of the Sirti group and the Italtel group led to a reduction in the number of employees of 17,857 offset by the addition of 17,567 units which have been added due to the change in scope of consolidation of the group during 2000 relating to the Nortel Inversora group (7,498 units), Maxitel (1,229 units) and the SEAT group (7,515 units).

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 will be made for the three years 2000-2002, amounting to Lit. 150 billion for each year to be charged to the companies which have employees registered in the abolished fund. Telecom Italia Group's contribution will be charged on an accrual basis over the three year period.

In March and July 2000 agreements were reached with the unions concerning the development and reorganization of Telecom Italia. The agreements allow the Company to reach stated objectives in terms of employees cutbacks and operating cost reductions. As a result, Telecom Italia should be in a stronger and more efficient position to face a market characterized by extremely rapid evolution and growing competition.

Approximately 2% of the Group's employees held executive positions at December 31, 2000.

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 will expire 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, 2000 broken down by geographical areas:

	Manager	Professional	White-collar	Blue-collar	Total
Italy	2,035	4,470	77,009	10,067	93,581
Europe excluding Italy	50	1,696	5,949	33	7,728
North America	2	7	97		106
South America	113	590	6,799	5,681	13,183
Asia	1	4	64		69
Africa and Oceania			2		2
Group Total	2,201	6,767	89,920	15,781	114,669

The following table represents the personnel of the Group at December 31, 2000 by category of activity:

	Number of employees at end of period	
	2000	1999
Wireline telecommunications in Italy	66,541	76,113
Mobile telecommunications in Italy	9,634	9,375
Satellite telecommunications	1,194	1,287
International telecommunications	15,943	5,714
Information technology activities	11,280	10,206
Manufacturing activities	–	5,153
Installation activities	–	12,704
Sub-total	104,592	120,552
Other activities and eliminations	10,077	2,110
Consolidated total	114,669	122,662

COMPENSATION OF DIRECTORS AND OFFICERS

The total compensation paid in 2000 by Telecom Italia or by any of Telecom Italia subsidiaries to (i) the members of the Board of Directors was Lit. 15,702 million (which includes Lit. 7,000 million in bonus compensation) (ii) to the executive officers was Lit. 19.35 billion [(1)] (iii) and to the members of the Board of Statutory Auditors was Lit. 1,593 million.

The following table lists the Directors and the Board of Statutory Auditors of Telecom Italia during 2000 and their respective compensation for the year ended December 31, 2000.

Board of Directors

Name	Position	Period	Compensation Base	Bonus	Other Compensation
			(in millions of Lit.)		
Roberto COLANINNO	Chairman and Chief Executive Officer	Jan. 01/00 – Dec.31/00	6,800(2)	7,000(3)	200 (4)
Antonio TESONE	Honorary Chairman	Jan. 01/00 – Dec.31/00	122		
Sergio EREDE	Deputy Chairman	Jan. 01/00 – Dec.31/00	205		(5)
Angelo BENESSIA	Director	Jan. 01/00 – Dec.31/00	205		(6)
Enrico BONDI	Director	Jan. 01/00 – May 14/00	37		
Peter A. COHEN	Director	Jan. 01/00 – Dec.31/00	205		
Salvatore DONATO	Director	Jan. 01/00 – Dec.31/00	125		
Paolo FERRO-LUZZI	Director	Jan. 01/00 – Dec.31/00	95		
Ettore LONATI	Director	May 15/00 – Dec.31/00	78		
Emilio GNUTTI	Director	Jan. 01/00 – Dec.31/00	122		
Jeffrey E. LIVINGSTON	Director	Jan. 01/00 – Dec.31/00	208		
Domenico GIOVANNI SINISCALCO	Director	Jan. 01/00 – Dec.31/00	208		
Joseph M. TUCCI	Director	Jan. 01/00 – Dec.31/00	110		
Gèrard WORMS	Director	Jan. 01/00 – Dec.31/00	182		

Board of Statutory Auditors

Paolo GERMANI	Chairman	July 03/00 - Dec. 31/00	112		
Mario BOIDI	Statutory Auditor	Jan. 01/00 - Dec. 31/00	175		47 (7)
Paolo GOLIA	Statutory Auditor	July 03/00 - Dec. 31/00	75		
Fabrizio QUARTA	Statutory Auditor	Jan. 01/00 - Dec. 31/00	175		
Gianfranco ZANDA	Statutory Auditor	Jan. 01/00 - Dec. 31/00	175		238 (8)
Ugo LA CAVA	Chairman	Jan. 01/00 -July 02/00	125		191 (9)
Piero ADONNINO	Statutory Auditor	Jan. 01/00 - July 02/00	100		180 (10)

(1) Such amount includes:

- Lit. 3.9 billion paid by Telecom Italia to certain employees who are no longer employed by Telecom Italia and employees who no longer qualify as executive officers but were included as executive officers in 2000.
- Lit. 300 million paid by TIM to Marco De Benedetti as compensation for his services as Chief Executive Officer of TIM.
- amounts paid by SEAT to Lorenzo Pellicioli of (a) Lit. 93 million for his employment with SEAT, (b) Lit. 1 billion as Chief Executive Officer and member of the executive committee of SEAT and (c) Lit. 98 million in non monetary benefits.

Such amount does not include the compensation paid to Roberto Colaninno which is disclosed in the table above.

Bonus compensation represents 33% of executive officers' total compensation. Such bonus compensation is determined by the Chief Executive Officer 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 2000 Telecom Italia reserved Lit. 314 million as supplemental retirement benefits for its executive officers.

(2) Aggregate of base compensation (Lit. 3,800 million) and bonus (Lit. 3,000 million) paid pursuant to an individual contract between Roberto Colaninno and Telecom Italia. Such cumulative base compensation covers all corporate functions of Roberto Colaninno with any company of the Group and their affiliates.

(3) Payment of non-recurring bonus approved by The Board of Directors at their meeting of December 15, 2000.

(4) Compensation for the position of Chairman of TIM Board of Directors, paid to Telecom Italia.

(5) The professional association Bonelli Erede Pappalardo, of which Sergio Erede is a partner, in 2000 received Lit. 10,300 million for professional services rendered by its members to Telecom Italia and its subsidiaries.

(6) In 2000 Angelo Benessia received Lit. 645 million for professional services rendered to Telecom Italia and its subsidiaries.

(7) Compensation for the position of statutory auditor of Stet International and Chairman of the board of statutory auditors of Tin.it.

(8) Compensation for the position of statutory auditor of Finsiel, Immsi, Telespazio and TIM.

(9) Compensation for the position of statutory auditor of Sogei and chairman of the board of statutory auditors of Finsiel, Immsi, Pathnet and Saiat.

(10) Compensation for the position of chairman of the board of statutory auditors of TIM.

In addition to the base and bonus compensation described above, Mr. Colaninno's contract also provides for:

- reimbursement of expenses related to his role as Chairman and Chief Executive Officer
- entitlement to the use of certain Telecom Italia premises in Rome
- Telecom Italia to provide certain life, health and disability insurance.

The contract also provides that if Mr. Colaninno's employment is terminated with or without just cause he will be entitled to the compensation provided for under the contract until the end of its term. The contract term is three years from his appointment on June 28, 1999.

OPTIONS TO PURCHASE SECURITIES FROM REGISTRANT OR SUBSIDIARIES

Stock option plan

The Board of Directors, for a maximum period of five years from the date of the shareholders' resolution authorizing the transaction (such resolution dated December 15, 1998 was subsequently amended on August 10, 2000 and May 3, 2001) has the power to increase the Company's share capital by payment, in one or more installments and to issue new Shares, which will rank for dividend pari passu, to be offered for subscription to managers and executive officers of Telecom Italia or its subsidiaries selected by the Board of Directors as participants in the Stock Option plan. See "Item 10. Additional Information—Description of By laws and of Capital Stocks — Capital Stock".

The stock option plan provides the Company with an effective tool to develop corporate loyalty and offers incentives, in line with internationally accepted practices.

Within this framework in 1999, a group of executives employed by Telecom Italia and its subsidiaries were assigned a total of 16,595,400 options to be subscribed against payment for the same number of new Shares. The options are personal and non-transferable. The Board of Directors established the subscription price according to the terms of the authorization it received.

With respect to options granted:

- 4,905,500 Shares were subscribed to and issued by the end of the year 1999;
- with respect to 5,754,900 Shares, the subscription period began on January 2, 2001 after having reached the established targets based on stock market performance;
- for the remaining Shares, the subscription period begins from January 2002 on condition that the Shares reach a predetermined performance target in December 2001.

The period to exercise the options granted in 1999 was fixed at three years from notification of having reached the set targets; therefore, the capital increase servicing the 1999 stock option plan will close on January 31, 2005.

During 2000, also in view of changes in the tax laws covering stock option plans, a decision was made to propose to the extraordinary stockholders' meeting a change in the mechanism for fixing the subscription price of the Shares servicing the plan (that was, the average official price of the Shares on Telematico in the six months preceding the incentive period), granting the Board of Directors the discretion to determine, each time, the price for each tranche of share capital increase.

These proposed changes in the original mandate were approved by the extraordinary stockholders' meeting of August 10, 2000 and the related resolutions were homologated by decree of the Turin Courts on September 29, 2000, successively confirmed by decree of the Appeals Court in Turin on October 20, 2000 only for the part covering the change in price. Subsequent to this change, all aspects of the stock option cycle begun in February 2000 were decided and, accordingly, a total of 51,430,000 options were granted, valid for the subscription of the same number of newly issued Shares (corresponding to 0.6% of outstanding share capital at December 31, 2000), against payment of an exercise price equal to the arithmetic average of the official prices of Shares on Telematico during the period August 11, 2000 to September 11, 2000, consistent with existing applicable laws. Such options can be exercised, also in part, in three distinct lots, subject to having reached the performance targets represented by the comparison of the ratio between the average market prices recorded by the stock in specific periods and the ratio between the arithmetic average of the closing prices of the Dow Jones EuroStoxx TLC index representing a basket of stocks in the sector over the same periods; however, in the event the established targets are only reached for the second or third tranche, the beneficiaries of the previous tranches will nevertheless be allowed to exercise their rights. In addition, the most important senior management who have the most impact on the Group's business have been assigned an additional extraordinary number of options which can be exercised provided that, when the conditions for exercising the rights of the third tranche are met, the market price of the Shares will have also appreciated to a predetermined level. The period to exercise these options has been established at five years from notification of having reached the corresponding incentive targets; therefore, the capital increase servicing the 2000 stock option plan will be closed in July, 2008.

The following summary of the essential elements of the stock option plan existing at December 31, 2000 is provided as set forth by the recommendation contained in CONSOB Communication No. 11508 of February 15, 2000.

	Year ended December 31, 2000		
	Number of shares	Exercise price (euro)	Market price (euro.) (1)
a. Outstanding options January 1, 2000	11.689.900	6.791	14.118
b. New options assigned during 2000	51.430.000	13.815	13.571
c. Options exercised during year	-	–	–
d. Options expired and not exercised during year	–	–	–
e. Options forfeited during the year	(278)	6.791	14.542
f. Options outstanding at December 31, 2000(2)	62.841.500	12.539	11.902

(1) Weighted average market price for the quantities indicated in (b) and (e); actual price for (a) and (f).

(2) Of which none are held by Directors and 17,574,800 are held by Executive Officers.

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 15, 2001, 54.96% of the Shares of Telecom Italia. The Conversion Offer may result in a significant reduction of such stake (see "Item 4. — Information on the Company — Recent Developments — Conversion of Saving Shares for Shares and Tender Offer for Shares")

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 15, 2001, 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 (13 Directors and 15 Executive Officers)	331.512	0.01
	Board of Statutory Auditors as a group (5 persons)	0	0
Savings Shares	Directors and executive officers as a group (13 Directors and 15 Executive Offers)	339.766	0.02
	Board of Statutory Auditors as a group (5 persons)	0	0

The following table shows the ownership of Shares and Savings Shares by the directors and statutory auditors as of December 31, 2000

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 2000
Board of Directors						
Roberto COLANINNO	(1)	Shares	23,000	494,000	225,000	292,000
		Savings Shares	—	910,000	380,000	530,000
Antonio TESONE		—	—	—	—	—
Sergio EREDE		—	—	—	—	—
Angelo BENESSIA		—	—	—	—	—
Peter A. COHEN		—	—	—	—	—
Salvatore DONATO		—	—	—	—	—
Paolo FERRO-LUZZI		—	—	—	—	—
Ettore LONATI	(2)	Shares	109,250	2,250	111,500	—
		Savings Shares	7,500	109,000	10,500	106,000
Emilio GNUTTI	(1)	Shares	660,000	703,500	1,362,000	1,500
Jeffrey E. LIVINGSTON		—	—	—	—	—
Domenico Giovanni SINISCALCO		—	—	—	—	—
Joseph M. TUCCI		—	—	—	—	—
Gérard WORMS		—	—	—	—	—
Enrico BONDI		—	—	—	—	—

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 2000
Board of Statutory Auditors						
Paolo GERMANI		—	—	—	—	—
Mario BOIDI		—	—	—	—	—
Paolo GOLIA		—	—	—	—	—
Fabrizio QUARTA		—	—	—	—	—
Gianfranco ZANDA		—	—	—	—	—
Piero ADONNINO	(3)	Shares	1,100	1,000	—	2,100
		Savings Shares	—	1,000	—	1,000
		Shares (1)	—	3,000	—	3,000
		Savings Shares (1)	—	1,000	—	1,000

(1) Shares not held directly

(2) Shares held from May 15, 2000, beginning term of office.

(3) Shares held until July 2, 2000, date of the end of office.

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 15, 2001, 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 By-laws. See "Item 10. Additional Information — Description of By Laws and Capital Stock — Capital Stock—Limitations on Voting and Shareholdings — Special Powers of the State" for a description of such special powers and Item 6. "Directors, Senior Management and Employees of Registrant".

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 By-laws must be exercised according to the terms and in compliance with the principles provided for by the Golden Share Decree.

RELATED PARTY TRANSACTIONS

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. Telecom Italia believes that 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. See "Item 4. Information on the Company — Recent Developments".

The following related party transactions are reflected in the statement of income for the year ended December 31, 2000:

Operating revenues: comprise mainly revenues from SEAT (Lit. 409 billion in 2000 and Lit. 308 billion in 1999), Teleleasing (Lit. 219 billion in 2000), Stream (Lit. 198 billion in 2000 and Lit. 153 billion in 1999), Nortel Inversora group (Lit. 157 billion in 2000 and Lit. 177 billion in 1999), Lottomatica (Lit. 112 billion in 2000 and Lit. 85 billion in 1999) and Auna group (Lit. 110 billion in 2000). In the aggregate, operating revenues were Lit. 1,620 billion in 2000 (Lit. 1,078 billion in 1999).

Cost of materials and other external charges: refers mainly to expenses regarding Siemens Informatica (Lit. 155 billion in 2000 and Lit. 73 billion in 1999), SEAT (Lit. 119 billion in 2000 and Lit. 176 billion in 1999), Teleleasing (Lit. 114 billion in 2000), Entel Chile Group (Lit. 77 billion in 2000), Etec S.A. (Lit. 46 billion in 2000) and IM.SER (Lit. 44 billion in 2000). In the aggregate, cost of materials and other external charges accounted for Lit. 730 billion in 2000 (Lit. 469 billion 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 Lit. 37 billion in 2000 (Lit. 50 billion in 1999).

Interest income, net: comprises dividends received from the Eutelsat satellite consortium (Lit. 123 billion in 2000) and interest earned on loans made to some foreign unconsolidated subsidiaries and affiliated companies and interest expense payable to Teleleasing (Lit. 60 billion in 2000) for financial leasing transactions. In the aggregate, interest income, net was Lit. 105 billion in 2000 (Lit. 37 billion in 1999).

The following related party transactions are reflected on the balance sheet as of December 31, 2000:

Loans in long-term investments: refers to loans granted to Bouygues Décaux Télécom (BDT) (Lit. 198 billion at December 31, 2000) and other foreign unconsolidated subsidiaries and affiliated companies. In the aggregate such loans were Lit. 268 billion at December 31, 2000 (Lit. 293 billion at December 31, 1999).

Trade accounts receivables: comprises mainly trade accounts receivable from Telekom Srbija (Lit. 127 billion at December 31, 2000 and Lit. 48 billion at December 31, 1999), Auna group (Lit. 92 billion at December 31, 2000), Golden Lines International (Lit. 49 billion at December 31, 2000 and Lit. 35 billion at December 31, 1999), Stream (Lit. 45 billion at December 31, 2000 and Lit. 215 billion at December 31, 1999), Nortel Inversora group (Lit. 43 billion at December 31, 2000 and Lit. 58 billion at December 31, 1999), Consortium CSIA (Lit. 26 billion at December 31, 2000) and Etec S.A. (Lit. 25 billion at December 31, 2000). In the aggregate trade accounts receivables were Lit. 540 billion at December 31, 2000 (Lit. 800 billion at December 31, 1999).

Trade accounts payable: pertains to supplier relationships connected with investments and transactions. In particular, they comprise trade accounts payable to Italtel group (Lit. 536 billion at December 31, 2000), Entel Chile group (Lit. 79 billion at December 31, 2000), Siemens Informatica (Lit. 74 billion at December 31, 2000 and Lit. 117 billion at December 31, 1999), Telekom Srbija (Lit. 44 billion at December 31, 2000), Teleleasing (Lit. 43

billion at December 31, 2000), Golden Lines International (Lit. 32 billion at December 31, 2000), Auna group (Lit. 25 billion at December 31, 2000), Etec S.A. (Lit. 22 billion at December 31, 2000) and Telekom Austria group (Lit. 20 billion at December 31, 2000). In the aggregate trade accounts payable were Lit. 1,386 billion at December 31, 2000 (Lit. 613 billion at December 31, 1999).

Long-term debt: refers to account payables to Teleleasing for financial leasing contracts. Such long-term debt was Lit. 1,073 billion in the aggregate at December 31, 2000.

Short-term debt: includes payables to IM.SER (Lit. 156 billion at December 31, 2000), Webegg (Lit. 57 billion at December 31, 2000) and Italtel group (Lit. 38 billion at December 31, 2000). In the aggregate short-term debt was Lit. 266 billion at December 31, 2000.

Short-term financial receivables: refers mainly to receivables from the affiliates of SEAT (Lit. 116 billion at December 31, 2000), Stream (Lit. 106 billion at December 31, 2000 and Lit. 56 billion at December 31, 1999) and Telekom Srbija (Lit. 41 billion at December 31, 2000 and Lit. 37 billion at December 31, 1999). In the aggregate short-term financial receivables were Lit. 339 billion at December 31, 2000 (Lit. 221 billion at December 31, 1999).

Other current assets: refers mainly to prepaid expenses for lease payments to IM.SER (Lit. 89 billion at December 31, 2000). In the aggregate other current assets accounted for Lit. 95 billion at December 31, 2000.

Other current liabilities: comprise mainly payables to Astrolink (Lit. 183 billion at December 31, 2000 and Lit. 322 billion at December 31, 1999) for capital contributions payable. In the aggregate other current liabilities accounted for Lit. 229 billion at December 31, 2000 (Lit. 694 billion at December 31, 1999).

Long and short-term contracts: refers to contract work in process by Telespazio for Astrolink. In the aggregate such work in process accounted for Lit. 138 billion at December 31, 2000.

Capital expenditures: consist mainly of acquisitions from Italtel (Lit. 357 billion in 2000 and Lit. 754 billion in 1999) and Siemens Informatica (Lit. 61 billion in 2000 and Lit. 153 billion in 1999). In the aggregate investments in fixed and intangible assets accounted for Lit. 453 billion in 2000 (Lit. 1,238 billion in 1999).

SEAT

In connection with the 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, 2000 holds approximately 55 per cent of Telecom Italia. A dividend of approximately Lit. 1,719 billion was paid to Tecnost (now merged into Olivetti) in 2000 (approximately Lit. 767 billion in 1999).

Directors and Executive Officers

Based on a contract signed on March 15, 2000 by Telecom Italia, Huit II, Huit and its shareholders, and Lorenzo Pellicioli (the CEO of SEAT), regarding the integration of Tin.it into SEAT, and furthermore, by virtue of previous agreements, Lorenzo Pellicioli 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 Lit. 37 billion to the benefit received by Lorenzo Pellicioli.

A director of the Group is a partner in a law firm (Bonelli Erede Pappalardo Studio Legale) that provides legal services to the Group on a recurring basis. The Group paid legal fees to this law firm totaling Lit. 10,300 million in 2000 (Lit. 1,725 million in 1999).

One of the group directors, Mr Peter Cohen, is a managing member of Ramius Capital Group who is a 50/50 partner with Telecom Italia in a partnership which oversees an investment entity called Saturn Venture Partners. Saturn Venture Partners invests in private equity transactions in telecommunications and related businesses.

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.

U.S. GAAP Unaudited Pro Forma Condensed Consolidated Statement of Income of Telecom Italia for the year ended December 31, 2000

The following unaudited pro forma condensed consolidated statement of income is presented to illustrate the effects of acquiring a controlling stake in SEAT, which consisted of

- the purchase of SEAT shares through a tender offer and other negotiated purchases; and,
- the contribution by Telecom Italia of Tin.it S.p.A to SEAT in exchange for a controlling interest in SEAT;

on the historical operating results of Telecom Italia for the year ended December 31, 2000.

Telecom Italia has accounted for the SEAT acquisition ("the Acquisition") using the purchase method of accounting, under which tangible and identifiable intangible assets acquired and liabilities assumed are recorded at their respective fair values. The unaudited pro forma condensed consolidated statement of income includes such adjustments as are necessary to give effect to events directly attributable to the Acquisition, which are expected to have a continuing impact on the Group's results and are factually supportable.

The unaudited pro forma condensed consolidated statement of income is presented in accordance with U.S. GAAP and covers the following aspects of the Acquisition:

- The acquisition on August 3, 2000, from Huit II S.a.r.l., a holding company in which Telecom Italia has an indirect interest, of ordinary shares representing approximately 15 percent of the share capital of SEAT for cash consideration of Lit. 7,199 billion. In November, a further 0.01 percent of share capital of SEAT was acquired from Huit II for cash consideration of Lit. 12 billion. These transactions increased current liabilities and goodwill based on the difference between the purchase price and the fair market value of the net assets acquired;
- the acquisition on August 18, 2000, of approximately 12 percent of the share capital of SEAT for cash consideration of Lit. 4,620 billion as a result of the voluntary tender offer by Telecom Italia in May 2000 for the ordinary and savings shares of SEAT. This transaction increased current liabilities and goodwill based on the difference between the purchase price and the fair market value of the net assets acquired;
- the demerger transaction on November 10, 2000, whereby Telecom Italia transferred to SEAT 8.168 percent of the share capital of Tin.it. In exchange, SEAT issued new ordinary shares, representing, on a fully diluted basis, approximately 4 percent of the share capital of the combined SEAT and Tin.it company, to Telecom Italia's shareholders. This transaction has been reflected as a non-cash dividend by Telecom Italia at fair value, with a gain being recognized by Telecom Italia for the difference between the fair value of the SEAT ordinary shares distributed to Telecom Italia's shareholders and the carrying value of the interest in Tin.it distributed. The gain was Lit. 2,574 billion as determined by reference to the quoted market price of SEAT shares on November 10, 2000, the date the shares were issued directly to Telecom Italia's shareholders. This gain has not been reflected in the attached unaudited pro forma condensed consolidated statement of income because the impact is non-recurring;
- the exchange on November 15, 2000, of the remaining 91.832 percent interest in Tin.it for approximately an additional 28 percent interest in SEAT. The fair value of the transaction has been determined by reference to 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. After this transaction Telecom Italia had approximately a 60 percent interest in the combined SEAT and Tin.it

company. Telecom Italia has recognized a gain to the extent of its reduced ownership in Tin.it. This gain has not been reflected in the unaudited pro forma condensed consolidated statement of income because the impact is non-recurring. The gain was Lit. 12,657 billion (Lit. 7,974 billion, net of taxes);

- the acquisition on November 20, 2000 of ordinary shares representing approximately 0.5 percent of the share capital of SEAT for cash consideration of Lit. 500 billion. This transaction increased current liabilities and goodwill based on the difference between the purchase price and the fair market value of the net assets acquired; and

- the agreement announced on December 5, 2000, whereby a company in the Chase Manhattan Group ("Chase") acquired from Huit II a put option previously issued in March 2000, by Telecom Italia to Huit II. The option granted Huit II the right to put approximately 710 million SEAT shares to Telecom Italia at Euro 4.20 per share after the conclusion of the SEAT/Tin.it merger. The agreement resulted in Chase acquiring approximately 710 million SEAT shares from Huit II along with Huit II's put option for Euro 2,985 million, delaying the initial put strike for at least three years and issuing a call option to Telecom Italia for approximately 660 million SEAT shares, referred to collectively as the "SEAT put/call". This transaction has been accounted for as the financing of an acquisition of an additional interest in SEAT.

The goodwill arising on the Acquisition is approximately Lit. 26,787 billion. Since the announcement of the Acquisition in February 2000, technology companies, particularly those in the internet sector, have experienced significant declines in market valuations, many of which can be considered other than temporary. In particular, significant changes to the valuations of these companies have occurred due to, among other things, the downward adjustments of future growth rates, expected profitability and cash flows. The current valuations for these companies, including SEAT, suggest that acquisition valuations performed in early 2000 are no longer considered sustainable. As of the end of 2000, Telecom Italia has reviewed the total amount of goodwill recorded for the SEAT acquisition in accordance with FAS 121, Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of . Following an analysis of the SEAT business plan, a discounted cash flow analysis was performed and Telecom Italia determined the investment to be impaired, resulting in an impairment charge of Lit. 15,424 billion for U.S. GAAP purposes.

The unaudited pro forma condensed consolidated statement of income for the year ended December 31, 2000 has been prepared as if the series of transactions had occurred on January 1, 2000. The unaudited pro forma condensed consolidated statement of income is presented for informational purposes only and, because of its nature, is not necessarily indicative of the results of operations of Telecom Italia had these transactions in fact occurred on such date nor of the results of operations of Telecom Italia for any future period.

U.S. GAAP UNAUDITED PRO FORMA CONDENSED CONSOLIDATED STATEMENT OF INCOME FOR THE YEAR ENDED DECEMBER 31, 2000

	Telecom Italia U.S. GAAP Historical Year ended December 31, 2000 (1)	SEAT U.S. GAAP Historical Nine Months ended September 30, 2000 (2)	Acquisition of SEAT (3)	Other adjustments (4)	Total	Telecom Italia U.S. GAAP Pro-forma Year ended December 31, 2000	Telecom Italia U.S. GAAP Pro-forma Year ended December 31, 2000
			(Unaudited)				
	(Billions of Lire, except per share and per ADS amounts)	(Billions of Lire)	(Billions of Lire)	(Billions of Lire)	(Billions of Lire)	(Billions of Lire, except per share and per ADS amounts)	(Millions of U.S.$, except per share and per ADS amounts) (5)
Total revenues	54,096	1,678	-	(415) (a)	1,263	55,359	25,143
Cost of materials	(3,749)	(225)	-	11 (a)	(214)	(3,963)	(1,800)
Personnel costs	(9,361)	(184)	-	-	(184)	(9,545)	(4,335)
Depreciation and amortization	(10,900)	(688)	(1,790) (a)	180 (b)	(2,298)	(13,198)	(5,994)
Other external charges	(20,001)	(929)	-	404 (a)	(525)	(20,526)	(9,323)
Capitalized internal construction costs	1,609	-	-	-	-	1,609	731
SEAT impairment	(15,424)	-	-	-	-	(15,424)	(7,005)
Total operating expenses	(57,826)	(2,026)	(1,790)	595	(3,221)	(61,047)	(27,726)
Operating income (loss)	(3,730)	(348)	(1,790)	180	(1,958)	(5,688)	(2,583)
Interest expense, net	(2,800)	(63)	(704) (b)	-	(767)	(3,567)	(1,620)
Other income (loss), net	(88)	(3)	-	-	(3)	(91)	(42)
Gains on merger, demerger, subsidiary dilution and share conversions	20,284	-	(15,231) (c)	-	(15,231)	5,053	2,295
Net income (loss) before income taxes and minority interest	13,666	(414)	(17,725)	180	(17,959)	(4,293)	(1,950)
Income tax (expense) benefit	(4,887)	39	4,944 (d)	-	4,983	96	44
Minority interest	(1,806)	2	-	163 (c)	165	(1,641)	(745)
Net income (loss) from continuing operations(*)	6,973	(373)	(12,781)	343	(12,811)	(5,838)	(2,651)
Net income per Ordinary Share – Basic (6)	937					(795)	(0.36)
Net income per Ordinary Share – Diluted (6)	934					(795)	(0.36)
Net income per Ordinary Share ADS – Basic (6)	9,367					(7,949)	(3.61)
Net income per Ordinary Share ADS – Diluted (6)	9,341					(7,949)	(3.61)
Net income per Savings Share – Basic (6)	957					(775)	(0.35)
Net income per Savings Share ADS – Basic (6)	9,567					(7,749)	(3.52)

* The Telecom Italia's Historical U.S. GAAP statement of income for the year ended December 31, 2000 does not include a charge of Lit. 154 billion (net of tax) relating to the cumulative effect of the accounting change in revenue recognition.

Notes to the Unaudited Pro Forma Condensed Consolidated Statement of Income

1. The Telecom Italia statement of income for the year ended December 31, 2000 has been derived from the audited Italian GAAP consolidated financial statements of Telecom Italia, after taking into account the significant differences between Italian and U.S. GAAP. For a discussion of the principal differences between Italian and U.S. GAAP, please refer to Notes 26, 27 and 28 of Telecom Italia's consolidated financial statements for the year ended December 31, 2000 included elsewhere herein.

2. The SEAT statement of income for the period ended September 30, 2000 has been derived from the unaudited Italian GAAP consolidated financial statements of SEAT, after taking into account the significant differences between Italian and U.S. GAAP.

3. The adjustments in this column relate to the elimination of non-recurring items included within Telecom Italia's historical U.S. GAAP statement of income for the year ended December 31, 2000, and the adjustments required to the statement of income as if the acquisition had occurred on January 1, 2000.

For the purposes of U.S. GAAP, the acquisition was considered effective as of October 1, 2000, the date that operating control of SEAT was passed to Telecom Italia. As a result, for U.S. GAAP purposes the last three months of SEAT's 2000 results of operations are fully consolidated with the historical results of Telecom Italia. Any pro forma adjustments required to Telecom Italia's U.S. GAAP statement of income for the year ended December 31, 2000 relate to the SEAT results for the nine months ended September 30, 2000. The adjustments are as follows:

(a) Goodwill amortization of Lit. 1,790 billion for the nine month period ended September 30, 2000. Goodwill is being amortized over a period of 12 years. The total amortization charge for the year is Lit. 2,482 billion (including the amortization of the historical goodwill in SEAT which is attributable to Telecom Italia's interest), of which Lit. 692 billion is already included within Telecom Italia's historical U.S. GAAP statement of income for the year ended December 31, 2000.

(b) The adjustment of Lit. 704 billion relates to interest expense on acquisition financing (Lit. 456 billion) and the amortization charge of the premium of the SEAT put/call (Lit. 248 billion).

The interest expense of Lit. 456 billion relates to the Lit. 12,331 billion of acquisition financing. The annual charge is Lit. 637 billion, of which Lit. 181 billion is already included within Telecom Italia's historical U.S. GAAP statement of income for the year ended December 31, 2000. The interest expense has been computed based on an estimated average interest rate of 5.2 percent per annum. An increase in the average interest of 1/8 percent would increase annual interest expense by approximately Lit. 15 billion.

The amortization charge of Lit. 248 billion relates to the amortization of the Lit. 1,474 billion relating to the premium and associated costs of the SEAT put/call financing, which has been accounted for as a deferred expense and is being amortized over five years using the effective interest rate method. The annual amortization charge is Lit. 266 billion, of which Lit. 18 billion was included within Telecom Italia's historical U.S. GAAP statement of income for the year ended December 31, 2000.

(c) The adjustment to eliminate the pre-tax gains on the merger (Lit. 12,657 billion) and the demerger (Lit. 2,574 billion). These are included in the Telecom Italia's historical U.S. GAAP statement of income for the year ended December 31, 2000 and are non-recurring in nature.

(d) Income tax benefit of Lit. 4,944 billion relates to the fiscal benefit arising on the interest expense (Lit. 169 billion), the amortization of the SEAT put/call (Lit. 92 billion) and on the elimination of the gain on the merger (Lit. 4,683 billion).

4. The adjustments in this column of the unaudited pro forma condensed consolidated statement of income relate to the elimination of intercompany revenues and expenses upon consolidation of SEAT by Telecom Italia. The intercompany transactions principally relate to the royalties on advertising and production costs.

(a) The adjustments to eliminate intercompany revenues and costs for the nine months ended September 30, 2000.

(b) The adjustments to eliminate Lit. 180 billion of goodwill amortization on SEAT's pre-acquisition goodwill.

(c) Lit. 163 billion to reflect the minority interest in the net loss of SEAT (Lit. 125 billion) and the net loss of Tin.it (Lit. 38 billion) for the nine months ended September 30, 2000.

The preliminary allocation of the purchase price is shown in the following table:

	Lit. Billions	
Cash purchase price	12,331	
Fair value of merger transaction and acquisition financing of additional equity interest (SEAT put/call)	18,602	
Transaction costs	95	
Total consideration		31,028
Less:		
Book value of net assets acquired	7,046	
Minority interests	(2,805)	
		(4,241)
Goodwill from the Acquisition		26,787

5. Solely for the convenience of the reader, Italian lire amounts have been translated into U.S. dollars at the rate of Lit. 2,201.80 per U.S. $1.00 based on the Lire equivalent of the U.S. dollar-euro noon buying rate on March 30, 2001. Telecom Italia does not represent that either the Lire or Euro could be converted into U.S. dollars at this rate or at any other rate.

6. Net income per share has been calculated using the two-class method since Telecom Italia has both ordinary 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 ordinary shares and savings shares was 7,398,247,829 for the year ended December 31, 2000. The calculations take into account the requirement that holders of savings shares are entitled to an additional Lit. 20 (based on 2 percent of the par value of savings shares) above the dividends paid on ordinary shares. This takes into account the par value of Lire 1,000 per share as of December 31, 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 Euros, the new par value per share is equal to Euro 0.55.

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.

Telecom Srjbija

In the first quarter of 2001 Italian newspaper reports alleged that improper payments were made in connection with the Company investment in Telekom Srjbija. 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 Srjbija, 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 Srjbija for approximately DM 893 million and OTE acquired a 20% interest for approximately DM 675 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 are 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 have stated that no facts have emerged, at the present 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. See "Item 4. Information on the Company—Recent Developments—Report of Statutory Auditors".

Telecom Italia is not aware of any improper payments under Italian law made by it in connection with its investment in Telekom Srjbija. Therefore, Telecom Italia believes its Italian statutory and consolidated financial statements for the fiscal years 1997, 1998, 1999 and 2000 are fairly stated. Telecom Italia also believes that its stock purchase agreement relating to Telekom Srjbija is valid and binding. Since Telecom Italia believes that its investment in the Serbian telecommunications sector is a part of its international strategy in the region of Southern Europe and the Mediterranean basin, Telecom Italia intends to maintain the current contract. Telecom Italia is, however, currently discussing the ongoing commercial terms of certain ancillary aspects of the stock purchase agreement with its partners in Telekom Srjbija.

The executive members of Telecom Italia's current board of directors were appointed in June 1999, following the successful completion of Olivetti's takeover of Telecom Italia. Telecom Italia's management is committed to transparency and is collaborating with the Italian public prosecutors in connection with their investigation. See "Item 4. Information on the Company — Recent Developments".

Social Security Charges

The Company is a party, together with INPS, to test cases, 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 on 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 then 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.

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, 2000 relating to such contributions for principal will range from approximately Lit. 1,900 billion to approximately Lit. 2,500 billion (Lit. 509 billion of which has already been paid) net of the amount of Lit. 1,377 billion already recorded by Iritel and presently appearing in Telecom Italia's and TIM's financial statements following the Telecom Merger. As of December 31, 2000 INPS had submitted formal requests for about 96% of the employees whose change in insurance status will result in a charge to Telecom Italia. Based on the formal request made by the INPS through December 31, 2000, the remaining liability for obligations under Law n° 58/1992, which is payable in 15 installments, amounts to Lit. 2,923 billion, broken down as follows:

- Lit. 1,911 billion in principal amount (except for the portion attributable to Iritel employees)

- Lit. 1,012 billion in 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 reservation - in fifteen equal annual installments, payable in arrears, including interest at an annual rate of 5%, up to the end of 1999, for a total amount of Lit. 216 billion. In compliance with the ruling handed down by 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 (with respect to the remaining amount of Lit. 789 billion , of which lit. 68 billion relates to the amount due for 2000). The charge to income for the year 2000 (under "extraordinary expense") amounts to Lit. 297 billion, inclusive of accrued interest. During 2000, Telecom Italia paid INPS the above-mentioned charges also on behalf of other Group companies - mainly TIM and CSELT - 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. The recovered amount is recorded in the statement of income under "extraordinary income" and amounts to Lit. 4 billion.

Management does not believe however, that an adverse resolution of this dispute would have a material adverse effect on the Group's consolidated financial position in view of the fact that sums due under Law 58/1992 are to be paid over a period of 15 years. See Note 18 of Notes to the Consolidated Financial Statements included elsewhere herein.

Pagine Italia — Telecom Italia/SEAT

Telecom Italia and SEAT had previously been notified (on March 22, 2000) of the claim by Pagine Italia in which the Court of Appeals of Turin was asked to: (i) nullify the contract giving SEAT the concession for the exclusive collection of advertising in the "alphabetical" telephone directory since this violated fair trade practices; (ii) declare the illegitimacy of the investment by Telecom Italia in SEAT on the grounds of abuse of a dominant position under the same law; and (iii) prohibit the continuation of such relations.

At a hearing held on October 17, 2000, Telecom Italia and SEAT raised preliminary exceptions regarding inadmissibility; Pagine Italia filed an urgent petition, asking the Court of Appeals to forbid the continuation of the exclusive collection of advertising by SEAT and to order Telecom Italia to arrange a bid for the collection of advertising in the official telephone directories, for each single local directory.

At a hearing held on November 21, 2000, the Court of Appeal rejected the urgent petition presented by Pagine Italia, which filed an official complaint against the decision. The complaint was also rejected by court order of February 14, 2001. The case was adjourned to May 15, 2001. On May 15, 2001 the Court of Appeals requested the parties to present their final arguments within 30 days and allowed for eventual counter-arguments to be presented within 20 days of the presentation of the final arguments.

Buy-back of Telecom Italia savings shares

January 10, 2001 marked the end of the period for the buy-back of Telecom Italia savings shares authorized by resolution of the stockholders' meeting of January 14, 2000.

Elliott International L.P. and Liverpool Limited Partnership, mutual fund investment companies of the American Group Elliott, filed a claim for damages against Olivetti and Telecom Italia, as well as the Chairman and Deputy Chairman of Telecom Italia for a total of euro 18.9 million (Lit. 36.6 billion). The claim is based on the alleged non-fulfillment of the commitments stated in the "Offer Document" relating to the take-over and exchange bid by Olivetti and Tecnost for Telecom Italia, and also the resolutions passed by the stockholders' meeting of January 14, 2000, especially in relation to the mandate to purchase treasury Savings Shares on the screen trading market, as set forth by applicable laws, subsequent to the end of the period for the tender offer.

The first hearing in the case was held on April 2001. A second hearing has been scheduled for November 2001.

The resolution passed by the stockholders' meeting of January 14, 2000, was contested in March 2001 by the stockholder Alberto Reale, who claimed that the resolution was null and void because the proposal that was put to the stockholders' meeting had been changed from the one previously deposited. On March 6, 2001, the judge, after hearing the parties, exhausted all attempts to reconcile the parties. The next hearing is scheduled for July, 2001.

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, which is recognized as an "unfair burden" for Telecom Italia, was divided among Omnitel, Infostrada and TIM. While judgment is pending, Omnitel and Infostrada have not paid their share (totaling Lit. 18 billion) to the special fund set up by the Ministry of Communications, thus preventing TIM from paying the whole amount owed to Telecom Italia (Lit. 52 billion).

At the hearing to decide on the request for the suspension of the ruling filed by Omnitel (January 24, 2001), the TAR fixed May 30, 2001 as the date for hearing the case without commenting on the appeal. The hearing was further postponed until July 11, 2001.

Infostrada/Albacom — Telecom Italia: services with access in ADSL technology and RING services

On July 21, 1999, Infostrada accused Telecom Italia, before the Antitrust Authority, of marketing network access services for data transmission using ADSL technologies. As a consequence, this could give Telecom Italia an unfair advantage on the data and Internet services market for companies and Internet Service Providers, given the impossibility of its competitors to supply their customers with access services; and constituted an unfair trade practice. The Antitrust Authority conducted an investigation to evaluate whether, under the circumstances, this can be construed as an abuse of a dominant position. On April 27, 2001 the Antitrust Authority ruled that an abuse of a dominant position took place and imposed a fine of Lit. 115 billion on Telecom Italia. Telecom Italia promptly declared its intention of appealing the ruling and the fine to the TAR of Lazio.

Pursuant to an order of August 16, 2000 by the Court of Appeals in Rome, following an urgent appeal presented by Infostrada and Albacom, Telecom Italia was forbidden to "promote and/or offer and/or directly conclude contracts for RING services or their equivalent, under whatever name". After the appeal was upheld, Telecom Italia suspended the offering of services for an indefinite period of time. Telecom Italia filed a complaint, which was rejected on February 13, 2001.

Full Business Company/permanent Virtual Channel

On December 6, 2000, Telecom Italia notified the National Regulatory Agency that an appeal had been filed with the TAR of Lazio asking for the suspension and nullification of the November 22, 2000 ruling whereby the National Regulatory Agency suspended the Company's offering known as "Full Business Company", and forbade the Company to continue to market or promote the said offering.

The offering includes in the supply of telecommunications services based on access using XDSL technology (the so-called broadband technology). Competing operators are disputing the failure of the Company to apply the regulatory ruling by which any offering of such services to the public (*retail*) must always be accompanied by a corresponding and symmetrical *wholesale* offering to the competition.

After a series of postponements, the date for the hearing on the merits has been scheduled for July 4, 2001.

In the meantime, the National Regulatory Agency issued Resolution No. 15/00/CIR, establishing Telecom Italia's obligation to make a *wholesale* offering ("permanent virtual channel") for access to *XDSL* technologies to other operators. Telecom Italia challenged this resolution before the TAR of Lazio, asking for the annulment of some of the offering terms established by the National Regulatory Authority. However, subsequently, the National Regulatory Authority issued Resolution No. 4/01/CIR of February 22, 2001, approving the contents of the *wholesale* offering and allowing the marketing of the "Full Business Company" and "Ring" services to resume (with effect 30 days after the approval of Telecom Italia's *wholesale* offering).

Some other licensed operators contested this decision, asking that it should be suspended; the TAR of Lazio rejected the appeals on March 21, 2001.

TIM/Omnitel Antitrust Proceeding

On January 7, 1999, the Italian Antitrust Authority started a formal proceeding to ascertain the existence of agreements or concerted practices between TIM and Omnitel restricting competition in the mobile telecommunications market. The investigation was based on three elements: (i) introduction and simultaneous application of identical charges to customers for calls from Telecom Italia fixed line network to TIM and Omnitel mobile networks; (ii) similarity of conditions in the services offered to customers for calls made from mobile phones for interconnection to mobile networks; (iii) similarity of conditions in services offered to other telecommunications operators (in particular, interconnection charges). These alleged agreements and concerted practices were reviewed by the Italian Antitrust Authority for their potential negative impact on competition in the market concerned. On May 7, 1999 TIM was notified that the results of the Italian Antitrust Authority's preliminary investigation confirmed the alleged restriction of competition in the telecommunications market. On June 18, 1999 TIM submitted a final brief challenging the findings of the Italian Antitrust Authority's preliminary investigation.

On September 28, 1999 the Italian Antitrust Authority concluded that TIM and Omnitel had restricted competition based on (i) concerted practices, fixing during 1998 the same prices for fixed-mobile communication; (ii) January 6, 1999 agreement related to rebalancing fixed-mobile charges to end users; and (iii) practices related to termination price of other competitors. For those breaches, the Authority imposed a fine against TIM of about one hundred billion Lit.. TIM (and Omnitel) applied to the TAR Lazio (Tribunale Amministrativo Regionale) against such proceeding, requesting a suspension. On May 31, 2000 TAR Lazio rejected the appeal, confirming the fine imposed by the Italian Antitrust Authority. TIM appealed against this decision before the Consiglio di Stato, Italy's highest administrative court. The Consiglio di Stato, through a decision deposited on March 22, 2001, partially upheld the appeals filed by TIM and Omnitel. In fact, the Consiglio di Stato cancelled the most serious of the three sanctions (equal to approximately Lit. 62 billion), regarding alleged price-fixing in 1998. The fine originally imposed on TIM of Lit. 100 billion (paid on June 29, 2000 so as not to incur the risk of further legal sanctions) was thus reduced to Lit. 38 billion.

Telecom Italia/Tiscali Albacom

On September 8, 1999 the Italian Antitrust Authority started a new investigation of Telecom Italia on the basis of a claim brought by Tiscali S.p.A. and Albacom S.p.A., two Italian licensed operators for public voice services, for alleged abuse of its dominant position in the interconnection market, and damaging the development of Tiscali and Albacom's telecommunications businesses. The proceeding was concluded and no fine was imposed on Telecom Italia.

Acquisition of TeleMonteCarlo

In August 2000, SEAT agreed to purchase Cecchi Gori Communications S.p.A., the owner of the TeleMonteCarlo television network, or TMC, from Cecchi Gori Media Holding Group S.r.l. and its parent company, the Cecchi Gori Group FIN.MA.VI S.p.A. TMC is the third largest TV network in Italy, broadcasting two TV channels, TMC and TMC2. SEAT has already contributed Lit. 250 billion to TMC in the form of a capital increase and began the integration of new management. The remaining consideration will be paid through the issuance by SEAT of up to 109,867,484 ordinary shares in exchange for Cecchi Gori Communications ordinary shares. The acquisition is subject to regulatory approval. On January 17, 2001, the National Regulatory Agency, ruled that under currently applicable Italian law Telecom Italia is not permitted to operate a television broadcasting business while holding a public concession to provide telecommunications services. Telecom Italia and SEAT immediately appealed the ruling to the TAR of Lazio. Subsequent to the National Regulatory Agency's ruling, on January 23, 2001, the Italian Anti-Trust Authority cleared the acquisition, subject to satisfaction of certain conditions. Telecom Italia and SEAT intend to comply with these conditions.

On January 31, 2001, in an administrative legal procedure, the TAR of Lazio, suspended the effectiveness of the National Regulatory Agency's decision to block the TMC acquisition. The TAR of Lazio agreed that it is likely that its final ruling would be favorable to the acquisition. The TAR of Lazio requested that National Regulatory Agency reconsider its ruling. The National Regulatory Agency reconfirmed its ruling on February 20, 2001. On March 7, 2001, the TAR of Lazio issued its final ruling, upholding SEAT's appeal and overturning the National Regulatory Agency's ruling of February 20, 2001. The National Regulatory Agency has appealed the TAR of Lazio ruling to the Council of State, Italy's highest court for administrative matters. On May 30, 2001 the Council of State rejected the appeal of the National Regulatory Agency.

On February 28, 2001 Cecchi Gori Media Holding Group S.r.l. and Cecchi Gori Group FIN.MA.VI S.p.A. filed an emergency proceeding with the Civil Court of Rome claiming for an order of admission of the shareholder Cecchi Gori Media Holding Group S.r.l. (at the time owner of 75% of the share capital) to the regular assertion of the majority voting rights in the shareholders meetings and of the company administration. The claim was based on the following arguments: (i) the cancellation of the purchase and sale agreement relating to Cecchi Gori Communications for the non-acceptance of the condition (authorization of the Antitrust Authority) by January 31, 2001 and (ii) the damage caused by the expulsion from the company administration. The Civil Court of Rome, with an order of March 12, 2001 rejected the proceeding. On April 27, 2001, the ordinary and extraordinary shareholders' meeting of Cecchi Gori Communications approved the company's annual report and resolved to increase its capital in order to cover its losses for the fiscal year 2000. SEAT subscribed to the portion of the capital increase necessary to maintain its 25% interest by paying Lit. 41 billion and also advanced Lit. 125 billion for Cecchi Gori Media Holdings's 75% portion.

The same parties contested in front of the Civil Court of Rome the resolution of the Ordinary and Extraordinary shareholders' meeting of Cecchi Gori Communications S.p.A. (on April 27, 2001), which approved the company annual report, resolved to cover the losses for the year 2000 and increased the capital. The hearing has been fixed for July 16, 2001. At the same time, the same subjects filed with separate claim, suspension petitions of the above described resolutions of the Cecchi Gori Communications S.p.A. shareholders' meeting. The Civil Court of Rome rejected such request.

Investigation on Equality of Treatment

In July 2000, the National Regulatory Agency commenced an investigation relating to a review of the Italian telecommunications market for purposes of determining whether telecommunications companies operate in a situation of level playing field/equality of treatment. Among the measures which certain competitors of Telecom Italia have requested the National Regulatory Agency to consider in order to promote equality of treatment in access to the wireline network, there is the requirement that Telecom Italia, as the incumbent in the Italian market and as an operator that is vertically integrated, implement a higher degree of accounting and organizational unbundling or a corporate unbundling with respect to its telecommunications network. Telecom Italia has already implemented the separation of its telecommunications network from an accounting point of view. Telecom Italia believes that there is no legal ground on which it could be required to undertake alternative measures. The National Regulatory Agency is expected to complete its investigation in July of 2001.

Farallon

On April 23, 2001, upon request by Farallon Telco Argentina Llc. ("Farallon"), a minority shareholder of Nortel Inversors S.A. ("Nortel"), together with certain individuals, was served a notice to attend a mediation hearing to be held on May 9, 2001, before the Commercial Courts of the City of Buenos Aires, Republic of Argentina. The purpose of such hearing was to find possible agreements in respect of the claim for invalidation of resolutions adopted by Nortel's shareholders' meeting on January 19, 2001, related to, among others, the approval of the financial statements of Nortel for the fiscal year ended September 30, 2000.

The mediation proceeding is still pending. Argentine law provides that, if the mediation is concluded without any agreement among the parties, Farallon, as plaintiff, is entitled to initiate a litigation proceeding by serving, within a certain time frame, a full complaint presenting its claims in detail.

WTC

In March 1999, Telecom Italia S.p.A. (“Telecom Italia”) filed a lawsuit in the United States District Court for the Southern District of Florida against Wholesale Telecom Corporation (“WTC”) to recover US $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 claims against Telecom Italia. WTC’s counterclaim sought compensatory damages of at least US $10 million and punitive damages of at least US $50 million, plus interest.

The claim is for breach of contract where WTC alleges (i) that Telecom Italia breached the terms of the agreement with respect to prices, quality of service, and invoicing; and (ii) tortuous interference with contract against Telecom Italia. In August 2000, the district court stayed the case because of a pending appeal by the third-party defendant in the case (described below) and denied WTC’s motion with leave to refile. Telecom Italia anticipates that WTC will refile its motion for leave to amend its counterclaim now that the appeal by the third-party defendant has been resolved.

WTC filed a third-party complaint in August 1999 against Telemedia International U.S.A.. Inc. (“TMI”), an indirectly wholly-owned subsidiary of Telecom Italia that operates telecommunications networks in the United States. WTC has asserted claims for conspiracy and tortuous interference with contract, contending that TMI interfered with WTC’s contract with Telecom Italia. In the third-party complaint, WTC seeks compensatory damages in excess of US $10 million and punitive damages in excess of US $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 appealed this decision. The district court’s order was affirmed on appeal in April 2001. Such claim for tortuous interference together with the claims by WTC against Telecom Italia will be examined, by the United States District Court for the Southern District of Florida.

Brazil Telecom

A complaint was filed in April 2001 in the 22nd Civil Court in Rio de Janeiro by Brazil Telecom against Telecom Italia and SIN and extended against two directors of Brazil Telecom. By means of such complaint Brazil Telecom seeks to collect from defendants alleged losses and damages associated with the purchase of CRT’s shares (see “Item 4. Information on the Company — Telecommunications Services — International Telecommunications Services) and the participation of the company in the Personal Communication Services Tender. Although the claim is based on two distinct grounds (Telecom Italia and SIN are being sued under the Brazilian Civil Code and the abovementioned directors under the tort rules set forth in the Brazilian Corporate Law), the factual background and legal arguments are the same for all defendants. SIN and Telecom Italia have so far presented a motion to dismiss for lack of jurisdiction, the motion is still pending. This litigation, regardless of its outcome, is not expected to affect Telecom Italia’s Latin American strategy.

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 S.p.A. (“Borsa Italiana”). (see “— Securities Trading in Italy”). The Shares are also quoted on SEAQ International, the London Stock Exchange’s quotation system for equity securities of non-United Kingdom incorporated companies.

Ordinary and Savings Share ADSs, each representing respectively ten Shares and ten Savings Shares, have been quoted on the NYSE since July 27, 1995. Morgan Guaranty Trust Company of New York is the Company’s Depositary issuing American Depositary Receipts (“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.$)	
1997:				
First Quarter	8.46	6.39	51 1/8	41 3/4
Second Quarter	10.18	7.17	61 1/4	42 2/8
Third Quarter	12.06	9.78	68 5/16	57 15/16
Fourth Quarter	11.70	10.13	67 9/16	60
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 (2)	14.02	11.59	121 14/16	97 8/16
2001:				
January	13.65	11.61	127.50	111.06
February	13.64	11.53	127.25	104.30
March	11.82	10.68	110.98	95.55
April	12.45	11.52	113.00	100.20
May	12.55	11.12	113.25	95.70
June (through June 15)	11.07	10.64	94.00	90.50

(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 15, 2001, there were 2,819,745 Ordinary Share ADSs outstanding held by 117 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.$)	
1997:				
First quarter	6.83	4.70	$40^{1/8}$	30
Second quarter	7.00	5.43	$40^{1/2}$	$32^{7/8}$
Third quarter	6.87	5.70	$38^{1/8}$	$34^{3/8}$
Fourth quarter	7.66	6.03	42	$37^{1/2}$
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:				
January	7.03	6.05	63.38	58.50
February	7.03	6.15	63.37	55.25
March	6.43	5.59	57.00	52.50
April	7.00	6.18	61.00	52.00
May	7.08	6.24	61.00	56.50
June (through June 15)	6.25	6.03	52.50	52.50

(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 15, 2001, there were 21,934 Savings Share ADSs outstanding held by 8 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 15, 2001, the Noon Buying Rate for the euro was Lit. 2,241 = U.S.$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.

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 S.p.A. 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 of all trades effected during the trading day and a “reference price” calculated as a weighted average of the last 10% of the trades effected during such day are published. 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), 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.

In order to expedite trading, shares ordinarily may be traded only in minimum lots of prescribed size (or multiples thereof). The currently prescribed minimum lot for both the Shares and the Savings Shares is 50. Lots smaller than the prescribed minimum may be traded on Telematico subject to certain limitations.

Starting form 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 5.50 p.m. to 8.30 p.m. on every trading day, substantially under the same rules as Telematico except that the price of every securities 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. See Part II. “Item 14. Description of Securities — Description of Capital Stock — The Draghi Law”.

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 the Bank of Italy and 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). See “Item 14. Description of Securities — Description of Capital Stock”.

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 Lit., 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 Bylaw 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 Lit. 20 million 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 Lit. 20 million 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 Lit. 20 million 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 Lit. 20 million 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.

Under Italian law, 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.

Under Italian Law 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, the one of Chairman or 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 please see "Item 6. Directors, Senior Management and Employees — Compensation of Directors and Officers".

There are no provisions in Italian law and in Telecom Italia's by-laws that set age or shareholding requirements for directors' qualification.

Generally, under Italian Law, directors, as well as general managers and statutory auditors are not permitted to get loans and warranties, either directly or indirectly, from the company and its affiliates. Obtaining such loans or warranties is punished as a criminal offence.

Capital Stock

General

At the extraordinary shareholders' meeting held on May 3, 2001 Telecom Italia's share capital was converted from Lit. into euros by rounding up the par value of the shares, from Lit. 1,000 to euro 0.55, partially through the cancellation of 112,998,070 Savings Shares held in treasury. As of June 15, 2001 the full paid-in capital stock amounted to euro 4,022,941,728.30 and was constituted by 5,261,317,481 Shares and 2,053,122,025 Savings Shares, each of euro 0.55 par value. For a maximum period of five years from the date of the shareholder' 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 managers and executive officers of Telecom Italia or its subsidiaries, up to a maximum of euro 40,150,000 (which corresponds to the issuance of 73,000,000 Shares, with a par value of euro 0.55 each), at a price determined by the Board of Directors for each capital increase, within the limits permitted by law.

On December 17, 1999, the Board of Directors, in partial implementation of the authorization granted by the shareholders on December 15, 1998, passed a resolution to increase the share capital by payment of up to a nominal maximum of euro 9,127,470, (such amount being the result of the conversion and recalculation of the previous Lit. amount following the May 3, 2001 shareholders' meeting, which corresponds to the issuance of a maximum of 16,595,400 Shares with a par value of euro 0.55), which will rank for dividend pari passu, to be offered for subscription to managers and executive officers of Telecom Italia or its subsidiaries selected by the Board of Directors as participants in the Stock Option plan. On June 12, 2001, the Board of Directors, in further implementation of the aforementioned authorization, passed a resolution to increase the share capital by payment of up to a maximum of euro 8,398,500 (which corresponds to the issuance of a maximum of 15,270,000 Shares with a par value of euro 0.55), which will rank for dividends pari passu, to be offered for subscription to managers and executive officers of Telecom Italia or its subsidiaries selected by the Board of Directors as participants in the Stock Option Plan. See "Item 6. Options to Purchase Securities from Registrant or Subsidiaries".

In particular, to execute such increase, a total of 6,185,850 Shares were issued as of June 15, 2001.

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 managers and executive officers and to other employees of Telecom Italia or 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)

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 euro 4,099,839,510.80, constituted by 5,401,131,631 Shares and 2,053,122,025 Savings Shares.

According to Article 145 of the Draghi 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.

Form and Transfer

The Dematerialization Decree introduced in the Italian legal system 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 the Bank of Italy and certain of the major Italian banks and financial institutions, which will open an account in the name of each company in its register. All intermediaries receiving share certificates from their clients must physically deliver such certificates to the company issuing the shares. Once such company has checked that such certificates are validly issued, Monte Titoli will open an account in the name of such bank in its register. From January 1, 1999, all share transactions must be completed electronically.

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 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.

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. Additional Information — Description of By Laws and Capital Stock—Taxation".

According to the By-laws 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.

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 or deemed necessary. See "— The Draghi Law."

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 By-laws, 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, pursuant to the Draghi Law. 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. Recently introduced 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 Shareholders' Meeting held on August 10, 2000 resolved that a specific new clause be inserted in the By-laws. Such new clause foresees 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 has been revised by the Draghi Law and its implementing regulations issued by CONSOB and 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.

Powers of minority shareholders: 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 could 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.

Holders of Savings Shares are not entitled to vote in meetings of holders of Shares.

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. Special Meetings may be called 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. The Joint Representative is appointed for a maximum three year term. Special Meetings are called by the Joint Representative or by the Board of Directors within two months from the issue of Savings Shares or conversion of Savings Shares, or upon request by saving shareholders representing at least 1% of the outstanding Savings Shares. Pursuant to Article 13 of Telecom Italia By-Laws the Joint Representative is kept informed by the Company regarding corporate events that can affect the prices trend of Savings Shares.

Currently the holders of Savings Shares are not represented by any Joint Representative. The mandate of Carlo Pasteris, their former representative expired on June 7, 2001.

The Board of Directors, on June 28, 2001, resolved to convene a special meeting of savings shareholders to appoint a new Joint Representative, giving a mandate to the Chairman and Chief Executive Officer to establish the dates on which the special meeting will take place.

To attend any Special Meeting, the holders of Savings Shares must be in possession of an appropriate certification issued by an authorized intermediary, pursuant to the Draghi Law. 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".

Voting rights relating to Savings Shares that have not been deposited with Monte Titoli may be exercised by depositing them with an intermediary authorized to operate in the collective management system, pursuant to Article 51 of CONSOB Resolution No. 11768 of December 23, 1998, with appropriate issuance of the necessary certification. The Company may also be requested to perform the abovementioned functions of an intermediary, pursuant to Article 24 of CONSOB Resolution No. 11768.

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. Pursuant to Article 132 of the Draghi Law, 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 S.p.A. 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 Telecom Italia Ordinary Shareholders Meeting held on January 14, 2000 approved a buy-back program for 742,615,722 Savings Shares, at a price of euro 6.50 per Savings Share over a maximum period of 18 months in accordance with article 2357 of the Italian civil code. Such Buy-back was carried out through a tender offer. The tender offer period started on February 17, 2000 and expired on March 17, 2000. As a result 1,793,820 Savings Shares were tendered, representing 0.0828% of all outstanding Savings Shares.

Because the number of Savings Shares tendered was less than the maximum number allowed, according to the provisions of the ordinary shareholders meeting resolution the Chairman and the Vice Chairman of the Board of Directors were authorized to place open market purchase orders of Savings Shares, on Telematico at a price of 6.50 euro per Savings Share over a period of nine months following the expiration date of the tender offer. At the extraordinary stockholders meeting held on May 3, 2001 (second call), in connection with the rounding up of the par value of the share capital from Lit. 1000 to €0.55, 112,998,070 Savings Shares, purchased and held in treasury, were cancelled.

The Shares or the Savings Shares, as long as they are owned by the Company, are not entitled to receive dividends. The dividends related to such Shares or Savings Shares accrue to the other holders of Shares and Savings Shares so long as they are held by the Company. A corresponding reserve equal to the purchase price of such Shares or Savings Shares has to be created on the Company's balance sheet, and 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.

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 the 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: (1) 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 by-laws.

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

General. There are no limitations imposed by Italian law or by the By-laws 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.

Limitations on Shareholdings. The provision regarding a maximum limit on shareholding of 3% of the voting shares, contained in the Company by-laws, was removed after the resolution of the extraordinary shareholders' meeting held on August 10, 2000. Other than as described in this section, there are currently no limitations on shareholdings.

Special Powers of the State. Telecom Italia's By-laws include special powers granted to the State as permitted by the Privatization Law. The Privatization Law contemplates special by-law provisions and the granting to the State of special powers prior to any transfer of a controlling interest in companies operating in public service sectors including the telecommunications sector. See "Item 7. Major Shareholders and Related Party Transactions — Continuing Relationship with the Treasury."

The special powers included in Telecom Italia's By-laws 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 By-laws, the election of directors and statutory auditors, other than those appointed pursuant to the special powers described above or designated pursuant to the Public Concessions, 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 Directors, such requirement was not subject to amendment so long as the maximum limit on shareholding remained effective (See "—Special Powers of the State" above); 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, Morgan Guaranty Trust Company of New York, 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 Lit. 1,000 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 Lit. 1000 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 Morgan Guaranty Trust Company of New York (together with any successor or successors thereto, the “Custodian”). An ADR may evidence any number 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 and expense 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 summary thereof 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 By-laws (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 By-laws 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 By-laws 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 (1) 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 By-laws and (2) 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 By-laws 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.

Morgan Guaranty Trust Company of New York

The Depositary is Morgan Guaranty Trust Company of New York, a New York banking corporation, which has its principal office located in New York, New York. Morgan Guaranty Trust Company of New York 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 & Co. Incorporated ("J.P. Morgan"), the parent corporation of Morgan Guaranty Trust Company of New York, 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 Morgan Guaranty Trust Company of New York and By-Laws 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 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, 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 if they provide adequate evidence that their dividend income is subject to income tax in their home country in an amount at least equal to the total refund claimed, within 18 months from the date of payment of the Italian 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 by the U.S. tax authorities stating that the beneficial owner is a U.S. resident and that to the best of such tax authorities' knowledge, the beneficial owner has no permanent establishment in Italy. The certification is valid until March 31 of the year following the submission.

The certification procedure will require the Share or ADR holder to obtain from the U.S. Internal Revenue Service a certificate (Form 6166) with respect to each dividend payment. The request for that certificate must include a statement, signed under penalties of perjury, to the effect that the Share or ADR holder is a U.S. resident individual or corporation and does not maintain a permanent establishment in Italy, and must set forth other required information. 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 transfer 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 take place are (i) banks, exchange agents or (ii) banks, SIMs or exchange agents on one hand, and non-residents on the other hand or (iii) banks, SIMs or resident or non-resident exchange agents, on one hand, and investment funds on the other hand. In any other case, transfer tax is currently payable at the following rates:

- Lit. 140 per Lit. 100,000 (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;

- Lit. 50 per Lit. 100,000 (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

- Lit. 12 per Lit. 100,000 (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 (i.e., 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 resident individuals and all non-resident individuals or corporations on the sale or transfer of Telecom Italia Shares or ADRs. Capital gains realized on the sale of qualified shareholdings (as described below) in companies resident in Italy for tax purposes are subject to CGT at a rate of 27%. 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.

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

Italian inheritance and gift tax is payable on the transfer of Telecom Italia Shares or ADRs by reason of death or donation, even if the Telecom Italia Shares or ADRs are held outside Italy. Pursuant to Law No. 342 of November 21, 2000, subject to limited exceptions, the inheritance and gift tax is applicable on the value of the inheritance or gift, after the deduction of a tax free amount, at rates varying from 3% to 8% depending on the relationship between the donee or beneficiary and the donor or decedent, respectively.

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;
- insurance companies;
- tax-exempt entities;
- dealers in securities;
- 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 share or ADR 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 Italian lire, including the amount of any Italian tax withheld, will be equal to the U.S. dollar value of such Italian lire 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 Italian lire 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 ADRSs 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 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 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 DISCLOSURE 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 By-laws 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, 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, 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.**

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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).

4.1 Public Telecommunications Licenses

(a) Decision No. 820/00/CONS of 22.11.2000

Individual licence 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

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 licence 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*).

4.2 *Employment Contracts*

English Summary of Employment Agreement of Chairman and Chief Executive Officer Roberto Colaninno

10(a) *Reports and consents of Auditors*

(i) Consent relating to Telecom Italia S.p.A. of PricewaterhouseCoopers S.p.A, Independent Accountants dated June 25, 2001.

(ii) Consent relating to Telecom Italia Mobile S.p.A. of Arthur Andersen S.p.A, Independent Accountants dated June 25, 2001.

(iii) Consent relating to Telecom Italia S.p.A. of Arthur Andersen S.p.A, Independent Accountants dated June 25, 2001.

(iv) Consent relating to Telecom Italia S.p.A. of PricewaterhouseCoopers S.p.A Independent Accountants, dated June 25, 2001.

(v) Consent relating to FINSIEL Consulenza e applicazioni informatiche S.p.A of Deloitte & Touche S.p.A. Independent Accountants dated June 25, 2001.

Consent relating to Sirti S.p.A of Deloitte & Touche S.p.A. Independent Accountants dated June 25, 2001.

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/ Roberto Colaninno
Chairman and Chief Executive Officer

Dated June 29, 2001

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 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 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 Lire 34,255,013 million and total revenues of Lire 15,411,424 million 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.

Sede legale: Milano 20124 Via Vittor Pisani 20 Tel. 0267831 Fax 0266981433 Cap. Soc. 7.220.000.000 i.v. Reg. Imp. Milano N. 278920/1999 C.F. e P. IVA 12979880155 Iscritta all'Albo Consob – Altri uffici: Ancona 60123 Via Corridoni 2 Tel. 07136881 – Bari 70125 Viale della Repubblica 110 Tel. 0805429863 – Bologna 40122 Via delle Lame 111 Tel. 051526611 – Brescia 25124 Via Cefalonia 70 Tel. 0302219811 – Firenze 50129 Viale Milton 65 Tel. 0554627100 – Genova 16121 Piazza Dante 7 Tel. 0105702013 – Milano 20122 Corso Europa 2 Tel. 0277851 – Napoli 80121 Piazza dei Martiri 30 Tel. 0817644441 – Padova 35137 Largo Europa 16 Tel. 0498762677 – Palermo 90141 Via Marchese Ugo 60 Tel. 091349737 – Parma 43100 V.le Tanara 20/A Tel. 0521242848 – Roma 00154 Largo Fochetti 29 Tel. 06570251 – Torino 10129 Corso Montevecchio 37 Tel. 011556771 – Trento 38100 Via San Francesco 8 Tel. 0461237004 – Treviso 31100 Piazza Crispi 8 Tel. 0422542726 – Udine 33100 Via Marinoni 12 Tel. 043225789 – Verona 37122 Corso Porta Nuova 125 Tel. 0458002561

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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 Lire for the period ended December 31, 2000 and the determination of consolidated stockholders' equity and consolidated financial position also expressed in Lire 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)

TELECOM ITALIA S.p.A.
CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 1999 AND 2000

	December 31, 1999	December 31, 2000	
	(Billions of Lire)	(Billions of Lire)	(Millions of U.S. Dollars)
ASSETS			
CURRENT ASSETS:			
Cash and cash equivalents	1,312	2,526	1,147
Marketable securities (Note 4)	2,583	4,754	2,159
Receivables (Note 5)	15,908	16,363	7,432
Inventories (Note 6)	1,995	1,405	638
Other current assets (Note 7)	2,887	6,697	3,042
TOTAL CURRENT ASSETS	24,685	31,745	14,418
Fixed assets	123,452	127,629	57,966
Less — accumulated depreciation	(77,934)	(82,271)	(37,365)
FIXED ASSETS, NET (Note 8)	45,518	45,358	20,601
INTANGIBLE ASSETS, NET (Note 9)	5,299	31,052	14,103
OTHER ASSETS (Note 10):			
Investments in affiliates	12,326	14,712	6,682
Treasury stock	–	1,281	582
Securities	5	12	5
Other receivables	1,348	2,694	1,223
TOTAL ASSETS	89,181	126,854	57,614
LIABILITIES AND STOCKHOLDERS' EQUITY			
CURRENT LIABILITIES:			
Short term debt (Note 11)	9,622	29,307	13,311
Payables, trade and other (Note 12)	20,495	19,561	8,884
Accrued payroll and employee benefits	1,539	2,108	957
Accrued income taxes	1,184	572	260
Other accrued liabilities (Note 13)	944	1,664	756
TOTAL CURRENT LIABILITIES	33,784	53,212	24,168
LONG TERM DEBT (Note 11)	10,002	16,010	7,271
RESERVES AND OTHER LIABILITIES:			
Deferred income taxes	292	390	177
Other liabilities (Note 14)	3,893	5,257	2,388
Employee termination indemnities (Note 15)	2,896	2,554	1,160
TOTAL LIABILITIES	50,867	77,423	35,164
STOCKHOLDERS' EQUITY:			
Share capital (Note 16)	7,426	7,426	3,373
Additional paid-in capital	3,491	3,491	1,585
Reserves, retained earnings and profit of the year (Note 17)	22,087	25,526	11,593
Total stockholders' equity before minority interest	33,004	36,443	16,551
Minority interest	5,310	12,988	5,899
TOTAL STOCKHOLDERS' EQUITY	38,314	49,431	22,450
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	89,181	126,854	57,614

The accompanying notes to the consolidated financial statements
are an integral part of these financial statements

Exchange rate: Lire 2,201.80 = U.S.$ 1.00 as of March 30, 2001

TELECOM ITALIA S.p.A.
CONSOLIDATED STATEMENTS OF INCOME
FOR THE YEARS ENDED DECEMBER 31, 1998, 1999 AND 2000

	1998	1999	2000	2000
	(Billions of Lire)			Millions of U.S. Dollars
Operating revenues	48,507	52,481	55,979	25,424
Other income (Note 19)	1,085	998	826	375
Total revenues	49,592	53,479	56,805	25,799
Cost of materials	4,535	4,795	4,373	1,986
Salaries and social security contributions	9,665	9,636	9,729	4,419
Depreciation and amortization	10,480	10,338	10,933	4,965
Other external charges (Note 20)	17,552	18,561	20,893	9,489
Changes in inventories	262	(251)	(537)	(244)
Capitalized internal construction costs	(2,088)	(2,056)	(1,765)	(802)
Total operating expenses	40,406	41,023	43,626	19,813
Operating income	9,186	12,456	13,179	5,986
Interest income (Note 21)	1,579	1,073	1,636	743
Interest expense (Note 22)	(1,681)	(2,837)	(4,779)	(2,171)
Other income and (expense), net (Note 23)	133	(981)	(415)	(188)
Income before income taxes	9,217	9,711	9,621	4,370
Income taxes (Note 24)	(3,965)	(5,046)	(3,912)	(1,777)
Net income	5,252	4,665	5,709	2,593
Minority interest	(1,422)	(1,301)	(1,782)	(809)
Net income, after minority interest	3,830	3,364	3,927	1,784

The accompanying notes to the consolidated financial statements
are an integral part of these financial statements

Exchange rate: Lire 2,201.80 = U.S.$ 1.00 as of March 30, 2001

TELECOM ITALIA S.p.A.
CONSOLIDATED STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED DECEMBER 31, 1998, 1999 AND 2000

	1998	1999	2000	2000
	(Billions of Lire)			(Millions of U.S. Dollars)
OPERATING ACTIVITIES:				
Net income, after minority interest	3,830	3,364	3,927	1,784
Minority interest	1,422	1,301	1,782	809
Depreciation and amortization	10,480	10,338	10,933	4,965
Net change in deferred taxes	(179)	(169)	98	45
(Gains) losses on disposals of fixed assets and investments	(294)	116	(2,112)	(959)
Write-off of fixed and intangible assets and investments	2,195	1,189	2,195	997
Net change in other liabilities	911	(635)	1,364	619
Net change in reserve for employee termination indemnities	233	185	(342)	(155)
Changes in operating assets and liabilities	(234)	(599)	(7,312)	(3,321)
Other movements, net	(51)	292	364	165
Net cash flows from operating activities	18,313	15,382	10,897	4,949
INVESTING ACTIVITIES:				
Investments in fixed assets	(9,423)	(7,503)	(7,530)	(3,420)
Investment grants	98	128	52	24
Addition to intangible assets	(2,236)	(3,057)	(25,402)	(11,537)
Addition to other long-term assets	(7,224)	(2,517)	(5,810)	(2,639)
Proceeds from the sale of fixed assets and other investments	1,675	1,063	8,348	3,791
Net cash flows used in investing activities	(17,110)	(11,886)	(30,342)	(13,781)
FINANCING ACTIVITIES:				
Changes in short-term debt	1,289	468	19,055	8,654
Increase in long-term debt	2,479	1,485	2,822	1,282
Repayment of and other changes to long-term debt	(2,891)	(2,509)	(3,397)	(1,543)
Paid in capital in subsidiaries	—	80	8,082	3,671
Dividends paid	(1,900)	(3,278)	(5,903)	(2,681)
Net cash flows from (used in) financing activities	(1,023)	(3,754)	20,659	9,383
Increase (decrease) in cash and cash equivalents	180	(258)	1,214	551
CASH AND CASH EQUIVALENTS:				
Beginning of year	1,390	1,570	1,312	596
End of year	1,570	1,312	2,526	1,147

The accompanying notes to the consolidated financial statements
are an integral part of these financial statements

Exchange rate: Lire 2,201.80 = U.S.$ 1.00 as of March 30, 2001

TELECOM ITALIA S.p.A.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
FOR THE YEARS ENDED DECEMBER 31, 1998, 1999 AND 2000

		Attributable to Telecom Italia			Attributable to minority interest	
	Share Capital	Additional Paid in Capital	Reserves, retained earnings and Profit of the year	Total	Reserves, retained earnings and profit of the year	Total
			(Billions of Lire)			
BALANCES AS OF DECEMBER 31, 1997	7,421	3,431	19,059	29,911	3,123	33,034
Dividends paid (Lire 190 per ordinary share and Lire 210 per savings share)	—	—	(1,453)	(1,453)	(447)	(1,900)
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	(637)	(637)	(64)	(701)
Net income for the year	—	—	3,830	3,830	1,422	5,252
BALANCES AS OF DECEMBER 31, 1998	7,421	3,431	20,799	31,651	4,034	35,685
Dividends paid (Lire 280 per ordinary share and Lire 300 per savings share)	—	—	(2,121)	(2,121)	(688)	(2,809)
Distribution of reserves	—	—	—	—	(469)	(469)
Stock options	5	60	—	65	—	65
Consolidation on a line by line basis of Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes	—	—	—	—	1,082	1,082
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	45	45	50	95
Net income for the year	—	—	3,364	3,364	1,301	4,665
BALANCES AS OF DECEMBER 31, 1999	7,426	3,491	22,087	33,004	5,310	38,314
Dividends paid (Lire 603 per ordinary share and Lire 623 per savings share)	—	—	(4,505)	(4,505)	(1,398)	(5,903)
Changes in consolidation area	—	—	716	716	2,084	2,800
Conversion of TIM's savings share	—	—	3,236	3,236	4,837	8,073
Net difference arising on the translation of foreign currency financial statements and other minor adjustments	—	—	65	65	373	438
Net income for the year	—	—	3,927	3,927	1,782	5,709
BALANCES AS OF DECEMBER 31, 2000	7,426	3,491	25,526	36,443	12,988	49,431
BALANCES AS OF DECEMBER 31, 2000 (millions of U.S. Dollars)	3,373	1,585	11,593	16,551	5,899	22,450

The accompanying notes to the consolidated financial statements are an integral part of these financial statements

Exchange rate: Lire 2,201.80 = U.S.$ 1.00 as of March 30, 2001

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, 2000 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, 1999 and 2000 and on consolidated net income for each of the three years in the period ended December 31, 2000 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.

These consolidated financial statements are presented in Italian Lire ("Lire") and, for 2000, are also presented in U.S. dollars solely for the convenience of the reader, at the exchange rate of Lire 2,201.80 = U.S.$ 1.00, using the noon buying rate in the city of New York for cable transfers in foreign currencies as announced by the U.S. Federal Reserve Bank of New York for customs purposes for the euro on March 30, 2001 of euro 1.1371349 = U.S.$ 1.00 multiplied by the fixed euro/lire exchange rate of Lire 1,936.27= euro 1.00 established on December 31, 1998. No representation is made that these Lire amounts have been, could have been, or could be converted into U.S. dollars at that or any other rate.

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). The proportional method of consolidation, pursuant to Article 37 of Italian Law 127/1991, is used to consolidate the following companies controlled jointly with other stockholders’ at 50%: Nortel Inversora and the controlled Telecom Argentina group (Nortel Inversora group) and Viasat and its subsidiary Viasat Assistance (Viasat group). Prior to 2000 the Nortel Inversora group was accounted for on the equity method. The consolidation of investments on a proportional basis was effected by including the individual items of assets, liabilities, costs and revenues of the companies jointly controlled, in proportion to the percentage of ordinary shares held. The consolidated financial statements therefore present the portion of receivables, payables, costs and revenues of the companies consolidated on a line-by-line basis not eliminated against the underlying share of the companies consolidated on a proportional basis. The value of investments consolidated proportionally has been eliminated against the corresponding share of the net equity of such investments; the minority interest in the stockholders' equity will include any proportional share of the net equity in the event of the consolidation of a group.

The other affiliated companies in which Telecom Italia holds, directly or indirectly, between 20% and 50% of the voting rights are generally 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 the first half of 1998, the Group sold shares equivalent to 16.67% of the share capital of its subsidiary STET Hellas, a Greek GSM mobile telephone operator for a total of U.S. $ 327 million. The shares were sold through an international public offering and listed on NASDAQ and on the Amsterdam Stock Exchange.

- In July 1998, the Group was awarded certain fixed line and mobile concessions in connection with the privatization of Telebras in Brazil. For wired network telecommunications, the holding Solpart Participacoes (of which the Group holds a 38% of voting rights) acquired 51.79% of Brazil Telecom Participacoes S.A. (formerly Tele Centro Sul Participacoes), and for wireless telecommunications, Bitel (a subsidiary of Telecom Italia) acquired 25.9% of the voting rights of Tele Celular Sul Participacoes and Tele Nordeste Celular Participacoes. The total purchase price was Lire 2,180 billion.

- In December 1998, the Group acquired approximately 25% of the share capital of Telekom Austria, the principal operator of telecommunications in Austria that also holds 75% of Mobilkom Austria (25% is held by STET Mobile Holding). The purchase price was Lire 3,837 billion. In November 2000, the state stockholder, OIAG, floated 25.8% of Telekom Austria (128.8 million shares) on the Vienna and New York stock exchanges. Following this event, the Telecom Italia Group received an additional 4.8% stake, bringing its holding in the company from approximately 25% to 29.8%. The new stockholder composition of the company after the float is as follows: OIAG 47.8%, Telecom Italia Group 29.8% and market float 22.4%.

- In March 1999, the Group acquired for about 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 US$ 265 million. Nortel Inversora is the holding company that now owns a controlling stake (54.74%) in Telecom Argentina. A five year renewal of the "management contract" was also signed.

- In April 2000, Telecom Italia purchased 50 million of Telecom Italia Mobile ("TIM") ordinary shares at a price of Lire 1,231 billion, in order to strengthen 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 US $ 810 million.

- 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 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 GSM license in 1998 and is operating in the Venezuelan Central Region which, including Caracas and other major cities, is the most important region of Venezuela, with 60% of the national GDP.

- 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 US $ 240 million. TIM now controls 90% of Maxitel S.A. ordinary shares.

- 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, 2000 Telecom Italia owns, directly and indirectly, approximately 60% 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 the 60% of this company to Beni Stabili, a leading Italian real estate operator, (45%) 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.

SEAT group, Jet Multimedia group, Mageos, Corporacion Digitel and Maxitel group, acquired in the last part of fiscal 2000, are consolidated as of December 31, 2000 only in the balance sheet.

Sirti group and Italtel group, disposed of during the last part of fiscal 2000, are consolidated only in the statement of income for the period from January 1, 2000 to September 30, 2000.

With respect to recently acquired foreign holdings operating in the "new economy", no writedowns were effected notwithstanding the fall in the market values of this sector. This determination was made after taking into consideration the prospects for business in the medium and long-term which are deemed unchanged and also on account of the industrial – and thus strategic – nature of such investments in relation to the competitive positioning of the Telecom Italia Group in the relevant markets. Nevertheless, due to the rapid changes in this sector, these holdings will be continually and carefully monitored.

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 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.

- All significant intercompany transactions are eliminated, together with the unrealized intercompany profits included in inventory.

- Unrealized intercompany profits, and related tax effects, on the sale of equipment and installations which were made at market prices by Group Companies principally to Telecom Italia and TIM were eliminated. 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 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 income for the year.

- The financial statements of foreign subsidiaries are translated into Italian Lire applying the exchange rates in effect at year-end for the assets and liabilities. The average exchange rate in effect for the year is used for translating the statement of income. Translation gains or losses are reflected in the Group's consolidated stockholders' equity.

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 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 National Regulatory Agency 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;
- access deficit contributions;
- 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 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.

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 annually for the unamortized discount or premium.

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 receivables and payables

Accounts receivables and payables 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.

Until 1998, accounts receivables and payables in foreign currencies were recorded at the exchange rate prevailing at the date of the transaction and adjusted to reflect year-end rates only in the case where balances translated at year-end exchange rates produce a net exchange loss. Starting from 1999, accounts receivables and payables in foreign currencies are adjusted to reflect year-end rates with gains or losses on the translation accounted for as “interest income” or “interest expense”.

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. Until 1998, long-term contracts were valued using the completed contract method. Starting from 1999, 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.

Scheduled depreciation is taken at rates that are deemed sufficient to allocate the cost of the assets over the remaining useful life.

Depreciation is calculated on a straight line basis over the estimated useful lives of the assets using the following rates:

Land and 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 and includes advances to suppliers. 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.

The Group periodically evaluates potential impairment loss relating to long-lived assets, including goodwill, when a change in circumstances occurs by assessing whether the carrying amount can be recovered over the remaining life. 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 statements of income.

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 income 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

Employee termination indemnities

The reserve to cover employee termination indemnities is calculated on the basis of current legal and labor contracts' requirements and reflects the undiscounted amount of the vested obligation for all employees at the date of the consolidated financial statements.

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 1998, 1999 and 2000 gross research and development costs charged to income (before revenue grants) amounted to Lire 730 billion, Lire 640 billion and Lire 520 billion, 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 income 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 when the service is provided.

   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.

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 prepaid and deferred income taxes that are determined under the liability method. Deferred and prepaid income taxes represent liabilities to be paid or assets to be received, respectively, in the future and reflect the tax consequences on future years of temporary differences between the tax bases of assets and liabilities and their financial reporting amounts.

Deferred tax assets and deferred tax liabilities are off set, whenever allowed by local tax laws.

The tax benefit of tax loss carryforwards is recorded when there is a reasonable expectation of realization.

Accounting for leases

Leases are capitalized when the contract contains a purchase option to acquire the asset during the holding period. The assets 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 income. 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.

Interest rate swaps involve the exchange of flows of interest between the counterparts calculated on the notional amount of reference at the agreed fixed or variable rates at the specified maturity date. The differential between the two interest rates is paid or received and included in interest expense or interest income.

Cross currency and interest rate swaps are used both to hedge interest rate risk and exchange risk on loans denominated in foreign currencies, making it possible to convert the notional amount in foreign currency to the domestic currency and from a variable rate to a fixed rate and viceversa.

The interest paid or received or the differential paid or received is recorded on an accrual basis in the statement of income in specific accounts under interest expense and interest income.

Reclassifications

Certain reclassifications have been made to the prior year's financial statements to conform with the 2000 presentation.

Note 4 — Marketable Securities

The Lire 2,171 billion increase in marketable equity and debt securities is mainly due to the consolidation of Maxitel (Lire 527 billion) and Telecom Argentina (Lire 331 billion) and the increase in marketable securities of Softe, Sogerim and Telecom Italia. As of December 31, 2000, this item includes Lire 740 billion (Lire 122 billion as of December 31, 1999) of listed shares of consolidated subsidiaries.

Note 5 — Receivables

	As of December 31,	
	1999	**2000**
	(Billions of Lire)	
Trade	16,175	16,912
Reserve for bad debt	(1,297)	(1,433)
	14,878	15,479
Unconsolidated subsidiaries	75	79
Affiliated companies	953	800
Parent companies	2	5
	15,908	16,363

The Lire 455 billion increase in receivables is mainly attributable to the inclusion in the consolidation of Nortel Inversora group and the acquisition of SEAT group. These increases were partly offset by the reduction in the trade accounts receivable of Telecom Italia and the mobile telephony companies. The reduction for Telecom Italia is due to a decrease in revenues and the assignment of receivables to factoring companies while, for the mobile telecommunications companies, the reduction derives from the ever-increasing amount of traffic generated by the prepaid service as opposed to subscriptions.

Note 6 — Inventories

	As of December 31,	
	1999	**2000**
	(Billions of Lire)	
Raw materials and supplies	189	40
Purchased finished goods	403	415
Work in progress and semi-finished products	134	26
Finished products	23	3
Long and short-term contracts	1,217	905
Advances to suppliers	29	16
	1,995	1,405

Inventories include Lire 878 billion as of December 31, 2000 (Lire 844 billion as of December 31, 1999) attributable to telecommunications service companies and Lire 420 billion as of December 31, 2000 (Lire 303 billion as of December 31, 1999) attributable to IT software and service companies. Inventories held by the telecommunications service companies include satellite system equipments for data transmission which are classified in long and short-term contracts as well as telephone and telematic products and mobile phone equipment for sales to third parties which are classified in purchased finished goods. The total decrease in inventories of Lire 590 billion is essentially due to the disposal of the manufacturing and installation companies.

Note 7 — Other Current Assets

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Receivables from banks and other loans	67	1,803
Receivables from national government and public agencies for subsidies and contributions	112	82
Cash receipts in transit	532	362
Tax receivables	442	1,116
Deferred tax assets	364	1,107
Prepaid expenses	86	652
Accrued income	94	139
Other	1,190	1,436
	2,887	6,697

The increase of Lire 1,736 billion in receivables from banks and other loans is mainly due to the loan of securities made by Telecom Italia to unrelated parties and covered by the specific guarantee contracts.

The Lire 674 billion increase in tax receivables is principally due to the tax benefits on investments utilized by TIM.

Deferred tax assets, including those under Other assets (see Note 10), totaled Lire 1,928 billion (Lire 940 billion as of December 31, 1999), while deferred income taxes amounted to Lire 390 billion (Lire 292 billion as of December 31, 1999). Net deferred tax assets (Lire 1,538 as of December 31, 2000) increased by Lire 890 billion principally due to lower deferred tax liabilities of Telecom Italia as a result of the reclassification of the "reserve for accelerated depreciation" included in shareholders' equity, pursuant to the application of art. 14 of Law No. 342/2000.

Deferred tax assets are mainly related to the writedowns of receivables and software and the reserve for risks and charges; deferred income taxes mainly originate from deferred gains.

Tax loss carryforwards, which have not been considered in the determination of deferred tax assets, amount to approximately Lire 5,000 billion.

Other current assets includes miscellaneous receivables due from the Italian government and other public institutions and advances to personnel.

During 2000, TIM assigned trade accounts receivable to factoring companies for Lire 6,203 billion without recourse. As of December 31, 2000, receivables sold and not yet due amounted to Lire 510 billion.

Telecom Italia assigned receivables without recourse, not due on December 31, 2000, to factoring companies for a total of Lire 400 billion, with a loss on the sale of Lire 5 billion.

Note 8 — Fixed assets, net

Fixed asset balances, net of accumulated depreciation, are detailed as follows:

	As of December 31, 1999	As of December 31, 2000		
		Cost	Accumulated Depreciation	Net book value
		(Billions of Lire)		
Land and buildings	9,823	8,645	2,939	5,706
Telecommunications systems and equipment, machinery and installations	31,991	109,877	74,781	35,096
Industrial and commercial equipment	240	1,938	1,786	152
Other	1,097	4,384	2,765	1,619
Construction in progress and advances to suppliers	2,367	2,785	—	2,785
	45,518	127,629	82,271	45,358

As of December 31, 2000, fixed assets associated with telecommunications activities amounted to Lire 43,776 billion (Lire 42,639 billion as of December 31, 1999), comprising mainly machinery and installations of Lire 34,685 billion and land and buildings of Lire 4,827 billion.

As of December 31, 2000 fixed assets include leased assets with a net book value of Lire 1,203 billion (gross value of Lire 1,472 billion less accumulated depreciation of Lire 269 billion).

An analysis of the movements in fixed assets for each of the years is as follows:

	1999	2000
	(Billions of Lire)	
Balance, at beginning of the year	45,665	45,518
Investments in fixed assets	7,503	7,530
Disposals	(330)	(199)
Sale by Telecom Italia of a portion of its real estate portfolio	-	(4,632)
Depreciation (*)	(8,425)	(8,741)
Write-downs	(138)	(22)
Changes in consolidation area and other	1,243	5,904
Balance, end of the year	45,518	45,358

The increase related to the changes in consolidation area and other mainly refers to the inclusion of Nortel Inversora group (Lire 5,056 billion), SEAT group (Lire 340 billion), Maxitel group (Lire 734 billion) and Digitel (Lire 207 billion), partially offset by the effect of the disposal of Sirti and Italtel totaling Lire 734 billion.

(*) A breakdown of depreciation is as follows:

	1999	2000
	(Billions of Lire)	
Land and buildings	528	513
Telecommunications systems and equipment, machinery and installations	7,165	7,443
Industrial and commercial equipment	146	95
Other	586	690
	8,425	8,741

A detail of investments in fixed assets during each of the years is as follows:

	1999	2000
	(Billions of Lire)	
Fixed line services Italy	4,574	3,675
Mobile services Italy	1,582	1,668
Satellite services	56	57
International telecommunication services	955	1,974
IT software and services	73	232
Manufacturing	46	34
Installation	58	27
	7,344	7,667
Other activities and intercompany eliminations	159	(137)
	7,503	7,530

Investments in fixed assets in 2000 are in line with those of 1999 because of a decrease in fixed line investments in fixed assets by Telecom Italia that were offset by higher investments in fixed assets by the mobile telephony companies and the inclusion of Nortel Inversora group.

Note 9 — Intangible Assets

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Licenses, trademarks and similar rights	296	6,787
Goodwill	1,975	19,942
Software and other rights	1,639	1,585
Leasehold improvements	357	506
Work in progress and advances	755	1,626
Other	277	606
	5,299	31,052

- Licenses, trademarks and similar rights primarily include the UMTS license acquired by TIM in Italy (Lire 4,680 billion), and the residual amount, net of amortization, of the mobile telephony licenses of Maxitel (Lire 1,055 billion), Telecom Argentina (Lire 368 billion) and TIM Perù (Lire 366 billion).

- The increase of goodwill is mainly due to the purchase of the controlling interest in SEAT (Lire 12,736 billion) and the increase of the ownership in TIM (Lire 1,525 billion), both net of the amortization charge for the year. This item also includes the goodwill related to Jet Multimedia group and the Europe Explorer group (Lire 1,381 billion), Digitel (Lire 700 billion), Maxitel group (Lire 646 billion), TDL Infomedia (Lire 595 billion), Tele Celular Sul Participacoes (Lire 506 billion) and Tele Nordeste Celular Participacoes (Lire 503 billion). It also includes Lire 1,044 billion relating to the companies in the SEAT group.

- Software and other rights principally includes software for telecommunications services.

- Work in progress and advances relate primarily to costs of developing software projects, mainly for internal use.

Movements in intangible assets during the year are as follows:

	(Billions of Lire)
Additions	25,402
Amortizations	(2,192)
Other movements, net	2,543
	25,753

Additions include goodwill deriving from the acquisition of subsidiaries for Lire 17,637 billion mainly related to the following transactions (gross):

- acquisition of controlling interest in SEAT (Lire 13,159 billion);
- acquisition of controlling interest, through 9Télécom Reseau, in Jet Multimedia group and Europe Explorer group (Lire 1,381 billion);
- acquisition, by Telecom Italia of 50 million TIM ordinary shares (Lire 1,196 billion);
- acquisition of the controlling interest in Maxitel (Lire 646 billion) and Digitel (Lire 700 billion);
- transactions involving the reorganization of the international telecommunications business (Lire 409 billion).

Additions in 2000 also refer to the cost of the UMTS license acquired by TIM (Lire 4,680 billion) and a PCS 1900 license obtained through TIM Perù (Lire 381 billion).

Other net movements are mainly due to the inclusion of Nortel Inversora group (Lire 931 billion), Maxitel group (Lire 1,055 billion) and SEAT (Lire 1,238 billion) and to the exclusion of Italtel and Sirti (decrease of Lire 375 billion).

Note 10 — Other assets

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Investments in:		
Unconsolidated subsidiaries	235	41
Affiliated companies	11,512	14,302
Other companies	579	369
Total investments	12,326	14,712
Treasury stock	-	1,281
Other securities	5	12
Deferred tax asset	576	821
Other receivables	772	1,873
	13,679	18,699

Investments in affiliated companies increased by Lire 2,790 billion compared to 1999, chiefly due to the purchase of the investment in GLB Servicos Interativos, the Internet company of Globo Organizacoes (acquisition of a 30% participation for Lire 1,686 billion), the formation of the company IS TIM, which won the third GSM l800 license in Turkey (Lire 594 billion) and the consolidation of SEAT (Lire 436 billion).

The largest investments in affiliated companies are:

- Telekom Austria (Lire 3,523 billion), the dominant carrier in the country of wireline telephone services, Internet and data;
- GLB Servicos Interativos (Lire 1,566 billion), an Internet company in Brazil that manages a portal dedicated to the Portuguese-speaking community worldwide; in 2000, the company also began developing an ISP business;
- Mobilkom Austria (Lire 1,135 billion), the holder of licenses to provide wireless telephone services;
- Etec S.A. (Lire 1,043 billion), the Cuban operator for national and international wired telecommunications services;
- Auna, formerly Retevision (Lire 986 billion), a Spanish holding company that provides mobile, fixed and multimedia services;
- Solpart Participacoes (Lire 893 billion), a holding company for wired network services in Brazil;
- Entel Chile (Lire 733 billion), the leading operator in the long distance telephony sector, the mobile telephony sector and the data-transmission/internet segment in Chile;
- IS TIM (Lire 684 billion), a mobile telecommunications company in Turkey;
- Astrolink (Lire 507 billion), the project to provide, through geostationery satellites and on a worlwide basis, broadband interactive services;
- Eutelsat (Lire 419 billion) a European telecommunications satellite organization;
- IM.SER (Lire 395 billion) a real estate management company;
- Telekom Srbija (Lire 378 billion), the wireline carrier and the country's second largest mobile operator;
- Bouygues Décaux Télécom (Lire 333 billion), a holding company which controls the investments of the Bouygues group in the telecommunications industry.

Treasury stock (Lire 1,281 billion) refers to 104,978,070 Telecom Italia savings share bought during the year by Telecom Italia.

Other receivables include the non current portion of the expenses relating to the deferral of the premium paid for the put option on the SEAT shares, as well as receivables from affiliated companies, capital contributions to the Jilin Huatai Communications joint ventures, bond deposits and other miscellaneous receivables from third parties and employees.

Note 11 — Financial Debt

	As of December 31, 1999	As of December 31, 2000		
	Total	Denominated in Italian Lire	Denominated in Foreign Currency(*)	Total
		(Billions of Lire)		
Short-term debt	7,110	21,136	5,029	26,165
Current portion of long term debt	2,512	1,998	1,144	3,142
	9,622	23,134	6,173	29,307
Long-term debt	10,002	9,346	6,664	16,010
Total financial debt	19,624	32,480	12,837	45,317

(*) Includes Lire 1,948 billion in Euro currencies.

The increase in total financial debt is mainly due to the acquisition of the controlling interest in SEAT, the acquisition and subscription of capital increases in investment holdings abroad, the acquisition of a UMTS license by TIM, dividends paid, the buy-back of savings shares by Telecom Italia and changes in the scope of consolidation.

Long-term debt consists of the following:

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Payables to banks	7,136	8,318
Payable to other financial institutions	1,276	2,454
Debenture loans	1,578	3,229
Payables to affiliates	-	980
Note payables	-	97
Suppliers	8	62
Other	4	870
	10,002	16,010

Payables to banks are secured by mortgages and liens on land and buildings of Lire 402 billion.

Payable to other financial institutions refers primarily to the loans payable by SEAT of Lire 1,848 billion to SEAT Pagine Gialle Finance S.r.l., a corporate vehicle operating under Law No. 130/1999 on securitization and to the medium/long term loans from the Cassa Depositi e Prestiti and IRI to Telecom Italia.

The debenture loans comprising their current portion include:

- debentures maturing between 2001 and 2008 issued by Nortel Inversora group for a total of Lire 1,936 billion;

- Telecom Italia 1992-2010 debenture loan reserved for staff in service and retired. Balances outstanding as of December 31, 1999 and 2000 were Lire 825 billion and Lire 282 billion, respectively;

- debentures maturing between 2001 and 2002 issued by Softe through different financial institutions for US$ 229 million, equivalent to Lire 477 billion;

- debentures issued by TDL Infomedia Ltd (SEAT group), maturing beyond 2005, for Lire 392 billion;
- debentures maturing between 2002 and 2005 issued by the Brazilian companies Tele Nordeste Celular and Tele Celular Sul for Lire 425 billion.

Long-term debt as of December 31, 2000 classified by maturity is as follows (in billions of Lire):

2001 (current portion of long-term debt)	3,142
2002	4,364
2003	5,296
2004	1,751
2005	1,252
Beyond 2005	3,347
	19,152

A grouping of the financial debt by interest rates is as follows:

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Up to 2.5%	3,411	1,943
From 2.5% to 5%	9,671	7,500
From 5% to 7.5%	5,240	26,799
From 7.5% to 10%	1,284	3,349
Over 10%	18	4,046
	19,624	43,637
Non-interest bearing	–	1,680
	19,624	45,317

The non-interest bearing financial payables relate to certain stock lending agreements entered into by Telecom Italia for the loan of SEAT shares.

Financial debt denominated in foreign currency as of December 31 of each year is as follows:

	In Foreign Currency (Millions)		(Billions of Lire)	
	1999	2000	1999	2000
U.S. $	1,364	4,063	2,629	8,531
Euro currencies	342	1,006	662	1,948
GBP	320	253	964	756
GRD	44,700	-	262	-
BRL	515	1,342	555	1,428
JPY	2,393	8,153	36	141
Other			39	33
			5,147	12,837

Note 12 — Payables, trade and other

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Advances from customers	733	716
Trade payables	11,648	12,599
Payables to affiliated companies	1,145	1,124
Other taxes payable	1,100	1,223
Payables to customers	3,394	3,261
Other	2,475	638
	20,495	19,561

The Lire 951 billion increase in trade payables is mainly due to the inclusion of Nortel Inversora group, Maxitel group and SEAT group.

Payables to customers consist of deposits paid by customers and pre-billed basic charges (attributable mainly to January and February), as well as prepaid traffic.

Note 13 — Other accrued liabilities

Other accrued liabilities consist of accrued expenses (primarily interest) of Lire 240 billion as of December 31, 1999 and Lire 434 billion as of December 31, 2000 and deferred income of Lire 704 billion as of December 31, 1999 and Lire 1,230 billion as of December 31, 2000. Deferred income include, 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,	
	1999	2000
	(Billions of Lire)	
Reserve for taxes	309	307
Reserves for pensions and similar obligations	-	30
Reserve for restructuring costs	284	318
Reserve for contract and other risks	1,121	2,380
Payable to INPS and other accruals	2,179	2,222
	3,893	5,257

- The reserve for restructuring costs includes Lire 295 billion set up in 2000 by Telecom Italia for corporate restructuring costs.

- The reserve for contract and other risks mainly reflects the estimated liabilities to be incurred in connection with contract commitments as well as outstanding disputes with staff and others. Such reserve includes Lire 775 billion recognized by TIM to meet the risks originating from the mobile market due to technological advances. This provision includes estimates determined by evaluating risks related to the evolution of third-generation technologies. Besides the economic risks arising as a result of the development of new technologies and the expenses necessary to replace certain types of network installations in advance, the reserve also includes risks associated with the need to make important and early revisions to the billing system in order to accommodate new types of services.

- 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 non current portion of 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 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 analysis of the reserve for each of the years is as follows:

	1999	2000
	(Billions of Lire)	
Balance, at beginning of the year	2,711	2,896
Provision for the year	487	469
Indemnities paid	(233)	(390)
Advances	(41)	(90)
Other variations	(28)	(331)
Balance, end of the year	2,896	2,554

Other variations are mainly due to the change in the scope of consolidation, principally the exclusion of the manufacturing and installation companies (Lire 333 billion), partially offset by the entry of the SEAT group (Lire 75 billion).

Note 16 — Share capital

The share capital of Telecom Italia as of December 31, 2000 of Lire 7,426 billion, unchanged compared to December 31, 1999, is fully paid-in and is represented by 5,260,037,131 ordinary shares and 2,166,120,095 savings shares all with a unit par value of Lire 1,000.

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 of the year

	As of December 31,	
	1999	2000
	(Billions of Lire)	
Reserves and retained earnings	18,723	21,599
Net income, after minority interest	3,364	3,927
	22,087	25,526

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, 2000, the Group has purchase commitments totaling Lire 9,344 billion (Lire 1,086 billion as of December 31, 1999).

In particular, the purchase commitments refer to:

- Lire 5,780 billion of Telecom Italia for the put option on SEAT shares. Under the contract entered into on March 15, 2000 (as subsequently amended and integrated), Telecom Italia gave Huit II a put option on 710,777,200 SEAT shares at a strike price of Euros 4.20 each. The contract provided for the exercise of such option after the deed of merger between SEAT 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 shares. On December 4, 2000, CEL renegotiated the contract with Telecom Italia, extending the put-option period to five years, with the possibility of an early exercise of the option in April and May 2003, 2004 and 2005. The time extension made it possible to defer the financial impact of settling the put. Stet International Netherlands ("SIN") then purchased from CEL, through the Liberator Ltd. trust, a call option on 660,777,200 SEAT shares with the same expiry date and strike price as the put option, paying a total premium of Euros 747,016,226 (Lire 1,446,425 million) to CEL. 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 SIN. The implicit rate of interest was 6.2%. As of December 31, 2000, the market price of SEAT ordinary shares is significantly lower than the strike price. At the expiration of the put-option, the purchase of SEAT shares will result in additional goodwill equal to the cost of acquisition less the fair value of SEAT net assets acquired at that date.

As of December 31, 1999 and 2000, the Group has given guarantees of Lire 2,557 billion and Lire 5,675 billion, respectively. The amount of the guarantees provided as of December 31, 2000 is not comparable to that of the prior year since, beginning in 2000, the amount is presented net of counter-guarantees received amounting to Lire 1,085 billion as of December 31, 2000.

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, 2000 relating to such contributions can be estimated to range from Lire 1,900 billion to Lire 2,500 billion (of which Lire 509 billion has already been paid), net of the residual amount already recorded in 1993 by IRITEL and presently appearing in Telecom Italia's and TIM's financial statements following the IRITEL merger (Lire 1,377 billion).

As regards pre-amortization interest and the related accrued interest payment of the residual amount of Lire 789 billion, this amount was suspended from June 2000 in compliance with ruling No. 4242 of April 5, 2000 handed down by the Court of Cassation.

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 and interest rate options (to reduce the interest rate exposure on fixed-rate and floating-rate bank loans and bonds) and cross-currency and interest rate swaps ("CIRS") (to convert foreign currency loans – US dollar, pound sterling, Japanese yen and euro – into the functional currencies of the various subsidiaries).

The following table gives a description of the financial derivative contracts outstanding as of December 31, 2000 to hedge medium/long-term debt positions.

(in billions of lire)	Notional amount/ Capital exchanged at 12/31/2000	Market value of derivatives at 12/31/2000 (a)	Market value of underlying debt positions at 12/31/2000 (b)	Market value of debt including related derivatives at 12/31/2000 (c)=(b-a)
Interest rate swaps and interest rate options	5,629	46	5,637	5,591
Cross-currency and interest rate swaps	2,367	38	2,264	2,226

IRS (interest rate swaps) and IRO (interest rate options) involve the exchange of flows of interest calculated on the notional 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.

Generally, the counterparties to derivative contracts are only the best rated banks and financial institutions, and they are continually monitored in order to minimize the risk of non-performance.

The same also applies to CIRS 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 market value of CIRS reflects the differential between the fixed rate paid by the Telecom Italia Group and the market interest rate for the same maturities. The CIRS also reflect the difference between the forward exchange rate at the closing of the swap and the market rate as of December 31, 2000.

To determine the market value of the above financial derivatives, the Telecom Italia Group uses pricing models.

Hedges were also considered for the USD Libor in respect of USD loans contracted by Telecom Argentina, consolidated at 50%.

Besides derivative contracts used for managing debt positions, as of December 31, 2000, the Luxembourg subsidiary Softe had IRS and CIRS to hedge investments in bonds for a notional amount of Lire 526 billion.

Lastly, in addition to the various transactions to hedge the short-term positions of SOFTE, there were also transactions to hedge the interest rate exposure on short-term US dollar loans contracted by TIM.

Note 19–Other income

Other income includes operating grants received to cover the costs of research and development, technological innovation and personnel training of Lire 39 billion in 2000, Lire 39 billion in 1999 and Lire 38 billion in 1998, and miscellaneous income of Lire 787 billion in 2000, Lire 959 billion in 1999, Lire 1,047 billion in 1998 derived in part from the amount credited to income associated with capital grants and for amounts received by Telecom Italia and TIM from telephone subscribers who were late in paying their phone bills or other charges.

Note 20–Other external charges

	Year ended December 31,		
	1998	1999	2000
	(Billions of Lire)		
Costs of external services rendered	11,082	14,289	16,252
Rents and lease payments	1,285	1,363	1,546
Provision for bad debts	705	702	924
Provision for risk	345	155	231
Write-downs of fixed assets and intangibles	1,840	142	93
TLC license fee	1,029	1,174	1,107
Other provisions and operating charges	1,266	736	740
	17,552	18,561	20,893

The increase in other external charges is mainly due to the inclusion of the Nortel Inversora group and the increase in the costs of operating and developing mobile telecommunications services.

Note 21–Interest income

	Year ended December 31,		
	1998	1999	2000
	(Billions of Lire)		
Capital gain on sale of investments	838	167	323
Dividends	100	115	267
Interest and capital gains on fixed-income securities	192	187	202
Interest and commission from:			
– Unconsolidated subsidiaries and associated companies	35	35	29
– Banks	84	104	143
– Customers	19	24	6
Gain on foreign exchange	118	270	379
Other	193	171	287
	1,579	1,073	1,636

Capital gain on the sale of investments include Lire 312 billion of gains realized by Telecom Italia on the sale of TIM shares and venture capital investments.

Note 22–Interest expense

	Year ended December 31,		
	1998	1999	2000
		(Billions of Lire)	
Interest and commission paid to:			
Banks, on short and long term loans	763	680	1,313
Other financial institutions, on short and long term loans	182	130	115
Suppliers	1	54	62
Interest and other charges on debenture loans	124	96	287
Losses on foreign exchange	116	317	338
Write-downs and equity in losses in unconsolidated subsidiaries, affiliated and other companies, net	345	1,095	1,984
Write-downs of marketable securities	4	-	259
Other	146	465	421
	1,681	2,837	4,779

Interest and commission paid to banks are net of the Italian government's 3% subsidy.

The increase in 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 differences that arose upon the acquisition of these investments (Lire 877 billion in 2000, Lire 356 billion in 1999 and Lire 258 billion in 1998). The higher expenses are essentially due to the losses incurred by the Maxitel group (Lire 433 billion), Stream (Lire 392 billion), Auna group (Lire 340 billion) and Telekom Austria (Lire 101 billion).

Note 23–Other income and expense, net

	Year ended December 31,		
	1998	1999	2000
		(Billions of Lire)	
Restructuring costs	(369)	(495)	(953)
Charges as required under Law n. 58/1992 (see Note 18)	(333)	(364)	(297)
Gains on the disposal of investments	70	50	2,219
Deferred tax assets related to prior years	683	-	-
Other, net	82	(172)	(1,384)
	133	(981)	(415)

Gains on the disposal of investments mainly arose from the divestiture plan of the Group (Lire 1,877 billion), which refers to the sale of 80.1% of the Italtel group (Lire 760 billion), the Meie group (Lire 450 billion), Teleleasing (Lire 41 billion), the Sirti group (Lire 22 billion) and the sale of a portion of the real estate portfolio through the sale by Telecom Italia of the 60% of IM.SER (Lire 604 billion) to third parties. The remaining gains of Lire 342 billion are related to the sale of other investments and intangibles, fixed assets and business segments, of which Lire 107 billion comes from the sale of the investment in the Bharti group.

Other, net include:

- Lire 775 billion for the provision made by TIM to the reserve for technological risk;

- Lire 349 billion of expenses and provisions connected to the transactions for the disposal of investment holdings and the real estate portfolio;

- Lire 150 billion for an extraordinary annual contribution to INPS - as established by the 2000 Finance Bill ("the Bill") for the three years 2000 - 2002 to meet the higher financial requirements covered by the rules of the Fondo Previdenza Telefonici (FPT) that under the same Bill was abolished and now become part of the general "Employee Pension Fund";

- Lire 78 billion for the fine imposed on TIM by the Antitrust Authority for the alleged violation of rules against price-fixing. This amount is equal to the difference between the fine (Lire 100 billion) and the amount accrued by TIM in the 1999 financial statements (Lire 22 billion).

Note 24–Income taxes

Income taxes include the current, deferred and prepaid income taxes of individual consolidated companies.

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 is principally due to utilization of the tax benefits on investments made by TIM, 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".

Note 25–Subsequent events

Buy-back of Telecom Italia savings shares

January 10, 2001 marked the end of the period for the buy-back of Telecom Italia savings shares authorized by resolution of the ordinary stockholders' meeting of January 14, 2000. The resolution called for:

- a tender offer to purchase a maximum of 742,615,722 Telecom Italia savings shares at a price of Euros 6.5 per share, for a maximum equivalent amount of Euros 4,827 million (Lire 9,346 billion), successively carried out during the period February 17 to March 17, 2000;

- the purchase of treasury savings shares, within nine months after the end of the tender offer period, up to a maximum number equal to the difference between the maximum number of 742,615,722 and any lower number of shares tendered under the offer, by placing orders on the screen-trading market, as set forth by applicable laws, at the same price of Euros 6.5 per share.

1,793,820 shares were tendered under the offer; Telecom Italia subsequently purchased savings shares up to January 10, 2001, the expiration date of the authorization, taking into account the suspensions and extension voted by the stockholders' meeting of July 3, 2000.

As of the end of the period, the Company had purchased a total of 112,998,070 of its savings shares, equal to about 5.2% of savings share capital, for a total equivalent amount of about Euros 711 million (Lire 1,376.5 billion).

Conversion of savings shares and buy-back of ordinary shares of Telecom Italia

On March 31, 2001, the Board of Directors of Telecom Italia approved certain changes relating to the voluntary conversion of the savings shares and buy-back of ordinary shares presented on February 5, 2001. The project, which was modified as a result of the performance of the stock market and the indications emerging from the market in response to the original proposal, covers the following:

- the re-denomination of Telecom Italia share capital into euros, increasing the par value per share to Euro 0.55, to be effected by the cancellation of the treasury shares held and, for the remaining amount, by a credit to share capital of a part of the reserve for inflation adjustments Law No. 72 of March 19, 1983, with the related increase in share capital;

- the voluntary conversion of Telecom Italia savings shares into an equivalent number of ordinary shares plus the cash payment of a conversion premium per share and the subsequent tender offer for up to a maximum of 10% of the total outstanding share capital after such voluntary conversion. The total cash outflow for the tender offer will not be more than the cash inflow from the conversion. If the amount of cash inflows exceeds the amount used in the tender offer, such excess amount will be distributed, subject to a resolution passed by the stockholders' meeting, to all stockholders as an extraordinary dividend. The Board has been granted full authority to decide when to launch the offer for the conversion, with a deadline of December 31, 2001.

Fiscal audit

At the end of February 2001, the revenue authorities completed a general fiscal audit of Telecom Italia begun on February 3, 2000. The findings, which are based upon interpretations, will be appealed according to the normal procedures followed in such cases. Although it is currently not possible to determine to what extent the findings formulated by the tax auditors will give rise to adjustments in the tax returns which have been filed, the existing provisions are deemed sufficient to meet any contingencies.

UMTS

On January 10, 2001 the National Regulatory Agency informed the five highest bidders (TIM, Omnitel, Wind, Andala and Ipse) that they had been awarded the licenses and frequencies to supply services using UMTS technology. This technology forms the basis for the third-generation mobile telecommunications system that is expected to be fully applied commercially by 2002. TIM has committed to pay Euros 2.4 billion for its license, with approximately Euros 2.0 billion having been paid in December 2000. The remaining Euros 0.4 billion will be payable over a three year period. The licenses are valid for 15 years starting January 1, 2002. The award of the license, which was scheduled for December 20, 2000, had been postponed owing to problems encountered on some frequency bands, which were suspected of creating problems of interference and for which a technical solution was proposed by the same operators.

Local loop unbundling

On January 12, 2001, Telecom Italia was informed that resolution No. 14/00/CIR had been passed by the National Regulatory Agency on December 21, 2000. This resolution approves Telecom Italia's offering to supply services for unbundling local loops, subject to certain changes. The Company therefore presented the price list for the various ways of providing access, on copper or fiber optic cable, and supplied detailed information about the numbering groups available and about the exchanges which have been equipped with areas to house the other operators' equipment. By March 2001, 30 operators had already presented Telecom Italia with a request for interconnection to the so-called "last mile"; the necessary operational agreements have already been finalized with some of them.

Wireless local loop

On January 15, 2001, the Regulator issued a call for the advisor who will supervise the auction of the frequency licenses for the wireless local loop (disaggregated access via radio to the local wireline network). The advisor will collaborate with the Regulator during all the various stages of the auction, from the preparation of the rules, to the verification and evaluation of the applications for participation, and the preparation of the disclosure documents about the status of the bidding.

Commercial agreements and new services

During the first few months of the year, Telecom Italia concluded important agreements with technical partners, particularly with Alcaltel, with a view to augmenting efficiency and network capacity through SDH transmission systems, and with Marconi Communications to strengthen the fiber optic network using the new “smartphotonix” systems, which are capable of significantly increasing the capacity of broadband networks and, hence, the traffic of the Company.

During the first part of 2001, TIM signed agreements with: the banking group Credem, thus acquiring an important new partner in the sphere of e-banking solutions; with the Local Health Authority and the San Raffaele Hospital in Milan to design “Medguard”, the tele-medicine and tele-assistance service via GSM; with Telegate Italia (the SEAT group) for the launch of a new mobile phone service for receiving, through a call center, directory information about subscribers, commercial businesses and for direct connection to the number requested; with Webraska, a global supplier of wireless services and navigation technologies, to enable its customers, wherever they are, to find the best route to their destination.

In January 2001 IT Telecom, through Finsiel and Banksiel, launched a euro portal for the companies and organizations facing the changeover to the new European currency, thus acquiring the role of an information “link” between institutions and companies.

International development strategies

At the beginning of 2001, Telecom Italia signed an agreement with the American carrier Teleglobe to supply high-speed IP connectivity services over the next five years.

In January 2001, TIM signed a commercial agreement with the German operator, T-Mobil, based on reciprocal “privileged” roaming. Also in January, TIM signed agreements with Sony Computer Entertainment and with the operators KPN Mobile (the Netherlands) and NTT DoCoMo (Japan) to develop Internet services on the mobile network using UMTS technology.

On January 2, 2001, SEAT signed an agreement with RSL, holder of a minority interest in Telegate Holding, in order to purchase, in 2001, 48.63% of the share capital of the same company.

On January 31, 2001, the Regional Administrative Court (“TAR”) of Lazio suspended effectiveness of the National Regulatory Agency’s decision to block the TeleMonteCarlo (“TMC”) acquisition. The TAR of Lazio agreed that it is likely that its final ruling would be favorable to the acquisition. The TAR of Lazio requested that the National Regulatory Agency reconsider its ruling. The National Regulatory Agency reconfirmed its ruling on February 20, 2001. On March 7, 2001, the TAR of Lazio issued its final ruling, upholding SEAT’s appeal and overturning the National Regulatory Agency’s ruling of February 20, 2001.

In Brazil, in February 2001, TIM was awarded two GSM licenses for the areas of San Paolo and Brasilia, for a total cost of Lire 1,500 billion; in March 2001, for approximately Lire 550 billion, it was awarded a third license for the northern, northwest and central southern regions, thus becoming the leading mobile telephony operator in the country.

In February 2001, TIM announced the launch of “In Europe”, a global tariff offer for all customers covering an area of 30 countries through preferential roaming agreements with foreign and other local operators. “In Europe” is a one rate tariff program for calls originated from the partners’ networks (Euros 0.65) and non-partners’ network (Euros 0.90) and terminated inside the coverage area.

Also in February 2001, SEAT purchased 54.5% of the share capital of Consodata, a company listed on the Paris Nouveau Marchè and a leader in information marketing. The acquisition was completed through the issuance by SEAT of 63,789,104 of its ordinary shares in exchange for Consodata shares held by certain funds and management and the contribution by SEAT to Consodata of its business information activity. Based on SEAT’s share price on

February 9, 2001, the value of consideration paid was Euros 130 million which represents the value of the acquired shares and of the contribution in kind. SEAT is in the process of launching a public exchange offer (16 SEAT shares for each Consodata share) for the remainder of the Consodata share capital it does not currently own.

On February 15, 2001, Telecom Italia Group, in connection with the December 2000 memorandum agreement, purchased 100% of NetCreations Inc. for approximately US$ 109 million. NetCreations Inc. is a U.S. company listed on the United States NASDAQ, as well as a leader in e-mail marketing services.

In March 2001, the Company concluded an agreement for the sale of 30% of Mediterranean Nautilus S.A. to a company in the Fishman group, a leader in the media and telecommunications sectors in Israel. The agreement aims to develop the backbone in the Eastern Mediterranean.

On March 12, 2001 the share transfer (totaling 28.61%) was completed giving SIN control of Entel Chile. The group's original stake in Entel Chile was acquired by SIN in 1996. SIN acquired the additional stake from two existing shareholders for consideration of approximately US$ 905 million. Entel Chile is Chile's principal domestic and international long-distance operator and the leading supplier of private corporate networks and internet access. Entel Chile also has a significant presence in the Spanish speaking US market through a US subsidiary which offers long-distance and data transmission services between Latin America and the US.

Conversion of Public Concessions into Licenses

In accordance with the Italian Telecommunication Regulations and the Ministry of Communications Decree of November 25, 1997 concerning the issue of individual licenses and general authorizations in the telecommunications sector, and pursuant to an order of the National Regulatory Agency notified to Telecom Italia on January 19, 2001, the public operating concessions ("Public Concessions") under which Telecom Italia had been operating were converted into licenses ("Licenses"). The general effect of the new Licenses is to reduce certain public service obligations and regulatory constraints that were previously applicable to Telecom Italia.

TIM concessions are currently in the process of being converted into licenses.

Corporate transactions

On March 1, 2001, Telecom Italia's "Venture Capital" unit was transferred to CSELT, which then changed its name to Telecom Italia Lab.

Within the scope of the reorganization of the Information Technology business and its allocation to the "IT services" Business Unit, on March 1, 2001, Telesoft received, from Telecom Italia, the "Development" going concern which is devoted to developing information systems and creating applications software, with 619 employees and, from Finsiel, the "Telecommunications" business segment, with 234 employees.

Telecom Italia notes exchangeable for TIM or SEAT shares

On January 23, 2001, the Board of Directors of Telecom Italia approved the issue of exchangeable 5-year notes exchangeable for TIM or SEAT shares for an amount of Euros 2 billion and with a green shoe option of Euros 500 million. The deal was announced on January 29.

The notes were issued by Sogerim S.A., a wholly-owned indirect subsidiary of Telecom Italia, unconditionally guaranteed by Telecom Italia, on March 15, 2001 and the conversion into TIM or SEAT shares can begin as from June 1, 2001. The annual coupon is 1% and note holders are entitled to early redemption at the end of the third year of issue.

Note 26–Reconciliation to Generally Accepted Accounting Principles 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. The comments on the significant differences are 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 pre-1997 transactions, 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 is 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. The U.S. GAAP reconciliation treats this excess 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.

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 intangibles and fixed assets and related depreciation

Until 1993, the Group did not eliminate intercompany profit on sales of intangibles and fixed assets. Therefore, certain intangibles 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.

Deferred taxes

The differences between Italian GAAP and U.S. GAAP are related to the tax treatment for capital grants received by the Group prior to 1998.

Contributions to telephone workers social security fund

As discussed in Note 18 of the financial statements for the year ended December 31, 2000, 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, the minimum amount of the range of the liability is reflected in the U.S. GAAP reconciliation net of any payments made and expensed through the Italian GAAP income statement.

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. This is 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 market value within current assets. Write-downs below historical cost are reversed in subsequent periods up to the original cost, if the fair market value of the equity securities increases. Write-downs and any subsequent reversals are recorded in the income statement.

Under U.S. GAAP, the value of the investment in subsidiary stock has been adjusted to original cost and has been eliminated upon consolidation of the Group. The elimination of the investment results in additional goodwill, the reversal of any write-downs 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 (e) 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 Lire 13,159 billion was created under Italian GAAP. For purposes of U.S. GAAP the acquisition, including the shares exchanged, was accounted for at fair value. For U.S. GAAP purposes the distribution of the subsidiary's shares to SEAT generated a gain of Lire 12,657 billion representing the difference between the fair market 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 Lire 2,574 billion.

- 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 the U.S. GAAP purchase accounting requirements, the fair market value of the SEAT acquisition was Lire 31,028 billion. Included in this amount was acquisition goodwill relating to SEAT of Lire 26,787 billion. 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 reduction was considered a possible indication of impairment, thereby requiring an analysis of SEAT based upon SFAS 121, as discussed in the U.S. GAAP policy Note 28. Based on this review, an impairment charge of Lire 15,424 billion was recorded to U.S. GAAP net income to reduce the value of the SEAT investment.

- After the acquisition of SEAT by the Group, SEAT made additional acquisitions in the fourth quarter of 2000. 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 market 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 no gain recognition is allowed. See also Note 28 (m) for a further discussion of the real estate transaction.

Non-capitalizable expenses

The Group entered into several transactions in 2000 for which certain costs were capitalized under Italian GAAP. These costs include expenses related to the SMH 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.

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 Italian GAAP financial statements reflect reserves for Lire 775 billion taken to accrue the estimated costs to rework these systems. U.S. GAAP requires that certain conditions must be met before reserves can be established. 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.

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 common 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 equity movements. 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 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 occurred in the Italian GAAP financial statements.

Under U.S. GAAP, transactions between entities under common control require predecessor basis accounting. Therefore, the 2000 increase in equity and goodwill has been reversed.

Treasury stock

Telecom Italia has purchased and holds its own savings shares. Under Italian GAAP, these savings shares are recorded at historical cost within long-term investments. Under U.S. GAAP, the cost of the acquired shares is shown as a deduction from stockholders' equity.

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 owners and distributions to owners. Investments classified as 'available for sale securities' under U.S. GAAP have been recognized as a component of comprehensive income.

Other

Other is comprised of the following:

Stock options

During 1999 and 2000, Telecom Italia and TIM 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. For U.S. GAAP purposes the Group uses 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.

Investments in marketable equity securities

Telecom Italia Group holds marketable equity securities of unrelated companies 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 would be classified as trading and available for sale, respectively. The Group's "trading securities" are recorded at fair market value, with unrealized gains and losses included in earnings.

Available for sale securities would be carried at fair market value, with any unrealized holding gains or losses each balance sheet date being reflected in other comprehensive income on a net of tax basis. Declines in fair value that are other than temporary are reflected in the Consolidated Statement of Income.

Revenue Recognition

Under Italian GAAP, non-refundable activation and installation fees, and related costs, are generally charged and recognized at the outset of a service contract. Under U.S. GAAP, up front revenues related to non-refundable fees and certain related direct costs must be deferred and recognized over the expected customer relationship period, which is estimated to be 8 years.

Significant differences and the effect of the above on consolidated net income and stockholders' equity are set out below:

	Years ended December 31,			
	1998	1999	2000	2000
	(in billions of Lire)			(in millions of U.S. Dollars) (*)
NET INCOME				
Net income as reported in the consolidated statements of income	5,252	4,665	5,709	2,593
Minority interest	(1,422)	(1,301)	(1,782)	(809)
Net income, net of minority interest applicable for U.S. GAAP purposes	3,830	3,364	3,927	1,784
Items increasing (decreasing) reported net income:				
Goodwill deriving from STET-Old Telecom Italia merger	(375)	(375)	(375)	(170)
Purchase method accounting transactions	(113)	(113)	(81)	(37)
Revaluation of fixed assets	154	164	165	75
Elimination of intercompany profit on sales of intangibles and fixed assets and related depreciation	183	88	80	36
Capitalization of interest on tangible and intangible assets under construction and related depreciation	19	(121)	(57)	(26)
Deferred taxes	(782)	7	(33)	(15)
Contributions to telephone workers social security fund	183	75	(4)	(2)
Accounting for long-term contracts under the percentage of completion method	(28)	(56)	–	–
Investment in stock of subsidiary companies	–	–	150	68
SEAT – Tin.it transaction:				
SEAT acquisition	–	–	15,231	6,918
Effects of SEAT's 4th quarter results	–	–	(310)	(141)
SEAT impairment	–	–	(15,424)	(7,005)
Gain on subsidiary dilution	–	–	770	350
Sale of real estate portfolio	–	–	(609)	(277)
Non-capitalizable expenses	–	–	(183)	(83)
Reversal of provisions	–	–	788	358
Subsidiary stock conversions	–	–	4,283	1,945
Other	–	(130)	47	21
Net adjustments	(759)	(461)	4,438	2,015
U.S. GAAP income before reconciliation effects of income taxes, minority interest and cumulative effect of accounting change in revenue recognition	3,071	2,903	8,365	3,799
Income taxes:				
Tax effect of reconciling items	(203)	(58)	(1,245)	(565)
U.S. GAAP income before reconciliation effect of minority interest and cumulative effect of accounting change in revenue recognition	2,868	2,845	7,120	3,234
Minority interest on reconciling items	86	70	(147)	(67)
Net income in accordance with U.S. GAAP, before cumulative effect of accounting change in revenue recognition	2,954	2,915	6,973	3,167
Cumulative effect of accounting change in revenue recognition (net of tax)	–	–	(154)	(70)
Net income in accordance with U.S. GAAP	2,954	2,915	6,819	3,097

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

Earnings Per Ordinary Share Amounts in Accordance with U.S. GAAP (*)

	Years ended December 31,			
	1998	1999	2000	2000
		(Lire)		(U.S. Dollars) (**)
Basic EPS - per Ordinary Share amounts in accordance with U.S. GAAP before cumulative effect of accounting change in revenue recognition	392	387	937	0.43
Diluted EPS - per Ordinary Share amounts in accordance with U.S. GAAP before cumulative effect of accounting change in revenue recognition	392	387	934	0.42
Basic EPS - per Ordinary Share amounts in accordance with U.S. GAAP	392	387	916	0.42
Diluted EPS - per Ordinary Share amounts in accordance with U.S. GAAP	392	387	913	0.42

Earnings Per Savings Share amounts in accordance with U.S. GAAP (*)

	Years ended December 31,			
	1998	1999	2000	2000
		(Lire)		(U.S. Dollars) (**)
Basic EPS - per Savings Share amounts in accordance with U.S. GAAP before cumulative effect of accounting change in revenue recognition	412	407	957	0.44
Diluted EPS - per Savings Share amounts in accordance with U.S. GAAP before cumulative effect of accounting change in revenue recognition:	412	407	954	0.44
Basic EPS - per Savings Share amounts in accordance with U.S. GAAP	412	407	936	0.43
Diluted EPS – per Savings Share amounts in accordance with U.S. GAAP	412	407	933	0.42

(*) 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 Savings Share stockholders are entitled to a Lire 20 premium (based on 2 percent of Savings Share par value) over dividends on Ordinary Shares. This takes into account the par value of Lire 1,000 per share as of December 31, 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 Euros, the new par value per share is equal to Euro 0.55. For purposes of these calculations the weighted average number of Shares was 7,421,251,726 as of December 31, 1998, 7,421,660,518 as of December 31, 1999 and 7,398,247,829 as of December 31, 2000.

(**) Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

	As of December 31,		
	1999	2000	2000
	(Billions of Lire)		(Millions of U.S. Dollars) (*)
STOCKHOLDERS' EQUITY			
Stockholders' equity as reported in the consolidated balance sheets	38,314	49,431	22,450
Minority interest	(5,310)	(12,988)	(5,899)
Stockholders' equity, net of minority interest	33,004	36,443	16,551
Items increasing (decreasing) reported stockholders' equity:			
Goodwill deriving from STET-Old Telecom Italia merger	5,061	4,686	2,128
Purchase method accounting transactions	1,052	971	441
Revaluation of fixed assets	(1,354)	(1,236)	(561)
Elimination of intercompany profit on sales of intangibles and fixed assets and related depreciation	(528)	(447)	(203)
Capitalization of interest on tangible and intangible assets under construction and related depreciation	1,188	1,144	520
Deferred taxes	227	192	87
Contributions to telephone workers social security fund	(1,525)	(1,529)	(694)
Investment in stock of subsidiary companies	–	120	55
SEAT – Tin.it transaction:			
SEAT acquisition	–	10,945	4,972
Effects of SEAT's 4th quarter results	–	(310)	(141)
SEAT impairment	–	(15,424)	(7,005)
Purchase accounting for acquisitions by the SEAT group	–	9,713	4,411
Sale of real estate portfolio	–	(609)	(277)
Non-capitalizable expenses	–	(183)	(83)
Reversal of provisions	–	788	358
Cumulative effect of accounting change (net of tax) in revenue recognition	–	(154)	(70)
Common control transactions	–	(409)	(186)
Treasury stock	–	(1,281)	(582)
Other	—	142	64
Tax effect of reconciling items	850	(2,715)	(1,233)
Minority interest on reconciling items	90	(3,829)	(1,739)
Stockholders' equity in accordance with U.S. GAAP	38,065	37,018	16,813

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

Note 27–Condensed GAAP consolidated financial statements

The condensed consolidated financial statements as of December 31, 1999 and 2000 presented below have been restated to reflect the principal differences between the Group's accounting policies and U.S. GAAP discussed above.

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,		
	1999	2000	2000
	(Billions of Lire)		(Millions of U.S. Dollars) (*)
ASSETS			
Current assets	25,141	29,753	13,513
Fixed assets, net	44,825	44,192	20,071
Goodwill	8,088	34,991	15,892
Other intangible assets	3,324	11,642	5,287
Other long-term assets:			
Deferred tax assets	906	-	-
Other	13,102	17,919	8,138
Total assets	95,386	138,497	62,901

	As of December 31,		
	1999	2000	2000
	(Billions of Lire)		(Millions of U.S. Dollars) (*)
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities	33,784	50,743	23,046
Long-term debt	10,002	24,138	10,963
Reserves and other liabilities:			
Deferred tax liabilities	-	2,122	963
Other liabilities	5,419	7,280	3,307
Employee termination indemnities	2,896	2,554	1,160
Total liabilities	52,101	86,837	39,439
Minority interest	5,220	14,642	6,649
Stockholders' equity	38,065	37,018	16,813
Total liabilities and stockholders' equity	95,386	138,497	62,901

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

	Years ended December 31,			
	1998	1999	2000	2000
	(in billions of lire)			(in millions of U.S. Dollars) (*)
STATEMENTS OF INCOME				
Operating revenues (**)	48,507	52,481	53,316	24,215
Other income	1,085	998	780	354
Total revenues	49,592	53,479	54,096	24,569
Operating expenses (**)	(40,566)	(41,566)	(42,402)	(19,258)
SEAT impairment	--	–	(15,424)	(7,005)
Operating income/(loss) (**)	9,026	11,913	(3,730)	(1,694)
Interest income and expenses and other income and expenses, net (**)	(469)	(2,670)	(2,888)	(1,312)
Gains on merger, demerger, subsidiary dilution and share conversions	–	–	20,284	9,213
Income before income taxes	8,557	9,243	13,666	6,207
Tax expense	(4,267)	(5,097)	(4,887)	(2,220)
Income before minority interest and cumulative effect of accounting change in revenue recognition	4,290	4,146	8,779	3,987
Minority interest	(1,336)	(1,231)	(1,806)	(820)
Income before cumulative effect of accounting change in revenue recognition	2,954	2,915	6,973	3,167
Cumulative effect of accounting change in revenue recognition (net of tax)	–	–	(154)	(70)
Net income, after minority interest	2,954	2,915	6,819	3,097

(*) Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(**) Beginning in 1999 Telecom Italia has changed the way in which it accounts for operating revenues, calculating such revenues gross of interconnection and service charges payable to other operators and service providers of telecommunication services and accounting for such interconnection and service charges as an operating expense. In prior fiscal years, they were accounted for net of interconnection and service charges. Due to this change, operating revenues and operating expenses have increased by the same amount: Lire 3,042 billion in 1998. This accounting change has had no impact on reported net income for 1998. In 1998, the item “total operating expenses” also takes into account additional expenses (Lire 19 billion) included in “other income and expense, net” in the consolidated financial statements in Telecom Italia’s 1998 Annual Report on Form 20-F.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY

	Share Capital	Additional Paid In Capital	Reserves, Retained Earnings and Profit of the Year	Total
		(in billions of Lire)		
Balance as of December 31, 1997	7,421	3,431	25,103	35,955
Dividends paid (Lire 190 per Ordinary Share and Lire 210 per Savings Share)	–	–	(1,453)	(1,453)
Translation adjustments on foreign currency financial statements	–	–	(527)	(527)
Equity investments and other minor adjustments	–	–	140	140
Net income for the year	–	–	2,954	2,954
Balance as of December 31, 1998	7,421	3,431	26,217	37,069
Dividends paid (Lire 280 per Ordinary Share and Lire 300 per Savings Share)	–	–	(2,121)	(2,121)
Stock option plans	5	120	36	161
Translation adjustments on foreign currency financial statements	–	–	114	114
Equity investments and other minor adjustments	–	–	(73)	(73)
Net income for the year	–	–	2,915	2,915
Balance as of December 31, 1999	7,426	3,551	27,088	38,065
Dividends paid (Lire 603 per Ordinary Share and Lire 623 per Savings Share)	–	–	(4,505)	(4,505)
Dividend on demerger of Tin.it	–	–	(2,574)	(2,574)
Stock option plans	–	86	-	86
Treasury stock	–	–	(1,281)	(1,281)
Marketable securities	–	–	(10)	(10)
Translation adjustments on foreign currency financial statements	–	–	65	65
Equity investments and other minor adjustments	–	–	353	353
Net income for the year	–	–	6,819	6,819
Balance as of December 31, 2000	7,426	3,637	25,955	37,018
Balance as of December 31, 2000 (in millions of U.S. Dollars) (*)	3,373	1,652	11,788	16,813

(*) Exchange rate: Lire 2,201.80 = U.S. $1.00 as of March 30, 2001.

Other Comprehensive Income:

	1998	1999	2000	2000
		(in billions of Lire)		(in millions of U.S. Dollars) (*)
Net income for the year under U.S. GAAP	2,954	2,915	6,819	3,097
Translation adjustment on foreign currency financial statements during the year	(527)	114	65	30
Unrealized gains/(losses) on available for sale securities during the year	–	–	(10)	(5)
Total comprehensive income under U.S. GAAP	2,427	3,029	6,874	3,122

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

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 U.S. GAAP purposes, Telecom Italia follows the provisions of SFAS No. 109. Under SFAS No. 109, Telecom Italia recognizes deferred tax assets and liabilities for the expected future tax consequences of events that have been included in the financial statements or tax returns. Prior to 1998, in accordance with Italian GAAP, Telecom Italia provided deferred taxes only for certain temporary differences. Beginning in 1998, Italian GAAP is substantially consistent with U.S. GAAP.

Deferred tax assets and liabilities are determined based on the temporary differences between the financial and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse.

Deferred tax amounts also arise as a result of the other Italian GAAP to U.S. GAAP adjustments. A valuation allowance is established when it is more likely than not that some portion or all of the deferred tax assets will not be realized.

A detail of the provision for income taxes for 1998, 1999 and 2000 is as follows:

	1998	1999	2000	2000
		(Billions of Lire)		(Millions of U.S. Dollars) (*)
Current	4,610	5,585	4,627	2,102
Deferred	(343)	(488)	260	118
Total provision for income taxes	4,267	5,097	4,887	2,220

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

The actual provision for income taxes is different from income taxes computed by applying the Italian Statutory Tax rate (41.25% in 1998, 1999 and 2000), primarily as a result of non-deductible and non-taxable items (goodwill, certain non-recurring gains and other expenses).

The components of the net deferred tax assets (liabilities) as of December 31, 1999 and 2000 are as follows:

	1999	2000	2000
	(Billions of Lire)		(Millions of U.S. Dollars) (*)
Deferred tax assets:			
Intercompany profits on intangible and fixed assets	527	569	259
Accrued pension obligation	564	560	254
Revaluation of fixed assets	558	472	214
Asset impairments	–	5,707	2,592
Other	1,991	1,723	783
Subtotal	3,640	9,031	4,102
Less- valuation allowance	(266)	-	-
	3,374	9,031	4,102
Deferred tax liabilities:			
Accelerated tax depreciation	(950)	(287)	(131)
Capitalization of interest on fixed and intangible assets	(490)	(414)	(188)
Deferred gains on assets	–	(4,683)	(2,127)
Share conversions	–	(1,584)	(719)
Purchase accounting for acquisitions by the SEAT group	–	(2,376)	(1,079)
Other	(208)	(554)	(252)
Subtotal	(1,648)	(9,898)	(4,496)
Net deferred tax asset/(liability)	1,726	(867)	(394)

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(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 instruments held. The Group has not estimated the value of 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.

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 fair values and carrying amounts of financial instruments are as follows:

	As of December 31,					
	1999		2000		2000	
	Carrying amount	Estimated fair value	Carrying amount	Estimated Fair value	Carrying amount	Estimated fair value
	(Billions of Lire)				(Millions of U.S. Dollars) (*)	
Cash & cash equivalents	1,312	1,312	2,526	2,526	1,147	1,147
Marketable securities	2,583	2,645	4,754	4,825	2,159	2,191
Long- term investments:						
Affiliates:						
Practicable to determine	466	580	4,256	2,789	1,933	1,267
Not practicable	11,860	–	10,456	–	4,749	–
Other:						
Practicable to determine	5	5	12	12	5	5
Short term debt (excluding current portion of long-term debt)	7,110	7,110	26,165	26,165	11,884	11,884
Long-term debt (current portion included):						
Floating rates	5,259	5,259	10,598	10,598	4,813	4,813
Fixed rates:						
Subsidized	432	747	73	126	33	57
Not subsidized	6,823	7,034	8,481	8,653	3,852	3,931
	12,514	13,040	19,152	19,377	8,698	8,801

(*)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(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 income. 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 income statement.

The fair value of all portfolios is determined by quoted market prices.

December 31, 2000	Amortized cost (Lire billions)	Unrealized gains (Lire billions)	Unrealized losses (Lire billions)	Fair value (Lire billions)
Trading securities	4,990	71	(244)	4,817
Available for sale	23	–	(15)	8
Total marketable securities	5,013	71	(259)	4,825

December 31, 1999	Amortized cost (Lire billions)	Unrealized gains (Lire billions)	Unrealized losses (Lire billions)	Fair value (Lire billions)
Trading securities	2,583	62	–	2,645

December 31, 1999	Amortized cost (Lire billions)	Unrealized gains (Lire billions)	Unrealized losses (Lire billions)	Fair value (Lire billions)
Available for sale	–	–	–	–
Total marketable securities	2,583	62	–	2,645

(e) Acquisition of SEAT

On February 10, 2000, Telecom Italia announced that it had reached an agreement (the "Acquisition") to acquire a controlling interest in the Italian yellow page publisher, SEAT. In addition to its publishing business, SEAT also has Internet and television properties. The 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 Lire 11,819 billion in August 2000 and Lire 12 billion 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 Acquisition was accounted for as a dividend. On November 20, 2000, Telecom Italia paid Lire 500 billion to acquire a further 53 million ordinary shares.

For purposes of Italian GAAP, the cash consideration paid for SEAT's shares was treated as 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 Acquisition. For Italian GAAP purposes, the 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 on November 15, 2000 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 Acquisition was accounted for as a purchase as of that date.

As part of the acquisition of SEAT, a put option was granted to 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 Lire 5,780 billion 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 preliminary purchase price allocation to the fair value of the assets acquired and liabilities assumed. Differences between the amounts below and the final allocations are not expected to be material.

	Lire (billions)	
Cash purchase price	12,331	
Fair value of merger transaction and put/call financing of minority interest acquisition	18,602	
Transaction costs	95	
Total consideration (A)		31,028
Net assets acquired	7,046	
Minority interest	(2,805)	
(B)		4,241
Goodwill from acquisition (A-B)		26,787

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 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 Lire 15,424 billion reduction to the acquisition goodwill.

The remaining goodwill is being amortized on a straight-line basis over 12 years.

The following table reflects the results of operations on a pro forma basis as if the Acquisition had occurred as of January 1, 1999. The 2000 pro forma results of operations do not include the Lire 15,231 billion in non-recurring gains from the distribution of Tin.it's shares and a charge of Lire 154 billion (net of tax) relating to the cumulative effect of the accounting change in revenue recognition. The following unaudited pro forma information also excludes the effects of synergies and any other cost saving initiatives related to the Acquisition.

Unaudited	**1999**	**2000**	**2000**
	Billions of Lire (except per share amounts)		**Millions of U.S. Dollars (except per share amounts) (*)**
Revenues	54,936	55,359	25,143
Net income	26	(5,838)	(2,651)
Earnings per Share:			
Basic EPS – per ordinary share	(2)	(795)	(0.36)
Basic EPS – per savings share	18	(775)	(0.35)
Diluted EPS – per ordinary share	(2)	(795)	(0.36)
Diluted EPS – per savings share	18	(775)	(0.35)

(*) Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(f) Segment information

The Group operates predominantly in Italy and its core business is focused on domestic and international telecommunications services. Starting from 1999 domestic telecommunications services are segmented as follows: fixed line services managed by the parent company, Telecom Italia, mobile services conducted by TIM and satellite services provided by Telespazio.

With respect to international telecommunications activities, the Group's main operating units are located in Europe, as a natural extension of the Italian market, and in Latin America where it is already well established in the principal countries. Some of them are held directly by Telecom Italia, while others are held by the subsidiaries TMI – Tele Media International Italia, Stet International Netherlands and Stet Mobile Holding (which at December 31, 2000 is a wholly owned subsidiary of TIM). As of December 31, 2000, investments in affiliated companies are located approximately 69% in Europe, approximately 30% in Latin America and the remainder in the rest of the world.

The other Group activities are as follows: IT software and services managed by Finsiel, Telesoft, Netsiel and Sodalia; manufacturing by Italtel; and installation by Sirti. The Group holds 19.9% of Italtel at December 31, 2000 following the sale of 80.1% to a pool of foreign investors in the last quarter of 2000. The Group no longer has installation activities following the sale of Sirti S.p.A. in the last quarter of 2000.

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, 2000, 1999 and 1998 are as follows (in billions of Lire):

	Fixed line service Italy	Mobile service Italy	Satellite service	International telecommunications services	IT software and services	Manufacturing	Installation	Other activities (*)	Elimination and consolidated adjustments	Consolidated
1998										
Revenues										
-Third parties	31,080	11,094	534	1,273	1,916	1,041	1,221	349	-	48,507
-Intersegment (**)	5,212	810	205	247	650	934	944	670	(9,673)	0
	36,292	11,904	739	1,520	2,566	1,975	2,165	1,019	(9,673)	48,507
Operating income	5,042	4,117	58	(148)	219	55	243	(220)	(180)	9,186
Depreciation and amortization	8,404	1,302	55	286	138	88	42	373	(208)	10,480
Investments in fixed assets	6,756	1,742	82	522	83	106	31	469	(368)	9,423
Identifiable assets	73,040	10,540	1,168	15,291	2,883	4,253	3,098	5,360	(28,753)	86,880
1999										
Revenues										
-Third parties	30,953	13,722	443	3,069	2,127	959	837	371	-	52,481
-Intersegment (**)	4,903	703	176	184	947	817	664	783	(9,177)	0
	35,856	14,425	619	3,253	3,074	1,776	1,501	1,154	(9,177)	52,481
Operating income	7,096	5,126	(19)	(204)	237	(5)	76	147	2	12,456
Depreciation and amortization	7,766	1,505	59	664	138	89	45	352	(280)	10,338
Investments in fixed assets	4,574	1,582	56	955	73	66	58	409	(270)	7,503
Identifiable assets	74,843	17,440	1,613	18,905	3,313	2,334	2,178	6,060	(37,505)	89,181
2000										
Revenues										
-Third parties	29,419	14,701	509	7,435	2,164	385	772	594	-	55,979
-Intersegment (**)	4,304	651	150	180	973	836	393	713	(8,200)	0
	33,723	15,352	659	7,615	3,137	1,221	1,165	1,307	(8,200)	55,979
Operating income	6,961	5,542	(100)	579	251	(26)	20	60	(108)	13,179
Depreciation and amortization	7,201	1,711	64	1,737	142	51	29	122	(124)	10,933
Investments in fixed assets	3,675	1,667	56	1,968	231	34	27	284	(412)	7,530
Identifiable assets	92,803	33,542	1,840	36,090	3,795	0	0	15,971	(57,187)	126,854
2000					**(in millions of U.S. Dollars) (***)**					
Revenues										
-Third parties	13,361	6,677	231	3,377	983	175	350	270	-	25,424
-Intersegment (**)	1,955	296	68	82	442	379	178	324	(3,724)	0
	15,316	6,973	299	3,459	1,425	554	528	594	(3,724)	25,424
Operating income	3,162	2,517	(45)	263	114	(12)	9	27	(49)	5,986
Depreciation and amortization	3,271	777	29	789	64	23	13	55	(56)	4,965
Investments in fixed assets	1,669	757	25	894	105	16	12	129	(187)	3,420
Identifiable assets	42,149	15,234	836	16,391	1,723	0	0	7,254	(25,973)	57,614

(*) Other activities include only ancillary services.

(**) Intersegment sales consist of sales made between consolidated subsidiaries of the Group belonging to different sectors. Such sales between sectors are accounted for at selling prices which generally approximate prices to unaffiliated customers.

(***)Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001

(g) 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." During 2000, Telecom Italia and TIM offered stock-based compensation arrangements to managers of the respective organizations.

The status of the stock options granted under the Stock Option Plan of 1999 is as follows:

	Number of Shares	Average grant price (Lire)
Outstanding at January 1, 2000	11,689,900	13,150
Granted	-	-
Exercised	-	-
Forfeited	(278,400)	13,150
Outstanding at December 31, 2000	11,411,500	13,150

The average fair value of shares granted during 1999 was Lire 7,871. The fair value of each option grant is estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions used for estimating fair value:

Dividend Yield	0.49%
Risk-free interest rate	6.05%
Expected Life	3 years
Expected volatility	43.76%

The following table summarizes certain information for the stock options granted under the Stock Option Plan of 1999, which are outstanding at December 31, 2000:

	Options Outstanding			Options Exercisable	
Range of Grant Prices (Lire)	Shares	Weighted Average Remaining Life	Weighted Average Grant Price (Lire)	Shares	Weighted Average Grant Price (Lire)
13,150	11,411,500	1year	13,150	5,754,900	13,150

The status of the stock options granted under the Stock Option Plan of 2000 is as follows:

	Number of Shares	Average grant price (Lire)
Outstanding at January 1, 2000	-	-
Granted	51,430,000	26,750
Exercised	-	-
Forfeited	-	-
Outstanding at December 31, 2000	51,430,000	26,750

The average fair value of shares granted during 2000 was Lire 6,293. The fair value of each option grant is estimated using the Black-Scholes option-pricing model with the following weighted-average assumptions used for estimating fair value:

— Dividend Yield	1.5%
— Risk-free interest rate	5.4%
— Expected Life	2.9 years

— Expected volatility 40.8%

The following table summarizes certain information for the stock options granted under the Stock Option Plan of 2000, which are outstanding at December 31, 2000:

	Options Outstanding			Options Exercisable	
Range of Grant Prices	**Shares**	**Weighted Average Remaining Life**	**Weighted Average Grant Price**	**Shares**	**Weighted Average Grant Price**
(Lire)			**(Lire)**		**(Lire)**
26,750	51,430,000	2.9 year	26,750	--	--

The Group's pro forma earnings per share, had compensation costs been recorded in accordance with SFAS No. 123, are presented below, for both the 1999 and 2000 Plans:

	1999	**2000**
	(Millions of Lire, except per share amounts)	
Net income available to each class of shares	2,911,875	6,744,504
Basic EPS – per Ordinary Share	387	906
Basic EPS – per Savings Share	407	926
Diluted EPS – per Ordinary Share	386	903
Diluted EPS – per Savings Share	406	923

The effects of applying SFAS No. 123 in this pro forma disclosure should not be interpreted as being indicative of future effects.

(h) 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 Income.

(i) Earnings per Share

In accordance with SFAS No. 128, "Earnings per Share", Basic earnings per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding. The computation of diluted earnings per share is increased to include any potential common shares. Potential common shares include options, warrants and convertible securities.

The computations of basic and diluted earnings per share for the years ended December 31, 1998, 1999 and 2000, prepared in accordance with U.S. GAAP, are as follows:

	1998	1999	2000	2000
	(Millions of Lire, except per share amounts)			(Millions of US$, except per share amounts)(*)
Basic EPS(**)				
Net Income	2,954,313	2,915,100	6,819,400	3,097
Less: Lire 20 premium payable to savings shares	(43,322)	(43,322)	(42,764)	(19)
	2,910,991	2,871,778	6,776,636	3,078
Weighted average number of shares (millions)	7,421	7,422	7,398	7,398
Basic EPS – ordinary shares	392	387	916	0.42
Add: Lire 20 premium payable to savings shares (***)	20	20	20	0.01
Basic EPS – savings shares	412	407	936	0.43
Diluted EPS(**)				
Weighted average number of shares (millions)	7,421	7,422	7,398	7,398
Dilutive effect of stock options (millions)	0	6	21	21
Diluted weighted average number of shares (millions)	7,421	7,428	7,419	7,419
Diluted EPS – ordinary shares	392	387	913	0.42
Add: Lire 20 premium payable to savings shares (***)	20	20	20	—
Diluted EPS – savings shares	412	407	933	0.42

(*) Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(**) 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, 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 Euros, the new par value per share is equal to Euro 0.55.

(j) Effects of Regulation

As discussed in Note 2, Telecom Italia is subject to the regulatory control of the National Regulatory Agency 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.

(k) 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

	1998	1999	2000	2000
	(Billions of Lire)			(Millions of U.S. Dollars) (*)
Changes in Operating Assets and Liabilities				
Marketable securities	(156)	(17)	(2,171)	(986)
Receivables	(1,003)	(751)	(460)	(209)
Inventories	255	(136)	590	268
Other current assets	(717)	(697)	(4,260)	(1,934)
Payables, trade and other	574	1,148	(909)	(413)
Accrued payrolls and employee benefits	(41)	(55)	569	258
Accrued income taxes	921	(197)	(612)	(278)
Other accrued liabilities	(67)	106	(59)	(27)
	(234)	(599)	(7,312)	(3,321)
Cash Paid During the Year For:				
Interest	1,304	1,071	1,530	695
Income taxes	3,076	5,356	4,402	1,999

(*) Exchange rate: Lire 2,201.80 = U.S. $ 1.00 as of March 30, 2001.

(l) 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. 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 a discounted cash flow analysis is performed, with the difference between the carrying value and discounted cash flow analysis being charged to operations. See also the discussion under Note 28 (e) regarding the discussion related to the acquisition and impairment of SEAT.

(m) Sale of Real Estate

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 Lire 5,615 billion. The assets' net book value on the date of transfer was Lire 4,632 billion. Subsequently, the Group sold 60% of their interest in IM.SER to third parties for cash in the amount of Lire 3,369 billion. Telecom Italia subsequently leased back 90% of the buildings contributed to IM.SER. Telecom Italia received cash in the amount of Lire 5,228 billion, which was generated both from the sale of their 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 gain for the amount of Lire 604 billion (gross) 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 treated as a secured borrowing. This requires that the buildings continue to be 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, 2000 under U.S. GAAP reflects an increase in long-term debt of Lire 5,212 billion, an increase in buildings of Lire 4,611 billion (net of the depreciation from the date of transfer) and a reduction in investments for Lire 406 billion.

(n) Lease Commitments

The following is a summary of all future minimum lease payments as of December 31, 2000:

(Lire billions)

	Finance Leases
2001	141
2002	127
2003	97
2004	97
2005	92
Thereafter	628
Present value of future minimum lease payments	1,182
Less current portion	(141)
Long term portion	1,041

(o) New Accounting Standards

In 1998, the Financial Accounting Standard Board issued SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS No. 133 establishes accounting and reporting standards requiring that every derivative instrument (including certain derivative instruments embedded in other contracts) be recorded in the balance sheet as either an asset or liability measured at its fair value. SFAS No. 133 requires that changes in the derivative's fair value be recognized currently in earnings unless specific hedge accounting criteria are met. Special accounting for qualifying hedges allows a derivative's gains and losses to offset related results on the hedged item in the income statement, and requires that a Company must formally document, designate and assess the effectiveness of transactions that receive hedge accounting. On June 19, 2000, SFAS 133 was amended by SFAS 138, "Accounting for Certain Derivative Instruments". SFAS 133 and SFAS 138 are effective for fiscal years beginning after January 1, 2001. The Group has determined the effect of implementing this standard on the income statement to be a net gain of approximately Lire 28 billion as of January 1, 2001.

In December 1999, the SEC issued Staff Accounting Bulletin No. 101 (SAB 101) which provides guidance on revenue recognition. SAB 101 is effective for fiscal years beginning after December 15, 1999. During 2000 and prior years, consistent with industry practice and Italian GAAP, the Group recognized telecommunications service activation fees and certain related costs at the time of service initiation. Based on guidance in SAB 101, the Group changed its accounting policies, effectively deferring the recognition of revenue and certain related costs associated with new service activation over the expected life of the customer relationship. Costs are deferred only to the extent that revenue is deferred. SAB 101 was accounted for as a change in accounting principle effective January 1, 2000, and therefore the Group has not restated prior year financial statements. As of January 1, 2000, the cumulative effect of this change in accounting principles amounted to a decrease in net income of Lire 154 billion (net of income taxes of Lire 100 billion), or Lire 29 per ordinary share and Lire 72 per savings share on both a basic and a fully diluted basis. These revenues and costs are to be recognized over a period of approximately 8 years.

As a result of this change in policy, the Company recognized an increase in net income of Lire 44 billion (net of taxes of Lire 31 billion) during 2000. The increase (gross of taxes) of Lire 75 billion is comprised of the recognition of Lire 43 billion in additional revenues and deferral of Lire 32 billion in direct expenses, pertaining to amounts included in the cumulative effect adjustment for SAB 101 as of January 1, 2000.

At December 31, 2000, the deferral process associated with the adoption of SAB 101 had the effect of increasing other non-current assets by Lire 1,231 billion, whilst increasing other non-current liabilities by Lire 1,405 billion.

The amount of installation fees deferred via the cumulative effect of this change being "recycled" through operating revenues during the year ended December 31, 2000, is Lire 373 billion (gross of taxes), while the amount of related direct costs being recycled through operating expenses for the year ended December 31, 2000, is Lire 298 billion (gross of taxes).

Pro forma net income and net income per ordinary and savings shares assuming the new method of revenue recognition were applied retroactively are as follows for 1999 and 1998:

Year ended December 31	**1999**	**1998**
In accordance with U.S. GAAP		
Net income (Lire billions)	2,969	2,989
Basic earnings per ordinary share	394	397
Basic earnings per savings share	414	417
Diluted earnings per ordinary share	394	397
Diluted earnings per savings share	414	417

In September 2000 the FASB issued SFAS No. 140 "Accounting for Transfers and Servicing of Financial Assets and Extinguishments of Liabilities." This statement provides accounting and reporting standards for transfers and servicing of financial assets and extinguishments of liabilities and also provides consistent standards for distinguishing transfers of financial assets that are sales from transfers that are secured borrowings. SFAS No. 140 is effective for recognition and reclassification of collateral and for disclosures relating to securitization transactions and collateral for fiscal years ending after December 15, 2000, and is effective for transfers and servicing of financial assets and extinguishments of liabilities occurring after March 31, 2001. Telecom Italia believes that the adoption of this standard will not have a material effect on the Company's consolidated results of operations or financial position.

(p) 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.

The following related party transactions are reflected in the statement of income for the year ended December 31, 2000:

Operating revenues: comprise mainly revenues from SEAT (Lire 409 billion in 2000 and Lire 308 billion in 1999), Teleleasing (Lire 219 billion in 2000), Stream (Lire 198 billion in 2000 and Lire 153 billion in 1999), Nortel Inversora group (Lire 157 billion in 2000 and Lire 177 billion in 1999), Lottomatica (Lire 112 billion in 2000 and Lire 85 billion in 1999) and Auna group (Lire 110 billion in 2000). In the aggregate, operating revenues were Lire 1,620 billion in 2000 (Lire 1,078 billion in 1999).

Cost of materials and other external charges: refers mainly to expenses regarding Siemens Informatica (Lire 155 billion in 2000 and Lire 73 billion in 1999), SEAT (Lire 119 billion in 2000 and Lire 176 billion in 1999), Teleleasing (Lire 114 billion in 2000), Entel Chile Group (Lire 77 billion in 2000), Etec S.A. (Lire 46 billion in 2000) and IM.SER (Lire 44 billion in 2000). In the aggregate, cost of materials and other external charges accounted for Lire 730 billion in 2000 (Lire 469 billion 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 Lire 37 billion in 2000 (Lire 50 billion in 1999).

Interest income, net: comprises dividends received from the Eutelsat satellite consortium (Lire 123 billion in 2000) and interest earned on loans made to some foreign unconsolidated subsidiaries and affiliated companies and interest expense payable to Teleleasing (Lire 60 billion in 2000) for financial leasing transactions. In the aggregate, interest income, net was Lire 105 billion in 2000 (Lire 37 billion in 1999).

The following related party transactions are reflected on the balance sheet as of December 31, 2000:

Loans in long-term investments: refers to loans granted to Bouygues Décaux Télécom (BDT) (Lire 198 billion at December 31, 2000) and other foreign unconsolidated subsidiaries and affiliated companies. In the aggregate such loans were Lire 268 billion at December 31, 2000 (Lire 293 billion at December 31, 1999).

Trade accounts receivables: comprises mainly trade accounts receivable from Telekom Srbija (Lire 127 billion at December 31, 2000 and Lire 48 billion at December 31, 1999), Auna group (Lire 92 billion at December 31, 2000), Golden Lines International (Lire 49 billion at December 31, 2000 and Lire 35 billion at December 31, 1999), Stream (Lire 45 billion at December 31, 2000 and Lire 215 billion at December 31, 1999), Nortel Inversora group (Lire 43 billion at December 31, 2000 and Lire 58 billion at December 31, 1999), Consortium CSIA (Lire 26 billion at December 31, 2000) and Etec S.A. (Lire 25 billion at December 31, 2000). In the aggregate trade accounts receivables were Lire 540 billion at December 31, 2000 (Lire 800 billion at December 31, 1999).

Trade accounts payable: pertains to supplier relationships connected with investments and transactions. In particular, they comprise trade accounts payable to Italtel group (Lire 536 billion at December 31, 2000), Entel Chile group (Lire 79 billion at December 31, 2000), Siemens Informatica (Lire 74 billion at December 31, 2000 and Lire 117 billion at December 31, 1999), Telekom Srbija (Lire 44 billion at December 31, 2000), Teleleasing (Lire 43 billion at December 31, 2000), Golden Lines International (Lire 32 billion at December 31, 2000), Auna group (Lire 25 billion at December 31, 2000), Etec S.A. (Lire 22 billion at December 31, 2000) and Telekom Austria group (Lire 20 billion at December 31, 2000). In the aggregate trade accounts payable were Lire 1,386 billion at December 31, 2000 (Lire 613 billion at December 31, 1999).

Long-term debt: refers to account payables to Teleleasing for financial leasing contracts. Such long-term debt was Lire 1,073 billion in the aggregate at December 31, 2000.

Short-term debt: includes payables to IM.SER (Lire 156 billion at December 31, 2000), Webegg (Lire 57 billion at December 31, 2000) and Italtel group (Lire 38 billion at December 31, 2000). In the aggregate short-term debt was Lire 266 billion at December 31, 2000.

Short-term financial receivables: refers mainly to receivables from the affiliates of SEAT (Lire 116 billion at December 31, 2000), Stream (Lire 106 billion at December 31, 2000 and Lire 56 billion at December 31, 1999) and Telekom Srbija (Lire 41 billion at December 31, 2000 and Lire 37 billion at December 31, 1999). In the aggregate short-term financial receivables were Lire 339 billion at December 31, 2000 (Lire 221 billion at December 31, 1999).

Other current assets: refers mainly to prepaid expenses for lease payments to IM.SER (Lire 89 billion at December 31, 2000). In the aggregate other current assets accounted for Lire 95 billion at December 31, 2000.

Other current liabilities: comprise mainly payables to Astrolink (Lire 183 billion at December 31, 2000 and Lire 322 billion at December 31, 1999) for capital contributions payable. In the aggregate other current liabilities accounted for Lire 229 billion at December 31, 2000 (Lire 694 billion at December 31, 1999).

Long and short-term contracts: refers to contract work in process by Telespazio for Astrolink. In the aggregate such work in process accounted for Lire 138 billion at December 31, 2000.

Capital expenditures: consist mainly of acquisitions from Italtel (Lire 357 billion in 2000 and Lire 754 billion in 1999) and Siemens Informatica (Lire 61 billion in 2000 and Lire 153 billion in 1999). In the aggregate investments in fixed and intangible assets accounted for Lire 453 billion in 2000 (Lire 1,238 billion in 1999).

SEAT

In connection with the 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, 2000 holds approximately 55 per cent of Telecom Italia. A dividend of approximately Lire 1,719 billion was paid to Tecnost (now merged into Olivetti) in 2000 (approximately Lire 767 billion in 1999).

Directors and Executive Officers

Based on a contract signed on March 15, 2000 by Telecom Italia, Huit II, Huit and its shareholders, and Lorenzo Pellicioli (the CEO of SEAT), regarding the integration of Tin.it into SEAT, and furthermore, by virtue of previous agreements, Lorenzo Pellicioli 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 Lire 37 billion to the total benefit received by Lorenzo Pellicioli.

A director of the Group is a partner in a law firm (Studio Bonelli Erede Pappalardo) that provides legal services to the Group on a recurring basis. The Group paid legal fees to this law firm totaling Lire 10,300 million in 2000 (Lire 1,725 million in 1999).

ARTHURANDERSEN

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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

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ARTHUR ANDERSEN

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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. (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 each of the two 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 16% of total assets as of December 31, 1999, and operating revenues representing approximately 12% and 13% of consolidated operating revenues for each of the two years in the period ended December 31, 1999, respectively. 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 each of the two years 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 each of the two years 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

Sede Legale
Via della Moscova 3 20121 Milano

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Partita IVA 03689140153
Capitale Sociale Lire 3.000.000.000 i.v.

Bari Bologna Brescia Firenze
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PRICEWATERHOUSECOOPERS

PricewaterhouseCoopers SpA

REPORT OF INDEPENDENT AUDITORS

To the Shareholders of
ITALTEL S.p.A.

We have audited the consolidated balance sheets of *ITALTEL S.p.A. 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 millions of 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 nil and 4.6% of total assets as of December 31, 1999 and 1998, and operating revenues representing approximately nil, 6.5% and 13%, 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 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 *ITALTEL S.p.A. and Subsidiaries* as of December 31, 1999 and 1998, and the results of its operations and changes in its financial position for each of the three years in the period ended December 31, 1999 in conformity with generally accepted accounting principles in Italy.

Sede legale: Milano 20124 Via Vittor Pisani 20 Tel. 0267831 Fax 0266981433 Cap. Soc. 7.220.000.000 i.v. Reg. Imp. Milano N. 278929/1999 C.F. e P. IVA 12979880155 Iscritta all'Albo Consob – Altri uffici: **Ancona** 60123 Via Corridoni 2 Tel. 07136881 – **Bari** 70125 Viale della Repubblica 110 Tel. 0805429863 – **Bologna** 40122 Via delle Lame 111 Tel. 051526611 – **Brescia** 25124 Via Cefalonia 70 Tel. 0302219811 – **Firenze** 50129 Viale Milton 65 Tel. 0554627100 – **Genova** 16121 Piazza Dante 7 Tel. 0105702013 – **Milano** 20122 Corso Europa 2 Tel. 0277851 – **Napoli** 80121 Piazza dei Martiri 30 Tel. 0817644441 – **Padova** 35137 Largo Europa 16 Tel. 0498762677 – **Palermo** 90141 Via Marchese Ugo 60 Tel. 091349737 – **Parma** 43100 V.le Tanara 20/A Tel. 0521242848 – **Roma** 00154 Largo Fochetti 29 Tel. 06570251 – **Torino** 10129 Corso Montevecchio 37 Tel. 011556771 – **Trento** 38100 Via San Francesco 8 Tel. 0461237004 – **Treviso** 31100 Piazza Crispi 8 Tel. 0422542726 – **Udine** 33100 Via Marinoni 12 Tel. 043225789 – **Verona** 37121 Via Malenza 2 Tel. 0458002561

PRICEWATERHOUSECOOPERS

Milan, April 10, 2000

PricewaterhouseCoopers SpA

Enrico Picasso
(Partner)

Deloitte & Touche

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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

Deloitte & Touche S.p.A.
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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.

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