ANNEX I

PLAN FOR THE MERGER BY INCORPORATION OF TELECOM ITALIA MOBILE S.P.A. INTO TELECOM ITALIA S.P.A.

(under Article 2501-*ter* of the Italian Civil Code)

THIS IS AN ENGLISH TRANSLATION OF THE ORIGINAL ITALIAN DOCUMENT

January 23, 2005

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

The merger described herein relates to the securities of two foreign (non-U.S.) companies. The merger in which TIM ordinary shares and savings shares will be converted into Telecom Italia shares is subject to disclosure requirements of a foreign country that are different from those of the United States. Financial statements included in the document, if any, will be prepared in accordance with foreign accounting standards that may not be comparable to the financial statements of United States companies.

It may be difficult for you to enforce your rights and any claim you may have arising under the U.S. federal securities laws, since Telecom Italia and TIM are located in Italy, and some or all of their officers and directors may be residents of Italy or other foreign countries. You may not be able to sue a foreign company or its officers or directors in a foreign court for violations of the U.S. securities laws. It may be difficult to compel a foreign company and its affiliates to subject themselves to a U.S. court's judgment.

You should be aware that Telecom Italia may purchase securities of TIM otherwise than under the merger, such as in open market or privately negotiated purchases. Disclosure of such purchases will be made in accordance with, and to the extent required by, Telecom Italia's disclosure obligations under Italian law.

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Plan for the merger by incorporation of Telecom Italia Mobile S.p.A. into Telecom Italia S.p.A.

[under Article 2501-*ter* of the Italian Civil Code ("Civil Code")]

1. Companies participating in the Merger.

Absorbing Company

Telecom Italia S.p.A.

Telecom Italia S.p.A. ("**Telecom Italia**" or the "**Absorbing Company**"), with its registered office at 2 Piazza degli Affari, Milan, fully paid-up share capital of € 8,868,946,358.25, divided into 10,329,435,946 ordinary shares with a par value of €0.55 per share and 5,795,921,069 savings shares with a par value of €0.55 per share, tax code and Milan Company Register number: 00488410010.

Company to be Absorbed

Telecom Italia Mobile S.p.A.

Telecom Italia Mobile S.p.A., also known in abbreviated form as "T.I.M. S.p.A." or "Tim S.p.A." ("**Tim**" or the "**Company to be Absorbed**"), with its registered office at 6 Via Cavalli, Turin, fully paid-up share capital of € 515,728,777.86 divided into 8,463,410,468 ordinary shares with a par value of €0.06 per share and 132,069,163 savings shares with a par value of €0.06 per share, tax code and Turin Company Register number: 06947890015, a company subject to the direction of and coordination by Telecom Italia S.p.A..

In the context of the plan for the reorganization of the Telecom Italia Group, of which the Merger is a part, it is intended that, before the Merger, Tim will spin off its mobile communications business in Italy into Tim Italia S.p.A., a company established by means of a unilateral act by Tim and wholly owned by Tim. As a consequence of the Merger, Telecom Italia will succeed Tim in respect of Tim's assets and liabilities and will thus acquire direct ownership of 100% of the capital of Tim Italia S.p.A., the company to which Tim's domestic communications business will have been transferred.

2. Bylaws of the Absorbing Company and amendments thereto as a consequence of the Merger.

In connection with the Merger and as regards the bylaws of Telecom Italia, it is to be noted that Telecom Italia will increase its share capital by a maximum nominal amount of € 1,420,690,865.55 through the issuance of a maximum of 2,291,344,587 ordinary shares and 291,729,714 savings shares, all with a par value of €0.55 per share, as a result of applying the share exchange ratio and assignment procedure referred to in Sections 3 and 4 below. Furthermore, as a consequence of the Merger, Article 5 of the bylaws will be amended to reflect the share capital increases that the Telecom Italia shareholders' meeting will be called upon to approve for Tim's stock option plans, to the extent such plans are still effective.

The complete text of the bylaws of Telecom Italia, including the amendments to Article 5 resulting from the Merger, is annexed to this merger plan. It should be noted, however, that the figures contained in such article 5 will be finalized in the merger deed, as a result of applying principles and criteria described below in Sections 3 and 4. It should also be noted that Article 22 of the bylaws of Telecom Italia contains clauses which, pursuant to Article 2 of Law no. 474 of July 30, 1994, grant the Minister for the Economy and Finance, together with the Minister for Productive Activities, certain special powers, including the right to veto the adoption of merger resolutions. The Minister for the Economy and Finance, in agreement with the Minister for Productive Activities, has notified Telecom Italia that he does not consider the conditions exist for the exercise of the veto power with respect to the adoption of the merger resolution by Telecom Italia's shareholders' meeting.

3. Exchange ratio.

The Merger will be submitted for approval on the basis of the balance sheets at 30 September 2004, prepared in accordance with and for the purposes of Article 2501-*quater* of the Civil Code.

The exchange ratio has been fixed as follows:

- 1.73 Telecom Italia ordinary shares with a par value of €0.55 per share for each Tim ordinary share with a par value of €0.06 per share;

- 2.36 Telecom Italia savings shares with a par value of €0.55 per share for each Tim savings share with a par value of €0.06 per share.

No cash consideration is envisaged.

4. Procedure for assigning shares of Telecom Italia.

The maximum amount of the increase in Telecom Italia's share capital for the purposes of the share exchange,

- considering the maximum amount by which Tim's existing share capital may be increased, among other things as a consequence of the exercise of stock options granted and still valid, and
- on the basis of the exchange ratios indicated in Section 3 above,

will be a maximum of € 1,420,690,865.55, through the issuance of a maximum of 2,291,344,587 new Telecom Italia ordinary shares and a maximum of 291,729,714 new Telecom Italia savings shares, all with a par value of €0.55 per share.

The maximum amount of the increase in Telecom Italia's share capital for purposes of the share exchange has been calculated without considering the Tim ordinary and savings shares held by Telecom Italia as a result of the voluntary partial tender offer for Tim ordinary shares and the voluntary tender offer for all Tim savings shares or Tim's treasury shares, which will not be exchanged in the Merger.

The Merger will be implemented by means of:

(i) the cancellation without exchange of Tim's ordinary shares held as treasury stock at the effective date of the Merger;

(ii) the cancellation without exchange of the Tim ordinary shares and savings shares held by Telecom Italia at the effective date of the Merger;

(iii) the cancellation with exchange of the Tim ordinary shares and savings shares outstanding at the effective date of the Merger. The authorized intermediaries will provide Tim minority shareholders with a service to handle any fractions of shares, at market prices and at no cost in terms of expenses, stamp duty or commissions, that will permit the number of newly issued shares to which the shareholders are entitled to be rounded up or down to the nearest whole number.

The newly issued shares earmarked for the exchange will be assigned to the persons entitled to such shares through their authorized intermediaries who are participants of the Monte Titoli S.p.A. central securities depository, at the effective date of the Merger. Non-dematerialized Tim shares may only be exchanged upon delivery of such shares to an authorized intermediary for deposit in the central securities depository on a dematerialized basis.

The newly issued Telecom Italia shares earmarked for the exchange will be listed on the same basis as the Telecom Italia shares already outstanding at the time they are issued.

5. Date from which the ordinary and savings shares assigned in exchange will be entitled to a share of profits.

The ordinary and savings shares issued by Telecom Italia in exchange for the Tim shares cancelled as a consequence of the Merger will have normal dividend entitlement and will therefore give their holders equivalent rights to those of the holders of outstanding Telecom Italia shares at the time they are issued.

6. Effectiveness of the Merger. Attribution and recording of Tim transactions in the accounts of Telecom Italia. Effectiveness of the Merger for Italian tax purposes.

Pursuant to Article 2504-*bis*, second paragraph, of the Civil Code, the Merger will be effective from the date of the last filing of the merger deed, or from such later date as may be specified in the merger deed itself.

In accordance with point 6 of Article 2501-*ter* of the Civil Code, the transactions effected by Tim will be attributed to and recorded in the accounts of Telecom Italia from 1 January of the year in which the Merger becomes effective. The Merger will also become effective for Italian tax purposes from such date.

It is expected that the spin-off of the mobile communications business in Italy, described in Section 1 above, will become effective prior to the effective date of the Merger.

7. Treatment reserved to special categories of shareholders or holders of securities other than shares. Special advantages for directors.

No special treatment is envisaged, in connection with the Merger, for any specific categories of shareholders or for holders of financial instruments other than the shares of Telecom Italia or the shares of Tim, provided, however, that:

- the rights of holders of Telecom Italia stock options will not be amended as a consequence of the Merger, and
- the number of shares obtainable by exercising Tim stock options will be amended to take account of the exchange ratio described in Section 3 above, with a corresponding updating of all the respective terms and conditions of such stock options.

The savings shares issued by Telecom Italia in exchange for the Tim savings shares will have equivalent rights to those of the Telecom Italia savings shares already outstanding and will therefore entitle holders to a smaller dividend premium compared to Telecom Italia ordinary shares than the dividend premium to which holders of the exchanged Tim savings shares are entitled compared to Tim ordinary shares. Consequently, holders of Tim savings shares who do not vote in favor of the Merger at the special meeting of savings shareholders called to approve the merger resolution adopted by the extraordinary shareholders' meeting will be entitled to withdrawal rights pursuant to Article 2437, first paragraph, subparagraph g), of the Civil Code.

No special advantages are envisaged for the directors of the companies participating in the Merger.

We reserve the right to make any numerical and other changes, additions and updates to this merger plan or to the bylaws of Telecom Italia annexed hereto that may be required by governmental authorities or on the occasion of filings with the Company Register or in connection with and/or resulting from the transactions envisaged in this plan.

Milan, 23 January 2005

TELECOM ITALIA S.p.A. TELECOM ITALIA MOBILE S.p.A.

Annex: Post-merger bylaws of Telecom Italia

TELECOM ITALIA - BYLAWS

Name - Registered office - Purpose and duration of the Company

Article 1

The name of the Company shall be "TELECOM ITALIA S.p.A."

Article 2

The registered office of the Company shall be in Milan.

Article 3

The Company's purpose shall be:

- the installation and operation, using any technique, method or system, of fixed and mobile equipment and installations, including space systems which use artificial satellites, radio stations, including shipboard stations, links for maritime wireless communications, and dedicated and/or integrated networks, for the purpose of providing and operating, without territorial restrictions, licensed telecommunications services for public use and telecommunications services in a free-market environment, including those resulting from technological progress, and the performance of activities directly or indirectly related thereto, including the design, construction, operation, maintenance and distribution of telecommunications, remote-computing, online and electronic products, services and systems;
- the performance of activities related to or otherwise serving the pursuit of the corporate purpose, including publishing, advertising, information technology, online and multimedia activities and, in general, all commercial, financial, property, research, training and consulting activities;
- the acquisition, provided it is not the Company's principal activity, of equity interests in other companies and undertakings falling within the scope of the corporate purpose or related, complementary or similar thereto, including companies involved in manufacturing electronic products and insurance;
- the control and the strategic, technical and administrative and financial coordination of subsidiary companies and undertakings, and the financial planning and management thereof, with the implementation of all related transactions.

Activities reserved to persons entered in a professional register, activities involving dealings with the public covered by Article 106 of Legislative Decree 385/1993, and those which are otherwise prohibited by applicable legislation shall be expressly excluded.

Article 4

The duration of the Company shall be until December 31, 2100. The extension of the time limit doesn't assign the right of withdrawal to shareholders who do not vote in favour of the resolution in question having the right of withdrawal.

Share Capital – Shares - Bonds

Article 5

The subscribed and fully paid-up share capital shall be equal to Euro 8,868,946,358.25, divided into 10,329,435,946 ordinary shares with a par value of Euro 0.55 each and 5,795,921,069 savings shares with a par value of Euro 0.55 each.

In resolutions to increase the share capital by issuing shares for cash, the right of preemption may be excluded for up to a maximum of ten per cent of the previously existing capital, provided the issue price corresponds to the market value of the shares and this is confirmed in a report prepared by the firm appointed to audit the accounts.

The Shareholders' Meeting of May 26, 2003, reiterating, updating and, where necessary, renewing earlier resolutions of the Shareholders' Meeting and the Board of Directors resolved to increase the share capital by up to a maximum of Euro 624,936,779.50 (at January 21, 2005 Euro 618,863,689.40), by means of the issue of up to a maximum of 1,136,248,690 (at January 21, 2005 1,125,206,708) ordinary shares with a par value of Euro 0.55 each to be reserved irrevocably and exclusively for the conversion of the "Olivetti 1.5% 2001-2010 convertibile con premio al rimborso" (now Prestito "Telecom Italia 1.5% 2001-2010 convertibile con premio al rimborso") convertible bonds, on the basis of 0.471553 ordinary shares for each bond presented for conversion.

The Shareholders' Meeting of May 26, 2003 also resolved to increase the share capital by up to a maximum of Euro 183,386,986.75 (at January 21, 2005 Euro 136,272,697.55), by means of the issue of up to a maximum of 333,430,885 (at January 21, 2005 247,768,541) ordinary shares with a par value of Euro 0.55 each, divided into the following divisible tranches:

1 a tranche of up to a maximum of Euro 37,398,868.65 (at January 21, 2005 Euro 19,425,568.80) for the exercise of the "Piano di Stock Option 2000" stock options, increase to be implemented by July 30, 2008 by means of the issue of up to a maximum of 67,997,943 (at January 21, 2005 35,319,216) shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 13.815 per option held (i.e. at a price of Euro 4.185259 for each newly-issued share);

2 a tranche of up to a maximum of Euro 58,916,834.35 (at January 21, 2005 Euro 58,022,367.15) for the exercise of the "Piano di Stock Option 2001" stock options, increase to be implemented by April 30, 2008 by means of the issue of up to a maximum of 107,121,517 (at January 21, 2005 105,495,213) shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 10.488 per option held (i.e. at a price of Euro 3.177343 for each newly-issued share);

3 a tranche of up to a maximum of Euro 21,422,652.90 (at January 21, 2005 Euro 17,755,377.20) for the exercise of the "Piano di Stock Option Top 2002" stock options, increase to be implemented by February 28, 2010 by means of the issue of up to a maximum of 38,950,278 (at January 21, 2005 32,282,504) shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 9.203 per option held (i.e. at a price of Euro 2.788052 for each newly-issued share);

4 a tranche of up to a maximum of Euro 50,268,799.90 (at January 21, 2005 Euro 41,069,384.40) for the exercise of the "Piano di Stock Option 2002" stock options, increase to be implemented by March 31, 2008 for the first lot, by March 31, 2009 for the second lot and by March 31, 2010 for the third lot by means of the issue of up to a maximum of 91,397,818 (at January 21, 2005 74,671,608) shares with a par value of Euro 0.55 each, to be subscribed for at a total price for the different options of respectively Euro 9.665, Euro 7.952 and Euro 7.721 per option held (i.e. at a price for the different options of respectively Euro 2.928015 Euro 2.409061 and Euro 2.339080 for each newly-issued share).

The Shareholders' Meeting of [-] also resolved to increase the share capital by up to a maximum of Euro 38.655.832,60, by means of the issue of up to a maximum of 70.283.332 ordinary shares with a par value of Euro 0.55 each, divided into the following divisible tranches:

1. a tranche of up to a maximum of Euro 11,705,656.05 for the exercise of the "2000-2002 Stock-Option Plans" stock options, increase to be implemented by December 31, 2008 by means of the issue of up to 21,283,011 Telecom Italia ordinary shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 6.42 per option held (i.e. at a price of Euro 3.710983 for each newly-issued share);
2. a tranche of up to a maximum of Euro 1,132,285 for the exercise of the "2001-2003 Stock-Option Plans" stock options, increase to be implemented by December 31, 2005 by means of the issue of up to 2,058,700 Telecom Italia ordinary shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 8.671 per option held (i.e. at a price of Euro 5.012139 for each newly-issued share);
3. a tranche of up to a maximum of Euro 474,798.50 for the exercise of the "2001-2003 Supplementary Plans" stock options, increase to be implemented by December 31, 2005 by means of the issue of up to 863,270 Telecom Italia ordinary shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 7.526 per option held (i.e. at a price of Euro 4.350289 for each newly-issued share);
4. a tranche of up to a maximum of Euro 22,150,920 for the exercise of the "2002-2003 Stock-Option Plans" stock options, increase to be implemented by December 31, 2008 by means of the issue of up to 40,274,400 Telecom Italia ordinary shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 5.67 per option held (i.e. at a price of Euro 3.277457 for each newly-issued share);
5. a tranche of up to a maximum of Euro 3,192,173.05 for the exercise of the "2003-2005 Stock-Option Plans" stock options, increase to be implemented by December 31, 2008 for the first lot, by December 31, 2009 for the second lot and by December 31, 2010 for the third lot by means of the issue of up to a maximum of 5,803,951 shares with a par value of Euro 0.55 each, to be subscribed for at a total price of Euro 5.07 per option held (i.e. at a price of Euro 2.930636 for each newly-issued share).

For five years starting from May 6, 2004 the Directors may increase the share capital in one or more tranches by up to a maximum total amount of Euro 880,000,000 by means of cash issues of up to a maximum of 1,600,000,000 ordinary shares, all or part of which:

(i) to be offered with the right of pre-emption to shareholders and holders of convertible bonds; or

(ii) to be offered for subscription to employees of Telecom Italia S.p.A. or its subsidiaries, with the exclusion of the right of pre-emption, provided such increase in capital does not exceed 1% of the capital attested at the date of the offering, pursuant to the combined effects of Article 2441, last paragraph, of the Civil Code and Articles 134(2) of Legislative Decree 58/1998.

Resolutions to increase the share capital adopted by the Board of Directors in exercising the powers attributed above shall set the subscription price (including any premium) and a time limit for the subscription of the shares; they may also provide, in the event that the increase approved is not fully subscribed within the time limit established for each issue, for the capital to be increased by an amount equal to the subscriptions received up to such time.

The Board of Directors may issue, in one or more tranches and for up to a maximum of five years from May 6, 2004, convertible bonds up to a maximum amount of Euro 880,000,000.

Article 6

The savings shares shall have the preferential rights set forth in this Article.

The net profit shown in the duly approved annual accounts, less the amount to be allocated to the legal reserve, must be distributed to the savings shares up to five per cent of their par value.

The net profit that remains after the allocation to the savings shares of the preferred dividend provided for in the second paragraph, payment of which must be approved by the Shareholders' Meeting, shall be divided among all the shares in such a way that the dividend per savings share is higher by two per cent of its par value than the dividend per ordinary share.

When the dividend paid on savings share in a fiscal year is less than that indicated in the second paragraph, the difference shall go to increase the preferred dividend in the next two fiscal years.

In the event of a distribution of reserves, the savings shares have the same rights as the other shares. If the net profit for the year is nil or insufficient to satisfy the property rights referred to in the preceding paragraphs, the Shareholders' Meeting called to approve the annual accounts may resolve to satisfy the right referred to in the second paragraph and/or the right to the premium referred to in the third paragraph by drawing on the reserves. Payment made by drawing on the reserves shall exclude application of the mechanism for carrying over, to the two following fiscal years, the right to preferred dividends not received through the distribution of profits referred to in the fourth paragraph.

A reduction of the share capital due to losses shall not entail a reduction of the par value of the savings shares, except for the amount of the loss that exceeds the total par value of the other shares.

Upon dissolution of the Company, the savings shares shall have priority in the repayment of the capital up to their entire par value.

If the Company's ordinary or savings shares are delisted, holders of saving shares may apply to the Company for their conversion into ordinary shares, in the manner approved by an Extraordinary Shareholders' Meeting called ad hoc within two months of the delisting.

Article 7

The shares shall be indivisible. In the event of joint ownership, the rights of the joint owners shall be exercised by a common representative. Fully paid-up shares may be bearer shares when the law permits. In such case, shareholders may apply for their shares to be converted, at their own expense, into registered shares or vice versa.

Vis-à-vis the Company, shareholders shall be deemed to elect domicile for all legal purposes at the domicile indicated in the Shareholders' Register.

The imposition or removal of restrictions on the circulation of shares doesn't assign the right of withdrawal to shareholders who did not vote in favour of the resolution in question having the right of withdrawal.

Article 8

The Company may issue bonds and shall establish the terms and conditions of their placement.

Board Of Directors

Article 9

The Company shall be managed by a Board of Directors consisting of not less than seven and not more than twenty-three members. The Shareholders' Meeting shall establish the number of members of the Board, which shall remain unchanged until the Meeting establishes a different number.

The Board of Directors shall be appointed on the basis of slates presented by the shareholders pursuant to the following paragraphs or by the outgoing Board of Directors, on which the candidates shall be listed by serial number.

When the Board of Directors presents its own slate, it shall be filed at the registered office of the Company and published in at least one Italian daily newspaper with national circulation, at least twenty days prior to the date set for the Shareholders' Meeting on the first call.

The slates presented by the shareholders shall be filed at the registered office of the Company and published at the expense of the shareholders in the manner indicated in the preceding paragraph at least ten days prior to the date set for the Shareholders' Meeting on the first call.

Each shareholder may present or participate in the presentation of only one slate and each candidate may appear on only one slate on pain of ineligibility.

Only 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 Ordinary Shareholders' Meeting may submit slates, subject to their proving ownership of the number of shares needed for the presentation of slates at least two days prior to the date set for the Shareholders' Meeting at the first call on pain of nullity.

Together with each slate, and within the respective time limits specified above, declarations must be filed in which the individual candidates agree to their candidacy and attest, on their own responsibility, that there are no grounds for ineligibility or incompatibility, and that they meet any requirements prescribed for the positions in question. Together with the declarations, a curriculum vitae shall be filed for each candidate setting out their main personal and professional data with an indication, where appropriate, of the grounds for their qualifying as independent.

Each person entitled to vote may vote for only one slate.

The Board of Directors shall be elected as specified below:

a) four fifths of the directors to be elected shall be chosen from the slate that obtains the majority of the votes cast by the shareholders, in the order in which they are listed on the slate; in the event of a fractional number, it shall be rounded down to the nearest whole number;

b) the remaining directors shall be taken from the other slates; to that end, the votes obtained by the various slates shall be divided first by one, then by two, then by three, then by four and then by five, up to the number of directors to be chosen. The quotients thus obtained shall be assigned to the candidates on each slate in the order specified thereon. On the basis of the quotients assigned, the candidates on the various slates shall be arranged in a single decreasing ranking. Those who have obtained the highest quotients shall be elected.

   If more than one candidate obtains the same quotient, the candidate from the slate that has not yet elected any director or that has elected the smallest number of directors shall be elected.

   If none of such slates has yet elected a director or all of them have elected the same number of directors, the candidate from the slate that obtained the largest number of votes shall be elected. If the different slates have received the same number of votes and their candidates have been assigned the same quotients, a new vote shall be held by the entire Shareholders' Meeting and the candidate obtaining the simple majority of the votes shall be elected.

In appointing directors who for any reason have not been appointed pursuant to the procedure specified above, the Shareholders' Meeting shall vote on the basis of the majorities required by law.

If in the course of the fiscal year one or more vacancies occur on the Board, the procedure specified in Article 2386 of the Civil Code shall be followed.

Should a majority of the seats on the Board of Directors become vacant for any cause or reason, the remaining directors shall be deemed to have resigned and they shall cease to hold office from the time the Board has been reconstituted by persons appointed by the Shareholders' Meeting.

Article 10

The Board of Directors shall elect a Chairman from among its member — if the Shareholders' Meeting has not already done so — and may also appoint a Deputy Chairman; both may be re-elected.

In the absence or disability to act of the Chairman, the Deputy Chairman, if one has been appointed, shall take his/her place or, if the Deputy Chairman is absent, the most senior director by age.

The Board of Directors may elect a Secretary who need not be a director.

Extracts from the register of the minutes of meetings of the Board of Directors signed by the Chairman or by two directors and countersigned by the Secretary shall be conclusive evidence.

Article 11

The Chairman or his/her substitute shall call meetings of the Board of Directors at the Company's registered office or elsewhere, whenever he/she deems this appropriate in the interests of the Company or receives a written request to do so from at least one fifth of the directors holding office or from the members of the Board of Auditors. The Chairman shall give advance notice of the matters to be discussed in Board meetings and arrange for adequate information on the questions to be examined to be provided to all the Directors, taking account of the circumstances of each case.

In general, meetings shall be called at least five days prior to the date thereof, except in urgent cases, when it may be given by telegram, fax or e-mail with at least twenty-four hours' notice.

Notice shall be given to the Board of Auditors within the same time limits.

Participation in Board meetings may – if the Chairman or his/her substitute verifies the necessity – be by means of telecommunication techniques that permit participation in the discussion and informational equality for all those taking part.

Article 12

The Board of Directors shall have the broadest possible powers of ordinary and extraordinary administration of the Company, since all matters not expressly reserved to the General Shareholders' Meeting by law or these bylaws are within its jurisdiction.

Within the limits established by law, the Board of Directors shall be entrusted with deciding on the merger of companies of which Telecom Italia owns at least 90% of the shares or capital parts, the reduction of the share capital in the event of the withdrawal of shareholders, the revision of the bylaws to conform with statutory provisions, the relocation of the registered office within Italy, and the opening and closing of secondary offices.

Article 13

To implement its own resolutions and manage the Company, the Board of Directors, subject to the limits provided for by law, may:

- create an Executive Committee, establishing its powers and the number of members;
- delegate suitable powers, establishing the limits thereof, to one or more directors, possibly with the title of Chief Executive Officer;
- appoint one or more General Managers, establishing their powers and duties;
- appoint attorneys, who may be members of the Board of Directors, for specific transactions and for a limited period of time.

The Board may set up committees from among its members charged with giving advice and making proposals and shall establish their powers and duties.

Article 14

Persons with delegated powers shall report to the Board of Directors and the Board of Auditors on the activities carried out, the general results of operations and their foreseeable development, and the transactions of greatest economic, financial or balance sheet significance concluded by the Company or its subsidiaries; in particular, they shall report on transactions in which they have an interest, directly or on behalf of third parties, or that are influenced by the person, if any, who performs the activity of direction and coordination. Such reports shall be made promptly, and at least once in each quarter, on the occasion of the meetings of the Board of Directors and the Executive Committee or in a written memorandum.

In accordance with the times and procedures for disclosing information to the market, the representative of the holders of savings shares must be informed by the Board of Directors or the persons delegated to that end of any corporate events that might affect the price of the shares of that class.

Article 15

The representation of the Company vis-à-vis third parties and in legal proceedings shall pertain to the Chairman and, in his absence or disability to act, the Deputy Chairman, if one is appointed; it shall also pertain severally to each of the directors with delegated powers.

Article 16

The directors shall be entitled to the reimbursement of expenses incurred in the performance of their duties. The Ordinary Shareholders' Meeting shall also decide the annual remuneration payable to the Board. Once fixed, this remuneration shall remain unchanged until the Meeting establishes a different amount.

Board Of Auditors

Article 17

The Board of Auditors shall consist of five or seven auditors. The Shareholders' Meeting shall establish the exact number, which shall remain unchanged until the Meeting establishes a different number. The Meeting shall also appoint two alternates.

The Board of Auditors shall elect a Chairman from among its members by majority vote. In the absence or disability to act of the Chairman, he/she shall be replaced by the most senior auditor by age.

Without prejudice to the situations of incompatibility established by law, persons who are members of the boards of auditors of more than five companies listed on Italian regulated markets may not be appointed auditors and shall forfeit the post if they are elected. Telecom Italia S.p.A. and its subsidiaries shall not be included when computing the above limit.

For the purposes of Articles 1(2)(b) and 1(2)(c) of the regulation referred to in Justice Minister Decree 162/2000, the following sectors of activity and matters shall be considered closely linked to those of the Company: telecommunications, information technology, online systems, electronics and multimedia technology, and matters related to private and administrative law, economics and business administration.

The appointment of the Board of Auditors shall be based on the slates presented by shareholders who individually or together with other shareholders hold a total number of shares representing at least 1% of the share capital entitled to vote at the Ordinary Shareholders' Meeting, subject to their proving ownership of the number of shares needed for the presentation of slates at least two days prior to the date set for the Shareholders' Meeting at the first call on pain of nullity.

Each shareholder may present or participate in the presentation of only one slate and each candidate may appear on only one slate on pain of ineligibility.

The slates must be filed at the registered office of the Company and published at the expense of the shareholders who present them in at least one Italian daily newspaper with national circulation, at least ten days prior to the date set for the Shareholders' Meeting on the first call.

Together with each slate, declarations must be filed in which the individual candidates agree to their candidacy and attest, on their own responsibility, that there are no grounds for ineligibility or incompatibility, and that they meet the requirements prescribed by law and these bylaws. Together with the declarations, a curriculum vitae for each candidate shall be filed setting out their main personal and professional data.

The slates shall be divided into two sections: one for candidates to the position of auditor and the other for candidates to the position of alternate. The first candidate in each section must be selected from among persons entered in the register of auditors who have worked on statutory audits for a period of not less than three years.

Each person entitled to vote may vote for only one slate.

The Board of Auditors shall be elected as specified below:

a) from the slate that obtains the majority of the votes cast by the shareholders (the Majority Slate) one alternate and all the auditors not chosen from the other slates (the Minority Slates) shall be chosen in the order in which they are listed on the slate;

b) from the Minority Slates two auditors shall be chosen. One alternate shall be chosen from the Minority Slate that obtains the largest number of votes.

   For the appointment of the auditors from the Minority Lists, the votes obtained by the various slates shall be divided first by one and then by two. The quotients thus obtained shall be assigned to the candidate auditors on each slate in the order specified thereon. On the basis of the quotients assigned, the candidates on the various slates shall be arranged in a single decreasing ranking and those who have obtained the highest quotients shall be elected.

   If more than one candidate obtains the same quotient, the candidate from the slate that has not yet elected an auditor shall be elected or, subordinately, there shall be a tiebreaker vote by the entire Shareholders' Meeting and the slate that obtains the simple majority of the votes shall prevail.

In appointing auditors who for any reason have not been appointed pursuant to the procedure specified above, the Shareholders' Meeting shall vote on the basis of the majorities required by law.

In the event of the substitution of an auditor chosen from the Majority Slate or one of the Minority Slates, the alternate chosen respectively from the Majority List or the Minority Lists shall take his/her place. Appointments to fill vacancies on the Board of Auditors pursuant to Article 2401 of the Civil Code shall be made by the Shareholders' Meeting on the basis of the majorities required by law.

After notifying the Chairman of the Board of Directors, the Board of Auditors, or at least two auditors, may call, as provided for by law, a meeting of the shareholders, the Board of Directors or the Executive Committee.

Participation in the meetings of the Board of Auditors may – if the Chairman verifies the necessity – be by means of telecommunication techniques that permit participation in the discussion and informational equality for all those taking part.

SHAREHOLDERS' MEETING

Article 18

An Ordinary Shareholders' Meeting must be called within 120 days or, where special circumstances make this necessary, within 180 days of the end of the fiscal year; if the meeting is called within 180 days, the Directors shall give the reasons for the delay in the report on operations included in the annual report.

An Extraordinary Shareholders' Meeting shall be called whenever it is deemed desirable by the Board of Directors and when it is required in accordance with the law. If the quorum is not reached at the second call, there may be a third call.

Ordinary and Extraordinary Shareholders' Meetings may be held in a place other than the Registered Office, provided it is in Italy.

Article 19

The shareholders, for which the Company has received the documentation pursuant to article 2370, second paragraph of the Civil Code, at least two days prior to the date set for each meeting and hold the suitable certification on the date the meeting takes place, are entitled to attend the Meeting.

Ordinary shareholders may exercise their right to vote by mail in accordance with the applicable law.

Every shareholder entitled to attend may be represented at the Shareholders' Meeting by giving a proxy to an individual or legal entity, subject to the restrictions established by law.

In order to facilitate the collection of proxies among employee shareholders of the Company and its subsidiaries who belong to shareholder associations satisfying the requirements established by law, special areas shall be made available in accordance with the procedures and time limits established by the Board of Directors either directly or through its agents where information can be provided and proxy forms collected.

Article 20

The Chairman of the Board of Directors or his/her substitute or, in the absence thereof, the person elected with the favourable vote of the majority of the capital represented at the meeting, shall chair the Shareholders' Meeting and govern its proceedings. To this end, the Chairman of the Meeting shall, amongst other things, verify its regularity, ascertain the identity and right to attend of those present, direct the business, including by establishing a different order for the discussion of the items indicated in the notice convening the Meeting.

The Chairman shall take appropriate measures to ensure the orderly conduct of the discussion and polls; he shall establish how each poll is to be conducted and verify the results; he may choose two or more scrutineers from among those present.

The Secretary shall be appointed with the favourable vote of the majority of the capital represented at the meeting and a person who is not a shareholder may be selected.

Shareholders' meetings shall be governed by the law, these bylaws and the Rules of Proceeding approved by the Ordinary Shareholders' Meeting.

FISCAL YEAR - DIVIDENDS

Article 21

The fiscal year shall end on December 31 of each year.

From the net profit reported in the annual accounts, 5% shall be allocated to the legal reserve until this reaches an amount equal to one-fifth of the share capital.

The remainder shall be used to pay the dividend determined by the Shareholders' Meeting, and for such other purposes as the Meeting deems most appropriate or necessary.

During the course of the fiscal year, the Board of Directors may distribute interim dividends to the shareholders.

SPECIAL POWERS

Article 22

Pursuant to Article 2(1) of Decree Law 332/1994, ratified with amendments by Law 474/1994, the Minister for the Economy and Finance, in agreement with the Minister for Productive Activities, shall have the following special powers:

a) approval, to be granted expressly upon the acquisition by parties subject to the limitations on share ownership referred to in Article 3 of Decree Law 332/1994, ratified with amendments by Law 474/1994, of major holdings, taken to mean holdings that, as specified by Treasury Minister Decree of March 24, 1997, are equal to at least 3% of the share capital represented by shares with a right to vote at the Ordinary Shareholders' Meeting. Approval must be granted within sixty days of the date of the communication that the Board of Directors must send at the time of the application for entry in the Shareholders' Register. Until approval has been granted and after expiration of the time limit without any action, the transferee may not exercise the voting rights or any rights other than the property rights attaching to the shares that represent the major holding. If approval is refused or the time limit expires without action, the transferee must sell the shares within one year. If this is not done, the Court, at the request of the Minister for the Economy and Finance, shall order the sale of the shares representing the major holding pursuant to the procedures established in Article 2359-ter of the Civil Code;

b) veto of any resolution to dissolve the Company, transfer the business, merge or divide the Company, transfer the registered office outside Italy, change the corporate object, or amend these bylaws with a view to eliminating or modifying the powers specified in subparagraphs a) and b).

Report of the Board of Directors of Telecom Italia S.p.A.
dated 23 January 2005
on the plan for the merger by incorporation of

Telecom Italia Mobile S.p.A.

into

Telecom Italia S.p.A.

pursuant to Article 2501-*quinquies of the Italian Civil Code*
and Article 70.2 of the Regulation approved by CONSOB with
Deliberation no. 11971 of 14 May 1999

This is an English translation of the original Italian document

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

The merger described herein relates to the securities of two foreign (non-U.S.) companies. The merger in which TIM ordinary shares and savings shares will be converted into Telecom Italia shares is subject to disclosure requirements of a foreign country that are different from those of the United States. Financial statements included in the document, if any, will be prepared in accordance with foreign accounting standards that may not be comparable to the financial statements of United States companies.

It may be difficult for you to enforce your rights and any claim you may have arising under the U.S. federal securities laws, since Telecom Italia and TIM are located in Italy, and some or all of their officers and directors may be residents of Italy or other foreign countries. You may not be able to sue a foreign company or its officers or directors in a foreign court for violations of the U.S. securities laws. It may be difficult to compel a foreign company and its affiliates to subject themselves to a U.S. court's judgment.

You should be aware that Telecom Italia may purchase securities of TIM otherwise than under the merger, such as in open market or privately negotiated purchases. Disclosure of such purchases will be made in accordance with, and to the extent required by, Telecom Italia's disclosure obligations under Italian law.

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Dear Shareholders,

We submit this report for your consideration; it describes, from a legal and economic perspective, the plan for the merger by incorporation of Telecom Italia Mobile S.p.A. ("**Tim**" or the "**Company to be Absorbed**") into Telecom Italia S.p.A. ("**Telecom Italia**" or the "**Absorbing Company**") and in particular the methods and criteria used to determine the exchange ratio of the shares of the companies involved in accordance with Article 2501 *quinquies* of the Italian Civil Code ("Civil Code") and Article 70.2 of the Regulation approved by CONSOB with Deliberation No. 11971 of 14 May 1999, as amended (the "**Regulation on Issuers**")

1. Description of the merger transaction and the reasons therefor

1.1 The merger transaction

1.1.1 The transaction submitted for your approval consists of the merger by incorporation of Tim into Telecom Italia pursuant to Article 2501 et seq. of the Civil Code (the "**Merger**"). Since the Merger involves issuers of securities listed on an Italian regulated securities exchange, it is also subject to the applicable provisions of Legislative Decree No. 58 of 24 February 1998 and the Regulation on Issuers.

For purposes of the Merger, reference is made to the respective balance sheets of Telecom Italia and Tim at 30 September 2004, prepared pursuant to Article 2501-*quater* of the Civil Code.

1.1.2 The Merger is the last step in the plan for the reorganization of the group headed by Telecom Italia – the guidelines of which were approved by the Boards of Directors of Telecom Italia and Tim in their meetings on 7 December 2004 and publicly disclosed on the same date – which also includes:

- a voluntary partial tender offer for Tim ordinary shares and a voluntary tender offer for all Tim savings shares (collectively, the "**Tender Offer**"); and
- the spin-off of the mobile communications business in Italy, currently operated by Tim, into a company wholly owned by Tim (the "**Spin-Off**").

The intention of the companies involved is to complete the Merger as soon as possible and, specifically, to arrange for it to become effective by the end of June 2005.

1.1.3 The Tender Offer, which commenced on 3 January 2005 and terminated on 21 January 2005, represented the first step in the above-mentioned reorganization plan and must be considered as connected with and serving the purposes of the Merger.

In view of the Merger, the Tender Offer was intended to contribute to optimizing the capital structure of the Absorbing Company. Since in implementing the Merger the Tim shares held by Telecom Italia will be cancelled without exchange, Telecom Italia's acquisition of Tim shares by means of the Tender Offer has increased the proportion of Tim's share capital that will be cancelled and consequently reduced the amount of equity to be issued in exchange. This will have a positive effect on earnings and free cash flow yield per share, to the benefit of all the post-Merger shareholders of Telecom Italia and Tim. From a financial perspective, the equity that is not issued will in effect be replaced, as a result of the settlement of the obligations arising from the Tender Offer, by an increase in Telecom Italia's net debt. The cost of this new debt – in terms of after-tax net financial expense – is lower than the cost – in terms of the expected dividends – which would have been incurred on the equity not issued in exchange for Tim shares purchased in the Tender Offer.

On the basis of the results of the Tender Offer, which are described below, the total consideration in respect of the Tim shares tendered is approximately €13.8 billion, of which €2.5 billion will be paid by Telecom Italia by using its own funds and approximately €11.3 billion will be raised through bank financing provided by a syndicate of banks led by JP Morgan plc (Global Coordinator), Mediobanca Banca di Credito Finanziario S.p.A. ("**Mediobanca**"), MCC S.p.A. – Capitalia Gruppo Bancario ("**MCC**"), UniCredit Banca Mobiliare S.p.A. and Banca Intesa S.p.A. (Mandated Lead Arrangers). Consequently, the net financial debt of the Telecom Italia Group, estimated at a little less than €30 billion at 31 December 2004, will amount, excluding the other costs related to the Tender Offer, to just under €44 billion. This figure does not take into account the exercise of the call options for approximately 42 million Tim ordinary shares and 21 million Tim savings shares which were previously disclosed to the market. Moreover, it should be noted that following requests to convert Telecom Italia (originally Olivetti) 1.5% 2001-2010 convertible bonds with redemption premium received by 21 January 2005 and not yet effected, the latter amount will be reduced by approximately €1 billion as a consequence of the issuance of the corresponding shares upon conversion.

The increase in debt following the Tender Offer has not led, in line with the indication given in the announcement of the plan to reorganize the Telecom Italia Group, to a reduction in Telecom Italia's credit rating (currently Baa2 for Moody's, BBB+ for Standard & Poor's, A– for Fitch). It should be noted that Standard & Poor's and Fitch, while confirming their respective ratings, have revised their outlooks from positive to stable and from stable to negative, respectively. The rating agencies arrived at these conclusions on the basis of the maximum estimated consideration payable in connection with the Tender Offer, equal to approximately €14.5 billion.

Approximately €11.3 billion of the Tender Offer is covered by the loan debt incurred in connection with an agreement Telecom Italia entered into on 8 December 2004 for a maximum amount of €12 billion. The loan is divided into three repayment tranches with different maturities (12, 36 and 60 months, with Telecom Italia having the option, at its discretion, to extend the maturities of the first two tranches by 12 months and 9 months, respectively).

The amount borrowed under the bank financing, equal to approximately €11.3 billion, may be refinanced in the capital markets, depending on market opportunities and conditions, probably in the next two years.

The progressive reduction in the debt incurred as a result of the Tender Offer will be made possible primarily by the cash flow that will be generated, which is expected to be at least in line with the plans announced in March 2004.

1.1.4 The next step in the planned reorganization of the Telecom Italia Group is the SpinOff, which, by maintaining the autonomy of the domestic mobile communications business, is in line with an assessment of what would be desirable from a regulatory and accounting perspective in the context of the overall reorganization plan and at the same time is an efficient way to meet the need for transparency in the relationship between fixed and mobile communications. As mentioned above, the business to be spun-off includes Tim's domestic mobile communications activities, but not the following items related primarily to Tim's international business: (i) the 100% equity interest held by TIM in TIM International N.V. ("**TIM International**"), the holding company for equity investments in foreign companies operating in the mobile communications sector with a book value, including payments for future increases in capital, of €4,582 million; (ii) the reserve for risks in respect of guarantees issued on behalf of foreign affiliates, amounting to €198 million; (iii) the guarantees granted and received in relation to the foreign sector, included in the memorandum accounts, for a total of €982 million; (iv) the advance taxes, related to the international assets, amounting to €813 million; (v) the balance of the current account held by TIM with Telecom Italia; and (vi) certain other financial and tax items. The above amounts, included here merely for explanatory purposes, are recorded in Tim's balance sheet at 30 September 2004.

In this respect it should be noted that Tim has established Tim Italia S.p.A., the company to which Tim's domestic mobile communications business is intended to be transferred in the Spin-Off ("**Tim Italia**"), by means of a unilateral act. Tim has also applied, pursuant to Article 2343 of the Civil Code, for the appointment of an appraiser to prepare the valuation report for the business to be spun off. Likewise, for regulatory purposes, Tim has notified the Ministry for Communications pursuant to Article 25.8 of Legislative Decree No. 259 of 1 August 2003.

As a result of the Spin-Off and before the effective date of the Merger – since it is expected that the transfer deed will be executed and filed with the relevant office of the Company Register by the end of March 2005 – Tim Italia will succeed to the authorizations held by Tim for the provision of mobile communications services in Italy.

Accordingly, at the time of the Merger, Tim will have 100% control of Tim Italia, the company to which the domestic mobile communications business of Tim will be transferred, and of Tim International.

Under the proposed Merger, Telecom Italia will succeed to all of Tim's legal rights and obligations in respect of the latter's assets and liabilities, except for those pertaining to the business transferred to Tim Italia. At the same time, Telecom Italia will become the direct holder of 100% of the capital of both Tim Italia and Tim International and will be responsible for their direction and coordination.

1.1.5 At the end of the acceptance period of the Tender Offer on 21 January 2005, the following shares had been tendered: 2,639,154,665 ordinary shares (corresponding to approximately 31.2% of Tim's ordinary share capital and approximately 107.4% of the ordinary shares that were the subject of the ordinary share offer) and 8,463,127 savings shares (corresponding to approximately 6.4% of Tim's savings share capital and of the savings shares that were the subject of the savings share offer). Following the proration of the Tim ordinary shares tendered, Telecom Italia therefore owns, directly and indirectly, 7,190,583,124 Tim ordinary shares (corresponding to approximately 84.8% of the company's ordinary share capital and approximately 85.539% of its total share capital) and 8,463,127 Tim savings shares (corresponding to approximately 6.4% of the company's savings share capital and approximately 0.098% of its total share capital).

Telecom Italia's Board of Directors has favorably assessed the results of the Tender Offer, especially in view of the fact that the Tim ordinary shares tendered exceeded the number of Tim ordinary shares subject to the Tender Offer, thus demonstrating the market's appreciation of the transaction and making it possible to achieve the objective of optimizing Telecom Italia's balance sheet and financial structure upon completion of the Merger. For this reason, Telecom Italia's Board of Directors has decided to waive the Tender Offer effectiveness conditions concerning the minimum threshold of acceptances for Tim savings shares, thereby confirming the effectiveness of the Tender Offer and accepting to purchase the smaller quantity of Tim savings shares tendered, and to proceed with the integration process.

It should also be noted that, as a result of the exercise of the options which were previously disclosed to the market (for approximately 21 million Tim savings shares) and the execution of securities lending agreements (for approximately 37 million Tim savings shares), following the Tender Offer Telecom Italia will be entitled to vote approximately 50.3% of the shares entitled to vote in the special meeting of Tim savings shareholders that will be called to approve the Merger resolution.

1.1.6 Under Article 2504-*ter* of the Civil Code, the Merger will result in the cancellation of the Tim shares held by Telecom Italia at the effective date of the Merger without exchange and in the cancellation of the treasury shares held by Tim. Holders of Tim ordinary and savings shares other than Telecom Italia will instead be assigned newly issued Telecom Italia ordinary and savings shares on the basis of the exchange ratio described below (see primarily Section 4 below).

Regulations are being promulgated which mandate the adoption, in Italy, of the IAS/IFRS international accounting standards for the preparation of financial statements. In particular, for companies with shares listed on regulated securities exchanges, the adoption of these standards will be mandatory for their 2005 consolidated annual financial statements and optional for their company annual accounts.

Telecom Italia is currently analyzing and assessing whether to adopt the IAS/IFRS standards not only for the consolidated financial statements of the Telecom Italia Group, but also for the Telecom Italia S.p.A. 2005 annual financial statements for civil law purposes.

If the Italian accounting standards are applied for the 2005 annual financial statements of Telecom Italia S.p.A. for civil law purposes, it will be possible to account for the Merger at book value, thereby giving rise to both a "cancellation deficit" (the difference between the book value of the Tim shares held by Telecom Italia, including those acquired through the Tender Offer, and the value of the corresponding portion of shareholders' equity) and an "exchange deficit" (the difference between the increase in capital for the exchange and the corresponding portion of the Tim shareholders' equity acquired). The cancellation deficit could be allocated to increase the book value of Tim assets at the time of the Merger (the equity interests in Tim Italia and Tim International), while the exchange deficit could be allocated to the reduction of the reserves included in Telecom Italia's shareholders' equity.

As for the financial statements of the Telecom Italia Group, which will have to be prepared on the basis of the new IAS/IFRS accounting standards, the Merger will be accounted for on a fair value basis and the merger differences will therefore be allocated to the tangible and intangible assets and to the liabilities of TIM Italia and Tim International and their subsidiaries, while any portion not so allocated will be recorded as goodwill.

1.1.7 As part of the share exchange, holders of Tim savings shares will be assigned Telecom Italia savings shares.

It should be noted that, from a formal legal perspective, Telecom Italia savings shares are entitled to a smaller dividend premium compared to ordinary shares than that to which holders of Tim savings shares are currently entitled compared to Tim ordinary shares.

Tim savings shares entitle their holders, among other things, to the right to a premium with respect to any profit distributed to ordinary shareholders equal to 20% of their par value of €0.06 and to the right to the distribution of net profits, after deducting the amount to be allocated to the legal reserve, up to 5% of their par value. In contrast, Telecom Italia savings shares entitle their holders the right to the distribution of net profits up to 5% of their par value of €0.55, and the right to a premium with respect to any dividend distributed to ordinary shareholders equal to 2% of their par value.

Because of these different rights, the resolution approving the Merger Plan will be submitted for approval to the special meeting of Tim savings shareholders; holders of Tim savings shares who do not vote in favor of the Merger will be entitled to withdrawal rights pursuant to Article 2437, first paragraph, subparagraph g), of the Civil Code.

It should be noted, however, that from a substantive economic perspective, the exchange will lead to an improvement in the entitlement to profits of Tim savings shareholders as regards the quantification of their premium, since each Tim savings share with a par value of €0.06 will be exchanged for more than one Telecom Italia savings share with a par value of €0.55 (on the basis of the exchange ratio of 2.36 Telecom Italia savings shares for each Tim savings share; see Section 4 below), so that the post-exchange dividend premium for each former Tim savings share will be calculated with reference to a higher total par value of €0.55 x €2.36 = €1.30 instead of €0.06. Consequently, the post-exchange dividend premium for holders of Tim savings shares – with respect to the dividend premium compared to ordinary shares – for each Tim savings share held, equal to 20% x €0.06 = €0.012, will increase as a consequence of the exchange for Telecom Italia savings shares to 2% x €1.30 = €0.026. In this way the right to a smaller premium in relative terms will be more than offset in absolute terms.

1.1.8 On 14 December 2004, Telecom Italia published a notice in the Italian Official Gazette concerning the right of holders of Telecom Italia 1.5% 2001-2010 convertible bonds with redemption premium to exercise their conversion rights under Article 2503-*bis*, second paragraph, of the Civil Code.

The above-mentioned bonds are continuously convertible subject to the provision on the suspension of conversion rights contained in Article 6(iv) of the terms and conditions of the bonds. Under these terms and conditions, conversion rights will be suspended from the day after the meeting of the Board of Directors that calls the shareholders' meeting to approve the Merger Plan. However, as announced on 31 December 2004, in view of the planned addition of the approval of the annual financial statements to the agenda of such shareholders' meeting, the intention is to apply the special provision under the terms and conditions for the case in which the shareholders' meeting is called to approve the distribution of a dividend. Accordingly, from the day following the above-mentioned addition to the agenda, it will again be possible to exercise conversion rights for 14 days. From the 15th day following the meeting of the Board of Directors held to approve the financial statements for the year ended 31 December 2004 until the dividend payment day, inclusive, the right to exercise conversion rights will again be suspended.

1.1.9 The shareholders' meeting of Telecom Italia called to approve the Merger will also be called to approve the increases in share capital required by Tim's stock option plans, to the extent such plans are still effective. The number of shares obtainable upon the exercise of Tim stock options will be adjusted to take account of the exchange ratio.

1.1.10 Following the Merger, Telecom Italia's ordinary and savings shares will continue to be listed on the *Mercato Telematico Azionario* operated by Borsa Italiana S.p.A. and on the New York Stock Exchange in the form of ADSs (American Depository Shares, each of which represents ten ordinary or savings shares). As regards the listing of Telecom Italia's ordinary shares on the Frankfurt Stock Exchange, in the light of the decisions adopted by the Board of Admission of the Frankfurt Stock Exchange, the shares will be delisted by the effective date of the Merger.

1.1.11 Lastly, it should be noted that Article 22 of Telecom Italia's bylaws contains clauses which, pursuant to Article 2 of Law 474 of 30 July 1994, grant the Minister for the Economy and Finance certain special powers, to be exercised in agreement with the Minister for Productive Activities.

At the end of the meeting of Telecom Italia's Board of Directors on 7 December 2004, pursuant to Article 22.b) of the bylaws and Article 2 of Law 474 of 30 July 1994, the company notified the Minister for the Economy and Finance of the commencement of the plan for the reorganization of the Group.

The Minister for the Economy and Finance, in agreement with the Minister for Productive Activities, has notified Telecom Italia that he does not consider that the conditions exist for the exercise of the veto right with respect to the adoption of the Merger resolution by Telecom Italia's shareholders' meeting.

1.2 Companies participating in the Merger

1.2.1 Telecom Italia, together with the group of which it is the parent company, is one of the leading international groups operating in the telecommunications services sector and, more generally, in the information and communications technology sector.

The following tables provide selected historical operating, cash flow and financial data for the Telecom Italia Group and Telecom Italia, as reported in the financial statements for the first nine months of financial years 2004 and 2003 and in the 2003 financial statements.

Selected operating, cash flow and financial data for the Telecom Italia Group and Telecom Italia

TELECOM ITALIA GROUP

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	22,912	22,682	30,850
Gross operating profit	10,788	10,648	14,280
Operating income before amortization of goodwill on consolidation differences	6,607	6,639	8,619
Operating income	5,442	5,214	6,789
Income before taxes	3,690	3,858	3,442
Consolidated net income before minority interests	1,518	2,889	2,428
Consolidated net income: Telecom Italia	745	1,881	1,192
Consolidated cash flow[1]	6,399	7,901	9,207
Free cash flow from operations[2]	6,585	7,360	9,233

1. *Calculated as: Consolidated net income (loss) before minority interests plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	52,635	54,573	55,892
Working capital	(1,824)	(638)	(462)
Net invested capital	50,811	53,935	55,430
Financed by:			
Consolidated shareholders' equity:	19,390	20,589	21,177
• Telecom Italia	15,141	16,092	16,814
• Minority interests	4,249	4,497	4,363
Consolidated net financial debt:	31,421	33,346	34,253
• Medium/long-term	34,020	30,545	28,806
• Short-term	(2,599)	2,801	5,447

TELECOM ITALIA S.p.A.

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	11,793	11,872	16,033
Gross operating profit	5,526	5,510	7,433
Operating income	3,256	3,169	4,139
Income before taxes	1,664	1,378	1,728
Net income	894	2,012	2,646
Cash flow[1]	2,897	4,121	5,565
Free cash flow from operations[2]	3,782	3,669	4,702

1. *Calculated as: Net income (loss) plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	47,544	48,604	49,858
Working capital	230	3,079	1,063
Net invested capital	47,774	51,683	50,921
Financed by:			
Shareholders' equity:	15,533	16,356	15,688
• Share capital	8,858	8,854	8,846
• Reserves and retained earnings	5,781	4,856	4,830
• Net income for the period	894	2,646	2,012
Net financial debt (positive financial position)	32,241	35,327	35,233
• of which short-term	3,286	14,635	13,199

1.2.2 Tim, together with the group of which it is the parent company, is one of the leading international groups operating in the telecommunications services sector, and more specifically in mobile telecommunications under license or in a free market. Its activities include the design, implementation, management and sale of telecommunications, information and communication technology and electronic systems. Tim's main international markets are in South America and the Mediterranean basin.

The following tables provide selected historical operating, cash flow and financial data for the Tim Group and Tim, as reported in the financial statements for the first nine months of financial years 2004 and 2003 and in the 2003 financial statements.

Selected operating, cash flow and financial data for the Tim Group and Tim

TIM GROUP

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	9,499	8,635	11,782
Gross operating profit	4,574	4,157	5,502
Operating income before amortization of goodwill on consolidation differences	3,199	3,021	3,885
Operating income	3,129	2,944	3,786
Income before taxes	3,100	3,441	4,207
Consolidated net income before minority interests	1,724	2,041	2,456
Consolidated net income: Parent Company	1,664	1,970	2,342
Consolidated cash flow(1)	3,048	3,156	3,998
Free cash flow from operations(2)	2,829	3,123	3,746

1. *Calculated as: Consolidated net income before minority interests plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	9,247	9,276	9,064
Working capital	(1,925)	(2,407)	(2,015)
Net invested capital	7,322	6,869	7,049
Financed by:			
Consolidated shareholders' equity:	7,382	7,803	7,535
• Parent Company	6,827	7,295	7,049
• Minority interests	555	508	486
Consolidated net financial debt	(60)	(934)	(486)
• Medium/long-term	490	585	668
• Short-term	(550)	(1,519)	(1,154)

TIM S.p.A.

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	7,381	6,980	9,469
Gross operating profit	4,076	3,805	5,035
Operating income	3,201	2,969	3,863
Income before taxes	3,376	3,081	3,852
Net income	2,143	1,846	2,322
Cash flow(1)	2,977	2,634	3,405
Free cash flow from operations(2)	3,038	3,409	4,201

1. *Calculated as: Net income (loss) plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	9,741	9,161	8,576
Working capital	(1,347)	(1,622)	(1,170)
Net invested capital	8,394	7,539	7,406
Financed by:			
Shareholders' equity:	8,899	8,957	8,481
• Share capital	514	514	514
• Reserves and retained earnings	6,242	6,121	6,121
• Net income for the period	2,143	2,322	1,846
Net financial debt	(505)	(1,418)	(1,075)
• of which short-term	(505)	(1,418)	(1,075)

1.3 Reasons for the Merger, business objectives and plans to achieve them

The Merger satisfies a series of business needs prompted by the progressive, increasing integration between fixed and mobile communications platforms. The evolution of the market and the defense of the creation of value also require an adaptation of business models and organizational strategies, an objective that the merger by incorporation of Tim into Telecom Italia is intended to promote, in order to strengthen the competitiveness of the post-Merger company.

To capture the benefits made available by the integration of platforms and services, at a time of significant technological discontinuity, it is desirable to undertake a corporate structural reorganization that will guarantee the unitary governance of business processes that a situation of partial control of capital does not fully allow. The corporate integration that will be implemented will make it possible to overcome the constraints inherent in the existing ownership structure, notwithstanding the scope for coordination typical of a group structure. Today, in fact, the process of integration is inevitably conditioned by the existence of two sets of shareholders in the market, whose interests have to be pursued separately as regards strategic investments and business plans. Only complete integration can overcome these limitations, by eliminating every possible conflict and simultaneously promoting the most efficient distribution of costs and benefits between the parent company and the subsidiary.

The reorganization will make it possible to respond to the need for integration expressed by customers, to capitalize on the complementary features of the services offered in order to foster consumption, and at the same time to capture all the benefits deriving from the synergies between the different business areas.

The demand for telecommunications services is growing, driven by the spread of broadband in wireline business and by the new services supplied in the mobile segment. In particular:

– electronic communications on the wireline network have enriched the supply of traditional "voice" and "data" services by adding the innovative services made possible by XDSL technology and fiber optics;

– electronic communications on the new-generation mobile networks (GPRS, EDGE and UMTS) now afford mobility not only for voice services but also for data, Internet and media services.

There are sectors in which customers increasingly feel the need to use the services made possible by the new technologies seamlessly, regardless of where they are. Furthermore, technological innovation is significantly increasing the interaction between the different networks (fixed and mobile, voice and data) and between the supply of telecommunications services and that of adjacent sectors, such as information technology, media and consumer electronics.

The leading manufacturers of telecommunications equipment and terminals have oriented their technological investments to satisfying the market's new needs:

– telecommunications networks are rapidly evolving into "multimedia networks" thanks to the spread of the IP protocol and the adoption of homogeneous wireline and mobile multiservice platforms;

– the new wireline and mobile terminals satisfy multiple functions and convergent handsets permit seamless access to wireline and mobile services.

The rapid spread of this equipment will allow telecommunications operators to benefit from the potential synergies deriving from a more closely integrated management of wireline and mobile electronic communications businesses and thus to be well positioned to cope with a scenario likely to be characterized by the saturation of the market in traditional telephone services and the trend of eroding prices and margins.

The leading operators in the Italian and European telecommunications market are preparing to respond to the latest technological and market developments on three main fronts:

– better coordination and distribution of customer relations between the various segments (integration of sales channels and responsibilities for specific segments, brand management);

– strengthening of certain critical functions for comparative advantage (guidance of IT and network technological choices; management of research; purchasing; content acquisition and management; and coordination of supply policies);

– defense of margins through programs to recoup efficiency by exploiting synergies across the different business areas (common management of IT and network infrastructures, convergent evolution of applications platforms, and common content acquisition and management).

In this setting, the Telecom Italia Group already ranks in the top tier among European competitors in all business areas in terms of growth, profitability and product innovation. This is the result of the substantial investments made in technological innovation, which today provide the Group with a network infrastructure considered future-proof, ready to host and handle the portfolio of new generation products and services.

As mentioned above, however, the evolution of the market and the defense of the creation of value also require an adaptation of current business models and organizational strategies, an objective that the merger by incorporation of Tim into Telecom Italia is intended to promote.

The Merger, together with the Spin-Off, will simplify the Group's ownership structure by maintaining the domestic mobile communications business under an unlisted, wholly owned subsidiary of Telecom Italia, thereby creating optimal conditions for grasping the opportunities to realize the synergies referred to above.

The following additional advantages will also be pursued through the Merger:

– to optimize financial and cash flows within the Group by managing Group debt more efficiently and making better use of financial leverage. At the same time, Telecom Italia's current shareholders will have access to all the cash flow generated by the mobile communications business;

– to enable Telecom Italia to optimize, in conjunction with the Tender Offer, its own financial structure and to reduce the weighted average cost of capital employed compared with its current cost. In fact, the purchase of Tim shares is financed by means of an increase in net financial debt, whose cost, net of the tax effect, is lower than the cost which would have been incurred by the additional amount of equity not issued in exchange for Tim shares acquired in the Tender Offer. The consequent reduction in the weighted average cost of capital is likely to favor the full value potential of the shares of Telecom Italia as the company resulting from the Merger and thus the creation of value for the shareholders.

As mentioned above, the Merger serves to promote the adaptation of the Group's business models and organizational strategy to the evolution of the market and the defense of the creation of value for shareholders.

The integration process, involving actions designed to improve efficiency and to enhance strategic and operational effectiveness, primarily concerns the Networks and Information Technology, Customer Operations, the Supply of Innovative Services and Sales Channels business areas and will be implemented in compliance with applicable sector and antitrust laws. The main projects under consideration concern:

Networks and Information Technology

- Joint development of network and platform architectures for wireline and mobile products and services;
- Integration and synergies in connection with networks for access traffic and IP backbone traffic, for example, through joint planning of requirements and development processes;
- Joint development, operation and maintenance of network information systems;
- Design of the new integrated network model.

Customer Operations

- Joint development of IT applications providing support for the management of the business;
- Increase in customer care efficiency and service levels by adoption of the best practices developed in Telecom Italia and Tim;
- Synergies in connection with the supply of customer information services (e.g., the 12 and 412 customer information services).

Supply of Innovative Services and Sales Channels

- Development of convergent services for the consumer market (e.g., seamless access to mail, interoperability of fixed and mobile services, and standardization of mimicking) and for the business market (e.g., mobile use of corporate applications by means of extended enterprise models);
- Increase in the effectiveness of sales channels and search for efficiency gains in overlapping commercial services while maintaining separate offers;
- Development of a multimedia portal accessible from fixed and mobile network terminals and enhancement of Group contents and brands.

Procurement

- Optimization of the distribution logistics for commercial products;
- Exploitation of the synergies between network operating structures and joint evaluation of make-or-buy options;
- Elimination of duplication and harmonization of service standards in Facility Management and General Services.

Working groups have been formed to define the scope for integration, specify and develop integration plans and lay down how they are to be implemented. The groups are headed by an Integration Committee that provides guidance and control, by ensuring observance of specific responsibilities over the development of the overall integration plan. Consistently with the integration plan, the organizational and operational restructuring will be based on three guidelines: a market plan aimed at increasing the effectiveness of customer relations; an efficiency plan for the rationalization of internal and external structures; and an organizational development plan. The synergies expected from the Merger, the broad outlines of which have already been identified and whose economic benefits and other advantages will be detailed and announced by mid-April 2005, are the result of analyses and evaluations undertaken by the managers involved in the integration plans referred to above.

2. The values attributed to Telecom Italia and Tim for the purpose of determining the exchange ratio

For the valuations needed to establish the exchange ratio, Telecom Italia’s Board of Directors was assisted by qualified financial advisors, namely JPMorgan Chase Bank N.A. (“**JPMorgan**”), Mediobanca and MCC, acting as Lead Advisors. Furthermore, in accordance with international best practice, the Committee responsible for internal control and corporate governance (consisting exclusively of independent directors) appointed as additional financial advisor Goldman Sachs International (“**Goldman Sachs**”).

Telecom Italia’s Board of Directors — taking into account the foreseen distribution of dividends on Telecom Italia and TIM shares in April 2005, assumed to be in line with the respective dividends per share paid in May 2004, and after careful analysis of the valuations presented by the financial advisors, with whose valuation methodologies applied and described in Section 3 below it agreed — has identified the following ranges for the values of the shares of the companies participating in the Merger for purposes of establishing the exchange ratio:

	Minimum	Mean	Maximum
Values per Tim ordinary share (euros)	**5.07**	**5.33**	**5.58**

	Minimum	Mean	Maximum
Values per Tim savings share (euros)	**5.05**	**5.31**	**5.57**

	Minimum	Mean	Maximum
Values per Telecom Italia ordinary share (euros)	**2.89**	**3.12**	**3.34**

	Minimum	Mean	Maximum
Values per Telecom Italia savings share (euros)	**2.09**	**2.25**	**2.41**

It should be noted that the values in the above tables, as well as those in all the tables in Section 3 below, have been rounded, albeit without any material impact on the results.

3. The exchange ratio established and the methods applied in its determination

3.1 Valuation methodologies applied

3.1.1 As a preliminary matter, it should be noted that the aim of the valuation of the companies participating in a merger is to obtain values that are meaningfully comparable.

Consistent with this objective, and in accordance with standard practice, a uniform yardstick must be adopted throughout the whole valuation process in order to protect the interests of the shareholders of Telecom Italia and Tim, respectively. This does not necessarily mean that identical valuation methods must be used for all the companies directly or indirectly involved in a merger, especially if they operate in different sectors, but rather that the same approach to valuation must be adopted.

Since, as mentioned above, the exclusive objective of merger valuations is to establish meaningfully comparable values, it must be emphasized that the methods adopted in the context of valuations for merger purposes and the related results may differ from those used for valuations having different purposes.

Accordingly, the exchange ratio was established by applying valuation methodologies that are commonly used in Italy and internationally for transactions of this kind and for businesses active in the relevant sectors.

In particular, account was taken of the comparative valuation of the companies involved and priority was given to the homogeneity and comparability of the criteria applied rather than a simple estimate of the equity value of each company on a stand-alone basis.

In this perspective, the valuations were undertaken considering, as required, the two companies as separate entities notwithstanding the strategic, operational and financial synergies expected from the Merger, as well as control premiums and minority discounts associated with the holding of equity interests.

3.1.2 For the valuation of Tim, the fundamental method applied was the Discounted Cash Flow method.

The Discounted Cash Flow method determines the value of a company or an economic activity as a whole. It is based on the assumption that the value of a company or an economic activity is equal to the present value of future cash flows. These flows can be determined analytically as follows:

+ Earnings before interest and tax (EBIT)

- Taxes

+ Depreciation and other non-cash allowances

- Fixed investments

+/- Change in net working capital

Under this method, the value of the economic capital of a company or an economic activity is equal to the sum of (i) the discounted value of the expected cash flows and (ii) the terminal value of the company or the economic activity, less (iii) the net financial debt and minority interests, as expressed by the following formula:

$$W = \sum_{t=1}^{n} \frac{FC_t}{(1+WACC)^t} + \frac{VT}{(1+WACC)^n} - DF_{t0}$$

where:

W	=	Value of the economic capital
FC t	=	Annual cash flow expected in period t
VT	=	Terminal value
DF	=	Net financial debt and minority interests at time t=0
n	=	Number of projection periods
WACC	=	Weighted average cost of capital

The terminal value is the value of the company or economic activity to be valued at the end of the period covered by the projections and is determined assuming that the duration of the business is unlimited.

The terminal value was determined using two alternative methods:

(i) the perpetual growth method in accordance with the following formula:

$$VT = FC / (WACC - g)$$

where:

VT	=	Terminal value
FC	=	Normalized cash flow
g	=	Perpetual growth rate
WACC	=	Weighted average cost of capital

(ii) the exit multiple method, according to which the terminal value is determined based on a multiple of the EBITDA expected for the last year of the period covered by the projections considered.

The terminal value obtained in this way is treated as if it were an additional cash flow and thus is discounted using the weighted average cost of capital, which represents the weighted average (on the basis of the financial structure of the company economic activity) of the costs of the different forms of financing used (equity capital and debt capital net of tax effects):

$$WACC = Kd\,(1 - t)\,\frac{D}{D + E} + Ke\,\frac{E}{D + E}$$

where:

Kd	=	Cost of debt capital
Ke	=	Cost of equity capital
D	=	Debt capital
E	=	Equity capital
t	=	Tax rate

In particular, the cost of debt capital represents the long-term interest rate applicable to companies or economic activities with a similar risk profile, net of the tax effect. The cost of equity capital, in contrast, reflects the rate of return expected by the investor taking into account the relative risk, calculated using the Capital Asset Pricing Model, expressed in accordance with the following formula:

$$K_e = R_f + ß(R_m - R_f)$$

where:

K_e	=	Cost of equity capital
R_f	=	Rate of return on risk-free investments
ß	=	Coefficient that measures the correlation between the rate of return expected on an investment and the rate of return expected on the reference equity market
Rm	=	Expected equity market rate of return
(Rm – Rf)	=	Risk premium required by the equity market compared to the rate of return on risk-free investments

3.1.3 For the valuation of Telecom Italia, the fundamental method applied was the Sum-of-the-Parts method, which represents standard market practice for the valuation of a group operating in several sectors.

Under the Sum-of-the-Parts method, the value of a company's economic capital is calculated as the sum of the values of its separate units, as economic entities that can be valued independently, suitably adjusted to take into account the company's financial position and minority interests, where material, and other factors such as off-balance-sheet items and potential tax benefits.

As regards the separate units, in view of the complexity and extent of the structure of the Telecom Italia Group and of the many sectors in which it operates, it was deemed advisable to value each of them on the basis of the methodologies considered most appropriate to the specific circumstances. In particular, the valuation of the principal assets was based on the Discounted Cash Flow method, while the remaining assets, which are of limited importance in the overall valuation, were valued using, depending on the circumstances, the stock market price method, the market multiples method, balance sheet values, the Discounted Cash Flow method and/or the values published in analysts' research reports on such activities, where available.

3.1.4 The exchange ratios obtained by applying the above methods were tested using the stock market price method, which, in this case involves a consideration of the ratio between the stock market prices of the shares of the companies participating in the merger.

This method is considered significant in merger valuations when the average volumes traded are large; in such circumstances, the prices established by the financial markets provide a meaningful baseline for purposes of a comparison of the profitability, soundness, growth prospects and risk profile of the companies from the perspective of investors and thus for the ratio between the values of the companies involved in the merger.

In applying this method, it is necessary to strike a balance between the need to mitigate the volatility of daily share prices by considering a sufficiently long period and the need to use recent data that are indicative of the market values of the companies in question.

Since both Tim and Telecom Italia are listed on Borsa Italiana's *Mercato Telematico* electronic share market and are among the largest Italian companies in terms of market value, it was considered that the stock market prices method constituted a reliable benchmark.

3.2 Application of the chosen valuation methodologies

This subsection contains a description of the manner in which the valuation methods discussed in Subsection 3.1 above were applied to the companies participating in the Merger in order to determine the exchange ratios.

In the case of the activities for which the Discounted Cash Flow method was used, as mentioned in the previous subsection, the method was applied with a view to determining the fundamental value of the companies for financial investors and on the basis of the following approach:

– reference was made to the cash flows of the individual activities as set forth in the business and financial plans developed by the business units of the Telecom Italia Group;
– the growth rates used for the financial projections beyond 2007, used by certain financial advisors, as well as the growth rates for the calculation of the terminal value in accordance with the perpetual growth method, reflect growth prospects consistent with the relevant market benchmarks. The terminal value, where determined on the basis of this method, is consistent with the multiples implicit in the current prices of comparable companies. Moreover, multiples of comparable companies represent the basis for the calculation of the terminal value using the alternative exit multiple method;
– the weighted average cost of capital (WACC) reflects assumptions which are consistent with market benchmarks relating to the cost of debt capital and the cost of equity capital (rate of return on risk-free investments, Beta coefficient, risk premium required by the equity market), as well as with the capital structure of the activity to be valued.

In applying the Discounted Cash Flow method, reference was made to the cash flows from operations for the main activities based on the update, for the period 2004-2007, of the business and financial plans approved and announced to the market in March 2004. The plans were developed by management in accordance with the strategic, operating and financial objectives of the Group. Both the average annual organic growth rate (i.e. at constant scope of consolidation and exchange rates) of EBITDA (2003-2006 compound annual growth rate, or CAGR, in excess of 5.5%) and the Net Financial Position at 31 December 2004 (less than Euro 30 billion) were confirmed.

As regards the main Business Units, on the one hand, fixed telephony, in a market which continues to enjoy prospects of an average annual growth rate higher than 2%, confirms an average annual organic growth rate of EBITDA in excess of 2%, primarily due to a stable customer base, achieved by broadening the range of wireline services and products offered and by the growth of broadband services in Italy and abroad (France and Germany), also driven by the launch of new value added services (VAS) and innovative content.

On the other hand, mobile telephony confirms its main growth drivers in the domestic business: development and differentiation of the wireless services and products offered: enhancement of value added services (multi-messaging and interactive VAS); customer focus; technological strength (EDGE/UMTS and combined services); and an increase in the average revenue per user (ARPU). The growth of the international business, where it has been decided to exit the Venezuelan market, continues to be driven by Brazil. In Brazil, a substantial expansion of the customer base is expected and the second position will be maintained through the continuation of the strengthening of customer care, brand development and positioning innovation in the services and products offered, and improved territorial coverage. This allows a double-digit EBITDA average annual organic growth trend for the mobile communications activity as a whole and gross operating profits of more than 53% for the Italian market to be confirmed, in line with the figures announced to the market.

In reaching its own conclusions, Telecom Italia's Board of Directors acknowledged that, among a number of available valuation methods, each financial advisor used those valuation methods deemed more appropriate considering the activities of both the Absorbing Company and the Company to be Absorbed, and that, in spite of the different methods adopted, all financial advisors reached consistent conclusions.

3.2.1 Tim

As mentioned above, Tim was valued using the Discounted Cash Flow methodology as the fundamental method, for verification and control purposes, the methodologies of market multiples, transaction multiples and the values published in analysts' research reports, where available, were used.

The estimated Net Financial Position at 31 December 2004, adjusted to take account of minority interests, where material, the effects of the expected sale of Corporacion Digitel (Venezuela) and certain tax benefits, was added to the value calculated in accordance with the methodologies mentioned in the preceding paragraph.

The table below shows the minimum, mean and maximum values per Tim ordinary share, obtained using the fundamental method described above, before the distribution of dividends expected in April 2005, and thus before the completion of the Merger.

	Minimum	Mean	Maximum
Values per Tim ordinary share (euros)	**5.32**	**5.58**	**5.84**

The table below shows the minimum, mean and maximum values per Tim savings share calculated on the basis of the average market discount of the last month, last three months and last six months before 3 December 2004, as well as the discount on the last day of trading of Telecom Italia and Tim shares before the announcement of the transaction (3 December 2004), resulting in the application of a discount of approximately zero.

	Minimum	Mean	Maximum
Values per Tim savings share (euros)	**5.31**	**5.58**	**5.84**

The table below shows the minimum, mean and maximum values per Tim ordinary and savings share, obtained using the fundamental method described above, and adjusted for the distribution of dividends expected in April 2005.

	Minimum	Mean	Maximum
Values per Tim ordinary share (euros)	**5.07**	**5.33**	**5.58**
Values per Tim savings share (euros)	**5.05**	**5.31**	**5.57**

It should be noted that the potential exercise of financial instruments that may give rise to the subscription of Tim shares (stock options) was taken into account solely to the extent that their exercise was reasonably likely on the basis of their relative profitability.

3.2.2 *Telecom Italia*

As mentioned above, Telecom Italia was valued using the Sum-of-the-Parts methodology as the fundamental method.

In applying this method, the valuation of the principal activities (Telecom Italia S.p.A. and Tim) was based primarily on the Discounted Cash Flow method. In particular, Tim was valued based on the range of values obtained using this method. Depending on the circumstances, the remaining activities – listed below – were valued using the stock market price method, the market multiples method, balance sheet values, the Discounted Cash Flow method and/or the values published in analysts' research reports on such activities, where available:

- fixed telephony activities included in the Wireline division but outside the perimeter of Telecom Italia S.p.A.;
- Telecom Italia Media group;
- IT Services Market division;
- Olivetti Tecnost group;
- equity interests in Entel Bolivia and Entel Chile;
- other activities and equity interests.

The estimated net financial position at 31 December 2004, adjusted to take account of the effects of the proportional net indebtedness and minority interests, where material, certain off-balance-sheet items and tax benefits, as well as the pro forma effect of the conversion of the Telecom Italia 1.5% 2001-2010 convertible bonds with redemption premium (consistent with the fully-diluted method, which assumes the conversion into ordinary shares), was added to the sum of the values obtained in the manner described in the preceding paragraph.

The Telecom Italia treasury shares held both directly and indirectly were valued using the method which consists in determining the value of a Telecom Italia share by dividing the value of the company's economic capital (calculated without considering the holding of treasury shares) by the number of shares (fully-diluted), excluding the treasury shares.

The table below shows the minimum, mean and maximum values per Telecom Italia ordinary share, obtained using the Sum-of-the-Parts fundamental method, before the distribution of dividends expected in April 2005, thus before the completion of the Merger.

	Minimum	Mean	Maximum
Values per Telecom Italia ordinary share (euros)	**2.99**	**3.22**	**3.44**

The table below shows the minimum, mean and maximum values per Telecom Italia savings share calculated on the basis of the average market discount of the last month, last three months and last six months before 3 December 2004, as well as the discount on the last day of trading of Telecom Italia and Tim shares before the announcement of the transaction (3 December 2004), resulting in a discount of between 26% and 27%.

	Minimum	Mean	Maximum
Values per Telecom Italia savings share (euros)	**2.21**	**2.37**	**2.52**

The next table shows the minimum, mean and maximum values per Telecom Italia ordinary and savings share, obtained using the Sum-of-the-Parts fundamental method, and adjusted for the distribution of dividends expected in April 2005.

	Minimum	Mean	Maximum
Values per Telecom Italia ordinary share (euros)	**2.89**	**3.12**	**3.34**
Values per Telecom Italia savings share (euros)	**2.09**	**2.25**	**2.41**

It should be noted that the potential exercise of financial instruments that may give rise to the subscription of Telecom Italia shares (stock options and convertible bonds) was taken into account solely to the extent that their exercise was reasonably likely on the basis of their relative profitability.

It should also be noted that the effects of the Offer for Tim ordinary and savings shares do not require the Exchange Ratio to be altered since the Offer was made on terms consistent with the valuations used to determine the Exchange Ratio. In fact, in the context of the valuation of Telecom Italia, the acquisition of the Tim shares tendered in the Offer increases the value of the equity interest in Tim substantially equivalent to the increase in Telecom Italia's net financial debt, which, moreover, will be at a level consistent with Telecom Italia's current rating. The overall effect is that the value of Telecom Italia's equity will remain substantially unchanged.

3.2.3 Determination of the exchange ratios

The following table summarizes the range of the estimates of the exchange ratios calculated in accordance with the methods and the criteria discussed in the preceding subsections, as the quotient of the estimated value per Tim ordinary and savings share and the estimated value per Telecom Italia ordinary and savings share using the minimum and maximum values of the ranges reported earlier.

	Minimum	Mean	Maximum
Telecom Italia ordinary shares per Tim ordinary share	**1.67**	**1.71**	**1.75**
Telecom Italia savings shares per Tim savings share	**2.31**	**2.36**	**2.42**

The Board of Directors, in the light of the information provided by JPMorgan, Mediobanca, and MCC, as well as Goldman Sachs, and after considering the results of the application of the above-mentioned valuation methods, reached a conclusion with regard to the ratios existing between the economic values of the two companies participating in the Merger.

This conclusion was then compared with that reached by the Board of Directors of Tim, in taking into consideration the information provided by its own advisors, Lazard & Co. S.r.l and Credit Suisse First Boston, as well as Merrill Lynch International Milan office and Studio Casò, represented by Dott. Angelo Casò, who were directly appointed by Tim's Committee for Internal Control (consisting exclusively of independent directors).

At the end of the valuation process and the comparison between the results obtained, the Board of Directors of Telecom Italia and the Board of Directors of Tim determined that:

(i) the exchange ratio on the basis of which the assignment of the ordinary shares of Telecom Italia will be made is:

1.73 Telecom Italia ordinary shares, with a par value of Euro 0.55 per share
for each
1 Tim ordinary share, with a par value of Euro 0.06;

(ii) the exchange ratio on the basis of which the assignment of the savings shares of Telecom Italia will be made is:

2.36 Telecom Italia savings shares, with par value of Euro 0.55 per share
for each
1 Tim savings share, with a par value of Euro 0.06.

The above exchange ratios must be verified by the experts appointed under Article 2501-*sexies* of the Civil Code, namely the accounting firm of Reconta Ernst & Young S.p.A., appointed by the Turin Court, for Tim, and the accounting firm of Mazars & Guerard S.p.A., appointed by the Milan Court, for Telecom Italia, for purposes of issuing the opinion required by law.

3.2.4 Control methodologies

In order to verify the accuracy of the exchange ratios determined applying the methodologies described above, a further check was made using the stock market price method.

The method was applied taking into consideration the average exchange ratios (Telecom Italia ordinary shares per Tim ordinary share and Telecom Italia savings shares per Tim savings share) expressed by the market in different periods prior to the day on which Borsa Italiana S.p.A. suspended trading in the Telecom Italia and Tim securities in view of the forthcoming announcement of the transaction (the ratios given by the official prices recorded on 3 December 2004 and the averages of the official prices in the preceding 1, 3, 6 and 12 months), adjusted for the effect of the distribution of dividends expected in April 2005, before the completion of the Merger.

In contrast, the stock market prices of Tim and Telecom Italia shares after the announcement of the transaction were not taken into account because they were affected by the announcement and were therefore not deemed to be relevant.

The following table shows the average exchange ratios obtained with reference to the different periods specified above.

	3/12/04	1 month	3 months	6 months	12 months	12 months*
Telecom Italia ordinary shares per Tim ordinary share	**1.72**	**1.69**	**1.71**	**1.74**	**1.75**	**1.74**
Telecom Italia savings shares per Tim savings share	**2.47**	**2.41**	**2.36**	**2.39**	**2.44**	**2.45**

* *Average exchange ratios calculated by adjusting the official prices before 24 May 2004 for the distribution of reserves made that day.*

The next table shows the minimum, mean and maximum values of the average exchange ratios (Telecom Italia ordinary shares per Tim ordinary share and Telecom Italia savings shares per Tim savings share) expressed by the stock market in the periods considered above.

	Minimum	Mean	Maximum
Telecom Italia ordinary shares per Tim ordinary share	**1.69**	**1.72**	**1.75**
Telecom Italia savings shares per Tim savings share	**2.36**	**2.42**	**2.47**

The above figures are consistent with the exchange ratios determined using the fundamental values described in the previous subsection.

4. Procedure for assigning Telecom Italia shares

The newly issued shares earmarked for the exchange will be assigned to the persons entitled to such shares, through their authorized intermediaries who are participants of the Monte Titoli S.p.A. central securities depository, at the effective date of the Merger.

Non-dematerialized Tim shares may only be exchanged upon delivery of such shares to an authorized intermediary for deposit with the central securities depository on a dematerialized basis.

As part of the procedure for the assignment of Telecom Italia shares, the authorized intermediaries will provide Tim minority shareholders with a service to handle any fractions of shares, at market prices and at no cost in terms of expenses, stamp duty or commissions, that will permit the number of newly issued shares to which the shareholders are entitled on the basis of the exchange ratios to be rounded up or down to the nearest whole number.

5. Effective date of the Merger and entitlement date

Pursuant to Article 2504-*bis*, second paragraph, of the Civil Code, the Merger will be effective from the date of the last filing of the merger deed required by Article 2504, or from such later date as may be specified in the merger deed itself.

Accordingly, as of the effective date of the Merger, Telecom Italia will assume all of Tim's assets, rights and liabilities. Since the Spin-Off is to occur before the Merger is effective, Tim Italia will succeed to all the permits, concessions, licenses and administrative authorizations held by Tim for the provision of mobile communications services in Italy. The Merger will therefore result in Telecom Italia succeeding only to such Tim assets and liabilities as have not been transferred in connection with the Spin-Off.

In accordance with the combined effect of Articles 2504-*bis*, third paragraph, and 2501-*ter*, first paragraph, subparagraph 6, of the Civil Code, the transactions effected by Tim will be attributed to and recorded in Telecom Italia's accounts as of 1 January of the year in which the Merger becomes effective, or 1 January 2005, in accordance with the planned timetable for the Merger. The same date will apply to the tax effects, pursuant to Article 172.9 of Presidential Decree No. 917 of 22 December 1986.

The Telecom Italia shares issued in the exchange will have normal entitlement to all the rights appertaining thereto and will therefore have equivalent rights to the Telecom Italia shares outstanding at the time of issuance.

6. Italian Tax Effects of the Merger on Telecom Italia and Tim

6.1 Tax neutrality

For Italian income tax purposes, pursuant to Article 172.1 of the Consolidated Income Tax Law (Presidential Decree No. 917 of 22 December 1986), the Merger is tax neutral and therefore does not constitute a sale or distribution of capital gains and losses on the assets of the merged or incorporated company, including inventories and goodwill.

6.2 Merger goodwill

As regards the position of Telecom Italia, there is no merger goodwill to be recognized as income for tax purposes, and thus merger differences will have no material tax impact.

6.3 Reserves for tax-deferred income

The reserves for tax-deferred income reported in Tim's latest financial statements, and existing at the effective date of the Merger, will be treated in accordance with the specific provisions of Article 172.5 of Presidential Decree No. 917 of 22 December 1986, and, if applicable, will be re-established.

6.4 Registration fee

The merger deed is subject to a registration fee of €129.11, pursuant to Article 4.b) of the first part of the schedule attached to Presidential Decree No. 131 of 26 April 1986.

6.5 Italian Tax Effects on shareholders of Telecom Italia

Pursuant to Article 172.3 of Presidential Decree No. 917 of 22 December 1986, the exchange of Tim shares for Telecom Italia shares does not constitute a sale, a distribution of capital gains or losses, or a source of income, as the transaction merely involves the replacement in shareholders' portfolios of the shares of Tim by shares of Telecom Italia. Accordingly, the basis in the Tim shares will be transferred to the shares obtained in the exchange.

* * *

Shareholders resident in countries outside Italy are urged to consult their own tax advisors about the tax effects of the Merger in their own jurisdictions.

7. Expected major shareholdings and control of Telecom Italia

At 23 January 2005, on the basis of Telecom Italia's shareholder register and the disclosures made by shareholders pursuant to Article 120 of Legislative Decree No. 58 of 24 February 1998, persons holding directly or indirectly more than 2% of Telecom Italia's outstanding ordinary shares with voting rights were as follows:

Shareholders	Number of ordinary shares held	% of ordinary share capital
Olimpia S.p.A.	1,751,765,823	16.96
Brandes Investment Partners LLC (*)	372,896,243	3.61
Hopa S.p.A. (**)	361,364,703	3.50
Assicurazioni Generali S.p.A. (***)	288,964,287	2.80
Bank of Italy (****)	231,499,817	2.24

* *Disclosure pursuant to Article 121.3 of the Regulation on Issuers.*

** *Shares held through the subsidiary company Holinvest S.p.A.*

*** *The list of companies through which the shares are held is available on the Internet at www.consob.it.*

**** *Shares partly held by the Bank of Italy's supplementary pension fund.*

Telecom Italia's post-Merger shareholdings will be affected by a number of factors and, in particular, by the conversion of Telecom Italia (formerly Olivetti) 1.5% 2001-2010 convertible bonds with redemption premium and the number of Telecom Italia and Tim stock options that are exercised. As regards the bonds, at 21 January 2005 conversion requests had been received for 463,187,994 additional Telecom Italia shares, compared to the share capital recorded in the Company Register at the same date.

The following table summarizes the foreseeable composition of Telecom Italia shareholders with holdings in excess of 2% of the ordinary share capital, assuming that no bonds are converted (in addition to those related to the requests submitted by 21 January 2005, which are not yet reflected in Telecom Italia's share capital filed with the Company Register but are considered for purposes of this analysis) and that no stock options are exercised.

The table is based exclusively on information in the Telecom Italia shareholders' register or disclosed by shareholders pursuant to Article 120 of Legislative Decree No. 58 of 24 February 1998.

Shareholders	Number of ordinary shares held	% of ordinary share capital
Olimpia S.p.A.	1,751,765,823	13.46
Brandes Investment Partners LLC	372,896,243	2.87
Hopa S.p.A.	361,364,703	2.78
Assicurazioni Generali S.p.A.	288,964,287	2.22

It is also worth noting that, on 21 December 2004, Olimpia S.p.A. announced the approval by its extraordinary shareholders' meeting of an increase in capital of €2 billion by means of a rights issue, the proceeds of which will be used to purchase Telecom Italia shares. On 23 January 2005, Olimpia S.p.A. further announced that it had entered into two forward contracts to buy Telecom Italia ordinary shares and bonds convertible into Telecom Italia ordinary shares, respectively. The execution of these contracts – subject to the subscription of the above-mentioned capital increase – will entail an expenditure of appropriately €1 billion. On the same date, Olimpia S.p.A. also announced that the other parties to the contracts already held shares and convertible bonds corresponding to approximately 310 million Telecom Italia ordinary shares.

Upon completion of the Merger, no shareholder is expected to control Telecom Italia.

8. Effects of the merger on shareholders' agreements falling within the scope of Article 122 of Legislative Decree No. 58 of 24 February 1998

The parties to the shareholders' agreements falling within the scope of Article 122 of Legislative Decree No. 58 of 24 February 1998 that concern the companies participating in the Merger have not made any notifications concerning the possible effects of the transaction on such agreements.

9. Amendments to the bylaws

As mentioned above, in connection with the Merger, Article 5 of Telecom Italia's bylaws concerning the company's share capital will be amended as necessary to take into account the issuance of shares in relation to the exchange ratios referred to in Section 4 above.

The maximum increase in Telecom Italia's share capital for the purposes of the share exchange,

- considering the maximum amount by which Tim's existing share capital may be increased, among other things, as a consequence of the exercise of stock options granted and still valid; and
- on the basis of the exchange ratios indicated in Section 4 above,

will be a maximum of €1,420,690,865.55, through the issuance of a maximum of 2,291,344,587 new Telecom Italia ordinary shares and a maximum of 291,729,714 new Telecom Italia savings shares, all with a par value of €0.55 per share. The maximum amount of the increase in Telecom Italia's share capital for purposes of the share exchange has been calculated without considering the Tim ordinary and savings shares held by Telecom Italia as a result of the Tender Offer or Tim's treasury shares, which will not be exchanged in the Merger.

Article 5 of Telecom Italia's bylaws will also be amended to take into account the increases in capital for Tim's stock-option plans. Telecom Italia will take over these plans and issue a number of new ordinary shares for their implementation adjusted on the basis of the exchange ratio adopted for the Merger; while the exercise price of each option will remain unchanged.

In other words, the owners of Tim stock options will have the right to purchase at the predetermined price not the original number of ordinary shares of Tim but the larger number of ordinary shares of Telecom Italia, as the company resulting from the Merger, determined on the basis of the exchange ratio of 1 to 1.73. The unit price of ordinary shares deriving from the exercise of stock options will therefore be that obtained for each plan by dividing the original price by 1.73.

In more detail, Telecom Italia will approve an overall maximum increase in capital, divided into the following tranches, each of which is severable:

a) an increase of up to €11,705,656.05 for the exercise of stock options already granted by Tim under its "2000-2002 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 21,283,011 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim shareholders for purposes of the Merger at a price of €6.42 for each option held (i.e. €3.710983 for each newly issued share);

b) an increase of up to €1,132,285 for the exercise of stock options already granted by Tim under its "2001-2003 Stock-Option Plans", to be implemented by 31 December 2005 through the issuance of up to 2,058,700 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim shareholders for purposes of the Merger at a price of €8.671 for each option held (i.e. €5.012139 for each newly issued share);

c) an increase of up to €474,798.50 for the exercise of stock options already granted by Tim under its "2001-2003 Supplementary Plans", to be implemented by 31 December 2005 through the issuance of up to 863,270 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim shareholders for purposes of the Merger at a price of €7.526 for each option held (i.e. €4.350289 for each newly issued share);

d) an increase of up to €22,150,920 for the exercise of stock options already granted by Tim under its "2002-2003 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 40,274,400 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim shareholders for purposes of the Merger at a price of €5.67 for each option held (i.e. €3.277457 for each newly issued share);

e) an increase of up to €3,192,173.05 for the exercise of stock options already granted by Tim under its "2003-2005 Stock-Option Plans", to be implemented through the issuance of up to a total of 5,803,951 shares with a par value of €0.55 per share, by 31 December 2008 for the first lot, by 31 December 2009 for the second lot and by 31 December 2010 for the third lot. The shares will be offered to the holders of the above-mentioned stock options on the basis of the exchange ratio adopted for Tim shareholders for purposes of the Merger at a price of €5.07 for each option held (i.e. €2.930636 for each newly issued share).

The amendments to the bylaws described above will come into force on the effective date of the Merger pursuant to Article 2504-*bis* of the Civil Code and as provided for in the Merger Plan.

10. Board of Directors' evaluation of the conditions for exercise of withdrawal right

As the Absorbing Company, Telecom Italia will leave its bylaws concerning the company's purpose unchanged since the text as it stands does not differ significantly from that of the bylaws specifying Tim's corporate purpose, as regards either the activities the company can engage in or the related business risk. Furthermore, Telecom Italia's corporate purpose already allows the company to own equity interests in operating companies, and thus there is no need to make any amendments as a result of the Merger.

As regards holders of Tim savings shares, because of the difference between the dividend premium to which Tim savings shares are entitled and the dividend premium to which Telecom Italia savings shares are entitled, Tim savings shareholders who do not vote in favor of the Merger in the special meeting of Tim's savings shareholders will be entitled to withdrawal rights pursuant to Article 2437, first paragraph, subparagraph g), of the Civil Code, since their rights will be modified by the share exchange.

The value of Tim savings shares for purposes of such withdrawal rights will be determined as the arithmetic mean of the shares' closing prices in the six months prior to the publication, by the end of January 2005, of the notice calling the extraordinary meeting of Tim ordinary shareholders.

Consistent with its interest in purchasing all of Tim's savings shares, as evidenced by the Tender Offer, Telecom Italia has indicated that it intends to purchase all the savings shares for which the right of withdrawal is exercised by exercising its prerogatives in accordance with applicable law.

Milan, 23 January 2005

ANNEX III

MEETING OF THE BOARD OF DIRECTORS OF TELECOM ITALIA MOBILE S.p.A. HELD ON 23 JANUARY 2005

Report on the plan for the merger by incorporation of Telecom Italia Mobile S.p.A. into Telecom Italia S.p.A.

This is an English translation of the original Italian document

Milan, 23 January 2005

Telecom Italia Mobile S.p.A.

Telecom Italia Group – direction and co-ordination by telecom italia S.p.A.

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

The merger described herein relates to the securities of two foreign (non-U.S.) companies. The merger in which TIM ordinary shares and savings shares will be converted into Telecom Italia shares is subject to disclosure requirements of a foreign country that are different from those of the United States. Financial statements included in the document, if any, will be prepared in accordance with foreign accounting standards that may not be comparable to the financial statements of United States companies.

It may be difficult for you to enforce your rights and any claim you may have arising under the U.S. federal securities laws, since Telecom Italia and TIM are located in Italy, and some or all of their officers and directors may be residents of Italy or other foreign countries. You may not be able to sue a foreign company or its officers or directors in a foreign court for violations of the U.S. securities laws. It may be difficult to compel a foreign company and its affiliates to subject themselves to a U.S. court's judgment.

You should be aware that Telecom Italia may purchase securities of TIM otherwise than under the merger, such as in open market or privately negotiated purchases. Disclosure of such purchases will be made in accordance with, and to the extent required by, Telecom Italia's disclosure obligations under Italian law.

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REPORT OF THE BOARD OF DIRECTORS OF TELECOM ITALIA MOBILE S.P.A. ON THE PLAN FOR THE MERGER BY INCORPORATION OF TELECOM ITALIA MOBILE S.P.A. INTO TELECOM ITALIA S.P.A. PURSUANT TO ARTICLE 2501-*QUINQUIES* OF THE ITALIAN CIVIL CODE AND ARTICLE 70.2 OF THE IMPLEMENTING REGULATIONS OF LEGISLATIVE DECREE NO. 58 OF 28 FEBRUARY 1998 (THE "CONSOLIDATED LAW") RELATING TO THE RULES APPLICABLE TO ISSUERS, ADOPTED BY CONSOB RESOLUTION 11971/1999, AS AMENDED.

Dear Shareholders,

In accordance with Article 2501-*quinquies* of the Italian Civil Code ("**Civil Code**") and Article 70.2 of Consob Regulation 11971 of 14 May 1999, (the "**Regulation**"), we submit the plan (the "**Merger Plan**") for the merger by incorporation (the "**Merger**") of Telecom Italia Mobile S.p.A. ("**Tim**" or the "**Company to be Absorbed**") into Telecom Italia S.p.A. ("**Telecom Italia**" or the "**Absorbing Company**" or – after the Merger is effective – the "**Post-merger Company**") for your review and approval. This report is intended to describe and explain the reasons for the Merger Plan in legal and economic terms, particularly with respect to the exchange ratio.

This report is also intended to provide an accurate analysis of the business and financial rationale for the comprehensive reorganization of the activities of the Telecom Italia Group (the "**Reorganization Plan**") and consequently to explain how it is in the interests of the Company and its shareholders. The goal, both for Tim and Telecom Italia, is to improve their competitive position, due among other things to the greater operational and financial synergies and efficiencies that will arise, in line with the resolutions adopted by the Boards of Directors of both companies on 7 December 2004.

1. Description of the Merger and reasons therefor, with special emphasis on the business objectives of the companies participating in the Merger and the plans to achieve them

1.1 Description of the participating companies

1.1.1 Telecom Italia Mobile S.p.A.: Tim is a company limited by shares with its registered office in Turin at 6 Via Cavalli and its headquarters in Rome at 152 Via Pietro De Francisci, share capital of €515,728,777.86, divided into 8,595,479,631 shares with a par value of €0.06 per share, consisting of 8,463,410,468 ordinary shares and 132,069,163 savings shares. The Company to be Absorbed has its tax domicile at its registered office and is registered in the Turin Company Register. Its tax code number is 06947890015.

1.1.2 Telecom Italia S.p.A.: Telecom Italia is a company limited by shares with its registered office in Milan at 2 Piazza Affari, fully paid up share capital of €8,868,946,358.25, divided into 10,329,435,946 ordinary shares with a par value of €0.55 per share and 5,795,921,069 savings shares with a par value of €0.55 per share. The Absorbing Company has its tax domicile at its registered office and is registered in the Milan Company Register. Its tax code number is 00488410010.

1.2 Description of Tim's activities

1.2.1 Tim, together with the group of which it is the parent company, is one of the leading international groups operating in the telecommunication services sector, and more specifically in mobile telecommunications under licence or in a free market. Its activities include the design, implementation, management and sale of telecommunication, information and communication technology and electronic systems. Tim's main international markets are in South America and the Mediterranean basin.

1.2.2 The following tables provide selected historical operating, cash flow and financial data for the Tim Group and Tim, as reported in the financial statements for the first nine months of financial years 2004 and 2003 and in the 2003 financial statements.

Selected operating, cash flow and financial data for the Tim Group and Tim

Tim Group

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	9,499	8,635	11,782
Gross operating profit	4,574	4,157	5,502
Operating income before amortization of goodwill on consolidation differences	3,199	3,021	3,885
Operating income	3,129	2,944	3,786
Income before taxes	3,100	3,441	4,207
Consolidated net income before minority interests	1,724	2,041	2,456
Consolidated net income: Parent Company	1,664	1,970	2,342
Consolidated cash flow(1)	3,048	3,156	3,998
Free cash flow from operations(2)	2,829	3,123	3,746

1. *Consolidated net income (loss) before minority interests plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	9,247	9,276	9,064
Working capital	(1,925)	(2,407)	(2,015)
Net invested capital	7,322	6,869	7,049
Financed by:			
Consolidated shareholders' equity:	7,382	7,803	7,535
• Parent Company	6,827	7,295	7,049
• Minority interests	555	508	486
Consolidated net financial debt (positive financial position)	(60)	(934)	(486)
• Medium/long-term	490	585	668
• Short-term	(550)	(1,519)	(1,154)

Tim S.p.A.

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	7,381	6,980	9,469
Gross operating profit	4,076	3,805	5,035
Operating income	3,201	2,969	3,863
Income before taxes	3,376	3,081	3,852
Net income	2,143	1,846	2,322
Cash flow(1)	2,977	2,634	3,405
Free cash flow from operations(2)	3,038	3,409	4,201

1. *Net income (loss) plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**At 30 Sept. 2004**	**At 31 Dec. 2003**	**At 30 Sept. 2003**
Fixed assets, net	9,741	9,161	8,576
Working capital	(1,347)	(1,622)	(1,170)
Net invested capital	8,394	7,539	7,406
Financed by:			
Shareholders' equity:	8,899	8,957	8,481
• Share capital	514	514	514
• Reserves and retained earnings	6,242	6,121	6,121
• Net income for the period	2,143	2,322	1,846
Net financial debt (positive financial position)	(505)	(1,418)	(1,075)
• Of which short-term	(505)	(1,418)	(1,075)

1.3 Description of Telecom Italia's activities

1.3.1 Telecom Italia, together with the group of which it is the parent company, is one of the leading international groups operating in the telecommunication services sector and, more generally, in the information and communication technology sector.

1.3.2 The following tables provide selected historical operating, cash flow and financial data for the Telecom Italia Group and Telecom Italia, as reported in the financial statements for the first nine months of financial years 2004 and 2003 and in the 2003 financial statements.

Selected operating, cash flow and financial data for the Telecom Italia Group and Telecom Italia

TELECOM ITALIA GROUP

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	22,912	22,682	30,850
Gross operating profit	10,788	10,648	14,280
Operating income before amortization of goodwill on consolidation differences	6,607	6,639	8,619
Operating income	5,442	5,214	6,789
Income before taxes	3,690	3,858	3,442
Consolidated net income before minority interests	1,518	2,889	2,428
Consolidated net income: Telecom Italia	745	1,881	1,192
Consolidated cash flow(1)	6,399	7,901	9,207
Free cash flow from operations(2)	6,585	7,360	9,233

1. *Consolidated net income (loss) before minority interests plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**30 Sept. 2004**	**31 Dec. 2003**	**30 Sept. 2003**
Fixed assets, net	52,635	54,573	55,892
Working capital	(1,824)	(638)	(462)
Net invested capital	50,811	53,935	55,430
Financed by:			
Consolidated shareholders' equity:	19,390	20,589	21,177
• Telecom Italia	15,141	16,092	16,814
• Minority interests	4,249	4,497	4,363
Consolidated net financial debt :	31,421	33,346	34,253
• Medium/long-term	34,020	30,545	28,806
• Short-term	(2,599)	2,801	5,447

TELECOM ITALIA S.p.A.

Operating and cash flow data *(millions of euro)*	**1.1-30.9.2004**	**1.1-30.9.2003**	**Year 2003**
Sales and service revenues	11.793	11.872	16.033
Gross operating profit	5.526	5.510	7.433
Operating income	3.256	3.169	4.139
Income before taxes	1.664	1.378	1.728
Net income	894	2.012	2.646
Cash flow[(1)]	2.897	4.121	5.565
Free cash flow from operations[(2)]	3.782	3.669	4.702

1. *Net income (loss) plus amortization and depreciation.*

2. *Calculated as: Operating Income + Amortization and Depreciation – Industrial Investments – Change in Operating Working Capital.*

Balance sheet data *(millions of euro)*	**30 Sept. 2004**	**31 Dec. 2003**	**30 Sept. 2003**
Fixed assets, net	47,544	48,604	49,858
Working capital	230	3,079	1,063
Net invested capital	47,774	51,683	50,921
Financed by:			
Shareholders' equity:	15,533	16,356	15,688
• Share capital	8,858	8,854	8,846
• Reserves and retained earnings	5,781	4,856	4,830
Net income for the period	894	2,646	2,012
Net financial debt (positive financial position):	32,241	35,327	35,233
• Medium/long-term	28,955	20,692	22,034
• Short-term	3,286	14,635	13,199

1.4 Principal legal aspects of the Merger

1.4.1 The proposed transaction, consisting of the merger by incorporation of Tim into Telecom Italia, pursuant to and for the purposes of Article 2501 et seq. of the Civil Code, implements the corporate restructuring which forms the basis of the Reorganization Plan.

In order to implement this corporate restructuring, prior to the Merger and to its effectiveness, Tim is expected to spin off its mobile communications business in Italy (the "**Spin-off**") to a company wholly owned by Tim, to be known as Tim Italia S.p.A., with its registered office in Milan at 2 Piazza degli Affari ("**Tim Italia**"). The principal legal aspects of the Spin-off are described in Section 1.4.5 below.

1.4.2 The Boards of Directors of Telecom Italia and Tim (collectively, the "**Companies Participating in the Merger**") have adopted their respective balance sheets at 30 September 2004 as their balance sheets for purposes of Article 2501-*quater* of the Civil Code.

On 24 December 2004 Tim, pursuant to Article 2501-*sexies* of the Civil Code, applied to the Turin Court for the appointment of an expert to prepare the report on the exchange ratios for the Merger. In a decree dated 28 December 2004, the Turin Court appointed as expert the accounting firm of Reconta Ernst & Young S.p.A.

The Milan Court, pursuant to Article 2501-*sexies* of the Civil Code, has appointed the accounting firm of Mazars & Guerard to prepare the report on the exchange ratios for Telecom Italia

1.4.3 The Merger will result in the cancellation without exchange of the Tim ordinary and savings shares held by Telecom Italia at the effective date of the Merger and the assignment to holders of Tim ordinary and savings shares other than Telecom Italia of ordinary and savings shares issued by Telecom Italia. Under Article 2504-*ter* of the Civil Code, the treasury shares owned by Tim will be cancelled without exchange.

The intention of the Companies Participating in the Merger is to complete the Merger as soon as possible and, specifically, to arrange for it to become effective by the end of June 2005.

1.4.4 As a consequence of the Reorganization Plan, Tim will be merged into Telecom Italia, which will maintain its present bylaws with the amendments described in Section 9 of this Report.

Both the corporate purpose of Telecom Italia and that of Tim provide for the performance of telecommunication activities. Consequently, the implementation of the Reorganization Plan will not cause any significant changes in the activities performed by Telecom Italia and Tim before the Merger nor in the related business risks.

1.4.5 As mentioned above, before the Merger is completed and as the first step in implementing the Reorganization Plan, Tim will spin off its mobile communications business in Italy (the "**Domestic Communications Business**") by means of a contribution in kind to a new company in compliance with the prescribed procedures under applicable law.

To this end, on 29 December 2004, Tim established Tim Italia by means of a unilateral act. As stated above, this new company will acquire the Domestic Communications Business as a consequence of the Spin-off.

On 11 January 2005, Tim applied, pursuant to Article 2343 of the Civil Code, to the Milan Court for the appointment of an appraiser to prepare the valuation report on the Domestic Mobile Business to be contributed to Tim Italia. In a decree dated 12 January 2005, the Milan Court appointed Dott. Claudio Pastori, an accountant in Milan.

The Domestic Mobile Business to be spun off includes all the assets of Tim's mobile communications business in Italy and all the rights and obligations in any way related to the assets and liabilities to be transferred. All the contracts of employees and self-employed workers will also be transferred with the Domestic Communications Business.

The Domestic Communications Business will not include the assets and liabilities shown in Tim's balance sheet at 30 September 2004 related primarily to the Tim's international business, i.e.: (i) the equity interest held by Tim in Tim International N.V. ("**Tim International**"), the holding company for equity investments in foreign companies operating in the mobile communications sector with a book value, including payments for future increases in capital, of €4,582 million; (ii) the reserve for risks in respect of guarantees issued on behalf of foreign affiliates, amounting to €198 million; (iii) the guarantees granted and received in relation to the foreign sector, included in the memorandum accounts, for a total of €982 million; (iv) advance taxes, related to the international assets, amounting to €813 million; (v) the balance of the current account held by Tim with Telecom Italia; and (vi) certain other financial and tax items.

The Spin-off, implemented in accordance with Article 172.1 of the Consolidated Income Tax Law (Presidential Decree no. 917 of 22 December 1986), is tax neutral in terms of Italian taxation and, therefore, will not lead to the realization of capital gains or losses. In other words, Tim Italia will succeed, on a continuing basis, to Tim's tax situation in respect of the assets and liabilities contributed.

Another consequence of the Spin-off is that Tim Italia will succeed to the authorizations for the provision of electronic communications networks and services in Italy already held by Tim and to all the rights (including those temporarily assigned to Tim at the date of the transfer of the Domestic Communications Business) to use numbering systems and/or radio frequencies under public franchises, licences, general authorizations and special authorizations resulting from notifications declaring the commencement of activities. As regards the regulatory aspects, both Tim and Tim Italia have initiated all the registration formalities and notifications to the competent authorities. To this end, Tim has already notified the Ministry of Communications in accordance with Article 25.8 of Legislative Decree 259/2003.

Tim, Tim Italia and Telecom Italia will make the notifications concerning the transaction required by Article 47 of Law 428/1990, as amended by Article 2 of Legislative Decree 18/2001.

Following the Spin-off and until the Merger becomes legally effective, Tim will continue to control Tim Italia, the company owning the Domestic Communications Business, and Tim International, the holding company for equity investments in foreign companies operating in the mobile communications sector. Upon completion of the Merger, Telecom Italia will own 100% of the capital of both companies directly.

It is expected that the Spin-off will be completed, by means of the execution of a transfer instrument and its filing with the Milan Company Register, by the end of March 2005.

1.4.6 As part of the Reorganization Plan, Telecom Italia made a voluntary partial tender offer under Article 102 et seq. of the Consolidated Law for 2,456,534,241 Tim ordinary shares, representing 29.12% of Tim's ordinary share capital at 20 December 2004 and 28.67% of its total share capital at the same date and a voluntary tender offer for all 132,069,163 Tim savings shares, representing 100% of Tim's savings share capital and about 1.54% of its total share capital (although the offers were legally distinct, hereinafter the offer for Tim's ordinary shares and the offer for Tim's savings shares are referred to jointly as the "**Offer**"). The Offer price was 5.6 for each Tim ordinary and savings share and its effectiveness was subject to the condition, for both classes of shares, that two thirds of the number of shares subject of the Offer must be tendered.

In order to provide Tim shareholders and the market with the information needed to assess the Offer and an evaluation of the terms and purpose of the Offer, especially as regards the fairness of the proposed price, in its meeting on 22 December 2004, Tim's Board of Directors approved the Issuer's Statement pursuant to Article 103.3 of the Consolidated Law and Article 39 of the Regulation concerning Issuers.

The Offer commenced on 3 January 2005 and terminated on 21 January 2005. The number of shares tendered amounted to approximately 31.2% of Tim's ordinary share capital and 6.4% of its savings share capital. The Offer Document specified that, in the event of the number of shares tendered falling below the minimum thresholds set, Telecom Italia's Board of Directors would decide whether to acquire the smaller quantity of Tim ordinary and/or savings shares tendered and proceed with the planned reorganization by implementing the Merger.

Telecom Italia's Board of Directors has favorably assessed the results of the Offer, especially in view of the fact that the Tim ordinary shares tendered exceeded the number of Tim ordinary shares subject to the Offer, thus demonstrating the market's appreciation of the transaction and making it possible to achieve the objective of optimizing the Post-merger Company's balance sheet and financial structure upon completion of the Merger. For this reason, Telecom Italia's Board of Directors has decided to waive the Offer effectiveness conditions concerning the minimum threshold of acceptances for Tim savings shares, thereby confirming the effectiveness of the Offer and accepting to purchase the smaller quantity of Tim savings shares tendered, and to proceed with the Reorganization Plan and the related integration process.

It should also be noted that, as a result of the exercise of the options which were previously disclosed to the market (for approximately 21 million Tim savings shares) and the execution of securities lending agreements (for approximately 37 million Tim savings shares), following the Offer Telecom Italia will be entitled to vote approximately 50.3% of the shares entitled to vote in the special meeting of Tim savings shareholders that will be called to approve the Merger resolution.

As mentioned above, the Offer represented the first step in the Reorganization Plan and must therefore be considered as connected with and serving the purposes of the Merger.

In view of the Merger, the Offer was intended to contribute to optimizing the capital structure of the Absorbing Company. Since, in implementing the Merger, the Tim shares held by Telecom Italia will be cancelled without exchange, Telecom Italia's acquisition of Tim shares by means of the Offer has increased the proportion of Tim's share capital that will be cancelled and consequently reduced the amount of equity to be issued in exchange. This could have a positive effect (i) on the earnings per share of Telecom Italia post-Merger, thus improving the return on equity, and (ii) on the free cash flow yield per share, to the benefit of all the post-Merger shareholders of Telecom Italia and Tim. From a financial perspective, the equity that is not issued will in effect be replaced, as a result of the settlement of the obligations arising from the Offer, by an increase in Telecom Italia's net debt. The cost of this new debt – in terms of after-tax net financial expense – is lower than the cost in – terms of the expected dividends – which would have been incurred on the additional amount of equity (not issued in exchange for Tim shares purchased in the Offer).

The results of the Offer mean that Telecom Italia will pay a total consideration of approximately €13.8 billion, of which €2.5 billion will be paid by Telecom Italia through the realization of a portion of its liquid assets and approximately €11.3 billion will be raised through bank financing. Consequently, the net financial debt of the Telecom Italia Group, estimated at approximately €30 billion at 31 December 2004, is expected to increase, excluding other costs related to the Offer, to just under €44 billion.

The increase in debt following the Offer has not led, in line with the indication given in the announcement of the plan to reorganize the Telecom Italia Group, to a reduction in Telecom Italia's credit rating (currently Baa2 for Moody's, BBB+ for Standard & Poor's, A– for Fitch). It should be noted that Standard & Poor's and Fitch, while confirming their respective ratings, have revised their outlooks from positive to stable and from stable to negative, respectively. The rating agencies arrived at these conclusions on the basis of the maximum estimated consideration payable in connection with the Offer, equal to approximately €14.5 billion.

The bank financing may be refinanced in the capital markets, depending on market opportunities and conditions, probably in the next two years.

The progressive reduction in the debt incurred in connection with the Offer will be made possible primarily by the cash flow that will be generated, which is expected to be at least in line with the plans announced in March 2004.

1.4.7 As part of the share exchange, Telecom Italia will assign newly-issued savings shares of the Post-Merger Company to holders of Tim savings shares.

It should be noted that, from a formal legal perspective, Telecom Italia savings shares are entitled to a smaller dividend premium compared to ordinary shares than that to which holders of Tim savings shares are currently entitled compared to Tim ordinary shares.

Tim savings shares entitle their holders, among other things, to the right to a premium with respect to any profit distributed to ordinary shareholders equal to 20% of their par value of €0.06 and to the right to the distribution of net profits, after deducting the amount to be allocated to the legal reserve, up to 5% of their par value. In contrast, Telecom Italia savings shares entitle their holders the right to the distribution of net profits up to 5% of their par value of €0.55, and the right to a premium with respect to any dividend distributed to ordinary shareholders equal to 2% of their par value.

Since the Merger will result in holders of Tim savings shares receiving in exchange Telecom Italia savings shares that, as specified above, entitle the holders to a smaller dividend premium than the cancelled Tim savings shares, the Merger will be submitted for approval to a special meeting of Tim savings shareholders pursuant to Article 146.1b) of the Consolidated Law (the "**Special Meeting**").

Moreover, in view of the smaller dividend premium of the Telecom Italia savings shares that will be assigned in exchange to the existing holders of Tim savings shares, all of the latter who do not vote in favor of the resolution submitted to the Special Meeting will be entitled to withdrawal rights pursuant to Article 2437, first paragraph, subparagraph g), of the Civil Code, in view of the modification to their property rights as a consequence of the exchange.

It should be noted, however, that, from a substantive economic perspective, the Merger will lead to the above-mentioned change in the dividend premium being more than offset, in absolute terms, by an improvement in the entitlement to profits of each Tim savings shareholder (as regards the premium compared to dividends on ordinary shares). In fact, as a consequence of the exchange, each Tim savings share with a par value of €0.06 will be replaced by more than one Telecom Italia savings share with a par value of €0.55 on the basis of the exchange ratios (described below), so that the post-exchange dividend premium for each former Tim savings share will be calculated with reference to a higher total par value equal to €0.55 (par value) x 2.36 (exchange ratio) = €1.30 instead of €0.06. Consequently, the dividend premium attaching to each Tim savings share held, currently equal to €0.012 (20% x €0.06), will increase as a consequence of the exchange for Telecom Italia savings shares to €0.026 (2% x €1.30).

1.4.8 Telecom Italia will succeed to all Tim's legal rights and obligations in force at the effective date of the Merger, including those arising in connection with Tim's stock option plans (to this end, the Absorbing Company will make the necessary capital increases for purposes of such plans, as described in Section 9 below).

1.4.9 The Merger is technically subject to the veto right of the Minister for the Economy and Finance pursuant to the *Golden Share* provisions under Article 2 of Decree Law 332/1994, ratified by Law 474/1994, and Article 22.b) of Telecom Italia's bylaws.

At the end of the meeting of Telecom Italia's Board of Directors on 7 December 2004, in accordance with Article 22.b) of the Absorbing Company's bylaws and Article 2 of Decree Law 332/1994, ratified by Law 474/1994, Telecom Italia notified the Minister for the Economy and Finance of the commencement of the plan for the reorganization of the Group.

The Minister for the Economy and Finance, in agreement with the Minister for Productive Activities, has notified Telecom Italia that he does not consider that the conditions exist for the exercise of the veto right with respect to the adoption of the Merger resolution by Telecom Italia's shareholders' meeting.

1.4.10 Telecom Italia's ordinary and savings shares are and, following the Merger, will continue to be, listed on the *Mercato Telematico* operated by Borsa Italiana S.p.A.

In addition, following the Merger, Telecom Italia's ordinary and savings shares will continue to be listed on the New York Stock Exchange in the form of ADRs (American Depository Receipts, each of which represents ten ordinary or savings shares). As regards the listing of Telecom Italia's ordinary shares on the Frankfurt Stock Exchange, in the light of the decisions adopted by the Board of Admission of the Frankfurt Stock Exchange, the shares will be delisted by the effective date of the Merger.

1.5 Reasons for the Merger – Business objectives and plans to achieve them

1.5.1 The Merger satisfies a series of business needs prompted by the progressive, increasing integration between fixed and mobile telephony platforms. The evolution of the market and the defense of the creation of value also require an adaptation of business models and organizational strategies, an objective that the merger by incorporation of Tim into Telecom Italia is intended to promote.

To capture all of the benefits made available by the integration of platforms and services, at a time of significant technological discontinuity, it is desirable to undertake a corporate structural reorganization that will guarantee the unitary governance of business processes that a situation of partial control of capital does not fully allow.

The reorganization will make it possible to respond to the need for integration expressed by customers, to capitalize on the complementary features of the services offered in order to foster consumption, and at the same time to capture all the benefits deriving from the synergies between the different business areas.

The demand for telecommunications services is growing, driven by the spread of broad-band in wireline business and by the new services supplied in the mobile segment. In particular:

– electronic communications on the wireline network have enriched the supply of traditional "voice" and "data" services by adding the innovative services made possible by XDSL technology and fiber optics;

– electronic communications on the new-generation mobile networks (GPRS, EDGE and UMTS) now afford mobility not only for voice services but also for data, Internet and media services.

There are sectors in which customers increasingly feel the need to use the services made possible by the new technologies seamlessly, regardless of where they are. Furthermore, technological innovation is significantly increasing the interaction between the different networks (fixed and mobile, voice and data) and between the supply of telecommunications services and that of adjacent sectors, such as information technology, media and consumer electronics.

The leading manufacturers of telecommunications equipment and terminals have oriented their technological investments to satisfying the market's new needs:

– telecommunications networks are rapidly evolving into "multimedia networks" thanks to the spread of the IP protocol and the adoption of homogeneous wireline and mobile multiservice platforms;

– the new wireline and mobile terminals satisfy multiple functions and convergent handsets permit seamless access to wireline and mobile services.

The rapid spread of this equipment will allow telecommunications operators to benefit from the potential synergies deriving from a more closely integrated management of wireline and mobile electronic communications businesses and thus to be well positioned to cope with a scenario likely to be characterized by the saturation of the market in traditional telephone services and the trend of eroding prices and margins.

The leading operators in the Italian and European telecommunications market are preparing to respond to the latest technological and market developments on three main fronts:

– better coordination and distribution of customer relations between the various segments (integration of sales channels and responsibilities for specific segments, brand management);

– strengthening of certain critical functions for comparative advantage (guidance of IT and network technological choices; management of research; purchasing; content acquisition and management; and coordination of supply policies);

– defense of margins through programs to recoup efficiency by exploiting synergies across the different business areas (common management of IT and network infrastructures, convergent evolution of applications platforms, and common content acquisition and management).

In this setting, the Telecom Italia Group already ranks in the top tier among European competitors in all business areas in terms of growth, profitability and product innovation. This is the result of the substantial investments made in technological innovation, which today provide the Group with a network infrastructure considered future-proof, ready to host and handle the portfolio of new generation products and services.

As mentioned above, however, the evolution of the market and the defense of the creation of value also require an adaptation of current business models and organizational strategies, an objective that the merger by incorporation of Tim into Telecom Italia is intended to promote.

The Merger, together with the Spin-off, will simplify the Group's ownership structure by maintaining the Domestic Communications Business under an unlisted, wholly owned subsidiary of Telecom Italia, thereby creating optimal conditions for grasping the opportunities to realize the synergies referred to above.

The Merger is also intended to bring the following additional advantages:

– to optimize financial and cash flows within the Group by managing Group debt more efficiently and making better use of financial leverage. At the same time, Tim's current shareholders will become shareholders of a company with a more balanced financial structure, capable of being taken over and therefore better placed to enhance the value of the shares assigned in exchange;

– to enable Telecom Italia to optimize, through the Offer and the Merger, its own financial structure and to reduce the weighted average cost of capital employed compared with its current cost. In fact, as explained above, the purchase of Tim shares is financed by means of an increase in net financial debt, whose cost, net of the tax effect, is lower than the cost which would have been incurred by the additional amount of equity not issued in exchange for Tim shares acquired in the Offer. The consequent reduction in the weighted average cost of capital should favor the full value potential of the shares of Telecom Italia as the Post-Merger Company and thus the creation of value for shareholders, including the Tim shareholders who exchange their shares.

As mentioned above, the Merger serves to promote the adaptation of the Group's business models and organizational strategy to the evolution of the market and the defense of the creation of value for shareholders.

The integration process, involving actions designed to improve efficiency and to enhance strategic and operational effectiveness, primarily concerns the Networks and Information Technology, Customer Operations, the Supply of Innovative Services and Sales Channels business areas and will be implemented in compliance with applicable sector and antitrust laws. The main projects under consideration concern:

Networks and Information Technology

- Joint development of network and platform architectures for wireline and mobile products and services;
- Integration and synergies in connection with networks for access traffic and IP backbone traffic, for example, through joint planning of requirements and development processes;
- Joint development, operation and maintenance of network information systems;
- Design of the new integrated network model.

Customer Operations

- Joint development of IT applications providing support for the management of the business;
- Increase in customer care efficiency and service levels by adoption of the best practices developed in Telecom Italia and Tim;
- Synergies in connection with the supply of customer information services (e.g., the 12 and 412 customer information services).

Supply of Innovative Services and Sales Channels

- Development of convergent services for the consumer market (e.g., seamless access to mail, interoperability of fixed and mobile services, and standardization of mimicking) and for the business market (e.g., mobile use of corporate applications by means of extended enterprise models);

- Increase in the effectiveness of sales channels and search for efficiency gains in overlapping commercial services while maintaining separate offers;
- Development of a multimedia portal accessible from fixed and mobile network terminals and enhancement of Group contents and brands.

Procurement

- Optimization of the distribution logistics for commercial products;
- Exploitation of the synergies between network operating structures and joint evaluation of make-or-buy options;
- Elimination of duplication and harmonization of service standards in Facility Management and General Services.

Working Groups have been formed to define the scope for integration, specify and develop integration plans, and lay down how they are to be implemented. The groups are headed by an Integration Committee that provides guidance and control, by ensuring observance of specific responsibilities over the development of the overall integration plan.

Consistently with the integration plan, the organizational and operational restructuring will be based on three guidelines: a market plan aimed at increasing the effectiveness of customer relations; an efficiency plan for the rationalization of internal and external structures; and an organizational development plan.

The synergies expected from the Merger, the broad outlines of which have already been identified and whose economic benefits and other advantages will be detailed and announced by mid-April 2005, are the result of analyses and evaluations undertaken by the managers involved in the integration plans discussed above.

2. The values attributed to the Companies Participating in the Merger for the purpose of determining the Exchange Ratios

2.1 Purpose of the valuation

2.1.1 The purpose of the valuation is to determine the exchange ratio (the "**Exchange Ratio**") on the basis of which the participation in the Post-Merger Company of the shareholders of Telecom Italia and Tim, respectively, will be determined.

The aim of the valuation, therefore, is to value Telecom Italia and Tim in order to obtain significantly comparable values for the purpose of determining the Exchange Ratio for the Merger in question, considering all the shareholders of the Companies Participating in the Merger as parties interested in the valuation and the Exchange Ratio.

To achieve this objective, the valuations for the purpose of determining the Exchange Ratio require the identification and application of valuation methods based on uniform criteria for the Companies Participating in the Merger.

Such valuations may therefore differ from other valuations made in different contexts or for different purposes, including with respect to the selection of criteria and methodologies applied.

2.1.2 In the light of information provided by the Advisors (as specified below), the Board of Telecom Italia has reached its conclusions on the Exchange Ratio following a careful evaluation of the Companies Participating in the Merger, selecting from a range of valuation methods those generally considered most appropriate in consideration of the activities performed by the Absorbing Company and the Company to be Absorbed.

Furthermore, as suggested by corporate doctrine and standard professional practice, the values attributed to the Companies Participating in the Merger were compared on a going-concern basis.

It should also be noted that the effects of the Offer for Tim ordinary and savings shares do not require the Exchange Ratio to be altered since the Offer was made on terms consistent with the valuations used to determine the Exchange Ratio. In fact, in the context of the valuation of Telecom Italia, the acquisition of the Tim shares tendered in the Offer increases the value of the equity interest in Tim substantially equivalent to the increase in Telecom Italia's net financial debt, which, moreover, will be at a level consistent with Telecom Italia's current rating. The overall effect is that the value of Telecom Italia's equity will remain substantially unchanged.

2.1.3 For purposes of determining the Exchange Ratio, Tim's Board of Directors was assisted by leading financial Advisors, namely the investment banks Lazard & Co. S.r.l. as Sole Lead Advisor and Credit Suisse First Boston. In addition, as recommended by the Committee for Internal Control and Corporate Governance (consisting exclusively of independent directors), the Milan office of Merrill Lynch International and Studio Casò, in the person of Mr. Angelo Casò, were requested as advisors to prepare additional fairness opinions on the Exchange Ratio. In arriving at its conclusions, Tim's Board of Directors acknowledged that each financial Advisor chose from among the various possible valuation methods those it deemed most appropriate considering the activities performed by the Absorbing Company and the Company to be Absorbed and that, although they adopted different methods, the financial Advisors reached consistent conclusions.

For its part, the Board of Directors of Telecom Italia was assisted by the following financial Advisors: JPMorgan, MCC, Mediobanca and Goldman Sachs International.

2.1.4 Tim's Board of Directors, after carefully analyzing the valuations put forward by its financial Advisors, approved the valuation methods they had applied, described in Section 2.2 below.

2.2 Methods used and results obtained

2.2.1 Introduction

A. The valuation methods and criteria to be applied here were selected taking into account:

a) the specific objectives assigned to the valuations in connection with the Merger;

b) the nature of the activities performed by each of the Companies Participating in the Merger.

B. *Concerning the first aspect*, in selecting the valuation principles and criteria, reference was made, as is considered proper and desirable in every kind of valuation, to the purpose of the exercise and to the material factors allowing the value of the object of the valuation to be calculated. Given the objective of obtaining comparable values for the determination of the Exchange Ratio, valuation methods based on uniform criteria were adopted for both Companies Participating in the Merger.

In this case, the Exchange Ratio was determined on the basis of a comparison of the values of the Companies Participating in the Merger.

As indicated above, these values were obtained on a going-concern basis and can neither be considered as representative of stand-alone valuations of the two Companies Participating in the Merger nor compared with any potential acquisition or disposal prices (which normally take into account potential majority premiums and minority discounts). Nor do these values reflect the strategic, operational and financial synergies expected from the Merger.

As specified below, for the valuation of both Companies Participating in the Merger, the two methods used were the market-price method and the sum-of-parts method, the latter primarily through the application of the discounted cash flow or DCF methodology to the various business units. In particular, for the purpose of determining the Exchange Ratio, values obtained on the basis of uniform methods were compared: the ratio between market prices on the one hand and the ratio between fundamental values (sum-of-parts) on the other.

The valuation process was further supported by considering financial analysts' target prices for the Telecom Italia and Tim shares and making reference to market multiples for comparable companies.

C. *With regard to the second aspect*, account was taken, on the one hand, of the multiple operational areas of Telecom Italia and Tim and, on the other, of the fact that the controlling interest in Tim held by Telecom Italia represents a significant part of the latter's assets.

D. In the light of the above, the following methodologies were used to determine the values of Telecom Italia and Tim:

(i) **Market Prices**. In this regard, it is noted that where companies participating in a merger have shares listed on regulated securities exchanges, theory and professional practice suggest that account be taken of the results derivable from the market prices of the respective shares, averaged over appropriate periods of time. In this case, the market prices are considered to be particularly significant, taking into account the high capitalization and liquidity of Tim and Telecom Italia; the extensive coverage the two companies receive in analysts' research reports; and the existence among their shareholders of numerous international institutional investors;

(ii) Sum of the Parts. Under this method, a company's value is calculated as the sum of the values of its separate units (meaning economic entities that can be valued independently) adjusted to take into account the company's financial position and minority interests.

For purposes of determining the Exchange Ratio, the values of Telecom Italia's and Tim's equity were calculated both taking into account and excluding the effects of the distribution by the two companies of dividends in April 2005 (assumed to be equal to those distributed in 2004). The reason for considering the effects of the dividends is that the calendar of the Merger provides for the share exchange to take place after they have been paid.

E. The sections that follow describe the methods and principles adopted in valuing the Companies Participating in the Merger both from the theoretical point of view and from the point of view of the principal results achieved.

2.2.2 Market Price method

A. The Market Price method estimates the value of the capital on the basis of the stock market prices recorded in a significant period concluding at a date close to that on which the estimate is made.

The application of the Market Price method considered the prices of Telecom Italia and Tim shares over various periods prior to the announcement of the Merger (3 December 2004) and the beginning of rumors (the week of 16-19 November 2004), in order to focus on the values of the two companies expressed by market prices excluding possible announcement effects.

The period prior to the beginning of rumors is considered more significant since in the subsequent period both the market prices and the trading volumes showed anomalies and discontinuities compared, to their long-term trends. Analyses of the two companies stock market prices are reported below for various periods up to 16 November 2004. It is nonetheless worth noting that the differences between these values and those obtained for periods up to the Merger announcement date are not material.

B. On the basis of the market data at 16 November 2004 (the last day of trading before the beginning of rumors), it was found that:

a) both of the Companies Participating in the Merger had a large market capitalization and a significant and widely-distributed float;

b) as can be seen from the following table: (i) the daily volume of trading in Tim and Telecom Italia ordinary shares was high (approximately 1% of the float on average); and (ii) during the twelve months preceding the date of the beginning of rumors concerning the Merger:

- trades of Tim ordinary shares amounted to approximately 389.5% of the ordinary share capital (excluding the shares held by Telecom Italia), for a value of approximately €65 billion;
- trades of Telecom Italia ordinary shares amounted to approximately 201% of the ordinary share capital (excluding the shares held by Olimpia S.p.A.), for a value of approximately €43 billion.

Tim (ordinary shares)	Average daily trading volume (in € thousands)	Cumulative volume (in € thousands)	Average % of capital traded (*)	Cumulative % of capital traded (*)
Prices				
16/11/2004	65,758	65,758	1.8%	1.8%
1-month average	52,095	1,146,096	1.4%	31.1%
2-month average	50,586	2,175,181	1.4%	59.0%
3-month average	48,796	3,220,504	1.3%	87.4%
6-month average	47,803	6,310,041	1.3%	171.2%
12-month average	56,285	14,352,550	1.5%	389.5%

Telecom Italia (ordinary shares)	Average daily trading volume (in € thousands)	Cumulative volume (in € thousands)	Average % of capital traded (*)	Cumulative % of capital traded (*)
Prices				
16/11/2004	85,138	85,138	1.0%	1.0%
1-month average	71,326	1,569,170	0.8%	18.5%
2-month average	65,538	2,818,153	0.8%	33.3%
3-month average	59,735	3,918,770	0.7%	46.3%
6-month average	58,305	7,696,208	0.7%	90.9%
12-month average	66,690	17,005,946	0.8%	201.0%

(*) Percentage of the free float.

Source: Datastream.

c) both Companies represented a significant portion of the total capitalization of the Mibtel (Milan telematic index) and S&P/MIB stock indices. According to data provided by Borsa Italiana, at 16 November 2004:

- Telecom Italia represented 5.3% of the Mibtel index and 8.9% of the S&P/MIB index; and
- Tim represented 7.4% of the Mibtel index and 6.6% of the S&P/MIB index;

d) the Telecom Italia and Tim floats were significantly divided among Italian and foreign institutional investors and Italian retail investors.

C. In order to mitigate the short-term fluctuations that are typical of the financial markets, in line with best valuation practices, the analysis of the share prices was extended to the average figures recorded by the market over relatively long periods.

To this end, volume-weighted average prices were calculated for periods of up to 12 months, both excluding and taking into account the impact of the dividend distribution.

D. From the analysis of the market prices, the 1, 3, 6 and 12-month averages were identified as those that fell within a range of constant valuations, as can be seen from the following table.

	Stock market value not adjusted for dividend			Stock market value adjusted for dividend		
Market prices (ordinary shares)	Telecom Italia (€)	Tim (€)	Ratio (X)*	Telecom Italia (€)	Tim (€)	Ratio (X)*
Weighted averages						
16/11/2004	2.82	4.81	1.71	2.71	4.55	1.68
1 month	2.70	4.68	1.73	2.59	4.42	1.71
2 months	2.63	4.56	1.73	2.52	4.30	1.70
3 months	2.58	4.50	1.74	2.48	4.25	1.71
6 months	2.55	4.51	1.77	2.45	4.25	1.74
12 months	2.54	4.52	1.78	2.44	4.27	1.75

Source: Datastream.

* *Possible differences due to rounding.*

	Stock market value not adjusted for dividend			Stock market value adjusted for dividend		
Market prices (savings shares)	Telecom Italia (€)	Tim (€)	Ratio (X)*	Telecom Italia (€)	Tim (€)	Ratio (X)*
Weighted averages						
16/11/2004	2.05	4.78	2.33	1.94	4.51	2.33
1 month	2.01	4.62	2.30	1.89	4.35	2.30
2 months	1.95	4.53	2.32	1.84	4.26	2.32
3 months	1.92	4.48	2.34	1.80	4.22	2.34
6 months	1.86	4.45	2.39	1.75	4.18	2.39
12 months	1.84	4.45	2.42	1.72	4.18	2.43

Source: Datastream

* *Possible differences due to rounding.*

2.2.3 Sum-of-Parts Method

A. Under the Sum-of-Parts method, the value of Telecom Italia and Tim is calculated as the sum of the values of the individual units of each company, considered as economic entities that can be valued independently. Such sum is suitably adjusted to take account of the financial position and minority interests for each of the Companies Participating in the Merger.

B. For the valuation of the individual units, the Discounted Cash Flow or DCF methodology was primarily used, as applied to the principal assets of Telecom Italia and Tim: the Italian wireline and mobile services and the major subsidiaries abroad.

For the valuation of the remaining assets of Telecom Italia and Tim, reference was made to their stock market value, where available and deemed appropriate, and for those of minor importance or not consolidated, to their book value or to the estimates of financial analysts in research reports.

The Telecom Italia assets to which the above-mentioned methods were applied are summarized below:

– fixed telephony services included in the Wireline division;

– Mobile division (Tim, domestic and international activities);

– Internet Media division (TI Media S.p.A.);

– Latin America division (holdings in Entel Chile and Entel Bolivia);

– IT market division (Finsiel S.p.A.);

– Olivetti Tecnost group;

– other assets and shareholdings.

The DCF methodology was applied by discounting operating cash flows gross of any component of a financial nature (Free Cash Flows or "FCF"). Under this methodology, the value of a company is equal to the sum of the following components:

– operating cash flows that the company will be able to generate in the future, discounted at a rate representing the weighted average cost of capital;

– net financial position and minority interests, which in the case in question were calculated with reference to 31 December 2004.

The DCF method was applied to determine the fundamental value for financial investors and reflects the following assumptions and approaches:

– the Weighted Average Cost of Capital ("WAAC"), calculated on a target capital structure of the activity to be valued which is in line with the current capital structure and with the relevant market benchmarks;

– the growth rates used for the financial projections beyond the time periods covered by Telecom Italia's and Tim's business plans, where such projections were considered, and for the calculation of the terminal value, reflect growth prospects consistent with the relevant market benchmarks.

C. In applying the DCF methodology, reference was made to the cash flows of the main activities as shown by the update, for the period 2004-2007, of the business and financial plans approved and announced to the market in March 2004. The plans were developed by management in conformity with the Group's strategic, operational and financial objectives. The average rate of organic growth (i.e., at constant scope of consolidation exchange rates) of EBITDA compound annual growth rate (CAGR 2003-2006 >5.5%), and the net financial position at 31 December 2004 (less than €30 billion) are both confirmed.

As regards the fixed telephony activity, in a market with prospective annual growth of more than 2%, an average rate of organic growth of EBITDA of more than 2% is confirmed, primarily due to a stable customer base, achieved by broadening the range of wireline services and products offered and the growth of broadband services in Italy and abroad (France and Germany), also driven by the launch of new value added services (VAS) and innovative content.

In the case of the mobile telephony activity, the main lines of growth in Italy are confirmed: development and differentiation of the wireless services and products offered; enhancement of value added services (multi-messaging and interactive VAS); focus on customers; technological strength (EDGE/UMTS and combined services); and an increase in the average revenue per user (ARPU). The growth of the international business, where it has been decided to withdraw from the Venezuelan market, continues to be driven by Brazil. In Brazil, a substantial expansion of the customer base is expected and the second position in the domestic market will be maintained through the continuation of the strengthening of customer care, brand development and positioning, innovation in the services and products offered, and improved territorial coverage. This allows a double-digit EBITDA annual organic growth trend for the mobile communications activity as a whole and gross operating profits of more than 53% for the Italian market to be confirmed, in line with the figures announced.

D. The update for the period 2004-2007 of the business and financial plans approved and announced to the market in March 2004, which were developed by management in conformity with the Group's strategic, operational and financial objectives, provided the basis for determining both the operational cash flows for the forecasting period adopted and the terminal value at the end of the periods considered by the Advisors in their valuations ("**Terminal Value**").

For purposes of estimating the Terminal Value, theory and prevailing professional practice propose two alternatives:

– the value corresponding to the capitalization of the normalized operating cash flow (or the present value of the operating cash flows expected for the period subsequent to the time horizon of the explicit projection), which can be estimated as follows:

$$VT=\frac{FCFn}{(WACC-g)}$$

where:

VT = Terminal Value;
FCFn = normalized operating cash flow;
g = assumed perpetual growth rate;
WACC = weighted average cost of capital;

or,

– the value calculated on the basis of a multiple of the gross operating profit of the last year of the projection period considered.

Since the cash flows in question will be used to remunerate all the entities contributing capital, in discounting such cash flows it is necessary to use a rate representing the cost of all the financial resources utilized by the company. This rate is identified as the Weighted Average Cost of Capital (WACC) and is calculated with reference to a target capital structure of the activity to be valued and the relevant market benchmarks, as follows:

$$WACC= Kd\left(1\text{-}t\right)\frac{D}{D+E}+Ke\frac{E}{D+E}$$

where:

Kd = cost of debt capital;
Ke = cost of equity capital;
D = debt capital;
E = equity capital;
t = tax rate.

In particular, the prevailing practice is to calculate the cost of equity capital on the basis of the Capital Asset Pricing Model (CAPM), defined by the following formula:

$$Ke = Rf + Beta \times (Rm - Rf)$$

where:

Rf = rate of return on risk-free investments;
Beta = correlation coefficient between a share's effective rate of return and the overall rate of return of the reference share market;
Rm = overall rate of return of the reference share market;
(Rm - Rf) = premium required by the reference share market compared to the rate of return on risk-free investments.

The principle underlying this methodology rests on the hypothesis that, in a liquid and efficient market, investors determine the required rate of return considering exclusively the systematic (or market) risk of the investment, expressed by the relation between the variation in the price of the share and the variation in the share market (Beta). The specific risk of the investment (the share) is not considered, since it can be eliminated by the investor through appropriate diversification of investments.

E. In light of the above, in this case reference was made to the operating cash flows for the individual units as shown by the updated business and financial plans prepared by the management of both companies. Certain Advisors then extended the financial projections beyond the time horizon of the companies' business and financial plans. The growth rates used for these financial projections and for the determination of the Terminal Value, calculated using a perpetual normalized FCF growth rate, reflect growth prospects consistent with the relevant market benchmarks. Although the Advisors adopted different applications of the same methodology, Tim's Board of Directors noted that they arrived at similar and mutually consistent conclusions.

With respect to the WACC, reference was also made to the calculation of different WACCs for the individual activities. In particular, for the risk-free rate, the "normal" rate of return on risk-free investments in the reference market of the business unit considered was used, while the beta was calculated on the basis of the most appropriate market variables, taking into account the target financial structure of the activities to be valued and the relevant market benchmarks. With respect to the premium required by the share market, the most recent valuation practices and estimates of financial analysts published in research reports were used.

In the valuation of Telecom Italia and Tim, from the sum of the values of the assets, calculated as described above, the estimated net financial position at 31 December 2004 and the valuation of minority interests were deducted; these were determined primarily, depending on the circumstances, with reference to their book or market value, in view of their limited importance in relation to the overall valuation of the two companies.

In order to divide the results obtained for the equity value of the two companies between their ordinary and savings shares, reference was made to the average discounts implied by the 1, 2, 3, 6 and 12-month averages of the prices of Telecom Italia and Tim savings shares compared to those of their ordinary shares. The consensus view is that other methods of dividing the equity value between ordinary and savings shares would introduce discretionary factors into the valuation, unsupported by objective factors. However, in Tim's case, on the basis of the average historical discount between the prices of ordinary and savings shares, it was decided to assume a discount of 0% compared to the ordinary shares in determining the value of the savings shares. It needs to be stressed that the range value taken into consideration does not alter the economic substance of the dividend premium to which savings shares are entitled.

F. With reference to the Sum-of-the Parts method, after carefully examining the valuations put forward by the Advisors, Tim's Board of Directors identified the following ranges for the values of the ordinary and savings shares.

SUM-OF-THE-PARTS METHOD

	Values per share not adjusted for dividend			Values per share adjusted for dividend		
€	Telecom Italia	Tim	Ratio (X)	Telecom Italia	Tim	Ratio (X)
Value per ordinary share	2.97-3.28	5.26-5.50	1.68-1.77	2.86-3.17	5.1-5.25	1.65-1.75
Value per savings share	2.18-2.41	5.26-5.50	2.29-2.41	2.06-2.29	4.99-5.24	2.29-2.42

The results obtained by applying the Sum-of-the-Parts method confirm the relative values obtained by using the Market Price method.

G. In determining the Exchange Ratio, an analysis was also made of the reasonably foreseeable effects of the possible exercise of the right of withdrawal by holders of Tim savings shares. It was deemed, considering also the prices of the shares in the relevant period, that the result of such withdrawals would not require the Exchange Ratio to be modified, since it was reasonable to presume that the withdrawal price would be lower than the value attributed to Tim shares for the purposes of the Merger on the basis of the valuation methods applied.

3. Conclusions

3.1 Determination of the Exchange Ratio

3.1.1 Taking into account the valuations put forward by the Advisors, the Board of Directors has established the relative values of the Companies Participating in the Merger for the purpose of determining the Exchange Ratio.

3.1.2 The Exchange Ratio derived for the ordinary and savings shares by applying the foregoing methods is summarized below:

METHOD (ORDINARY SHARES)	EXCHANGE RATIO NOT ADJUSTED FOR DIVIDEND (X)	EXCHANGE RATIO ADJUSTED FOR DIVIDEND (X)
Market Price method		
– 16 November 2004	1.71	1.68
Weighted averages:		
– 1 month	1.73	1.71
– 2 months	1.73	1.70
– 3 months	1.74	1.71
– 6 months	1.77	1.74
– 12 months	1.78	1.75
Sum-of-the-Parts method	1.68-1.77	1.65-1.75

METHOD (SAVINGS SHARES)	EXCHANGE RATIO NOT ADJUSTED FOR DIVIDEND (X)	EXCHANGE RATIO ADJUSTED FOR DIVIDEND (X)
Market Price method		
– 16 November 2004	2.33	2.33
Weighted averages:		
– 1 month	2.30	2.30
– 2 months	2.32	2.32
– 3 months	2.34	2.34
– 6 months	2.39	2.39
– 12 months	2.42	2.43
Sum-of-the-Parts method	2.29-2.41	2.29-2.42

3.1.3 These conclusions were compared with those reached by the Board of Directors of Telecom Italia, taking into account the indications provided by its financial Advisors: JP Morgan, MCC, Mediobanca and Goldman Sachs. Following this valuation process and the comparison of the valuations obtained, the Exchange Ratio shown below was adopted.

3.2 Exchange Ratio

3.2.1 On the basis of the valuations of the Companies Participating in the Merger, the following Exchange Ratio, which determines the number of shares to be issued in connection with the Merger, was adopted:

- 1.73 Telecom Italia ordinary shares with a par value of €0.55 per share for each Tim ordinary share with a par value of €0.06;
- 2.36 Telecom Italia savings shares with a par value of €0.55 per share for each Tim savings share with a par value of €0.06.

3.2.2 No cash consideration is envisaged.

4. Procedure for assigning the shares of the Post-Merger Company and dividend entitlement date

4.1 Procedure for the exchange

4.1.1 In implementing the Merger, the Tim ordinary and savings shares held by Telecom Italia and the Tim ordinary shares held by Tim as treasury stock will be cancelled without exchange, whereas new Telecom Italia ordinary and savings shares will be issued to Tim's shareholders other than Telecom Italia in connection with the exchange.

Telecom Italia will effect the exchange by increasing its share capital by up to a maximum of €1,420,690,865.55, through the issuance of up to a maximum of 2,291,344,587 Telecom Italia ordinary shares and up to a maximum of 291,729,714 Telecom Italia savings shares, all with a par value of €0.55

per share. The maximum amount of the increase in Telecom Italia's share capital for purposes of the share exchange has been calculated without taking into consideration the Tim ordinary and savings shares held by Telecom Italia following the Offer or Tim's treasury shares, which will not be exchanged in the Merger.

As specified below, the amount of the increase was determined by also including the percentage of new shares to be issued in connection with the exercise of stock options previously granted by Telecom Italia and Tim to their respective employees and other employees of the Group (i.e. on a fully diluted basis).

4.1.2 The newly issued shares earmarked for the exchange will be assigned to the persons entitled to such shares, through their authorized intermediaries who are participants of the Monte Titoli S.p.A. central securities depository, at the effective date of the Merger. Non-dematerialized Tim shares may only be exchanged upon delivery of such shares to an authorized intermediary for deposit with the central securities depository on a dematerialized basis.

As part of the procedure for the assignment of Telecom Italia shares, Absorbing Company will arrange for the authorized intermediaries to provide Tim minority shareholders with a service to handle any fractions of shares, at market prices and at no cost in terms of expenses, stamp duty or commissions, that will permit the number of newly issued shares to which the shareholders are entitled on the basis of the exchange ratio to be rounded up or down to the nearest whole number.

4.2 Effective date of the Merger

4.2.1 Pursuant to Articles 2504-*bis*, third paragraph, and 2501-*ter*, first paragraph, subparagraph 5, of the Civil Code, the newly-issued Telecom Italia shares will have normal entitlement to all the rights appertaining thereto.

4.2.2 Pursuant to Article 2504-*bis*, second paragraph, of the Civil Code, the Merger will be effective, without prejudice to the effects referred to in Article 2501-*ter*, paragraphs 5 and 6, of the Civil Code, from the date of the last filing of the merger deed, or from such later date as may be specified in the merger deed itself.

Accordingly, as of that date, Telecom Italia will assume all of Tim's assets, rights and liabilities.

5. Effective date for accounting purposes

5.1.1 In accordance with the combined effect of Articles 2504-*bis*, third paragraph, and 2501-*ter*, first paragraph, subparagraph 6, of the Civil Code, and Article 172.9 of the Consolidated Income Tax Law (approved by Presidential Decree No. 917 of 22 December 1986), and in compliance with Article 6 of the Merger Plan, the transactions effected by Tim will be attributed to and recorded in Telecom Italia's accounts, for accounting and income tax purposes, as of 1 January of the year in which the Merger becomes effective, or 1 January 2005, in accordance with the planned timetable.

6. Italian tax effects of the Merger on Telecom Italia

6.1. Direct taxes: taxation of the Companies Participating in the Merger

6.1.1 For income tax purposes, pursuant to Article 172.1 of the Consolidated Income Tax Law (approved by Presidential Decree No. 917 of 22 December 1986), the Merger is tax neutral for Italian tax purposes and therefore does not constitute a sale or distribution of capital gains and losses on the assets of the merged or incorporated companies, including on inventories and goodwill. As regards the position of Telecom Italia, it should be noted that there is no merger goodwill to be recognized as income for tax purposes and thus merger differences will have no material tax impact. The reserves for tax-deferred income reported in Tim's latest financial statements, and existing at the effective date of the Merger, will be treated in accordance with the specific provisions of Article 172.5 of Presidential Decree No. 917 of 22 December 1986, and, if applicable, will be re-established.

6.1.2 On the effective date of the Merger, Telecom Italia will assume all of Tim's rights and obligations in relation to income taxes. In addition, since for accounting and tax purposes the Merger takes effect, retroactively, as of 1 January of the year in which the it becomes effective, there will not be a separate tax period between the closing date of Tim's last financial year and the effective date of the Merger.

6.1.3 Lastly, concerning the tax regime of the Spin-Off to be effected by Tim before the Merger, whereby it transfers its Domestic Communications Business to Tim Italia, it should be noted that the Spin-Off is tax neutral for Italian tax purposes and will therefore not give rise to taxable capital gains or tax-deductible losses.

6.2. Italian tax effects on shareholders

6.2.1 Pursuant to Article 172.3 of Presidential Decree No. 917 of 22 December 1986, the exchange of Tim shares for Telecom Italia shares does not constitute a sale, a distribution of capital gains or losses, or a source of income, as the transaction merely involves the replacement in shareholders' portfolios of the shares of Tim by shares of Telecom Italia. Accordingly, the basis in the Tim shares will be transferred to the shares obtained in the exchange.

Shareholders resident in countries outside Italy are urged to consult their own tax advisors about the tax effects of the Merger in their own jurisdictions.

6.3. Indirect taxes

6.3.1 The merger deed is subject to a registration fee of €129.11, pursuant to Article 4.b) of the first part of the schedule attached to Presidential Decree No. 131 of 22 December 1986.

7. Expected shareholdings in the Post-Merger Company

7.1 Tim shareholders

7.1.1 At 23 January 2005, on the basis of the shareholder register, disclosures made by shareholders and other information available, the following shareholder held more than 2% of Tim's ordinary shares:

Shareholders	Number of ordinary shares held	% of ordinary share capital
Telecom Italia S.p.A.	4,734,081,519	55.07%

7.2 Telecom Italia shareholders

7.2.1 At 23 January 2005, pursuant to the shareholder register, disclosures made by shareholders and other information available, the following shareholders held more than 2% of Telecom Italia's ordinary shares:

Shareholders	Number of ordinary shares held	% of ordinary share capital
Olimpia S.p.A.	1,751,765,823	16.96
Brandes Investment Partners LLC(*)	372,896,243	3.61
Hopa S.p.A.(**)	361,364,703	3.50
Assicurazioni Generali S.p.A.(***)	288,964,287	2.80
Bank of Italy(****)	231,499,817	2.24

* *Disclosure pursuant to Article 121.3 of CONSOB Regulation on Issuers.*

** *Shares held through the subsidiary company Holinvest S.p.A.*

*** *The list of companies through which the shares are held is available on the Internet at www.consob.it.*

**** *Shares partly held by the Bank of Italy's supplementary pension fund.*

7.3 Effects of the Merger on shareholders

7.3.1 Telecom Italia's post-Merger shareholdings will be affected by a number of factors and, in particular, by the conversion of Telecom Italia (formerly Olivetti) 1.5% 2001-2010 convertible bonds with redemption premium and the number of Telecom Italia and Tim stock options that are exercised. As regards the bonds, the information available to Tim indicates that conversion requests had been received for 463,187,994 additional Telecom Italia shares at 21 January 2005, compared to the share capital recorded in the Company Register.

The following table summarizes the foreseeable composition of Telecom Italia shareholders with holdings in excess of 2% of the ordinary share capital, assuming that no bonds are converted (in addition to those related to the requests submitted at 21 January 2005 referred to above, which are not yet reflected in the share capital recorded in the Company Register but are considered for purposes of the analysis below) and that no stock options are exercised.

The table is based exclusively on information in the Telecom Italia shareholder register or disclosed by shareholders in accordance with Article 120 of the Consolidated Law.

Shareholders	Number of ordinary shares held	% of ordinary share capital
Olimpia S.p.A.	1,751,765,823	13.46%
Brandes Investment Partners LLC	372,896,243	2.87%
Hopa S.p.A.	361,364,703	2.78%
Assicurazioni Generali S.p.A.	288,964,287	2.22%

It is also worth noting that, on 21 December 2004, Olimpia S.p.A. announced the approval by its extraordinary shareholders' meeting of an increase in capital of €2 billion by means of a rights issue, the proceeds of which will be used to purchase Telecom Italia shares. On 23 January 2005, Olimpia S.p.A. further announced that it had entered into two forward contracts to buy Telecom Italia ordinary shares and bonds convertible into Telecom Italia ordinary shares, respectively. The execution of these contracts – subject to the subscription of the above-mentioned capital increase – will entail an expenditure of approximately €1 billion. On the same date, Olimpia S.p.A. also announced that the other parties to the contracts already held shares and convertible bonds corresponding to approximately 310 million Telecom Italia ordinary shares.

Upon completion of the Merger, no shareholder is expected to control Telecom Italia.

8. Effects of the Merger on shareholders' agreements (Article 122 of Italian Legislative Decree 58/1998) relating to the shares of the Companies Participating in the Merger

The parties to the shareholders' agreements falling within the scope of Article 122 of Italian Legislative Decree 58/1998 that concern the Companies Participating in the Merger have not made any notifications concerning the possible effects of the Merger on such agreements.

9. Bylaw amendments

9.1 Telecom Italia's bylaws and amendments deriving from the Merger

9.1.1 In connection with the Merger, Telecom Italia will amend the article of its bylaws concerning the company's share capital to take account of the capital increase for the issuance of new ordinary and savings shares to be assigned in exchange to the holders of Tim ordinary and savings shares in accordance with the assignment procedure described in Section 4.1 above.

The maximum increase in Telecom Italia's share capital for the purposes of the share exchange,

- considering the maximum amount by which Tim's existing share capital may be increased, among other things as a consequence of the exercise of stock options granted and still valid; and
- on the basis of the Exchange Ratio indicated in Section 3.2 above, will be a maximum of €1,420,690,865.55, through the issuance of a maximum of 2,291,344,587 new Telecom Italia ordinary shares and a maximum of 291,729,714 new Telecom Italia savings shares, all with a par value of €0.55 per share. The maximum amount of the increase in Telecom Italia's share capital for purposes of the share exchange has been calculated without considering the Tim ordinary and savings shares held by Telecom Italia as a result of the Offer or Tim's treasury shares, which will not be exchanged in the Merger.

Provision has also been made for the amendments needed to permit the Post-Merger Company to take over stock option plans to the extent such plans are still effective.

The Absorbing Company will in fact succeed to Tim's obligations relating to its stock option plans and will therefore approve capital increases for the issuance of the required number of new ordinary shares, adjusted on the basis of the Exchange Ratio adopted for the Merger.

Consequently, holders of Tim stock options will have the right, when they exercise their options, to purchase at the predetermined strike price not the original number of ordinary shares of Tim but the larger number of ordinary shares of Telecom Italia, as the Post-Merger Company, determined on the basis of the Exchange Ratio of 1 to 1.73. The unit subscription price of the ordinary shares in respect of which stock options may be exercised will therefore be adjusted for each plan by dividing the original price by 1.73.

More specifically, Telecom Italia will approve an overall maximum increase in capital, divided into the following tranches, each of which is severable:

a) an increase of up to €11,705,656.05 for the exercise of stock options already granted by Tim under its "2000-2002 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 21,283,011 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the Exchange Ratio adopted for Tim shareholders for purposes of the Merger at a price of €6.42 for each option held (i.e. €3.710983 for each newly issued share);

b) an increase of up to €1,132,285 for the exercise of stock options already granted by Tim under its "2001-2003 Stock-Option Plans", to be implemented by 31 December 2005 through the issuance of up to 2,058,700 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the Exchange Ratio adopted for Tim shareholders for purposes of the Merger at a price of €8.671 for each option held (i.e. €5.012139 for each newly issued share);

c) an increase of up to €474,798.50 for the exercise of stock options already granted by Tim under its "2001-2003 Supplementary Plans", to be implemented by 31 December 2005 through the issuance of up to 863,270 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the Exchange Ratio adopted for Tim shareholders for purposes of the Merger at a price of €7.526 for each option held (i.e. €4.350289 for each newly issued share);

d) an increase of up to €22,150,920 for the exercise of stock options already granted by Tim under its "2002-2003 Stock-Option Plans", to be implemented by 31 December 2008 through the issuance of up to 40,274,400 Telecom Italia ordinary shares with a par value of €0.55 per share to be offered to the holders of the above-mentioned stock options on the basis of the Exchange Ratio adopted for Tim shareholders for purposes of the Merger at a price of €5.67 for each option held (i.e. €3.277457 for each newly issued share);

e) an increase of up to €3,192,173.05 for the exercise of stock options already granted by Tim under its "2003-2005 Stock-Option Plans", to be implemented through the issuance of up to a total of 5,803,951 shares with a par value of €0.55 per share, by 31 December 2008 for the first lot, by 31 December 2009 for the second lot and by 31 December 2010 for the third lot. The shares will be offered to the holders of the above-mentioned stock options on the basis of the Exchange Ratio adopted for Tim shareholders for purposes of the Merger at a price of €5.07 for each option held (i.e. €2.930636 for each newly issued share).

The amendments to the bylaws described above will come into force on the effective date of the Merger pursuant to Article 2504-*bis* of the Civil Code and as provided for in the Merger Plan.

10. Evaluation of the conditions for the exercise of the right of withdrawal (Articles 2437, 2437-*quinquies* and 2497-*quater* of the Civil Code)

10.1 Evaluation in relation to Article 2437-*quinquies* of the Civil Code

10.1.1 Telecom Italia's ordinary and savings shares are, and following the Merger will remain, listed on the *Mercato Telematico*, the electronic share market operated by Borsa Italiana S.p.A.

There is therefore no legal basis for Tim's shareholders to exercise the right of withdrawal under Article 2437-*quinquies* of the Civil Code.

10.2 Evaluation in relation to Article 2437 of the Civil Code

10.2.1 As already noted above, both Telecom Italia and Tim engage in telecommunication activities. The Merger will therefore not entail any significant change in the activities carried out by Telecom Italia and Tim, or in the related business risk.

It follows that it will not be necessary to change the corporate purpose in the bylaws of Telecom Italia, as the post-Merger company. Therefore, as far as this aspect is concerned, the Merger will not give rise to the conditions for the exercise of the right of withdrawal pursuant to Article 2437, first paragraph, subparagraph a), of the Civil Code.

10.2.2 As a result of the Merger, the holders of Tim savings shares will receive, in the share exchange, Telecom Italia savings shares which entitle holders to a smaller dividend premium than the cancelled Tim shares (see Section 1.4.7 above). The Merger will therefore be submitted for approval to the Special Meeting of Tim's savings shareholders, pursuant to Article 146.1b) of the Consolidated Law.

Moreover, for the reasons explained in Section 1.4.7 above concerning the smaller dividend premium of the Telecom Italia savings shares that will be assigned in the exchange to holders of Tim savings shares, holders of Tim savings shares who do not vote in favor of the Merger at the Special Meeting will be entitled to withdrawal rights pursuant to Article 2437, first paragraph, subparagraph g) of the Civil Code, since their property rights will be modified by the share exchange.

10.2.3 The exercise of the right of withdrawal by Tim's savings shareholders will be governed by Articles 2437-*bis* et seq. of the Civil Code. To this end, it should be noted in particular that, pursuant to the first paragraph of such article, Tim's savings shareholders who do not vote in favor of the Merger at the Special Meeting will be able to exercise their right of withdrawal within 15 days from the date of the filing of the merger resolution, which presupposes the approval of the Special Meeting, with the Company Register. This filing will be made public in accordance with applicable law and regulations. It should also be noted that, pursuant to Article 2437-*bis* of the Civil Code, shares for which the right of withdrawal is exercised may not be sold or transferred.

10.2.4 Consistent with its interest in purchasing all of Tim's savings shares, as evidenced by the Offer, Telecom Italia has indicated that it intends to purchase all the savings shares for which the right of withdrawal is exercised by exercising its prerogatives in accordance with applicable law.

10.3 Evaluation in relation to Article 2497-quater of the Civil Code

10.3.1 Following the Merger, Telecom Italia would in theory cease to perform its direction and supervision role with respect to Tim. However, since the companies are listed on regulated securities exchanges, there will be no legal basis for the holders of Tim shares to exercise the right of withdrawal under Article 2497-*quater* of the Civil Code.

TELECOM ITALIA MOBILE S.p.A.

ANNEX IV

TELECOM ITALIA S.p.A.
INTERIM FINANCIAL STATEMENTS AT SEPTEMBER 30, 2004

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BALANCE SHEETS

ASSETS		September 30, 2004		December 31, 2003
(in euro)				
RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS				
INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS				
- INTANGIBLE ASSETS				
Start-up and expansion costs		14,380,062		23,008,099
Industrial patents and intellectual property rights		1,172,266,452		882,699,375
Concessions, licenses, trademarks and similar rights		781,832		850,025
Goodwill		944,333		1,144,583
Work in progress and advances to suppliers		390,789,143		477,639,011
Other intangibles		156,981,657		99,238,269
TOTAL INTANGIBLE ASSETS		1,736,143,480		1,484,579,362
- FIXED ASSETS				
Land and buildings		1,126,560,324		1,106,851,118
Plant and machinery		9,386,824,709		10,050,719,281
Manufacturing and distribution equipment		12,837,708		10,048,945
Other fixed assets		43,960,946		48,846,328
Construction in progress and advances to suppliers		487,972,759		626,257,125
TOTAL FIXED ASSETS		11,058,156,447		11,842,722,798
- LONG-TERM INVESTMENTS				
Equity investments in				
subsidiaries		32,452,610,762		34,188,394,538
affiliated companies		354,385,465		450,394,506
other companies		203,989,644		220,159,093
Total equity investments		33,010,985,870		34,858,948,137
Advances on future capital contributions		1,518,944,440		136,237,932
Accounts receivable	(*)		(*)	
subsidiaries		71,380,205	2,890,502	67,097,561
affiliated companies	6,536,092	43,005,257	95,535	54,489,396
other receivables	18,193,207	103,705,571	68,613,790	157,428,512
Total accounts receivable	24,729,299	218,091,033	71,599,827	279,015,468
Treasury stock (total par value euro 700 thousand at 9/30/2004)		2,298,156		2,298,156
TOTAL LONG-TERM INVESTMENTS		34,750,319,499		35,276,499,693
TOTAL INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS		**47,544,619,426**		**48,603,801,852**
CURRENT ASSETS				
- INVENTORIES				
Contract work in process		32,885,410		23,341,218
Finished goods and merchandise		107,297,779		65,194,154
TOTAL INVENTORIES		140,183,188		88,535,372
- ACCOUNTS RECEIVABLE	(* *)		(* *)	
Trade accounts receivable		3,422,563,556		3,703,449,847
Accounts receivable from subsidiaries		1,921,885,667		3,075,289,042
Accounts receivable from affiliated companies		103,405,375		96,774,507
Taxes receivable		44,826,048		1,362,329,226
Deferred tax assets	2,055,138,575	2,845,094,308	2,055,138,575	3,229,915,964
Other receivables due from				
Government and other public entities for grants and subsidies		25,889,157		30,748,076
other receivables		597,277,286		807,653,267
Total other receivables		623,166,443		838,401,344
TOTAL ACCOUNTS RECEIVABLE		8,960,941,398		12,306,159,930
- SHORT-TERM FINANCIAL ASSETS				
Equity investments in subsidiaries		166,933,854		166,190,144
Other equity investments		8,800		21,314
Other securities		7,495,610		16,178,765
TOTAL SHORT-TERM FINANCIAL ASSETS		174,438,265		182,390,223
- LIQUID ASSETS				
Bank and postal accounts		775,813,849		204,634,612
Checks		40,255		47,595
Cash and valuables on hand		602,480		568,855
TOTAL LIQUID ASSETS		776,456,584		205,251,062
TOTAL CURRENT ASSETS		**10,052,019,434**		**12,782,336,589**
ACCRUED INCOME AND PREPAID EXPENSES				
Issue discounts and similar charges		115,444,954		110,621,576
Accrued income and other prepaid expenses		431,590,754		453,188,766
TOTAL ACCRUED INCOME AND PREPARED EXPENSES		**547,035,708**		**563,810,342**
TOTAL ASSETS		**58,143,674,568**		**61,949,948,783**

(*) Amounts due within 12 months

(*) Amounts due beyond 12 months*

LIABILITIES AND SHAREHOLDERS EQUITY	September 30, 2004		December 31, 2003	
(in euro)				
SHAREHOLDERS' EQUITY				
- SHARE CAPITAL		8,857,834,072		8,853,990,645
- ADDITIONAL PAID-IN CAPITAL		98,943,353		88,376,636
- RESERVES FOR INFLATION ADJUSTMENTS - Law No. 413, 12/30/1991		1,128,827		—
- LEGAL RESERVE		1,834,686,976		1,834,686,976
- RESERVE FOR TREASURY STOCK IN PORTFOLIO		2,298,156		2,298,156
- MISCELLANEOUS RESERVES				
. Reserve Law No. 488/9192		142,365,063		118,677,664
. Reserve L.D. No. 124/1993, ex art. 13		185,808		185,808
. Reserve D.P.R. No. 917/1986, ex art. 74		5,749,710		5,749,710
. Reserve for capital grants		507,937,032		498,701,503
. Miscellaneous reserves		119,012,282		119,012,282
. Merger surplus reserve		2,188,528,994		2,188,528,994
TOTAL MISCELLANEOUS RESERVES		2,963,778,889		2,930,855,961
- RETAINED EARNINGS		881,028,354		—
- NET INCOME		893,615,508		2,645,902,665
TOTAL SHAREHOLDERS' EQUITY		**15,533,314,135**		**16,356,111,039**
RESERVES FOR RISKS AND CHARGES				
Reserve for taxes and reserve for deferred taxes		130,864,595		119,410,092
Other reserves		628,284,150		657,917,133
TOTAL RESERVES FOR RISKS AND CHARGES		**759,148,745**		**777,327,225**
RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES		**1,035,429,431**		**972,412,757**
LIABILITIES	(* *)		(* *)	
Debentures	12,660,489,054	12,660,489,054	8,264,982,800	9,764,982,800
Convertible debentures	2,827,903,552	2,827,903,552	2,829,005,585	4,159,569,459
Due to banks	298,617,539	887,379,907	286,787,391	1,191,093,982
Due to other lenders	373,449,579	665,308,152	462,538,177	781,884,860
Advances		28,603,390		22,723,406
Trade accounts payable		1,390,027,240		1,929,794,121
Accounts payable to subsidiaries	12,979,857,370	18,002,784,906	9,071,133,778	20,543,520,078
Accounts payable to affiliated companies	764	95,687,867		84,770,489
Taxes payable		624,095,506		379,080,287
Contributions to pension and social security institutions	466,543,787	574,589,514	466,543,787	626,768,912
Other liabilities	441,373	1,362,979,312	441,373	1,911,283,963
TOTAL LIABILITIES	**29,607,303,018**	**39,119,848,400**	**21,381,432,892**	**41,395,472,357**
ACCRUED EXPENSES AND DEFERRED INCOME		**1,695,933,856**		**2,448,625,405**
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		**58,143,674,568**		**61,949,948,783**

(*) Amounts due beyond 12 months*

MEMORANDUM ACCOUNTS	September 30, 2004	December 31, 2003
(in euro)		
GUARANTEES PROVIDED		
Sureties		
on behalf of subsidiaries	24,522,456,332	29,654,575,978
on behalf of affiliated companies	145,542,631	106,450,253
on behalf of others	127,191,366	153,080,279
TOTAL GUARANTEES PROVIDED	**24,795,190,330**	**29,914,106,510**
COLLATERAL PROVIDED	—	—
PURCHASES AND SALES COMMITMENTS	**107,383,303**	**159,844,095**
OTHER MEMORANDUM ACCOUNTS	**13,943,138**	**18,549,141**
TOTAL MEMORANDUM ACCOUNTS	**24,916,516,771**	**30,092,499,746**

STATEMENTS OF INCOME	9 months to September 30, 2004	9 months to September 30, 2003
(in euro)		
PRODUCTION VALUE		
Sales and service revenues	11,793,168,540	11,872,225,646
Changes in inventory of contract work in process	9,544,192	5,649,798
Increases in capitalized internal construction costs	55,642,562	40,360,158
Other revenues and income		
operating grants	2,665,810	7,660,921
other	128,242,247	151,542,073
Total other revenues and income	130,908,057	159,202,994
TOTAL PRODUCTION VALUE	**11,989,263,350**	**12,077,438,595**
PRODUCTION COSTS		
Raw materials, supplies and merchandise	339,488,147	242,372,638
Services	3,825,376,273	3,844,030,870
Use of property not owned	444,939,708	532,718,016
Personnel costs		
wages and salaries	1,258,785,266	1,303,137,889
social security contributions	401,739,890	415,688,926
termination indemnities	98,373,573	101,848,910
other costs	29,979,083	32,154,514
Total personnel costs	1,788,877,812	1,852,830,238
Amortization, depreciation and writedowns		
amortization of intangible assets	426,637,083	417,130,877
depreciation of fixed assets	1,576,640,939	1,691,810,675
writedowns of receivables included in current assets and liquid assets	58,378,971	115,092,771
Total amortization, depreciation and writedowns	2,061,656,992	2,224,034,323
Changes in inventory of raw materials, supplies and merchandise	-42,103,624	-29,418,263
Provisions for risks	24,928,671	12,311,997
Miscellaneous operating costs		
losses on disposals of assets	15,938,426	9,578,329
TLC operating fees	17,359,591	16,003,662
other miscellaneous costs	256,713,934	203,702,172
Total miscellaneous operating costs	290,011,951	229,284,162
TOTAL PRODUCTION COSTS	**-8,733,175,930**	**-8,908,163,982**
OPERATING INCOME	**3,256,087,420**	**3,169,274,614**
FINANCIAL INCOME AND EXPENSE		
Income from equity investments		
dividends from subsidiaries	9,804,136	597,929,458
dividends from affiliated companies		
dividends from other companies	2,321,999	3,128,449
other income from equity investments	4,338,123	79,216,380
Total income from equity investments	16,464,258	680,274,287
Other financial income from		
accounts receivable included in long-term investments		
subsidiaries	2,784,382	2,563,024
affiliated companies	1,577,459	4,843,697
other	5,355,241	5,531,002
Total from accounts receivable included in long-term investments	9,717,082	12,937,723
securities, other than equity investments, included in long-term investments	240,725	1,642,385
other income		
interest and fees from subsidiaries	23,781,608	22,562,732
interest and fees from affiliated companies	47,631	355,307
interest and fees from others and miscellaneous income	120,750,355	40,267,853
Total other income	144,579,594	63,185,891
Total other financial income	154,537,401	77,765,999
Interest and other financial expense		
interest and fees paid to subsidiaries	566,296,197	657,199,262
interest and fees paid to affiliated companies	166,660	254,211
interest and fees paid to others and miscellaneous expense	881,004,217	1,384,820,146
Total interest and other financial expense	-1,447,467,074	-2,042,273,619
Foreign exchange gains and losses	-426,521	4,896,816
TOTAL FINANCIAL INCOME AND EXPENSE	**-1,276,891,935**	**-1,279,336,516**
VALUE ADJUSTMENTS TO FINANCIAL ASSETS		
Upward adjustments of equity investments	60,810,259	66,902,385
Total upward adjustments	60,810,259	66,902,385
Writedowns of equity investments	55,409,287	303,812,941
securities, other than equity investments, included in current assets	84,337	156,338
Total writedowns	-55,493,624	-303,969,279
TOTAL VALUE ADJUSTMENTS TO FINANCIAL ASSETS	**5,316,635**	**-237,066,894**
EXTRAORDINARY INCOME AND EXPENSE		
Income		
gains on disposals	10,522,928	32,969,363
elimination of tax interference	932,387	—
miscellaneous	32,144,743	956,589,661
Total income	43,600,059	989,559,025
Expense		
losses on disposals		387,804,138
prior years' taxes	1,271,238	4,697,879
provisions and writedowns of equity investments	112,415,547	146,139,000
miscellaneous	250,654,885	725,744,374
Total expense	-364,341,671	-1,264,385,392
TOTAL EXTRAORDINARY ITEMS	**-320,741,612**	**-274,826,367**
INCOME BEFORE TAXES	**1,663,770,508**	**1,378,044,836**
Income taxes, current and deferred	-770,155,000	634,081,000
NET INCOME	**893,615,508**	**2,012,125,836**

NOTES TO THE FINANCIAL STATEMENTS

INTRODUCTION

The interim financial statements for the nine months ended September 30, 2004 of Telecom Italia S.p.A. have been prepared in accordance with the provisions of the Italian Civil Code pertaining to statutory financial statements and revised by the introduction of the reform of corporate law pursuant to Legislative Decree No. 6 dated January 17, 2003, as amended.

The accounting policies adopted in preparing the interim financial statements for the nine months ended September 30, 2004, taking into account the adjustments required by the nature of interim financial reporting, have been applied on a basis consistent with those of the annual financial statements, with the exception of the policies for charging income taxes for the period (see the accounting policy for “reserves for risks and charges”) and dividends (see the accounting policy for “revenues”)

During the period, there were no exceptional cases causing recourse to the departures allowed by art. 2423, paragraph 4, of the Italian Civil Code.

The interim financial statements include the statement of cash flows presented in Annex 6.

All amounts are stated in thousands of euro, unless otherwise indicated.

Summary of significant accounting policies

Intangible assets

Intangible assets are recorded at acquisition or production cost and are amortized using the straight-line method over their estimated period of benefit.

Intangible assets are written down when there is a permanent impairment to below their net book value, in accordance with article 2426, paragraph 1, item 3 of the Italian Civil Code. The original recorded value will be reinstated in subsequent years if the underlying assumptions are no longer correct.

Intangible assets specifically refer to the following:

“Start-up and expansion costs”: these are amortized over a period of five years starting from the time the asset produces an economic benefit.

“Industrial patents and intellectual property rights”: these are amortized over their estimated period of benefit on a five-year basis (industrial patents) or on a three-year basis (software), starting from the time the asset produces an economic benefit.

“Concessions, licenses, trademarks and similar rights”: these refer mainly to satellite utilization rights and are amortized over the contract period.

“Goodwill:, this relates to the acquisition of the “administrative services” business segment from Holding Media e Comunicazioni, TIM, Finsiel and Telecom Italia Media and is amortized over five years.

“Other intangibles”: these refer almost entirely to leasehold improvements. Amortization is calculated on the basis of the lesser of the period of future economic benefit or the residual lease period, starting from the time the expenses are incurred or from the time the asset produces an economic benefit.

“Research, development and advertising costs” are charged to income in the year incurred.

Fixed assets

Fixed assets are recorded at acquisition or production cost and depreciated using the straight-line method at rates determined on the basis of their estimated remaining useful life and include inflation adjustments.

Fixed assets are written down when there is a permanent impairment to below their net book value, in accordance with article 2426, paragraph 1, item 3 of the Italian Civil Code. The original recorded value will be reinstated in subsequent years if the underlying assumptions are no longer correct. Construction in progress is stated at the amount of direct costs incurred (materials used for or intended for installations, third-party services, miscellaneous expenses, internal design costs, as well as company labor). The value of fixed assets does not include maintenance costs incurred for their upkeep to guarantee their expected useful life, their original capacity and productivity, and costs borne to repair malfunctions and failures; such expenses are charged to the statement of income in the year incurred.

Depreciation is calculated on the basis of the estimated useful lives of the installations.

Total accumulated depreciation for fixed assets was upwardly adjusted where called for by special laws.

The elimination, disposal or sale of fixed assets is recorded in the financial statement by eliminating the cost and accumulated depreciation from the financial statements and booking the related gain or loss in the statement of income.

Equity investments

Equity investments considered long-term in nature are recorded in long-term investments or, if acquired for subsequent sale, recorded in short-term financial assets.

The cost flow for equity investments recorded in long-term investments and current assets is calculated by reference to the "weighted average cost per movement" method.

Acquisition cost is increased by statutory inflation adjustments, as well as the voluntary one made to several investments during the preparation of the financial statements at December 31, 1981, as well as the cancellation deficit, attributed to Tim shares and which arose from the merger of Telecom Italia S.p.A. in Olivetti S.p.A., being the difference between the carrying value of the cancelled shares and the underlying share of net equity of the merged company.

The carrying value of investments recorded in long-term investments is adjusted for any reasonable expectations of a decline in profitability or recoverability in future years.

In the case of a permanent impairment, the value of such equity investments is written down and the impairment in value in excess of the corresponding carrying value is recorded in "*reserves for risks and charges*".

Equity investments included under current assets are stated at the lower of the cost of acquisition and estimated realizable value, represented by the period-end prices on the electronic trading market of the Italian stock exchange and the NASDAQ.

The cost of investments in foreign companies has been translated at the historical exchange rates prevailing at the time of acquisition or subscription or at the period-end rate, if lower, in the case the reduction is considered a permanent impairment.

Writedowns of investments, whether included in long-term investments or current assets, will be reversed in subsequent years if the underlying assumptions are no longer correct.

Other securities (other than equity investments) recorded in short-term financial assets

Securities recorded in current assets are valued at the lower of cost of acquisition and realizable value based on market prices at period-end; if, in future years, the underlying assumptions for the writedowns are no longer correct, the carrying value will be adjusted to market value up to the amount of original cost.

Inventories

Inventories – consisting of goods intended for sale, as well as stock on hand of technical materials and replacement parts to be used in the business during the year and for maintenance – are valued at the lower of cost, calculated using the weighted-average method, and realizable value.

The carrying value of goods in stock is reduced, through appropriate writedowns, for obsolete materials.

Inventories include the amount of work on behalf of third parties in progress at the end of the period, valued according to the "costs" already incurred.

Accounts receivable and liabilities

Accounts receivable are stated at estimated realizable value and classified under long-term investments or current assets. They include – as far as telecommunications services are concerned – the amount of services already rendered to customers, already billed or still to be billed, as well as invoices for the sale of telephone and on-line equipment.

Liabilities are shown at their nominal value.

Transactions in foreign currency

Monetary assets and liabilities are accounted for at the exchange rate as of the transaction date and updated to the exchange rates prevailing at period-end, taking into account hedging contracts. Unrealized positive and negative differences arising from recording foreign currency assets and liabilities at the exchange rates at the transaction date and at the period-end date are recorded in the statement of income and any unrealized net exchange gain is set aside in a specific reserve until realization.

Securitization

The total amount of receivables sold under securitization transactions commenced in 2001 is reversed from the balance sheet as the contra-entry for the consideration received on the sale; the amount paid is represented by the non-repeatable amount received immediately (without recourse) whereas the deferred portion is recorded in *Other receivables (financial)* in current assets. This balance sheet caption is presented net of the relative allowance account calculated on the basis of estimated realizable value; the change in the allowance account is booked in *Financial expense* in the statement of income. The difference between the carrying value of the receivables sold and the agreed consideration on the sale is recognized in the statement of income in *Miscellaneous operating costs,* for the trading portion, and in *Interest and other financial expense*, for the financial portion. The costs and expenses relating to the start-up and implementation of the securitization program (arrangement, underwriting, legal, rating, audit and other expenses) were charged directly to the 2001 statement of income in *Service* costs by the merged company.

Accruals and deferrals

These items are recorded on the accrual basis. "*Issue discounts and similar charges"* consist of costs in connection with long-term loans, which are charged to the statement of income over the period of the loan in proportion to the accrued interest.

Reserves for risks and charges

"Reserve for taxes and reserve for deferred taxes"

This includes: i) income taxes for the period calculated on the basis of the best possible estimate using available information and on a reasonable forecast of performance for the year up to the end of the tax period; ii) provisions for estimated tax charges (including any surtaxes and late payment interest) on positions not yet agreed or in dispute; iii) deferred taxes calculated on the basis of the temporary differences between the value attributed to the assets and liabilities for statutory purposes and the value attributed to the same assets and liabilities for tax purposes. Whenever the conditions exist, deferred tax liabilities are offset against deferred tax assets recorded in the caption "Deferred tax assets" in the balance sheet.

Deferred taxes on tax-deferred reserves and funds are booked if such reserves will be distributed or, in any case, utilized and their distribution or utilization gives rise to a tax charge.

"Other reserves": these reserves relate primarily to provisions to cover risks and charges for losses or liabilities of certain or likely existence whose amount or date of occurrence could, however, not be determined at the end of the period. The provisions reflect the best possible estimate, based on the commitments made and on the data available.

Reserve for employee termination indemnities

The amount of this reserve is determined in accordance with current laws (in particular Law No. 297 of May 29, 1982, which provides for fixed and variable cost-of-living adjustments) and collective bargaining agreements. The reserve is adjusted to the liability matured at the end of the period for personnel in force at that date and is net of advances paid.

Due to shareholders for loans

"Shareholders" are considered parties which hold directly at least 2% of share capital at the end of the period. At September 30, 2004, shareholders holding at least 2% of the share capital of Telecom Italia had made no loans to the company.

Employee benefit obligations under Law No. 58/1992

With regard to Telecom Italia's obligation under Law No. 58/1992 to guarantee a uniform insurance status under the Telephone Workers' Social Security Fund (which became part of the general "Employees Pension Fund" beginning January 1, 2000) to all employees in service as of February 20, 1992 in the companies Stet, Sip, Italcable and Telespazio, as well as those who moved from the Public Administration to Iritel, Article 66, paragraph 1 of Legislative Decree 331/1993 and converted into Law No. 427/1993, specifies that the sums due to the Fund should be recorded in the financial statements and are tax deductible in the years in which the fifteen equal annual deferred installments are paid to discharge this obligation.

At the present time, the amount of the liability, which will be determined by the National Social Security Institute (Istituto Nazionale della Previdenza Sociale - INPS), can be estimated only roughly, due to problems relating to the interpretation and application of the social security legislation and to the lack of certain data which only the social security institutions currently possess (at September 30, 2004, INPS had notified the Company of around 97% of the positions, the uniform insurance status of which gives rise to expenses for Telecom Italia).

A dispute concerning the application and interpretation of this law arose with INPS regarding the exclusion from the estimates under Law No. 58/1992 of all employees (except for employees of the former Iritel) who had already filed an application to join pursuant to Law No. 29/1979 before February 20, 1992, even though that application had not been processed by INPS. The position of the Telecom Italia is that the criteria set forth in Law No. 29/1979 – and, therefore, payment of the respective obligations – apply to these employees.

At the present time, the parties have agreed that the differences in interpretation shall be settled through test appeals for a final determination of the correct interpretation of the law in question. While awaiting these decisions, Telecom Italia has agreed to pay, with reservation, the amounts requested by INPS based on the criteria determined by the latter, subject to subsequent equalization adjustments, if the Courts ultimately accept the Company's interpretation.

Having said that, a reasonable estimate of the principal amount of the liability attributable to Telecom Italia (net of the amounts attributed to Group companies for the employees transferred to those companies) could vary between euro 954 million (partial application of Law 29/1979) and euro 1,275 million (full application of Law 58/1992), of which euro 568 million has already been paid, depending on conflicting interpretations and taking into account all personnel involved. In either case, the impact of the charge should definitely be compatible with the income of future years, since, as allowed under Article 5, paragraph 3 of Law No. 58/1992, the payments requested by INPS are made in fifteen equal annual deferred installments (including annual interest of 5%), based on notification of the expenses by INPS.

The remaining liability for obligations under Law No. 58/1992, to be paid in fifteen annual installments on the basis of the positions notified by INPS up to September 30, 2004 and the interpretation of said positions, totals (net of the amounts attributed to Group companies for the employees transferred to those companies) euro 946 million, of which euro 691 million is for the principal amount and euro 255 million for accrued interest.

Nevertheless, these financial statements at September 30, 2004 include euro 530 million of residual payables to INPS, (net of the amount attributed to Group companies for the employees transferred to those companies), relating to the estimate made for the employees of the former State Company for Telephone Services (ASST) by the special Ministerial Commission established under Law No. 58/1992 upon the transfer of the assets of the Post and Telecommunications Administration to Iritel, and recorded by the latter company in its financial statements at December 31, 1993. As a result, these charges will have no impact on the results of future years, since they were already included in the aforementioned calculation.

The expenses recorded in the first nine months of 2004 in "extraordinary expenses" amount to euro 123 million and include accrued interest. This amount takes into account the above-mentioned expenses paid by Telecom Italia to INPS also on behalf of other Group companies for those employees transferred to them and covered by the obligation of a uniform insurance status under Law No. 58/1992, recovering the amounts paid from these same companies. The recovery is recorded in the statement of income under "extraordinary income" and amounts to euro 2 million.

Grants

Operating grants (directly credited to the statement of income) and capital grants or grants for installations are recorded in the accounting period in which the paperwork documenting the grants is received, or in the period in which the respective costs are incurred, provided that the certainty of payment is confirmed by established procedures.

Capital grants and grants for installation are recorded under “deferred income” and credited to the statement of income in relation to the depreciation taken on the assets to which the grants refer.

Revenues and expenses

Revenues and expenses are recorded on an accrual basis. Revenues relating to telecommunications services are shown gross of the amounts due to other carriers which are recorded, for the same amount, in production costs.

Fees for new access lines and line transfers are recorded as income when the service is provided. As usual, dividends from subsidiaries arising from the current year’s earnings are not included in the results for the first nine months of 2004 but are recorded at the end of the year in accordance with the maturity principle.

Dividends from affiliated companies and other companies, on the other hand, are recognized in the statement of income according to the accrual principle, that is, in the year in which the respective right to the receivable arises, following the declaration of dividends approved by the shareholders’ resolution of those companies.

Leased assets

Capital goods acquired under leasing agreements are recognized in the financial statements by a method consistent with current legislation, which requires that leasing payments be recorded as operating costs.

Memorandum accounts

“*Guarantees provided*” are shown for the amount of the remaining liability or other obligation guaranteed; those provided in foreign currencies are translated at period-end exchange rates.

“*Purchases and sales commitments*” are determined on the basis of the unperformed portion of contracts outstanding at the end of the period which do not fall under the normal “operating cycle”.

Derivative financial instruments

Derivative financial instruments are used by Telecom Italia S.p.A. to hedge exposure to interest rate and exchange rate risks.

For derivative financial instruments used to hedge interest rate risks, the interest differentials are recorded in the statement of income in “financial income and expense” based on the accrual principle.

For financial instruments used to hedge exchange rate risks, the cost (or “financial component” calculated as the difference between the spot rate at the date of stipulating the contract and the forward rate) is recorded in the statement of income in “financial income and expense” based on the accrual principle.

Premiums relating to option-type financial instruments are recorded in “other liabilities” or “other receivables” and, if exercised, are considered as an incidental charge to the purchase or sale value of the underlying instruments; if the option is not exercised the premium is recorded in the statement of income under financial income (financial expense).

In this manner, the derivative financial instruments are valued consistently with the underlying asset and liability, for each transaction, and any net expense is recognized in the statement of income.

Option-type derivative financial instruments existing at the end of the period are valued at the lower of cost and market value at the balance sheet date.

BALANCE SHEETS - ASSETS

INTANGIBLES, FIXED ASSETS AND LONG-TERM INVESTMENTS

Intangible assets ***euro 1,736,144 thousand***
(euro 1,484,579 thousand at December 31, 2003)

A summary of the changes in intangible assets during the period is presented below:

(in thousands of euro)	9 months to 9/30/2004
- additions	688,179
- amortization	(426,637)
- eliminations and other movements	(9,977)
Total	**251,565**

An analysis of the composition and the changes in intangible assets during the period is presented in the following tables:

12/31/2003					
(in thousands of euro)	**Cost**	**Upward adjustments**	**Writedowns**	**Accumulated amortization**	**Total**
Start-up and expansion costs	152.755			(129.747)	23.008
Industrial patents and intellectual property rights	4.102.823			(3.220.124)	882.699
Concessions, licenses, trademarks and similar rights	92.506			(91.656)	850
Goodwill	1.335			(190)	1.145
Work in progress and advances to suppliers	477.639				477.639
Other intangibles(*)	416.695			(317.457)	99.238
Total	**5.243.753**	**—**	**—**	**(3.759.174)**	**1.484.579**
(*) of which:					
Leasehold improvements	416.294			(317.056)	99.238

Changes during the period					
(in thousands of euro)	**Additions**	**Reclassifications**	**Sales/ Retirements/ Other movements**(a)	**Amortization**	**Total**
Start-up and expansion costs				(8.628)	(8.628)
Industrial patents and intellectual property rights		688.640		(399.072)	289.568
Concessions, licenses, trademarks and similar rights				(68)	(68)
Goodwill				(201)	(201)
Work in progress and advances to suppliers	688.179	(767.997)	(7.032)		(86.850)
Other intangibles(*)		80.528	(4.116)	(18.668)	57.744
Total	**688.179**	**1.171**	**(11.148)**	**(426.637)**	**251.565**

(*) of which:
Leasehold improvements — *80.528* *(4.116)* *(18.668)* *57.744*

(a) Broken down as follows:

	Cost	Upward adjustments	Writedowns	Accumulated amortization	Net value
Industrial patents and intellectual property rights	*(156.118)*			*156.118*	*0*
Work in progress and advances to suppliers	*(7.032)*				*(7.032)*
Other intangibles	*(89.738)*			*85.622*	*(4.116)*
Total	*(252.888)*			*241.740*	*(11.148)*

	9/30/2004				
(in thousands of euro)	**Cost**	**Upward adjustments**	**Writedowns**	**Accumulated amortization**	**Total**
Start-up and expansion costs	152.755			(138.375)	14.380
Industrial patents and intellectual property rights	4.635.345			(3.463.078)	1.172.267
Concessions, licenses, trademarks and similar rights	92.506			(91.724)	782
Goodwill	1.335			(391)	944
Work in progress and advances to suppliers	390.789			0	390.789
Other intangibles(*)	407.485			(250.503)	156.982
Total	**5.680.215**	**—**	**—**	**(3.944.071)**	**1.736.144**
(*) of which:					
Leasehold improvements	407.084	—	—	(250.102)	156.982

In particular:

"Start-up and expansion costs" consist of underwriting commissions connected with share capital increases.

"*Industrial patents and intellectual property rights"* consist almost entirely of applications software.

"*Work in progress and advances to suppliers"* mainly refer to software projects for network and operating program applications. All acquisitions of intangibles are managed through specific work orders and recorded in this caption. Reclassifications refer to assets that came into use during the period.

"Other intangibles" refer to leasehold improvements made to properties owned by third parties and include the costs incurred to meet the operating requirements of the Company in the rented premises.

Fixed assets ***euro 11,058,157 thousand***

(euro 11,842,723 thousand at December 31, 2003)

A summary of the changes in fixed assets during the period is presented as follows:

(in thousands of euro)	**9 months to 9/30/2004**
- additions	805,534
- disposals and other movements	(13,459)
- depreciation	(1,576,641)
Total	**(784,566)**

An analysis of the composition and the changes in fixed assets during the period is presented in the following tables:

12/31/2003

(in thousands of euro)	Cost	Upward adjustments	Writedowns	Accumulated depreciation	Total
Land and buildings					
. non-industrial	21.281	792		(1.189)	20.884
. industrial	1.899.071	392.275	(4.827)	(1.200.552)	1.085.967
	1.920.352	393.067	(4.827)	(1.201.741)	1.106.851
Plant and machinery	46.662.097	730.392	(727.730)	(36.614.040)	10.050.719
Manufacturing and distribution equipment	767.876	2.693		(760.520)	10.049
Other fixed assets	554.248	4.251		(509.652)	48.847
Construction in progress and advances to supplies	626.257				626.257
Total	**50.530.830**	**1.130.403**	**(732.557)**	**(39.085.953)**	**11.842.723**

Changes during the period

(in thousands of euro)	Additions	Reclassifications	Sales/ Retirements/ Other movements[(a)]	Writedowns/ Writebacks	Depreciation	Total
Land and buildings						
. non-industrial		66	(382)		(111)	(427)
. industrial		80.414	(2.607)		(57.671)	20.136
	0	80.480	(2.989)	0	(57.782)	19.709
Plant and machinery		846.772	(15.892)		(1.494.774)	(663.894)
Manufacturing and distribution equipment		8.331	(64)		(5.478)	2.789
Other fixed assets		12.675	1.046		(18.607)	(4.886)
Construction in progress and advances to supplies	805.534	(949.429)	5.611			(138.284)
Total "fixed assets"	805.534	(1.171)	(12.288)	0	(1.576.641)	(784.566)

(a) Broken down as follows:

	Cost	Upward adjustments	Writedowns	Accumulated depreciation	Net value
Land and buildings					
. non-industrial	*(458)*			*76*	*(382)*
. industrial	*(3.704)*	*(1.250)*	*55*	*2.292*	*(2.607)*
	(4.162)	*(1.250)*	*55*	*2.368*	*(2.989)*
Plant and machinery	*(184.625)*	*(2.973)*		*171.706*	*(15.892)*
Manufacturing and distribution equipment	*(239.300)*			*239.236*	*(64)*
Other fixed assets	*(3.479)*	*(14)*		*4.539*	*1.046*
Construction in progress and advances to supplies	*5.611*				*5.611*
TOTAL	*(425.955)*	*(4.237)*	*55*	*417.849*	*(12.288)*

9/30/2004					
(in thousands of euro)	Cost	Upward adjustments	Writedowns	Accumulated depreciation	Total
Land and buildings					
. non-industrial	20.889	792		(1.224)	20.457
. industrial	1.975.661	391.025	(4.772)	(1.255.811)	1.106.103
	1.996.550	391.817	(4.772)	(1.257.035)	1.126.560
Plant and machinery	47.324.244	727.419	(727.730)	(37.937.108)	9.386.825
Manufacturing and distribution equipment	536.907	2.693		(526.762)	12.838
Other fixed assets	563.444	4.237		(523.720)	43.961
Construction in progress and advances to supplies	487.973				487.973
Total "fixed assets"	**50.909.118**	**1.126.166**	**(732.502)**	**(40.244.625)**	**11.058.157**

All fixed asset purchases are managed using specific work orders and recorded in "construction in progress and advances to suppliers". Reclassifications refer to fixed assets that came into use during the period.

Accumulated depreciation at September 30, 2004 is considered sufficient in relation to the remaining period of utilization of the assets and is determined on the basis of the estimated useful lives of the installations making up the domestic telecommunications network. Depreciation is calculated at the rates used in the previous year. Accumulated depreciation, net of writedowns, covers 78.4% of fixed assets at September 30, 2004 compared to 76.7% at December 31, 2003.

In accordance with the contract signed January 16, 2004 by Telecom Italia S.p.A. and Fintecna S.p.A., containing reciprocal options for the purchase and sale (put / call) of seven properties owned by Fintecna S.p.A., at a total price of euro 72,000 thousand, on June 22, 2004, Telecom Italia S.p.A., after exercising the option in April 2004, signed the deed for the purchase of the seven properties for the contractually agreed price.

Moreover, in accordance with the changes introduced by Legislative Decree No. 6 dated January 17, 2003 and next changes (Reform of Corporate Law), as well as the principles issued on the subject by the Italian Accounting Board, tax interference relative to accelerated deprecation charges (euro 932 thousand) made in prior years by the merging company Olivetti, in accordance with tax laws, has been eliminated with a contra-entry to extraordinary income; the relevant reserve for deferred taxes was booked with a contra-entry to other extraordinary expenses (prior years' taxes).

Leased assets purchased through finance lease contracts

The Company has fixed assets purchased through sale and leaseback contracts as well as finance lease contracts. These are accounted for using the liability method by which lease payments are charged to costs under the use of property not owned caption. Any gains on the sale of the assets under sale and leaseback transactions are recognized immediately in the statement of income. Had these contracts been accounted for using the financial method, entries would have been made in the statement of income for the interest on the financed principal and for the depreciation charge attributable to the leased assets; additionally, entries would have been made to record the assets in fixed assets and the residual debt under liabilities. Furthermore, use of this method would also have resulted in the deferral of gains, in constant parts, on sale and leaseback transactions over the period of the finance lease contract.

The effects of this accounting treatment are described in the following table:

	BALANCE SHEET EFFECT AT SEPTEMBER 30, 2004	(millions of euro)
a)	**Outstanding contracts**	
	Book value of leased assets under finance contracts at December 31, 2003, net of euro 27 million and accumulated depreciation of euro 201 million	1,434
	Assets acquired under finance lease contracts in the period 1/1 – 9/30/2004 (+)	—
	Assets redeemed under finance lease contracts in the period 1/1 – 9/30/2004 (-)	—
	Depreciation charge for the period 1/1 – 9/30/2004 (-)	(65)
	Writedowns/writebacks on assets under finance lease contracts in the period 1/1 –9/30/2004 (+/-)	—
	Book value of leased assets under finance contracts at September 30, 2004 net of euro 27 million and accumulated depreciation of euro 266 million	1,369
b)	**Assets redeemed in the period 1/1 – 9/30/2004**	
	Total higher value of assets redeemed, calculated according to the financial method, compared to their accounting net book value	—
c)	**Prepaid expenses at September 30, 2004**	—
d)	**Liabilities**	
	Implicit liabilities for finance lease transactions at December 31, 2003 (of which euro 62 million due within 12 months, euro 277 million due between 12 months and 60 months and euro 1,369 million due beyond 60 months)	1,708
	Implicit liabilities arising in the period 1/1 – 9/30/2004 (+)	1
	Repayment of principal and assets redeemed in the period 1/1 – 9/30/2004 (-)	(43)
	Implicit liabilities for finance lease transactions at September 30, 2004 (of which euro 67 million due within 12 months, euro 292 million due between 12 months and 60 months and euro 1,307 million due beyond 60 months)	1,666
e)	**Total gross effect at September 30, 2004 (a+b+c-d)**	**(297)**
f)	**Tax effect**	**(76)**
g)	**Balance sheet effect at September 30, 2004 of leasing transactions recognized using the financial method (e-f)**	**(221)**

STATEMENT OF INCOME EFFECT FOR 9 MONTHS TO SEPTEMBER 30, 2004	(million of euro)
Reversal of installments on finance lease transactions	(143)
Recognition of financial expenses on finance lease transactions	100
Recognition of:	
- depreciation charge:	
. on outstanding contracts	65
. on assets redeemed	—
- writedowns/writebacks on assets under finance lease contracts	—
Effect on income before taxes	(22)
Recognition of tax effect	(8)
Statement of income effect for 9 months to September 30, 2004 of leasing transactions recognized using the financial method	**(14)**

The use of financial method relating to the sale and leaseback transactions would have resulted, at September 30, 2004, a decrease of shareholders' equity by euro 226 million and a decrease of net income of the first nine months of 2004 by euro 15 million.

Long-term investments ***euro 34,750,319 thousand***
(euro 35,276,500 thousand at December 31, 2003)

Details are as follows:

(in thousands of euro)	**9/30/2004**	**12/31/2003**
Equity investments in:		
• subsidiaries	32,452,611	34,188,395
• affiliated companies	354,385	450,394
• other companies	203,989	220,159
	33,010,985	**34,858,948**
Advances on future capital contributions	**1,518,945**	**136,238**
Accounts receivable:		
• subsidiaries	71,380	67,098
• affiliated companies	43,005	54,490
• other receivables	103,706	157,428
	218,091	**279,016**
Treasury stock	**2,298**	**2,298**
Total	**34,750,319**	**35,276,500**

Equity investments *euro 33,010,985 thousand*

Annex 1 presents the movements in each investment during the period together with the corresponding amount at the beginning of the year and at September 30, 2004.

In summary, investments in subsidiaries, affiliates and other companies decreased by euro 1,847,963 thousand compared to December 31, 2003 mainly as a result of the distribution of reserves by Telecom Italia International.

Changes during the period are as follows:

(in thousands of euro)		
Increases:		
• **Subscription to capital increases, recapitalizations and loss coverage of:** Latin American Nautilus (40,801), Sky Italia (19,315), Edotel (1,459), Consorzio S.I.A.R.C (1), IM.SER (126), EUROFLY SERVICES (1,334). Consorzio ABI LAB (1), Consorzio DISTRETTO AUDIOVISIVO and ICT (5)		63,042
• **Definitive capital increase** from advances on future capital contributions relating to IT Telecom (110,440), Sky Italia (43,780), Edotel (1,200) and Netesi (435)		155,855
• **Writebacks of value** of Olivetti Tecnost (60,000) and Edotel (46)		60,046
Total increases	**(A)**	**278,943**
Decreases:		
Sales/reductions of shares/quotas in: Sky Italia (87,859), Siosistemi (1,600), Pirelli Real Estate (15,199) and TILAB GP (9)		(104,667)
Distribution of reserves of: Telecom Italia International (1,800,000), Tiglio I (47,985) and Olivetti Gestioni Ivrea (4,849)		(1,852,834)
Writedowns for losses of value charged to the statement of income of: Telecom Italia Media (112,416), IT Telecom (25,659), Latin American Nautilus (7,093), LI.SIT. (4,338), PAR.FIN (256), Netesi (79), TILAB SA (48) and TILAB GP (12),		(149,901)
Writedowns for losses of value covered by the reserve for losses of subsidiaries and affiliates of: IM.SER (168), Consorzio S.I.A.R.C. (1), Consorzio CO.TIM (2), Consorzio CI.MARK (3) and Consorzio di BIOINGEGNERIA ED INFORMATICA MEDICA (15).		(189)
Writedowns for losses of value covered by the reserve for contractual and other risks of Sky Italia (19,315)		(19,315)
Total decreases	**(B)**	**(2,126,906)**
Net change for the period	**(A-B)**	**(1,847,963)**

In particular, the following should be mentioned:

- on February 20, 2004, the Shareholders' Meetings of Olivetti International S.A. and Telecom Italia Finance approved the plan for the merger of Olivetti International S.A. in Telecom Italia Finance. Following this transaction, Telecom Italia Finance issued 30,000, new shares to Telecom Italia (the sole shareholder of Olivetti International S.A.) in exchange for the shares of the merged company. The merger is effective for accounting purposes as from January 1, 2004;
- on September 28, 2004, Telecom Italia sold its 19.9% interest in Sky Italia to the NewsCorp group. Consideration on the sale was euro 88 million. The transaction resulted in a gain over the carrying value at June 30, 2004 of euro 31.4 million which offsets the effect of the writedown made in the first half of the year. Accordingly, the economic impact of the transaction for Telecom Italia is basically nil.
- under the second stage of the Tiglio project (which calls for an end to the process of enhancing the real estate assets held by Tiglio I and Tiglio II by contributing the assets to real estate funds or by realizing profits through individual sale transactions), the affiliated company Tiglio I contributed real estate assets: i) to "TECLA – FONDO UFFICI" made up of 65 buildings for a total market value of about euro 926 million, to which a 15% discount was applied by virtue of their transfer en masse, in addition to a cash contribution of euro 25 million and ii) to "CLOE FONDO UFFICI", made up of 39 properties for a total market value of euro 877 million, to which a 15% discount was applied by virtue of their transfer en masse.

  With reference to "TECLA – FONDO UFFICI", its placement was concluded on March 1, 2004. The total placement offer, net of indebtedness of 60% of the value contributed, was equal to euro 288 million. 10% of this amount – as a voluntary gesture – was kept by Tiglio I, 2% was subscribed by Pirelli & C. Real Estate Sgr S.p.A., as manager of the fund, while the remaining 88% was entirely placed on the market.

  As for "CLOE – FONDO UFFICI", placed on the market on June 29, 2004, the offer totaled euro 298 million. 5% was subscribed by Pirelli & C Real Estate Sgr S.p.A. as manager of the fund, while the remaining 95% was entirely placed with Italian investors for about 70%, and foreign investors 30%.

  Following these transactions, in June and September 2004, Tiglio I proceeded with the distribution in cash (additional paid-in capital) for euro 47,985 thousand;
- for purposes of bringing Telecom Italia Finance's financial position into equilibrium, with transfer of the liquid resources available at Telecom Italia International, the following transactions took place during the month of September 2004:
  - purchase, by Telecom Italia, of 40% of the investment in Edotel held by TIM for euro 1,939 thousand. After this transaction, Telecom Italia's holding in Edotel rose from 60% to 100%;
  - distribution of additional paid-in capital by Telecom Italia International to Telecom Italia for euro 1,800,000 thousand;
  - advance on future capital contribution for euro 1,500,000 thousand made by Telecom Italia to Edotel.

  In October 2004, Telecom Italia subscribed to Telecom Italia Finance's capital increase by contributing the investment in Edotel;
- some investments in subsidiaries and affiliated companies are recorded at a amount in excess of the corresponding share of the underlying shareholders' equity, net of dividends and after consolidation adjustments. These investments are maintained at their carrying values since they are expected to show future earnings and their assets are worth more than their respective book values. In particular, with regard to the investment in TIM, the higher carrying value compared to the underlying net equity and the stock market price is due to the allocation of the merger deficit on the Olivetti – Telecom Italia merger. However, taking into account the current strategic positioning of the business as well as its potential for further growth, it is believed, consistent with a recent valuation conducted by an external consultant, that the carrying value is aligned to the effective value of the investment.

A comparison between the market price of listed shares at September 30, 2004 and their carrying value shows an unrealized loss of euro 6,841,328 thousand (of which euro 6,745,794 thousand can be ascribed to the investment held in TIM). Further details are given in Annex 2.

Advances on future capital contributions *euro 1,518,945 thousand*

Advances on future capital contributions increased by euro 1,382,706 thousand compared to December 31, 2003, and are shown net of the relative allowance accounts of euro 38,539 thousand. The increase since

December 31, 2003 is attributable to the aforementioned advance made to Edotel (euro 1,500,000 thousand). This caption also includes advances made to Telegono (8,840 thousand), EPIClink (euro 7,209 thousand) and Loquendo (euro 2,896 thousand).

Accounts receivable *euro 218,091 thousand*

Accounts receivable decreased by euro 60,925 thousand compared to December 31, 2003. Details are as follows:

		Changes during the period			
(in thousands of euro)	**12/31/2003**	**Disburse-ments**	**Reimburse-ments**	**Other changes**	**9/30/2004**
Subsidiaries	67,098	4,197	—	85	71,380
Affiliated companies	54,490	1,269	(3,914)	(8,840)	43,005
Other receivables	157,428	11,539	(65,261)	—	103,706
Total	**279,016**	**17,005**	**(69,175)**	**(8,755)**	**218,091**

Subsidiaries euro 71,380 thousand

Accounts receivables from subsidiaries refer mainly to loans made to Stet Hellas for the acquisition of the UMTS license (euro 60,000 thousand) and to Mediterranean Nautilus (euro 11,380 thousand) to meet financial requirements.

Affiliated companies euro 43,005 thousand

Accounts receivable from affiliated companies refer mainly to loans made to the companies Aree Urbane (euro 31,616 thousand), Telegono (euro 6,400 thousand), Tiglio II (euro 2,601 thousand for the purchase of properties) and Mirror International Holding (euro 2,252 thousand).

Other receivables euro 103,706 thousand

Accounts receivable mainly refer to:

- the remaining loans receivable from employees (euro 48,255 thousand);
- the prepayment of the tax on the reserve for employee termination indemnities (euro 51,195 thousand), required under Law No. 662 of December 23, 1996, revalued as set forth by law;
- security deposits of euro 3,917 thousand.

Treasury stock *euro 2,298 thousand*

Treasury stock remains unchanged compared to December 31, 2003. Treasury stock refers to 1,272,014 ordinary shares originally held by the merging company Olivetti.

* * *

As regards accounts receivable included in long-term investments, the portion due within and beyond five years is presented in the attached Annex 3.

Current assets

Inventories — ***euro 140,183 thousand***

(euro 88,535 thousand at December 31, 2003)

Inventories increased by euro 51,648 thousand compared to December 31, 2003 principally due to higher inventories connected with the marketing of Aladino cordless phones and videophones. Inventories consist of "contract work in process " (euro 32,885 thousand) and "merchandise " (euro 107,298 thousand).

Accounts receivable — ***euro 8,960,942 thousand***

(euro 12,306,160 thousand at December 31, 2003)

Accounts receivable decreased by euro 3,345,218 thousand compared to December 31, 2003. A breakdown and the changes that occurred during the period are provided in the table below:

		Changes during the period				
(in thousands of euro)	**12/31/2003**	**Utilizations**	**Provisions**	**Other**	**Total changes**	**9/30/2004**
Trade accounts receivable	4,021,325			(264,298)	(264,298)	3,757,027
. allowance for doubtful accounts	(317,875)	41,792	(58,379)		(16,587)	(334,462)
Total trade accounts receivable	**3,703,450**	**41,792**	**(58,379)**	**(264,298)**	**(280,885)**	**3,422,565**
Accounts receivable from subsidiaries	3,078,742			(1,153,404)	(1,153,404)	1,925,338
. allowance for doubtful accounts of subsidiaries	(3,453)					(3,453)
Total accounts receivable from subsidiaries	**3,075,289**			**(1,153,404)**	**(1,153,404)**	**1,921,885**
. *of which financial receivables*	*823,919*			*302,751*	*302,751*	*1,126,670*
Accounts receivable from affiliated companies	123,574			(20,168)	(20,168)	103,406
. allowance for doubtful accounts of affiliated companies	(26,800)			26,800	26,800	—
Total accounts receivable from affiliated companies	**96,774**			**6,632**	**6,632**	**103,406**
. *of which financial receivables*	*13,718*			*(11,361)*	*(11,361)*	*2,357*
Taxes receivable	**1,362,329**			**(1,317,503)**	**(1,317,503)**	**44,826**
Deferred tax assets	**3,229,916**			**(384,822)**	**(384,822)**	**2,845,094**
Other receivables	**838,402**	**18,230**		**(233,466)**	**(215,236)**	**623,166**
. Government and other public entities for grants and subsidies	30,748			(4,859)	(4,859)	25,889
. other receivables	860,176			(227,924)	(227,924)	632,252
. allowance for doubtful accounts	(52,522)	18,230		(683)	17,547	(34,975)
Total	**12,306,160**	**60,022**	**(58,379)**	**(3,346,861)**	**(3,345,218)**	**8,960,942**

Trade accounts receivable — *euro 3,422,565 thousand*

Trade accounts receivable decreased by euro 280,885 thousand compared to December 31, 2003 and are shown net of the relative allowance accounts (euro 334,462 thousand, of which euro 58,379 thousand was provided during the period).

They include euro 567,194 thousand of receivables from other wireline and mobile telecommunications operators.

Furthermore, the following accounts receivable discounting and securitization transactions were carried out:

- *Securitization*

  The program for the securitization of trade accounts receivable generated by services rendered to Telecom Italia Wireline clientele began during 2001 has continued during the period.

  In the first nine months of 2004, the total amount of trade accounts receivable sold under the securitization program were equal to euro 6,586 million and refers to Telecom Italia's receivables from consumer and microbusiness customers. At September 30, 2004, receivables sold amount to euro 811,066 thousand (euro 874,368 thousand at December 31, 2003), of which euro 682,000 thousand is not yet due.

  The securitization transaction led to a reduction in net financial indebtedness of euro 789,566 thousand at September 30, 2004 (euro 851,302 thousand at December 31, 2003).

  Furthermore, Telecom Italia posted a short-term financial payable (euro 209,814 thousand) for loans made by TI Securitisation Vehicle S.r.l. out of the excess liquid resources generated by the securitization transaction.

- *Factoring*

  In the first nine months of 2004, trade accounts receivable without recourse were sold to leading factoring companies for a total amount of euro 92,839 thousand (euro 379,271 thousand at December 31, 2003). The factoring transactions by Telecom Italia led to a reduction in net financial indebtedness at September 30, 2004 of euro 136,378 thousand (euro 334,909 thousand at December 31, 2003).

Accounts receivable from subsidiaries *euro 1,921,885 thousand*

Accounts receivable from subsidiaries decreased by euro 1,153,404 thousand, compared to December 31, 2003, and include trade, financial and other receivables. The reduction is mainly due to the collection of dividends from subsidiaries accrued at December 31, 2003.

Financial receivables, equal to euro 1,126,670 thousand, reflect current account transactions carried out at market rates for cash management purposes and loans. They principally include accounts receivable from *Olivetti Tecnost (euro 468,106 thousand), Telecom Italia Media (euro 256,071 thousand), IT Telecom (euro 284,251 thousand) and Finsiel (euro 23,632 thousand).* Trade accounts receivable (euro 551,595 thousand) relate to TLC services rendered mainly to *Telecom Italia Sparkle (euro 77,105 thousand), TIM (euro 188,844 thousand), IT Telecom (euro 89,420 thousand), Telecom Italia Media (euro 31,808 thousand), Path.Net (euro 49,083 thousand), Telecom Italia Learning Services (euro 27,637 thousand)* and management fees from *Telecom Italia International (euro 23,104 thousand).* Other receivables (euro 243,620 thousand) mainly include the receivables connected with the Group's VAT settlement system, specifically from *TIM (euro 211,812 thousand) and Telecom Italia Sparkle (euro 25,751 thousand).*

Accounts receivable from affiliated companies *euro 103,406 thousand*

Accounts receivable from affiliated companies increased by euro 6,632 thousand compared to December 31, 2003, and include trade, financial and other receivables.

Financial receivables total euro 2,357 thousand. Trade accounts receivable (euro 84,883 thousand) refer to *Teleleasing (euro 30,787 thousand)* for the sale of TLC products and services and *LI.SIT (euro 40,814 thousand)* for the supply of health cards to the Lombardy Region. Other receivables (euro 16,166 thousand) mainly refer to transactions with *Tiglio I (euro 7,035 thousand) and LI.SIT. (euro 9,131 thousand).*

The allowance for doubtful accounts was completely utilized during the period following the waiver of receivables due by the Telecom Italia Group from Sky Italia, sold on September 28, 2004.

Taxes receivable *euro 44,826 thousand*

Taxes receivable decreased by euro 1,317,503 thousand, compared to December 31, 2003, mainly due to the sale of IRPEG receivables of euro 1,103,000 thousand to TIM to be used to pay the 2004 on-account payment for IRES.

They specifically include:

- VAT receivable, euro 11,991 thousand;
- direct income taxes receivable, euro 20,311 thousand;
- other indirect taxes receivable, euro 12,524 thousand.

Deferred tax assets *euro 2,845,094 thousand*

Deferred tax assets decreased by euro 384,822 thousand, compared to December 31, 2003, due to the set-off against the reserve for deferred taxes.

Other receivables *euro 623,166 thousand*

Other receivables principally regard: credit positions (net of the relative allowance account) from TI Securitisation Vehicle S.r.l. for the deferred portion of trade accounts receivable securitization transactions (euro 241,213 thousand), customer payments in transit with the banking and postal systems (euro 129,524 thousand), employee-related receivables (euro 52,349 thousand), receivables from the Ministry of Industry, Commerce and Handicrafts, the European Union and the Ministry of Instruction, University and Research for grants in respect of research and training projects (euro 25,889 thousand) and advances to suppliers (euro 20,599 thousand).

* * *

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of receivables by geographical area is presented in Annex 5.

Short-term financial assets ***euro 174,439 thousand***
(euro 182,390 thousand at December 31, 2003)

The composition and changes during the period are shown in the following table:

		Changes during the period				
(in thousands of euro)	**12/31/2003**	**Acquisitions**	**Sales/Re-imbursements**	**Writedowns/ Writebacks**	**Total changes**	**9/30/2004**
Equity investments in subsidiaries	**166,190**	—	—	744	744	**166.934**
Other equity investments	**21**	—	—	(12)	(12)	**9**
Other securities	**16,179**	—	(8,599)	(84)	(8,683)	**7,496**
Total	**182,390**	**—**	**(8,599)**	**648**	**(7,951)**	**174,439**

Short-term financial assets total euro 174,439 thousand and mainly include the following:

- euro 166,899 thousand relating to 38,192,000 TIM ordinary shares and euro 35 thousand relating to 164,997 Telecom Italia Media savings shares purchased for subsequent trading;
- C.C.T. and B.T.P. treasury bills for a total of euro 7,496 thousand.

Further details are provided in Annex 2.

Liquid assets ***euro 776,457 thousand***
(euro 205,251 thousand at December 31, 2003)

Liquid assets rose by euro 571,206 thousand principally as a result of higher cash resources in Italian and foreign bank accounts.

Liquid assets are composed of the following:

(in thousands of euro)	**12/31/2003**	**9/30/2004**
Bank and postal accounts	204,635	775,814
Checks	47	40
Cash and valuables on hand	569	603
Total	**205,251**	**776,457**

Accrued income and prepaid expenses ***euro 547,036 thousand***
(euro 563,811 thousand at December 31, 2003)

Accrued income and prepaid expenses decreased by euro 16,775 thousand compared to December 31, 2003, and include the following:

(in thousands of euro)	**12/31/2003**	**9/30/2004**
Issue discounts and similar charges	110,622	115,445
Accrued income		
. financial income	20,423	43,008
. other	275	1,030
	20,698	44,038
Other prepaid expenses		
. trading expense	90,299	91,012
. financial expense	325,261	286,046
. other	16,931	10,495
	432,491	387,553
Accrued income and other prepaid expenses	453,189	431,591
Total	**563,811**	**547,036**

Issue discounts and similar charges *euro 115,445 thousand*

"Issue discounts and similar charges" refer to incidental costs on loans (euro 74,179 thousand) and costs relating to the issue of bonds (euro 41,266 thousand).

Accrued income and other prepaid expenses *euro 431,591 thousand*

Accrued financial income mainly includes euro 33,802 thousand of income on derivative financial instruments, euro 3,497 thousand of sundry financial income, euro 2,809 thousand of income from long-term loans made to subsidiaries, as well as euro 1,531 thousand of interest income subsidized until 1991 by the government under Law No. 67/1988, equivalent to three percentage points of the cost of the loans which replaced those assigned to the Company, through Cassa Depositi e Prestiti, under Law No. 887/1984.

Other prepaid expenses mainly pertain to building rents (euro 35,824 thousand), financial expenses (euro 284,310 thousand) for the portion of the premium on the redemption of convertible bonds relating to future years, fees regarding facilities (euro 10,495 thousand), insurance premiums (euro 13,248 thousand) and rental and maintenance charges (euro 7,691 thousand).

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A breakdown of receivables and accrued income by maturity and type is presented in Annex 3.

BALANCE SHEETS - LIABILITIES AND SHAREHOLDERS' EQUITY

Shareholders' equity — ***euro 15,533,314 thousand***

(euro 16,356,111 thousand at December 31, 2003)

Shareholders' equity includes the following:

(in thousands of euro)	**12/31/2003**	**9/30/2004**
Share capital	8,853,991	8,857,834
Additional paid-in capital	88,377	98,943
Revaluation reserve Law No. 413, 12/31/1991	—	1,129
Legal reserve	1,834,687	1,834,687
Reserve for treasury stock in portfolio	2,298	2,298
Miscellaneous reserves		
. Reserve Law No. 488/92	118,678	142,365
. Reserve, L.D. No. 124/93, ex art. 13	185	185
. Reserve D.P.R. No. 917/86 ex art. 74	5,750	5,750
. Reserve for capital grants	498,701	507,937
. Miscellaneous reserves	119,012	119,012
. Merger surplus reserve	2,188,529	2,188,529
Retained earnings	—	881,029
Net income for the year	2,645,903	—
	16,356,111	14,639,698
Net income for the period		893,616
Total	**16,356,111**	**15,533,314**

Share capital

The share capital of Telecom Italia S.p.A. at September 30, 2004 amounts to euro 8,857,834 thousand and consists of 10,309,231,790 ordinary shares and 5,795,921,069 savings shares, all with a par value of euro 0.55 each.

Share capital increased by euro 3,843 thousand compared to December 31, 2003 due to the following movements:

- conversion of 1,182,574 "Telecom Italia 1.5% 2001 – 2010 convertible bonds with a premium on redemption" for the issue of 557,554 new shares for a par value of euro 306 thousand;
- exercise of 1,948,120 stock options set aside for employees of the company for the issue of 6,430,493 new shares for a par value of euro 3,537 thousand.

Additional paid-in capital

Additional paid-in capital at September 30, 2004 amounts to euro 98,943 thousand, with an increase of euro 10,566 thousand compared to December 31, 2003. The change in this caption is due to the additional paid-in capital on the foregoing capital increases.

Reserves for inflation adjustments - Law No. 413, 12/30/1991

This reserve for inflation adjustments, which showed a nil balance at December 31, 2003 following its complete utilization to cover the loss for the year 2002 of the merging company Olivetti, was replenished at June 30, 2004 for the entire amount, equal to euro 1,129 thousand, pursuant to the resolution passed by the Shareholders' Meeting on May 6, 2004

Legal reserve

The legal reserve amounts to euro 1,834,687 thousand at September 30, 2004, unchanged from December 31, 2003.

Reserve for treasury stock in portfolio

This reserve amounts to euro 2,298 thousand at September 30, 2004, unchanged from December 31, 2003.

Miscellaneous reserves

Miscellaneous reserves amount in total to euro 2,963,778 thousand at September 30, 2004, with an increase of euro 32,923 thousand compared to December 31, 2003. The various components of miscellaneous reserves are analyzed in the following paragraphs.

Reserve Law No. 488/1992: this reserve, euro 142,365 thousand, increased by euro 23,687 thousand compared to December 31, 2003 as a result of the appropriation of net income for the year 2003, as voted by the Shareholders' Meeting on May 6, 2004, in order to obtain the benefits stated in Law 488/92 under the projects for investments in the South of Italy.

Reserve Law No. 124/1993, ex art. 13: this reserve, euro 185 thousand at September 30, 2004, is unchanged from December 31, 2003.

Reserve DPR No. 917/1986, ex art. 74: this reserve, euro 5,750 thousand at September 30, 2004, is unchanged from December 31, 2003.

Reserve for capital grants: this reserve, equal to euro 507,937 thousand at September 30, 2004, increased by euro 9,236 thousand compared to December 31, 2003 due to the transfer from the "reserves for risks and charges" of the portion of grants that became available during the period.

Miscellaneous reserves: these reserves, euro 119,012 thousand at September 30, 2004, are unchanged from December 31, 2003.

Merger surplus reserve: this reserve, euro 2,188,529 thousand at September 30, 2004, is unchanged from December 31, 2003.

Retained earnings

Retained earnings refer to the appropriation of net income for the year 2003, euro 881,029 thousand, pursuant to the resolution passed by the Shareholders' Meeting of May 6, 2004.

In order to complete disclosure on shareholders' equity, the following statements are presented:

- statement showing the reserves subject to restrictions for statutory purposes and the tax treatment applicable in the event of distribution;
- statement prepared according to ex art. 2427, paragraph 7 - bis, showing the items in shareholders' equity separately according to their source, possibility of utilization and distribution, in addition to their utilization in prior years;
- statement of changes in shareholders' equity during the prior year and in the first nine months of 2004.

Shareholders' equity reserves – Restrictions for statutory purposes and tax treatment

(in thousands of euro)	Amounts not subject to statutory restrictions (a)	Amounts subject to statutory restrictions (b)	September 30, 2004 (c)=(a+b)=(d+e+f)	Amounts of reserves which, in the event of distribution, form part of the taxable income of the company (d)	Amounts of other income reserves (e)	Amount of reserves which, in the event of distribution, do not form part of the taxable income of the company (f)
Reserves and retained earnings						
Additional paid-in capital	98,943	—	98,943	—	—	98,943
Legal reserve	63,120	1,771,567	1,834,687	1,834,667	—	20
Reserve for treasury stock in portfolio	—	2,298	2,298	—	2,298	—
Merger surplus reserve	2,188,529	—	2,188,529	—	—	2,188,529
Reserve Law No. 488/92	—	142,365	142,365	—	122,090	20,275
Reserve, L.D. No. 124/93, ex art. 13	185	—	185	185	—	—
Reserve D.P.R. No. 917/86 ex art. 74	5,750	—	5,750	5,750	—	—
Reserve for capital grants	507,937	—	507,937	507,937	—	—
Revaluation reserve Law No. 413/91	1,129	—	1,129	1,129	—	—
Miscellaneous reserves	104,632	14,380	119,012	—	643	118,369
Retained earnings	881,029	—	881,029	—	881,029	—
Total reserves and retained earnings	**3,851,254**	**1,930,610**	**5,781,864**	**2,349,668**	**1,006,060**	**2,426,136**

The amount of distributable reserves on which the Company does not bear tax charges is equal to euro 3,273,153 thousand.

Statement according to ex art. 2427, no. 7-bis of the Italian Civil Code

Nature/description				Summary of the amounts utilized during the last three years	
				for absorption of losses	for other reasons (*)
(in thousands of euro)	Amount	Possibility of utilization	Amount available	Total	Total
Share capital	**8,857,834**			**0**	**10,961**
Capital reserves:					
Additional paid-in capital	98,943	A, B, C	98,943	3,700,751	
Legal reserve	1,834,687	A, B, C	63,120	920,810	
Reserve Law No. 488/92	20,275	A, B	20,275		
Reserve, L.D. No. 124/93, ex art. 13	185	A, B, C	185		
Reserve D.P.R. No. 917/86 ex art. 74	5,750	A, B, C	5,750		
Reserve for capital grants	507,937	A, B, C	507,937		
Miscellaneous reserves	118,369	A, B, C	118,369	28,816	
Merger surplus reserve	2,188,529	A, B, C	2,188,529		
Income reserves:					
Revaluation reserve Law No. 413/91	1,129	A, B, C	1,129	1,129	
Reserve for treasury stock in portfolio	2,298	—	0		
Reserve Law No. 488/92	122,090	A, B	122,090		
Miscellaneous reserves	643	A, B, C	643		
Retained earnings	881,029	A, B, C	881,029		
Total	**14,639,698**		**4,007,999**	**4,651,505**	**10,961**
Amount not distributable(1)			156,745		
Remaining amount distributable			**3,851,254**		

Key:

A: for share capital increase
B: for absorption of losses
C: for distribution to shareholders

(*) *The amounts utilized do not include reclassifications among individual captions of shareholders' equity.*

(1) *Represents the amount not distributable due to: the reserve Law No. 488/1922 (euro 142,365 thousand) and the part set aside to cover unamortized intangible assets according to ex art. 2426, paragraph 5 (euro 14,380 thousand).*

Statement of changes in shareholders' equity

(in thousands of euro)	Share capital	Capital increases awaiting registration in Companies Register	Additional paid-in capital	Additional paid-in capital on capital increases awaiting registration in Companies Register	Revaluation reserve Law No. 413/91	Legal reserve	Reserve for treasury stock in portfolio	Reserve Law No. 488/92	Reserve L.D. No. 124/93, ex art. 13	Reserve D.P.R. No. 917/86 ex art. 74	Special reserve	Reserve for capital grants	Miscellaneous reserves	Merger surplus reserve	Retained earnings	Net income for the year	Net income for the period	Total
Balance at January 1, 2003	**8,845,240**	**200**	**3,765,365**	**127**	**1,129**	**920,810**	**2,298**				**1,888,261**		**147,828**		**(299,930)**	**(6,239,963)**		**9,031,365**
Appropriation of 2002 profit:																		
- Absorption of loss for the year (as voted by the Shareholders' Meeting of May 26, 2003)			*(3,400,820)*	*(127)*	*(1,129)*	*(920,810)*					*(1,888,261)*		*(28,816)*			*6,239,963*		*0*
Other changes:																		
- Absorption of the accumulated deficit (as voted by the Shareholders' Meeting of May 26, 2003)			*(299,930)*												*299,930*			*0*
- Changes connected with the Olivetti-Telecom Italia merger	*(10,961)*					*20*								*4,633,630*				*4,622,689*
- Reclassification of merger surplus						*1,834,667*		*118,678*	*185*	*5,750*		*485,821*		*(2,445,101)*				*0*
- Conversion of 385,731 "Telecom Italia 1.5% 2001-2004 convertible bonds with a premium on redemption" and 19,623,310 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption"	*13,457*		*7,170*															*20,627*
- Exercise of stock options	*6,055*		*16,592*															*22,647*
- Transfer from the "Reserves for risks and charges" of the portion of grants which became available during the year												*12,880*						*12,880*
- Other changes	*200*	*(200)*																*0*
Net income for the year 2003																2,645,903		2,645,903
Balance at December 31, 2003	**8,853,991**	**0**	**88,377**	**0**	**0**	**1,834,687**	**2,298**	**118,678**	**185**	**5,750**	**0**	**498,701**	**119,012**	**2,188,529**	**0**	**2,645,903**	**0**	**16,356,111**

Statement of changes in shareholders' equity (Continued)

(in thousands of euro)	Share capital	Capital increases awaiting registration in Companies Register	Additional paid-in capital	Additional paid-in capital on capital increases awaiting registration in Companies Register	Revaluation reserve Law No. 413/91	Legal reserve	Reserve for treasury stock in portfolio	Reserve Law No. 488/92	Reserve L.D. No. 124/93, ex art. 13	Reserve D.P.R. No. 917/86 ex art. 74	Special reserve	Reserve for capital grants	Miscellaneous reserves	Merger surplus reserve	Retained earnings	Net income for the year	Net income for the period	Total
Appropriation of 2002 profit (as voted by the Shareholders' Meeting of May 6, 2004)																		
– Declaration of dividends (€0.1041 per ordinary share; €0.1151 per savings share)																*(1,740,058)*		*(1,740,058)*
– Other appropriations					*1,129*			*23,687*							*881,029*	*(905,845)*		*0*
Other changes:																		
– Conversion of 1,182,574 "Telecom Italia 1.5% 2001-2010 convertible bonds with a premium on redemption"	*306*		*875*															*1,181*
– Exercise of stock options	*3,537*		*9,691*															*13,228*
– Exercise of warrants for shares of Telecom Italia ex Olivetti 1999-2004			*0*															*0*
– Transfer from the "Reserves for risks and charges" of the portion of grants which became available during the period												*9,236*						*9,236*
Net income for the 9 months to September 30, 2004																	893,616	893,616
Balance at September 30, 2004	**8,857,834**	**0**	**98,943**	**0**	**1,129**	**1,834,687**	**2,298**	**142,365**	**185**	**5,750**	**0**	**507,937**	**119,012**	**2,188,529**	**881,029**	**0**	**893,616**	**15,533,314**

As far as future potential changes in share capital are concerned, at September 30, 2004, the following are still outstanding:

– 2,388,870,888 “Telecom Italia 1.5% 2001 – 2004 convertible bonds with a premium on redemption” (formerly known as “Olivetti 1.5% 2001 – 2004 convertible bonds with a premium on redemption”), including 116,204 bonds for which conversion into shares had already been requested on September 30, 2004, with the consequent reduction in the quantity of bonds still convertible with a contra-entry for a liability with future shareholders (the corresponding 54,791 ordinary shares for a par value of euro 30 thousand plus additional paid-in capital of euro 86 thousand were issued on October 14, 2004).

  Such bonds originally allowed conversion into Olivetti shares, in a ratio of one Olivetti share for every bond converted.

  As a result of the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital of the merging company and in light of the ratio indicated above, such bonds now allow the conversion to Telecom Italia shares in a ratio of 0.471553 Telecom Italia ordinary shares for every bond converted.

  Against the above bonds that can still be converted, therefore, besides the above 54,791 shares, a further maximum 1,126,424,442 Telecom Italia ordinary shares could be issued, for a total par value of euro 619,533 thousand, plus additional paid-in capital of euro 1,769,221 thousand.

– 800,000 options of the ex Olivetti “Stock Option Plan 2002-2004”.

  Such options were originally valid for the subscription of the same number of Olivetti shares at a price which, after the adjustment for the capital increases against payment by Olivetti in 2001, was equal to euro 3.308 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute share capital and on the basis of the exchange ratio indicated above, such options are now valid for the subscription of 0.471553 Telecom Italia ordinary shares each, at a price of about euro 7.015 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 377,241 new Telecom Italia ordinary shares could be issued, for a total par value of euro 207 thousand, plus additional paid-in capital of euro 2,439 thousand.

– 5,940,000 options of the “Three-year Stock Option Plan February 2002-December 2004” ex Olivetti.

  Such options were originally valid for the subscription of the same number of Olivetti shares at a price which, after the adjustment for the capital increases against payment by Olivetti in 2001, was equal to euro 2.515 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute share capital and on the basis of the exchange ratio indicated above, such options are now valid for the subscription of 0.471553 Telecom Italia ordinary shares each, at a price of about euro 5.333 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 2,604,518 new Telecom Italia ordinary shares could be issued, for a total par value of euro 1,432 thousand, plus additional paid-in capital of euro 12,459 thousand.

– 3,147,309,291 options of the “Stock Option Plan 1999” ex Telecom Italia, net of 11,196,439 options for which exercise had already been requested at September 30, 2004 (the corresponding 36,958 shares for a par value of euro 20 thousand plus additional paid-in capital of euro 56 thousand were issued in October 2004).

  Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 6.79 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio of 3.300871 new Telecom Italia S.p.A. (former Olivetti S.p.A.) ordinary shares for every old Telecom Italia ordinary share, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about euro 2.057 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, besides the above 36,958 shares, a further maximum 10,388,791 new Telecom Italia ordinary shares could be issued, for a total par value of euro 5,714 thousand, plus additional paid-in capital of euro 15,656 thousand.

– 10,699,996 options of the “Stock Option Plan 2000” ex Telecom Italia.

  Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 13.815 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about euro 4.185 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 35,319,216 new Telecom Italia ordinary shares could be issued, for a total par value of euro 19,426 thousand, plus additional paid-in capital of euro 128,394 thousand.

– 32,080,000 options of the “Stock Option Plan 2001” ex Telecom Italia.

  Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 10.488 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about euro 3.177 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 105,891,314 new Telecom Italia ordinary shares could be issued, for a total par value of euro 58,240 thousand, plus additional paid-in capital of euro 278,213 thousand.

– 11,250,000 options of the “Stock Option Plan 2002 Top” ex Telecom Italia.

  Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at a price of euro 9.203 for every option exercised.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of about 2.788 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary, therefore, a maximum 37,134,780 new Telecom Italia ordinary shares could be issued, for a total par value of euro 20,424 thousand, plus additional paid-in capital of euro 83,110 thousand.

– 24,283,200 options of the “Stock Option Plan 2002” ex Telecom Italia.

  Such options were originally valid for the subscription of the same number of ordinary shares of the merged company Telecom Italia at the following prices for each option held: 23,243,200 options at a price of euro 9.665, 840,000 options at a price of euro 7.952 and 200,000 options at the price of euro 7.721.

  Subsequent to the merger of Telecom Italia S.p.A. in Olivetti S.p.A., following the process to redistribute the share capital and in light of the exchange ratio indicated above, such options are now valid for the subscription of 3.300871 Telecom Italia ordinary shares each, at a price of, respectively, about euro 2.928, about euro 2.409 and about euro 2.339 per share.

  Against the above options that can still be exercised, taking into account the maximum quantities of the shares that can be subscribed by each beneficiary and the different subscription prices, therefore, a maximum 80,155,261 new Telecom Italia ordinary shares could be issued, for a total par value of euro 44,085 thousand, plus additional paid-in capital of euro 188,783 thousand.

The Shareholders’ Meeting of May 6, 2004 also conferred the Board of Directors with the right (which, to date, has not been exercised), for a maximum period of five years beginning May 6, 2004, to increase against payment, at one or more times, the share capital for a maximum total amount of euro 880,000,000, through the issue of a maximum of 1,600,000,000 ordinary shares, in whole or in part

(i) to be offered as option rights to the shareholders and convertible bondholders, or

(ii) to be offered for subscription to the employees of Telecom Italia S.p.A. or to the companies which it controls, with the exclusion of the option rights, pursuant to the combined provision of art. 2441, last paragraph, of the Italian Civil Code, and art. 134, second paragraph, of Legislative Decree 58/1998.

The resolutions for capital increases passed by the Board of Directors in exercising the aforementioned right shall establish the subscription price (including any additional paid-in capital) and shall fix a specific deadline for the subscription of the shares; they may also provide that, in the event the increase voted by the Board is not subscribed to by the deadline set each time for that purpose, the capital shall be increased for an amount equal to the subscriptions received up to that deadline date.

Reserves for risks and charges ***euro 759,149 thousand***
(euro 777,327 thousand at December 31, 2003)

The reserves for risks and charges decreased by euro 18,178 thousand compared to December 31, 2003. The composition and changes in these reserves are described as follows:

		Changes during the period					
(in thousands of euro)	**12/31/2003**	**Provisions**	**Utilizations**	**Released to income**	**Reclassi-fications/ Other**	**Total changes**	**9/30/2004**
Reserve for taxes, reserve for deferred taxes	**119,410**	**800,155**	**(26,549)**	**—**	**(762,151)**	**11,455**	**130,865**
Other reserves	**657,917**	**38,742**	**(51,771)**	**(1,140)**	**(15,464)**	**(29,633)**	**628,284**
Reserve for litigation	113,489	24,929	(22,362)	—	—	2,567	116,056
Reserve for capital grants	88,876	—	—	—	(9,236)	(9,236)	79,640
Reserve for losses of subsidiaries and affiliates	10,264	11,313	(250)	—	—	11,063	21,327
Reserve for corporate restructuring	121,144	—	(4,729)	—	—	(4,729)	116,415
Reserve for contractual risks and other risks	324,144	2,500	(24,430)	(1,140)	(6,228)	(29,298)	294,846
Total	**777,327**	**838,897**	**(78,320)**	**(1,140)**	**(777,615)**	**(18,178)**	**759,149**

Reserve for taxes, reserve for deferred taxes

These reserves amount to euro 130,865 thousand and increased by euro 11,455 thousand compared to December 31, 2003. The increase refers to the provision for income taxes for the period. Reclassifications refer to the set off of the reserve for taxes and the reserve for deferred taxes with taxes receivable and deferred tax assets.

Other reserves

Other reserves amount to euro 628,284 thousand and decreased by euro 29,633 thousand compared to December 31, 2003.

In particular:

- the provision to the reserve for losses of subsidiaries and affiliates, euro 11,313 thousand, is principally due to losses in excess of the carrying values of Telecom Italia Learning Services for euro 10,036 thousand and Trainet for euro 1,000 thousand;
- the movements in the reserve for contractual risks and other risks mainly regard utilizations for euro 24,430 thousand and reclassifications/other changes for euro 6,228 thousand.

  Utilizations mainly refer to expenses incurred both for the dispute with OP Computers of euro 5,907 thousand and guarantees provided by Telecom Italia with regard to the sale of Telespazio (euro 5,867 thousand).

  Reclassifications principally relate to transfers to the allowance for doubtful accounts of affiliated companies for a total of euro 5,328 thousand as a result of receivables due from Sky Italia waived by the Telecom Italia Group.

Reserve for employee termination indemnities ***euro 1,035,429 thousand***
(euro 972,413 thousand at December 31, 2003)

The reserve for employee termination indemnities increased by euro 63,016 thousand compared to December 31, 2003. The amount and changes during the period are presented below:

(in thousands of euro)	
Balance at December 31, 2003	**972,413**
Changes during the period:	
- Provisions charged to income for amounts to fund employee termination indemnities accrued in favor of employees during the period plus the fixed and variable cost-of-living adjustments required under Law No. 297/1982	98,373
- Utilizations for:	
• Indemnities paid to employees who took retirement or resigned during the period	(8,234)
• Advances	(7,285)
• Supplementary benefits (Telemaco)	(13,045)
• Substitute tax on the revaluation of the reserve	(3,067)
- Transfers to/from subsidiaries and other movements	(3,726)
Balance at September 30, 2004	**1,035,429**

Liabilities ***euro 39,119,848 thousand***
(euro 41,395,472 thousand at December 31, 2003)

Liabilities decreased by euro 2,275,624 thousand compared to December 31, 2003. Details are as follows :

	9/30/2004			**12/31/2003**		
(in thousands of euro)	**Financial**	**Trade and other**	**Total**	**Financial**	**Trade and other**	**Total**
Debentures	12,660,489	—	**12,660,489**	9,764,983	—	**9,764,983**
Convertible debentures	2,827,904	—	**2,827,904**	4,159,570	—	**4,159,570**
Due to banks	887,380	—	**887,380**	1,191,094	—	**1,191,094**
Due to other lenders	665,308	—	**665,308**	781,885	—	**781,885**
Advances	—	28,603	**28,603**	—	22,273	**22,723**
Trade accounts payable	—	1,390,028	**1,390,028**	—	1,929,794	**1,929,794**
Accounts payable to subsidiaries	16,874,656	1,128,128	**18,002,784**	19,303,264	1,240,256	**20,543,520**
Accounts payable to affiliated companies	419	95,269	**95,688**	1,027	83,744	**84,771**
Taxes payable	70	624,025	**624,095**	23,430	355,650	**379,080**
Contributions to pension and social security institutions	—	574,590	**574,590**	626,769	—	**626,769**
Other liabilities	6,035	1,356,944	**1,362,979**	62,245	1,849,038	**1,911,283**
Total	33,922,261	5,197,587	**39,119,848**	35,287,498	6,107,974	**41,395,472**

Debentures *euro 12,660,489 thousand*

Debentures include the following:

- euro 6,898,572 thousand relating to notes issued under the "Global Note Program" as follows:
  - euro 2,500,000 thousand fixed-rate notes issued on February 1, 2002 in two tranches of euro 1,250,000 thousand each, maturing February 1, 2007 and February 1, 2012;
  - euro 3,000,000 thousand notes issued January 29, 2004, divided into three tranches: the first for euro 1,000,000 thousand, maturing October 29, 2007; the second for euro 750,000 thousand, maturing January 28, 2011; the third for euro 1,250,000 thousand, maturing January 29, 2019;
  - euro 110,000 thousand notes issued April 8, 2004, maturing March 30, 2009;
  - GBP 850 million notes (for an equivalent amount of euro 1,288,572 thousand) issued June 24, 2004, maturing June 24, 2019;

- euro 211,917 thousand relating to the 2002 – 2022 notes reserved for subscription by employees, in service and retired, of companies, directly and indirectly, controlled by Telecom Italia with headquarters in Italy. The 20-year notes, with a face value of euro 50 each, issued at face value, are not listed and can only be traded with Telecom Italia at face value. The semi-annual interest is payable in arrears on January 1 and July 1 of every year and is indexed to the 6-month Euribor;
- euro 2,500,000 thousand 2002-2012 fixed-rate notes originally subscribed to by the subsidiary Olivetti Finance N.V. (merged in Telecom Italia Finance effective June 1, 2004), issued June 26, 2002:
- euro 1,400,000 thousand 2002-2012 fixed-rate notes originally subscribed to by the subsidiary Olivetti Finance N.V. (merged in Telecom Italia Finance effective June 1, 2004), issued December 23, 2002:
- euro 1,500,000 thousand 2001-2011 fixed-rate notes subscribed to by Telecom Italia Finance, issued May 31, 2001:
- euro 150,000 thousand 2001-2011 fixed-rate notes subscribed to by Telecom Italia Finance issued December 28, 2001.

Convertible debentures *euro 2,827,904 thousand*

Details are as follows:

(in thousands of euro)	**12/31/2003**	**Changes during the period**	**9/30/2004**
Telecom Italia 1.5% 2001-2004 convertible notes with a premium on redemption			
. Residual face value	**1,266,268**	(1,266,268)	—
. Premium on redemption	**64,296**	(64,296)	—
Total	**1,330,564**	(1,330,564)	—
Telecom Italia 1.5% 2001-2010 convertible notes with a premium on redemption			
. Residual face value	**2,389,802**	(931)	**2,388,871**
. Premium on redemption	**439,204**	(171)	**439,033**
Total	**2,829,006**	(1,102)	**2,827,904**
TOTAL	**4,159,570**	(1,331,666)	**2,827,904**

Telecom Italia 1.5% 2001 – 2004 convertible bonds with a premium on redemption were fully repaid on January 1, 2004.

Due to banks *euro 887,380 thousand*

Due to banks decreased by euro 303,714 thousand compared to December 31, 2003. They include medium/long-term debt totaling euro 518,046 thousand and short-term borrowings amounting to euro 369,334 thousand, relating to bank overdrafts.

Due to other lenders *euro 665,308 thousand*

Due to other lenders decreased by euro 116,577 thousand compared to December 31, 2003. They consist of medium/long-term financing totaling euro 455,430 thousand and short-term loans payable amounting to euro 209,878 thousand.

Medium/long-term financing principally refers to liabilities for transactions in derivatives (euro 239,351 thousand) put into place with various banks to hedge loans made by subsidiaries, loans made by Cassa Depositi ePrestiti (euro 176,218 thousand) and by the Fondo per l'innovazione tecnologica (euro 34,459 thousand).

Short-term loans refer almost entirely to loans made by TI Securitisation Vehicle S.r.l. (euro 209,814 thousand) deriving from excess financial resources generated by securitization transactions.

Trade accounts payable *euro 1,390,028 thousand*

Trade accounts payable decreased by euro 539,766 thousand compared to December 31, 2003. The balance includes euro 287,027 thousand due to other telecommunications operators.

Accounts payable to subsidiaries *euro 18,002,784 thousand*

Accounts payable to subsidiaries decreased by euro 2,540,736 thousand compared to December 31, 2003. They consist of financial payables, trade accounts payable and other payables. Financial payables (euro 16,874,656 thousand) refer to current account transactions negotiated at market rates for cash management purposes and mainly include loans payable to *Telecom Italia Finance (euro 12,979,857 thousand), Telecom Italia Capital (euro 3,223,467 thousand), TIM (euro 498,684 thousand) and Telecom Italia Sparkle (euro 59,806 thousand).* Trade accounts payable (euro 1,085,364 thousand) mainly consist of accounts payable to *TIM (euro 168,691 thousand), Telecom Italia Sparkle (euro 240,457 thousand), and Telecom Italia Media (euro 31,801 thousand)* for the portion of TLC services invoiced by Telecom Italia to customers, and *IT Telecom (euro 553,674 thousand)* for supply transactions. Other payables (euro 42,764 thousand) mainly refer to payable payables for capital contributions particularly to *Path.Net (euro 18,074 thousand),* and sundry payables to *IT Telecom (euro 9,324 thousand)* and *Telecom Italia Sparkle (euro 6,681 thousand).*

Accounts payable to affiliated companies *euro 95,688 thousand*

Accounts payable to affiliated companies increased by euro 10,917 thousand compared to December 31, 2003. They consist of financial payables, trade accounts payable and other payables. Financial payables (euro 419 thousand) refer to current account transactions negotiated at market rates for cash management purposes mainly due to *Consorzio Telcal (euro 405 thousand).* Trade accounts payable (euro 95,269 thousand) mainly refer to supply transactions with *Italtel (euro 68,461 thousand)* and *Siemens Informatica (euro 15,329 thousand)* and rents payable to *Tiglio II (euro 4,712 thousand).*

Taxes payable *euro 624,095 thousand*

Taxes payable increased by euro 245,015 thousand, compared to December 31, 2003, and mainly refer to:

- VAT payable, euro 574,701 thousand;
- withholding taxes payable to the Italian Treasury as the substitute taxpayer, euro 28,475 thousand;
- local other taxes payable, euro 20,850 thousand.

Contributions to pension and social security institutions *euro 574,590 thousand*

Contributions to pension and social security institutions decreased by euro 52,179 thousand compared to December 31, 2003 They include amounts owed to social security and health institutions with regard to personnel. These specifically comprise euro 529,869 thousand payable to INPS for the estimated charges assessed pursuant to Law No. 58/1992, described under the accounting policies.

Other liabilities *euro 1,362,979 thousand*

Other liabilities decreased by euro 548,304 thousand compared to December 31, 2003. They include, in particular, liabilities for:

- customer-related items totaling euro 757,586 thousand, comprising, among other things, deposits by subscribers against telephone conversations and pre-billed basic charges;
- employee-related items amounting to euro 445,094 thousand.

Accrued expenses and deferred income ***euro 1,695,934 thousand***
(euro 2,448,626 thousand at December 31, 2003)

Accrued expenses and deferred income decreased by euro 752,692 thousand compared to December 31, 2003, and included the following:

(in thousands of euro)	**12/31/2003**	**9/30/2004**
Accrued expenses		
. trade	89	8,082
. financial	1,828,233	844,356
. other	—	19
	1,828,322	852,457
Deferred income		
. trade	504,084	738,189
. financial	3,880	3,695
. other	112,340	101,593
. *of which capital grants (unavailable portion)*	*110,532*	97,376
	620,304	843,477
Total	**2,448,626**	**1,695,934**

Accrued trade expenses primarily relate to lease payments.

Accrued financial expenses mainly regard interest on long-term loans from subsidiaries (euro 328,540 thousand) relating entirely to Telecom Italia Finance, interest on bonds (euro 424,072 thousand), as well as interest on derivative financial transactions (euro 68,661 thousand).

Deferred income mainly includes pre-billed basic subscriber charges, rentals and maintenance of telephone equipment (euro 602,713 thousand), interconnecting fees and line lease revenues from Telecom Italia Sparkle and TIM, the unavailable portion of capital grants received after December 31, 1992 and financial items principally connected with loans to employees.

* * *

An analysis of liabilities and accrued expenses by maturity and type is provided in Annex 4.

Disclosure required by art. 2427, art. 6 of the Italian Civil Code regarding the breakdown of liabilities by geographical area is presented in Annex 5.

MEMORANDUM ACCOUNTS

Memorandum accounts total euro 24,916,517 thousand at September 30, 2004 and can be analyzed as follows:

Guarantees provided ***euro 24,795,190 thousand***

Guarantees provided consist of sureties (net of counter-guarantees received totaling euro 1,328,533 thousand), of which euro 24,522,456 thousand are provided on behalf of subsidiaries, euro 145,543 thousand on behalf of affiliated companies and euro 127,191 thousand on behalf of others. The guarantees are given mainly in respect of the notes issued by Telecom Italia Finance (under the Global Medium Term Note Program) for euro 19,973,351 thousand, by Telecom Italia Capital for euro 4,271,094 thousand, and other medium/long-term financial transactions, supply contracts and guarantees on bids to acquire licenses abroad.

Purchases and sales commitments ***euro 107,384 thousand***

This item consists of commitments for purchases of euro 101,249 thousand and commitments for sales of euro 6,135 thousand.

Commitments for purchases particularly include future lease obligations plus related purchase options (euro 56,268 thousand).

Commitments for sales refer to the sale of the investment in LI.SIT to Lombardia Informatica for euro 1,573 thousand, at the expiry of the contract (September 15, 2009), as well as the commitment to sell the 80.1% holding in Atesia for euro 4,562 thousand (transaction finalized on November 12, 2004).

Other memorandum accounts ***euro 13,943 thousand***

Other memorandum accounts mainly refer to assets of third parties on loan, on deposit for safekeeping and securities of third parties held as guarantees.

***

Moreover:

- the Company issued weak letters of patronage totaling euro 967,257 thousand, chiefly on behalf of subsidiaries and affiliated companies to guarantee insurance polices, lines of credit and overdraft arrangements;
- assets held by third parties on loan, on deposit for safekeeping or for similar purposes amount to euro 212,453 thousand, and mainly consist of equipment leased to customers;
- guarantees provided by others for company obligations amount to euro 530,876 thousand to guarantee the proper performance of non-financial contractual obligations;
- the shares of employees and private shareholders deposited at September 30, 2004 with Telecom Italia, and therefore subdeposited with Monte Titoli S.p.A., are equal to euro 66,243 thousand, whereas those awaiting assignment or in the process of being replaced total euro 67 thousand
- the expense fund to safeguard the holders of savings shares, set up by resolution of the Shareholders' Meeting of June 21, 1999, amounts to euro 2,087 thousand at September 30, 2004;
- the total amount of commitments at September 30, 2004 for building lease obligations on contracts covering periods between 9 and 21 years amount to euro 4,089,641 thousand.

Derivative financial instruments

Transactions in derivative financial instruments at September 30, 2004 include combined cross currency & interest rate swaps (to covert some loan contracts in British pounds, US dollars and JPY to euro) and interest rate swaps (to covert loans originally at floating interest rates to fixed interest rates and to convert the indexing of debt linked with domestic parameters to the 6-month Euribor). The following table shows the notional values of the derivatives hedging medium/long-term debt at September 30, 2004.

DESCRIPTION	Notional amount in millions of euro
Floating to fixed IRS transactions put into place by Telecom Italia S.p.A.	6
Floating to floating IRS transactions put into place by Telecom Italia S.p.A.	197
CCIRS transactions put into place by Telecom Italia S.p.A. (*)	5,193
TOTAL	**5,396**

* *The protection structure is conditional on the loans being maintained performing by Telecom Italia S.p.A. for euro 345 million.*

- The floating to fixed IRS transactions (4.68%) put into place by Telecom Italia S.p.A. for a notional amount of euro 6 million refer to EIB loans at floating rates;
- The floating to floating IRS transactions put into place by Telecom Italia S.p.A. for a notional amount of euro 197 million refer to the indexed loans at domestic parameters (Rendint, Rolint, Robot) with conversion to the 6-month Euribor;
- CCIRS transactions put into place by Telecom Italia S.p.A. amounting to euro 5,193 million refer:
  - for *euro 3,409 million,* to the floating rate infragroup loan in USD, received from the subsidiary Telecom Italia Capital S.A. following the bonds issued in October 2003 for a total amount of US$ 4,000 million, with conversion of the loan to:
    - quarterly floating rate in euro maturing November 2008 for euro 851 million;
    - semiannual average 5.04% fixed rate in euro maturing November 2013 for euro 1,709 million, of which euro 470 million through two distinct and linked transactions ;
    - semiannual 5.99% fixed rate in euro maturing November 2033 for euro 849 million.

    Moreover, against the issue of fixed rate bonds for USD 4,000 million (euro 3,223 million at the euro/USD exchange rate of September 30, 2004), Telecom Italia Capital S.A. signed IRS contracts converting the semiannual 4% fixed rate coupon on USD 1,000 million maturing November 2008, the 5.25% rate on USD 2,000 million maturing November 2013, the 6.38% rate on USD 1,000 million maturing November 2033 to quarterly floating rates in USD;
  - for *euro 174 million*, with reference to the Dual Currency loan with a notional principal of JPY 20 billion with a 5% fixed interest rate with a step-up of +0.45% in USD maturing October 2029, originally received by Olivetti International Finance N.V., now carried by Telecom Italia Finance S.A., the following was put into place:
    - by Telecom Italia S.p.A., a CCIRS in which Telecom Italia S.p.A., with regard to the infragroup loan in JPY, receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is conditional on the loan being maintained performing by Telecom Italia S.p.A.;
    - by Telecom Italia S.p.A., an IRS with the conversion of the semiannual floating rate in euro to a 6.13% fixed rate up to October 2004 and after that to an annual 6.68% fixed rate (or a semiannual floating rate in euro as elected by the counterpart) up to maturity;
  - for *euro 171 million* with reference to the bonds 2002/2032 of JPY 20 billion with a 3.55% fixed rate coupon maturing May 2032 originally issued by Olivetti Finance N.V., the following was put into place:
    - by Telecom Italia S.p.A., a CCIRS contract on a floating rate infragroup loan in JPY in which Telecom Italia S.p.A. receives 6-month Libor in JPY and pays 6-month Euribor. This protection structure is conditional on the loan being maintained performing by Telecom Italia S.p.A.;
  - for *euro 150 million*, CCIRSs linked to an EIB loan in USD with conversion to a floating rate in euro;
  - for *euro 1,289 million*, with regard to bonds 2004/2019 with an annual 6.375% fixed rate in GBP, maturing June 2019, CCIRSs with three-year maturities with conversion to the semiannual Euribor.

At September 30, 2004, Telecom Italia S.p.A. has exchange rate transactions put into place for treasury management purposes for a notional amount of euro 180 million.

Consistent with the accounting principles disclosed previously, the negative difference, if any, on the valuation of the above detailed derivative financial instruments at fair value, is recognized in the statement of income under financial expenses.

STATEMENTS OF INCOME

PRODUCTION VALUE **euro 11,989,264 thousand**
(euro 12,077,438 thousand in the first nine months of 2003)

Production value includes the following captions:

Sales and service revenues *euro 11,793,169 thousand*

Sales and service revenues decreased by euro 79,057 thousand compared to the first nine months of 2003 and are shown gross of the amount due to other operators (euro 2,250,267 thousand), which are included in "service costs".

The breakdown of revenues by business segment, expressly required by art. 2427, point 10, of the Italian Civil Code, is presented in the following table, while the breakdown of revenues by geographical area, also required by the same article of the Italian Civil Code, is presented in Annex 5.

Breakdown by *business segment*

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Sales:			
- telephone products	372,985	241,923	131,062
- other goods	192	193	(1)
	373,177	**242,116**	131,061
Services:			
- Traffic	4,882,953	5,148,313	(265,360)
- Basic subscription charges (of which)	5,948,010	5,896,528	51,482
. for lines leased to other TLC operators	*834,171*	*863,992*	*(29,821)*
- Fees	255,202	210,776	44,426
- Miscellaneous income	333,827	374,493	(40,666)
	11,419,992	**11,630,110**	(210,118)
Total	**11,793,169**	**11,872,226**	(79,057)

Traffic revenues are detailed as follows:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
• Retail traffic:			
- phone	3,437,352	3,550,296	(112,944)
- internet (online dial-up and ADSL)	390,507	351,254	39,253
- VAS and data	505,004	713,114	(208,110)
	4,332,863	**4,614,664**	**(281,801)**
• National wholesale traffic	**550,090**	**533,649**	**16,441**
Total	**4,882,953**	**5,148,313**	**(265,360)**

Revenues from basic subscription charges are detailed below:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
• Retail subscription charges:			
- phone	3,711,161	3,769,575	(58,414)
- ADSL	264,754	164,827	99,927
- VAS and data	1,137,840	1,098,134	39,706
	5,113,755	**5,032,536**	**81,219**
• National wholesale subscription Charges	**834,255**	**863,992**	**(29,737)**
Total	**5,948,010**	**5,896,528**	**51,482**

Revenues from fees to activate service are detailed below:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
• Retail fees:			
- phone	113,116	96,412	16,704
- ADSL	49,265	6,699	42,566
- VAS and data	34,737	23,931	10,806
	197,118	**127,042**	**70,076**
• National wholesale fees	**58,084**	**83,734**	**(25,650)**
Total	**255,202**	**210,776**	**44,426**

Revenues from sales (euro 373,177 thousand) increased by euro 131,061 thousand compared to the first nine months of 2003. The increase is mainly due to higher sales of cordless phones (in particular, the Aladino model) and web service products.

Transactions for revenues from sales and services with subsidiaries and affiliated companies total euro 946,300 thousand. In particular, they refer to:

- *TIM (euro 453,567 thousand) - revenues for mobile-fixed interconnections and lines leased;*
- *Telecom Italia Media (euro 118,208 thousand) – telecommunications services;*
- *Teleleasing (euro 95,790 thousand) - sales of telecommunications products and services;*
- *Path.Net (euro 84,712 thousand) - TLC services and infrastructures dedicated to the Public Administration;*
- *Telecom Italia Sparkle (euro 45,225 thousand) – telecommunications services;*
- *LI.SIT. (euro 29,001 thousand) – supply of health cards to the Lombardy Region;*
- *IT Telecom (euro 26,834 thousand) – telecommunications services.*

Changes in inventory of contract work in process *euro 9,544 thousand*

Changes in inventory of contract work in process represents the increase for new work (in particular, for LI.SIT., the sanitary paper for the Lombardy Region) and the decrease as a result of completed contracts.

Increases in capitalized internal construction costs *euro 55,643 thousand*

These consist entirely of capitalized labor costs. Increases in capitalized internal construction costs rose by euro 15,283 thousand compared to the first nine months of 2003.

Other revenues and income *euro 130,908 thousand*

Other revenues and income decreased by euro 28,294 thousand compared to the first nine months of 2003. They include the following:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Operating grants	2,666	7,661	(4,995)
Gains on disposal of assets used in the production process	3,541	3,161	380
Reimbursements of costs for employees on loan at Group companies	16,683	21,044	(4,361)
Capital grants recorded in income	14,783	18,044	(3,261)
Late payment fees	50,734	58,954	(8,220)
Indemnification, reimbursements and recoveries and other miscellaneous income	42,501	50,338	(7,837)
Total	**130,908**	**159,202**	**(28,294)**

Transactions involving other revenues and income with subsidiaries and affiliated companies total euro 46,818 thousand. They refer to the recovery of costs for personnel on loan and sundry services, mainly in respect of:

- *TIM (euro 14,412 thousand);*
- *Telecom Italia Sparkle (euro 10,221 thousand);*
- *IT Telecom (euro 9,433 thousand);*
- *Finsiel (euro 3,227 thousand).*

PRODUCTION COSTS **euro 8,733,176 thousand**
(euro 8,908,163 thousand in the first nine months of 2003)

Production costs include the following:

Raw materials, supplies and merchandise *euro 339,488 thousand*

Raw materials, supplies and merchandise increased by euro 97,116 thousand, compared to the first nine months of 2003 (euro 242,372 thousand), mainly on account of higher purchases of telephone equipment for sale to customers.

They principally include "costs for purchases of telephone equipment to be resold to customers" for euro 171,741 thousand, "costs for purchases of inventory materials" for euro 122,402 thousand, "costs for purchases of materials for the management of corporate assets" for euro 24,643 thousand and "costs for purchases of supply materials" for euro 17,751 thousand.

Raw materials, supplies and merchandise costs include transactions with subsidiaries and affiliated companies of euro 29,939 thousand mainly in reference to IT Telecom (euro 12,029 thousand), Teleleasing (euro 7,329 thousand), TIM (euro 1,750 thousand) and Olivetti Tecnost (euro 2,947 thousand).

Services *euro 3,825,376 thousand*

Costs for services decreased by euro 18,655 thousand compared to the first nine months of 2003. They consist of the following:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Advertising and promotion	107,816	100,492	7,324
Selling expenses	204,263	187,882	16,381
Maintenance	225,543	164,851	60,692
Professional and consulting fees	114,989	112,734	2,255
Electricity and water	119,151	121,660	(2,509)
Telephone bill mailing expenses	32,531	32,313	218
Interconnection costs	26,213	26,640	(427)
Insurance	20,399	17,657	2,742
Amounts due to other operators	2,250,267	2,337,705	(87,438)
Distribution and logistics expenses	36,167	33,699	2,468
Other services	688,037	708,398	(20,361)
Total	**3,825,376**	**3,844,031**	**(18,655)**

Service costs include euro 1,622,607 thousand of transactions with subsidiaries and affiliated companies. They mainly regard:

- *TIM (euro 746,494 thousand) - telecommunications services and interconnection costs;*
- *IT Telecom (euro 253,834 thousand) – professional fees, maintenance and selling expenses;*
- *Telecom Italia Sparkle (euro 276,745 thousand) – telecommunications services and interconnection costs;*
- *Telecom Italia Media (euro 136,594 thousand) – telecommunications services and selling expenses;*
- *Telenergia (euro 97,139 thousand) – electricity;*
- Atesia (euro 13,213 thousand) – outsourcing costs for call center and assistance activities.

Use of property not owned *euro 444,940 thousand*

Use of property not owned decreased by euro 87,778 thousand, compared to the first nine months of 2003, mainly due to the absence of costs for the purchase of satellite capacity after Telespazio directly took over business dealings with the satellite consortia.

These costs consist of:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Rentals	347,206	333,343	13,863
Hires	80,458	186,725	(106,267)
Lease installments	13,870	11,091	2,779
Other	3,406	1,559	1,847
Total	**444,940**	**532,718**	**(87,778)**

This item comprises euro 191,284 thousand of costs for the use of property not owned relating to transactions with subsidiaries and affiliated companies, specifically with Tiglio I (euro 45,310 thousand) and Tiglio II (euro 18,685 thousand) for building rentals, Telecom Italia Sparkle (euro 58,063 thousand) for line leases, IT Telecom (euro 20,739 thousand) for hardware and software rentals, Teleleasing (euro 3,928 thousand) for hire and leasing installments.

Personnel costs *euro 1,788,878 thousand*

Personnel costs decreased by euro 63,952 thousand compared to the first nine months of 2003. They comprise "wages and salaries" (euro 1,258,785 thousand), "social security contributions" (euro 401,740 thousand), employee "termination indemnities" (euro 98,374 thousand) and "other costs" (euro 29,979 thousand). Personnel costs include the costs of employees on loan to other Group companies (euro 16,683 thousand) and recovered from the same Group companies; the income from the recovery of such costs is recorded in "*Other revenues and income*".

A comparative breakdown of the average number of employees by professional category in the first nine months of 2004 is presented as follows:

	9 months to 9/30/2004	9 months to 9/30/2003
Executives	904	927
Middle management	1,975	1,884
Clerical staff	47,144	46,297
Technicians	234	4,310
Total	**50,257**	**53,418**

Amortization, depreciation and writedowns *euro 2,061,657 thousand*

Details of this caption are provided as follows:

Amortization of intangible assets euro 426,637 thousand

Amortization of intangible assets increased by euro 9,506 thousand, compared to the first nine months of 2003, and refers to the following assets:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Start-up and expansion costs	8,628	20,794	(12,166)
Industrial patents and intellectual property rights	399,072	374,848	24,224
Concessions, licenses, trademarks and similar rights	68	7,480	(7,412)
Goodwill	201	120	81
Other intangibles	18,668	13,889	4,779
Total	**426,637**	**417,131**	9,506

Depreciation of fixed assets euro 1,576,641 thousand

Depreciation of fixed assets decreased by euro 115,170 thousand compared to the first nine months of 2003, and refers to the following assets:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Land and building	57,782	60,296	(2,514)
Plant and machinery	1,494,774	1,589,182	(94,408)
Manufacturing and distribution equipment	5,478	8,559	(3,081)
Other fixed assets	18,607	33,774	(15,167)
	1,576,641	**1,691,811**	(115,170)

Writedowns of receivables included in current assets and liquid assets *euro 58,379 thousand*

This caption includes the provision to the allowance for doubtful trade customers. accounts receivables from

Changes in inventories of raw materials, supplies and merchandise *- euro 42,104 thousand*

The change reflects purchases of equipment destined for sale and goods for maintenance unused and also takes into account writedowns for obsolete materials and materials with diminished utilization. The amount primarily refers to inventories connected with the marketing of Aladino cordless phone and videophones.

Provisions for risks *euro 24,929 thousand*

Provisions for risks refer to provisions made to the "*reserve for litigation*" to cover expenses connected with the probable outcome of disputes with third parties.

Miscellaneous operating costs euro 290,012 thousand

Miscellaneous operating costs increased by euro 60,729 thousand, compared to the first nine months of 2003, and include the following:

Losses on disposal of assets euro 15,938 thousand

These losses mainly refer to the disposal of fixed assets.

TLC operating fees euro 17,360 thousand

TLC operating fees mainly include the fee for the assignment of available numbers (euro 6,575 thousand) and the fee for the use of radio frequencies (euro 6,487 thousand) established by the Ministerial Decree of February 5, 1998, in addition to the fee for the operation of the regulatory body (euro 3,983 thousand).

Other miscellaneous costs euro 256,714 thousand

Other miscellaneous costs increased by euro 53,012 thousand, compared to the first nine months of 2003, and include the following:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
• other indirect duties and annual taxes, relating mainly to local property taxes, local duties, stamp and register tax, vehicle tax, production and electrical energy consumption taxes and permits and government concession taxes	69,323	74,500	(5,177)
• association dues and membership fees	12,667	13,263	(596)
• losses due to settlements	63,549	17,979	45,570
• losses on the sale of receivables	59,231	41,957	17,274
• other costs, essentially relating to compensation due to customers under service regulations for delays in hookups or line transfers, damages paid to third parties for line installations and maintenance	51,944	56,003	(4,059)
Total	**256,714**	**203,702**	**53,012**

FINANCIAL INCOME AND EXPENSE **- euro 1,276,892 thousand**

(- euro 1,279,337 thousand in the first nine months of 2003)

Financial income and expense shows an expense balance of euro 1,276,892 thousand. Details are as follows:

(in thousands of euro)		9 months to 9/30/2004	9 months to 9/30/2003	Change
Income from equity investments	(A)	16,464	680,274	(663,810)
Other financial income	(B)	154,538	77,766	76,772
Interest and other financial expense ..	(C)	1,447,467	2,042,273	(594,806)
Foreign exchange gains and losses ...	(D)	(427)	4,896	(5,323)
Total	**(A+B-C+D)**	**(1,276,892)**	**(1,279,337)**	2,445

Income from equity investments refers to the following:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Dividends from subsidiaries, affiliated companies and other companies	12,126	601,058	(588,932)
Other income from equity investments	4,338	79,216	(74,878)
Total	**16,464**	**680,274**	**(663,810)**

Dividends from subsidiaries, affiliated companies and other companies mainly refer to *TIM shares recorded in current assets* (euro 9,804 thousand). Dividends decreased by euro 588,932 thousand, compared to the first nine months of 2003, following the collection, in the period under comparison, of both dividends pre-merger by the merged company Telecom Italia (euro 511,245 thousand), and the reserves of the subsidiary TIM (euro 80,770 thousand).

Other income from equity investments refer to the recovery of the *share premium from the company LI.SIT.* and decreased by euro 74,878 thousand owing to the elimination of the tax credit on dividends following the tax reform introduced by Legislative Decree No. 344/2003.

Other financial income includes the following:

	9 months to 9/30/2004				
(in thousands of euro)	Included in long-term investments	Included in current assets	Total	9 months to 9/30/2003	Change
Interest and fees on:					
• accounts receivable					
. from subsidiaries	2,784	23,782	26,566	25,126	1,440
. from affiliated companies	1,578	48	1,626	5,199	(3,573)
. other	5,355		5,355	8,837	(3,482)
• securities	—	241	241	1,642	(1,401)
• banks and the Postal Administration	—	15,752	15,752	10,981	(4,771)
	9,717	**39,823**	**49,540**	**51,785**	**(2,245)**
Income on derivative financial instruments			88,885	14,661	74,224
Other income			16,113	11,320	4,793
			154,538	**77,766**	**76,772**

Other financial income includes euro 28,218 thousand of interest and fees on receivables from subsidiaries and affiliated companies, almost all of which refers to accrued interest on current accounts for cash management purposes, mainly with:

- *Olivetti Tecnost (euro 9,017 thousand);*
- *IT Telecom (euro 5,909 thousand);*

- *Stet Hellas (euro 2,560 thousand) relating to income on long-term receivables described in the note on long-term investments;*
- *Telecom Italia Finance (euro 2,039 thousand, financial fees);*
- *TIM (euro 1,326 thousand).*

Interest and other financial expense can be analyzed as follows:

(in thousands of euro)	9 months to 9/30/2004 Medium/long -term debt	Short-term borrowings	Total	9 months to 9/30/2003	Change
Interest and fees paid to subsidiaries	424,495	141,801	566,296	657,199	(90,903)
Interest and fees paid to affiliated companies	—	167	167	254	(87)
Interest and fees paid to others and miscellaneous expenses					
• on due to banks	14,191	6,569	20,760	90,060	(69,300)
• on debentures	596,799	—	596,799	1,093,328	(496,529)
• on due to other lenders	8,315	11,013	19,328	24,366	(5,038)
• on other items.					
- Accrued portion of issue discounts and similar charges on loans	—	41,942	41,942	45,852	(3,910)
- Provision to the allowance for doubtful accounts for the "Deferred Purchasing Price"	—	9,755	9,755	19,993	(10,238)
- Expenses on derivative financial instruments	—	153,886	153,886	44,008	109,878
- Other financial expense	14,417	24,117	38,534	67,213	(28,679)
Total	**1,058,217**	**389,250**	**1,447,467**	**2,042,273**	**(594,806)**

Interest on debentures (euro 596,799 thousand) includes interest by *Telecom Italia Finance (euro 296,483 thousand)* for bonds subscribed to by this company and described in a specific note.

Interest and other financial expense includes euro 566,293 thousand of interest and fees on payables to subsidiaries and affiliated companies principally with regard to:

- *Telecom Italia Finance (euro 430,440 thousand), Olivetti Holding B.V. (euro 43,273 thousand), Telecom Italia Capital (euro 55,389 thousand) and TIM (euro 29,693 thousand) – mainly for interest expenses accrued on current accounts for cash management purposes.*

Foreign exchange gains and losses include the following:

(in thousands of euro)		9 months to 9/30/2004	9 months to 9/30/2003	Change
Foreign exchange gains				
. from amounts realized		1,966	11,441	(9,475)
. from adjustments		3,693	6,520	(2,827)
Total	(A)	5,659	17,961	(12,302)
Foreign exchange losses				
. from amounts realized		2,661	3,013	(352)
. from adjustments		3,425	10,052	(6,627)
Total	(B)	6,086	13,065	(6,979)
Total.	**(A-B)**	**(427)**	**4,896**	**(5,323)**

VALUE ADJUSTMENTS TO FINANCIAL ASSETS **euro 5,317 thousand**
(- euro 237,067 thousand in the first nine months of 2003)

Value adjustments to financial assets include upward adjustments (euro 60,810 thousand) and writedowns of equity investments (euro 55,409 thousand) and writedowns of securities, other than equity investments, included in current assets (euro 84 thousand).

Upward adjustments relate to the writeback of value regarding the investment in Olivetti Tecnost (euro 60,000 thousand) carried out when the underlying assumption which gave rise to the writedowns in prior years no longer applied.

The writedowns of equity investments regarded the following companies:

		9 months to 9/30/2004				
(in thousands of euro)		**Writedowns to carrying values**	**Writedowns recorded in the reserve for losses of subsidiaries and affiliates**	**Total**	**9 months to 9/30/2003**	**Change**
Included in long-term investments						
. Netesi		79	—	79	1,950	(1,871)
. EPIClink		3,729	—	3,729	—	3,729
. Latin American Nautilus		7,093	—	7,093	12,506	(5,413)
. TILAB S.A.		48	277	325	7,062	(6,737)
. IT Telecom		25,659	—	25,659	101,227	(75,568)
. Sky Italia		—	—	—	64,248	(64,248)
. Telecom Italia Learning Services		2,521	10,036	12,557	32,631	(20,074)
. Olivetti Tecnost		—	—	—	16,571	(16,571)
. Olivetti International		—	—	—	33,200	(33,200)
. Trainet		—	1,000	1,000	900	100
. Olivetti Finance		—	—	—	3,611	(3,611)
. Telecom Italia America Latina		—	—	—	1,533	(1,533)
. Edotel		—	—	—	6,759	(6,759)
. Loquendo		329	—	329	—	329
. Siosistemi		—	—	—	1,405	(1,405)
. LI.SIT		4,338	—	4,338	—	4,338
. PAR.FIN		255	—	255	—	255
. Other companies		12	—	12	8,022	(8,010)
	(A)	**44,063**	**11,313**	**55,376**	**291,625**	**(236,249)**
Included in short-term financial assets						
. TIM		—	—	—	12,031	(12,031)
. Telecom Italia Media		20	—	20	33	(13)
. Portal Software		13	—	13	—	13
. Biesse		—	—	—	121	(121)
. Other companies		—	—	—	3	(3)
	(B)	**33**	**—**	**33**	**12,188**	**(12,155)**
Total	**(A+B)**	**44,096**	**11,313**	**55,409**	**303,813**	**(248,404)**

EXTRAORDINARY INCOME AND EXPENSE **- euro 320,742 thousand**
(- euro 274,826 thousand in the first nine months of 2003)

Details of the balance are as follows:

(in thousands of euro)		9 months to 9/30/2004	9 months to 9/30/2003	Change
Income				
. gains on disposals		10,523	32,969	(22,446)
. elimination of tax interference		932	—	932
. release of liability and reserve for risks for grants under Law 488/1998		—	921,872	(921,872)
. recoveries under Law 58/1992 and damage compensation		7,725	4,709	3,016
. other		24,420	30,009	(5,589)
	(A)	**43,600**	**989,559**	**(945,959)**
Expense				
. expenses under Law 58/1992		123,075	122,490	585
. losses on sale of Seat Pagine Gialle		—	347,703	(347,703)
. loss on sale of buildings		—	40,096	(40,096)
. provisions and writedowns of equity investments		112,416	146,139	(33,723)
. restructuring costs (employee reduction plans, territorial and other layoffs, CIGS)		59,572	75,645	(16,073)
. prior period expenses for telephone cards		—	56,434	(56,434)
. expenses on Olivetti/Telecom Italia merger and sale of Nuova Seat		—	173,037	(173,037)
. expenses for Pagine Italia settlement		—	55,000	(55,000)
. prior years' receivables writeoffs		—	182,992	(182,992)
. expenses for damages by third parties		14,142	13,022	1,120
. expenses and provisions for corporate transactions		6,348	6,000	348
. prior years' taxes		1,271	4,698	(3,427)
. other		47,518	41,129	6,389
	(B)	**364,342**	**1,264,385**	**(900,043)**
Total	**(A-B)**	**(320,742)**	**(274,826)**	**(45,916)**

Extraordinary income, equal to euro 43,600 thousand, relates to the following:

- gains (euro 10,523 thousand) realized principally on the sale of a part of Pirelli Real Estate shares (euro 9,044 thousand) and the sale of the "Document Management" business segment (euro 1,000 thousand);
- elimination of prior period tax interference (euro 932 thousand), pursuant to Legislative Decree No. 6 dated January 17, 2003, as amended, introducing the reform of corporate law, following accelerated depreciation taken in prior years by the acquiring company Olivetti as allowed by tax laws;
- recovery of expenses from companies of the Group relating to Law 58/1992 (euro 1,540 thousand) and from third parties for damage compensation (euro 6,185 thousand);
- other prior period income of euro (euro 24,420 thousand).

The reduction of euro 945,959 thousand, compared to the first nine months of 2003, is principally attributable to prior period income (euro 921,872 thousand) booked in 2003 as a result of the elimination of the telecommunications license fee and lower gains on the sale of fixed assets and long-term investments.

Extraordinary expense, equal to euro 364,342 thousand, comprises the following:

- expenses under Law 58/1992 (euro 123,075 thousand) to cover employees under the former fund "Telephone Employees Pension Fund" (FPT), which became part of the general "Employees Pension Fund", in accordance with the 2000 Finance Bill;

- provisions on the equity investment in Telecom Italia Media (euro 112,416 thousand);
- expenses (euro 59,572 thousand) for corporate restructuring relating to employee cutbacks and layoffs;
- expenses for damages sustained to the assets as a result of natural disasters or caused by third parties (euro 14,142 thousand);
- expenses (euro 3,848 thousand) following the guarantees connected with corporate transactions and the provisions associated with the sale of the "Document Management" business segment (euro 2,500 thousand);
- prior period taxes (euro 1,271 thousand);
- other prior period expenses (euro 47,518 thousand).

The reduction of euro 900,043 thousand, compared to the first nine months of 2003, is essentially due to the posting of the following items in 2003:

- loss on the sale of Nuova Seat Pagine Gialle (euro 347,703 thousand);
- expenses connected with the Olivetti - Telecom Italia merger and the sale of the company Nuova Seat Pagine Gialle (euro 173,037 thousand);
- prior period expenses relating to both the writeoff of accounts receivables balances in prior years (euro 182,992 thousand) and the adjustment of estimates regarding the value of prepaid telephone cards (euro 56,434 thousand);
- writedowns of the investments in EPIClink (euro 105,991 thousand) and Loquendo (euro 10,148 thousand) and provisions for guarantees provided upon the sale of the satellite consortia (euro 30,000 thousand);
- expenses relating to the settlement with Pagine Italia (euro 55,000 thousand).

Income taxes for the period, current and deferred *euro 770,155 thousand*

Income taxes for the period totaling euro 770,155 thousand consist of current income taxes calculated on the basis of the best possible estimate using available information and on a reasonable projection of performance for the year up to the end of the tax period.

Income taxes increased by euro 1,404,236 thousand compared to the corresponding period of 2003 which, as stated, had benefited from the posting of deferred tax credits (euro 1,286,000 thousand) which became recoverable thanks to the Olivetti – Telecom Italia merger.

* *

The following Annexes numbered 1 to 6 are an integral part of these notes.

LONG-TERM INVESTMENTS AND ADVANCES ON FUTURE CAPITAL CONTRIBUTIONS OF SUBSIDIARIES AND AFFILIATED COMPANIES

	12/31/2003										9/30/2004			
(in thousands of euro)	Cost	Upward adjust-ments	Writedowns	Carrying value	Purchases / Subscrip-tions	Reclassi-fications/	Disposals[1]	Writedowns(-) / Writebacks of value(+)	Capital Replenish-ments	Total	Cost	Upward adjust-ments	Writedowns	Carrying value
Equity investments in subsidiaries														
ATESIA	3,707	—	—	3,707		(380)				(380)	3,327	—	—	3,327
Consorzio Energia Gruppo Telecom Italia	5	—	—	5						—	5	—	—	5
DOMUS ACCADEMY	2,400	—	—	2,400						—	2,400	—	—	2,400
EDOTEL	9,056	—	(6,914)	2,142	1,459	1,200		46		2,705	4,847	—		4,847
EMSA SERVIZI	5,000	—	—	5,000						—	5,000	—	—	5,000
EPIClink	450	—	(450)	—						—	450	—	(450)	—
FINSIEL	364,680	—	(115,000)	249,680						—	364,680	—	(115,000)	249,680
I.T. TELECOM	171,521	—	(114,871)	56,650		110,440		(25,659)		84,781	167,090	—	(25,659)	141,431
INTELCOM SAN MARINO	—	—	—	—							—	—	—	—
IRIDIUM ITALIA (in liquidation)	775	—	(775)	—						—	775	—	(775)	—
LATIN AMERICAN NAUTILUS S.A.	5,241	—	(3,268)	1,973	40,801			(7,093)		33,708	46,042	—	(10,361)	35,681
LOQUENDO	7,820	—	(7,820)	—						—	7,820	—	(7,820)	—
MED-1 Submarine Cables	5	—	—	5						—	5	—	—	5
MEDITERRANEAN NAUTILUS S.A.	14,352	—	—	14,352						—	14,352	—	—	14,352
NETESI	14,745	—	(14,745)	—		435		(79)		356	435	—	(79)	356
OFI CONSULTING (ex-OLIVETTI FINANZIARIA				—						—				
INDUSTRIALE	78,940	—	(43,831)	35,109						—	78,940	—	(43,831)	35,109
OLIVETTI GESTIONI IVREA (ex-THEMA)	7,516	—	—	7,516			(4,849)			(4,849)	2,667	—	—	2,667
OLIVETTI INTERNATIONAL	442,740	—	(162,177)	280,563		(280,563)				(280,563)	—	—	—	—
OLIVETTI MULTISERVICES	41,042	—	(639)	40,403						—	41,042	—	(639)	40,403
OLIVETTI TECNOST	78,000	—	(27,749)	50,251				60,000		60,000	110,251	—	—	110,251
PATH.NET	25,820	—	—	25,820						—	25,820	—	—	25,820
SAIAT	34,743	11,616	—	46,359						—	34,743	11,616	—	46,359
TECNO SERVIZI MOBILI	53	—	—	53						—	53	—	—	53
TELECOM ITALIA AMERICA LATINA	13,220	—	(13,220)	—						—	13,220	—	(13,220)	—
TELECOM ITALIA AUDIT (ex-IN.TEL.AUDIT)	1,750	—	—	1,750						—	1,750	—	—	1,750
TELECOM ITALIA CAPITAL SA	2,388	—	—	2,388						—	2,388	—	—	2,388
TELECOM ITALIA DEUTSCHLAND HOLDING	243,201	—	—	243,201						—	243,201	—	—	243,201
TELECOM ITALIA INTERNATIONAL	7,851,463	—	(3,545,848)	4,305,615			(1,800,000)			(1,800,000)	4,629,735	—	(2,124,120)	2,505,615
TELECOM ITALIA LEARNING SERVICES	1,560	—	(1,560)	—						—	1,560	—	(1,560)	—
TELECOM ITALIA MEDIA	1,974,913	—	(1,227,787)	747,126				(112,416)		(112,416)	1,974,913	—	(1,340,203)	634,710
TELECOM ITALIA MOBILE	27,182,687	84,144	—	27,266,831						—	27,182,687	84,144	—	27,266,831
TELECONTACTCENTER	110	—	—	110		380				380	490	—	—	490
TELENERGIA	40	—	—	40						—	40	—	—	40
TELSY	14,512	—	—	14,512						—	14,512	—	—	14,512
TI FINANCE	607,507	38,057	(645,564)	—		280,563				280,563	888,070	38,057	(645,564)	280,563
TI LAB GENERAL PARTNER	33	—	(12)	21			(9)	(12)		(21)	—	—	—	—
TI LAB SA	131	—	(83)	48				(48)		(48)	131	—	(131)	—
TI SPARKLE	784,765	—	—	784,765						—	784,765	—	—	784,765
TRAINET (in liquidation)	674	—	(674)	—						—	674	—	(674)	—
	39,987,565	**133,817**	**(5,932,987)**	**34,188,395**	**42,260**	**112,075**	**(1,804,858)**	**(85,261)**	**—**	**(1,735,784)**	**36,648,880**	**133,817**	**(4,330,086)**	**32,452,611**

(1)

	OLIVETTI GESTIONI IVREA	I.T. TELECOM	NETESI	TILAB GP (in liquidation)	EDOTEL	TELECOM ITALIA INTERNATIONAL
Cost	4,849	114,871	15,960	33	6,868	3,221,727
Writedowns		(114,871)	(15,960)	(24)	(6,868)	(1,421,727)
	4,849	—	—	9	—	1,800,000

(in thousands of euro)	12/31/2003 Cost	Upward adjust- ments	Write- downs	Carrying value	Purchases / Subscrip- tions	Reclassi- fications/	Disposals (1)	Writedowns(-) / Writebacks of value(+)	Capital Replenish- ments	Total	9/30/2004 Cost	Upward adjust- ments	Write- downs	Carrying value
Equity investments in affiliated companies														
AREE URBANE	5,589	—	—	5,589						—	5,589	—	—	5,589
ASSCOM INSURANCE BROKERS	20	—	—	20						—	20	—	—	20
CARTESIA	50	—	—	50						—	50	—	—	50
Consorzio ARS (in liquidation)	—	—	—	—						—	—	—	—	—
Consorzio DREAM FACTORY	89	—	(89)	—						—	89	—	(89)	—
Consorzio EO (in liquidation)	16	—	—	16						—	16	—	—	16
Consorzio LABORATORIO DELLA CONOSCENZA	14	—	(4)	10						—	14	—	(4)	10
Consorzio NAVIGATE CONSORTIUM	300	—	—	300						—	300	—	—	300
Consorzio S.I.A.R.C. (in liquidation)	1	—	—	1	1	(1)				—	1	—	—	1
Consorzio TELCAL	211	—	—	211						—	211	—	—	211
Consorzio TELEMED (in liquidation)	10	—	—	10						—	10	—	—	10
EUROFLY SERVICE	—	—	—	—		2,035				2,035	2,312	—	(277)	2,035
IM.SER	399	—	—	399		(168)			126	(42)	357	—	—	357
IN.VA.	206	—	(45)	161						—	206	—	(45)	161
LI.SIT.	37,400	—	(3,258)	34,142				(4,338)		(4,338)	37,400	—	(7,596)	29,804
LOCALPORT	145	—	(145)	—						—	—	—	—	—
MIRROR INTERNATIONAL HOLDING	124,689	—	(70,000)	54,689						—	124,689	—	(70,000)	54,689
NORDCOM	29,045	—	(26,902)	2,143						—	29,045	—	(26,902)	2,143
OCN TRADING (in liquidation)	1	—	—	1						—	1	—	—	1
SIEMENS INFORMATICA	2,417	1,424	—	3,841						—	2,417	1,424	—	3,841
SINOPIA INFORMATICA (in bankruptcy)	—	—	—	—							—	—	—	—
SIOSISTEMI	3,305	—	(1,705)	1,600			(1,600)			(1,600)	—	—	—	—
SITEBA	—	—	—	—						—	—	—	—	—
SKY ITALIA (ex-Stream)	282,358	—	(238,279)	44,079	19,315	24,465	(87,859)			(44,079)	—	—	—	—
SOFORA TELECOMUNICACIONES S.A.	1	—	—	1						—	1	—	—	1
TELBIOS	3,375	—	—	3,375						—	3,375	—	—	3,375
TELEGONO	413	—	—	413						—	413	—	—	413
TIGLIO I	227,273	—	—	227,273			(47,985)			(47,985)	179,288	—	—	179,288
TIGLIO II	72,070	—	—	72,070						—	72,070	—	—	72,070
VOICE MAIL INTERNATIONAL (in liquidation)	3,801	—	(3,801)	—						—	3,801	—	(3,801)	—
	793,198	**1,424**	**(344,228)**	**450,394**	**19,316**	**26,331**	**(137,444)**	**(4,338)**	**126**	**(96,009)**	**461,675**	**1,424**	**(108,714)**	**354,385**

(1)

	SIOSISTEMI	LOCALPORT	Cons. S.I.A.R.C.	IM.SER	TIGLIO I	Sky Italia
Cost	3,305	145	1	168	47,985	345,453
Writedowns	(1,705)	(145)	(1)	(168)	—	(257,594)
	1,600	—	—	—	47,985	87,859

(in thousands of euro)	12/31/2003 Cost	12/31/2003 Upward adjust-ments	12/31/2003 Writedowns	12/31/2003 Carrying value	Purchases / Subscriptions	Reclassi-fications/	Disposals[1]	Writedowns(-) / Writebacks of value(+)	Capital Replenishments	Total	9/30/2004 Cost	9/30/2004 Upward adjustments	9/30/2004 Writedowns	9/30/2004 Carrying value
Equity investments in other companies														
ANCITEL	93	—	—	93						—	93	—	—	93
AZIENDA ESERCIZIO GAS	1	—	—	1						—	1	—	—	1
BIOINDUSTRY PARK DEL CANAVESE	52	—	—	52						—	52	—	—	52
CAF ITALIA 2000	—	—	—	—						—	—			
CERM L'AQUILA	266	—	—	266						—	266	—	—	266
CONSORTIUM	19,527	—	—	19,527						—	19,527	—	—	19,527
Consorzio ABI LAB	—	—	—	—	1					1	1	—	—	1
Consorzio C.I. MARK	3	—	—	3		(3)				(3)	—			
Consorzio CAISI (in liquidation)	—	—	—	—						—	—			
Consorzio CEFRIEL	36	—	—	36						—	36	—	—	36
Consorzio CIES	26	—	—	26						—	26	—	—	26
Consorzio CO.TIM (in liquidation)	4	—	(2)	2		(2)				(2)	—			
Consorzio COREP	10	—	—	10						—	10	—	—	10
Consorzio CRATI	—	—	—	—						—	—			
Consorzio BIOINGEGNERIA INFORMATICA MEDICA	15	—	—	15		(15)				(15)	—			
Consorzio DISTRETTO AUDIOVISIVO E dell'ICT	—	—	—	—	5					5	5	—	—	5
Consorzio DISTRETTO TECNOLOGICO CANAVESE	117	—	—	117						—	117	—	—	117
Consorzio ELIS	3	—	—	3						—	3	—	—	3
Consorzio ENERGIA FIERA DISTRICT	2	—	—	2						—	2	—	—	2
Consorzio GE.SE.CE.DI.	73	—	—	73						—	73	—	—	73
Consorzio MULTIMEDIA	—	—	—	—						—	—			
Consorzio Nazionale Imballaggi - CONAI	1	—	—	1						—	1	—	—	1
Consorzio NETTUNO	41	—	—	41						—	41	—	—	41
Consorzio QUALITAL	—	—	—	—						—	—			
Consorzio TECHNAPOLI	206	—	—	206						—	206	—	—	206
Consorzio TECNEDIN (in liquidation)	—	—	—	—						—	—			
Consorzio TOPIX	100	—	—	100						—	100	—	—	100
DIOMEDEA (in liquidation)	6	—	—	6						—	6	—	—	6
EDINDUSTRIA	44	—	(6)	38						—	44	—	(6)	38
EMITTENTI TITOLI	424	—	—	424						—	424	—	—	424
EUROFLY SERVICE	978	—	(277)	701	1,334	(2,035)				(701)	—			
FIN. - PRIV.	15,375	—	—	15,375						—	15,375	—	—	15,375
Fratelli ALINARI	2,974	—	(2,273)	701						—	2,974	—	(2,273)	701
FUNIVIE DEL PICCOLO S. BERNARDO	—	—	—	—						—	—			
IDROENERGIA	1	—	—	1						—	1	—	—	1
IMSER 60	59	—	—	59						—	59	—	—	59
INSULA	248	—	—	248						—	248	—	—	248
IST. ENCICLOPEDIA ITALIANA G. TRECCANI	5,256	—	(1,424)	3,832						—	5,256	—	(1,424)	3,832
ISTUD	6	—	—	6						—	6	—	—	6
ITALTEL CERM PALERMO	217	—	(24)	193						—	217	—	(24)	193
ITALTEL CERM S. MARIA CAPUA VETERE	255	—	(63)	192						—	255	—	(63)	192
MCC	36,018	—	—	36,018						—	36,018	—	—	36,018
MEDIOBANCA	113,119	—	—	113,119						—	113,119	—	—	113,119
MIX	10	—	—	10						—	10	—	—	10
MONTEROSA	20	—	—	20						—	20	—	—	20
PAR. FIN. (in bankruptcy)	256	—	—	256				(256)		(256)	256	—	(256)	—
PILA	6	—	—	6						—	6	—	—	6
PIRELLI RE	15,199	—	—	15,199			(15,199)			(15,199)	—			
S.A.G.I.T.	1	—	—	1						—	1	—	—	1
SIA	11,278	—	—	11,278						—	11,278	—	—	11,278
SODETEL	4	—	—	4						—	4	—	—	4
TELEPORTO ADRIATICO	—	—	—	—						—	—			
UBAE	1,898	—	—	1,898						—	1,898	—	—	1,898
	224,228	—	(4,069)	220,159	1,340	(2,055)	(15,199)	(256)	—	(16,170)	208,035	—	(4,046)	203,989
Total equity investments	41,004,991	135,241	(6,281,284)	34,858,948	62,916	136,351	(1,957,501)	(89,855)	126	(1,847,963)	37,318,590	135,241	(4,442,846)	33,010,985

(1)

	Consorzio BIOINGEGNERIA INFORMATICA	Consorzio C.I.MARK	Consorzio COTIM (in liquidation)	PIRELLI RE
Cost	15	3	4	15,199
Writedowns	(15)	(3)	(4)	—
	—	—	—	15,199

Advances on future capital contributions of subsidiaries and affiliated companies

(in thousands of euro)	12/31/2003 Cost	Upward adjust-ments	Writedowns	Carrying value	Purchases/ Subscrip-tions	Reclassi-fications/	Disposals[1]	Writedowns(-) / Writebacks of value(+)	Capital Replenishments	Total	9/30/2004 Cost	Upward adjust-Ments	Writedowns	Carrying value
EDOTEL	720			720	1,500,480	(1,200)				1,499,280	1,500,000			1,500,000
EPIClink	14,029	—	(3,091)	10,938				(3,729)		(3,729)	14,029	—	(6,820)	7,209
IT TELECOM	110,440	—	—	110,440		(110,440)				(110,440)	—			
LOCALPORT	—	—	—	—	61	(61)				—	—			
LOQUENDO	3,270	—	(46)	3,224				(328)		(328)	3,270	—	(374)	2,896
NETESI	1,650	—	(1,215)	435		(435)				(435)	—			
SKY ITALIA (ex-Stream)	7,960	—	—	7,960	35,820	(43,780)				(7,960)	—	—		
TELECOM ITALIA LEARNING SERVICES	31,344	—	(28,823)	2,521				(2,521)		(2,521)	31,344	—	(31,344)	—
TELEGONO	—	—	—	—		8,840				8,840	8,840		—	8,840
Total advances on future capital contributions of subsidiaries and affiliated companies	169,413	—	(33,175)	136,238	1,536,361	(147,076)	—	(6,578)	—	1,382,707	1,557,483	—	(38,538)	1,518,945

(1)

	LOCALPORT
Cost	61
Writedowns	(61)
	—

COMPARISON OF THE CARRYING VALUE OF LISTED SHARES WITH MARKET PRICES AT SEPTEMBER 30, 2004

		Market value		Carrying value		Difference	
	Number of shares held	Unit price (in euro)	Total (thousands of euro)	Unit price (in euro)	Total (thousands of euro)	Unit price (in euro)	Total (thousands of euro)
			(A)		(B)		(A-B)
Long-term investments							
MEDIOBANCA . . .	14,118,350	10.77	152,055	8.01	113,119	2.76	38,936
TELECOM ITALIA MOBILE - ordinary shares.	4,695,889,519	4.37	20,521,037	5.81	27,266,831	-1.44	-6,745,794
TELECOM ITALIA MEDIA - ordinary shares.	1,859,629,225	0.27	500,240	0.34	634,710	-0.07	-134,470
Short-term financial assets							
TELECOM ITALIA MOBILE - ordinary shares.	38,192,000	4.37	166,899	4.35	166,135	0.02	764
TELECOM ITALIA MEDIA - saving shares. . .	164,997	0.21	35	0.21	35	—	—
PORTAL SOFTWARE INC.	4,000	2.20	9	2.20	9	—	—

ACCOUNTS RECEIVABLE AND ACCRUED INCOME BY MATURITY AND TYPE
(in thousands of euro)

	9/30/2004				12/31/2003			
	Amounts due				Amounts due			
	Within one year	From two to five years	Beyond five years	Total	Within one year	From two to five years	Beyond five years	Total
Accounts receivable in long-term investments								
. subsidiaries		71,380		71,380	2,891	64,207		67,098
. affiliated companies	6,536	2,252	34,217	43,005	95	17,363	37,031	54,489
. others								
.. customers				0	269	67		336
.. employees	5,757	30,271	12,227	48,255	14,981	23,255	9,249	47,485
.. security deposits	3,543	3	371	3,917	262	3,110	12,566	15,938
.. time deposit on behalf of Getronics	0	0	0	0	32,067			32,067
.. miscellaneous	8,893	42,641		51,534	21,035	40,568		61,603
	24,729	146,547	46,815	218,091	71,600	148,570	58,846	279,016
Accounts receivable in current assets								
Other financial receivables from								
. subsidiaries	1,126,670			1,126,670	823,919			823,919
. affiliated companies	2,357			2,357	13,718			13,718
. others	246,352			246,352	366,594			366,594
	1,375,379			1,375,379	1,204,231			1,204,231
Trade accounts receivable from								
. customers	3,422,565			3,422,565	3,703,450			3,703,450
. subsidiaries	551,595			551,595	679,507			679,507
. affiliated companies	84,883			84,883	70,955			70,955
. others	129,524			129,524	87,984			87,984
	4,188,567			4,188,567	4,541,896			4,541,896
Other receivables from								
. subsidiaries	243,620			243,620	1,571,863			1,571,863
. affiliated companies	16,166			16,166	12,101			12,101
. taxes receivable	44,826			44,826	1,362,329			1,362,329
. deferred tax assets	789,956	2,055,138		2,845,094	1,174,778	2,055,138		3,229,916
. miscellaneous:								
.. Government and other public entities for grants and subsidies	25,889			25,889	30,748			30,748
.. miscellaneous	221,399			221,399	353,076			353,076
	1,341,856	2,055,138		3,396,994	4,504,895	2,055,138		6,560,033
Total accounts receivable in current assets	6,905,802	2,055,138		8,960,940	10,251,022	2,055,138		12,306,160
Accrued income								
. financial	43,008			43,008	20,423			20,423
. trading					275			275
. miscellaneous	1,030			1,030				
	44,038	0	0	44,038	20,698	0	0	20,698

LIABILITIES AND ACCRUED EXPENSES BY MATURITY AND TYPE
(in thousands of euro)

	9/30/2004				12/31/2003			
	Amounts due				Amounts due			
	Within one year	From two to five years	Beyond five years	Total	Within one year	From two to five years	Beyond five years	Total
Medium and long-term financial debt								
. Debentures		2,360,000	10,300,489	12,660,489	1,500,000	1,250,000	7,014,983	9,764,983
. Convertible debentures			2,827,904	2,827,904	1,330,564		2,829,006	4,159,570
. Due to banks	219,429	297,681	936	518,046	393,819	286,508	279	680,606
. Due to other lenders	81,980	162,418	211,032	455,430	77,552	213,131	249,407	540,090
. Accounts payable to subsidiaries		8,536,747	4,443,110	12,979,857	2,434,000	8,431,867	639,267	11,505,134
. Taxes payable	70			70	23,430			23,430
	301,479	11,356,846	17,783,471	29,441,796	5,759,365	10,181,506	10,732,942	26,673,813
Short-term borrowings								
. Due to banks	369,334			369,334	510,488			510,488
. Due to other lenders	209,878			209,878	241,795			241,795
. Accounts payable to subsidiaries	3,894,800			3,894,800	7,798,130			7,798,130
. Accounts payable to affiliated companies	419			419	1,027			1,027
. Other payables	6,035			6,035	62,245			62,245
	4,480,466			4,480,466	8,613,685			8,613,685
Trade accounts payable								
. Accounts payable to suppliers	1,390,028			1,390,028	1,929,794			1,929,794
. Accounts payable to subsidiaries	1,085,364			1,085,364	1,148,987			1,148,987
. Accounts payable to affiliated companies	95,269			95,269	59,405			59,405
	2,570,661			2,570,661	3,138,186			3,138,186
Other payables(1)								
. Accounts payable to subsidiaries	42,763			42,763	91,269			91,269
. Accounts payable to affiliated companies				0	24,339			24,339
. Taxes payable	624,026			624,026	355,650			355,650
. Contributions to pension and social security institutions	108,046	295,942	170,602	574,590	160,225	295,942	170,602	626,769
. Other liabilities	1,356,502	441		1,356,943	1,848,597	441		1,849,038
	2,131,337	296,383	170,602	2,598,322	2,480,080	296,383	170,602	2,947,065
Total liabilities(1)	9,483,943	11,653,229	17,954,073	39,091,245	19,991,316	10,477,889	10,903,544	41,372,749
Accrued expenses								
. financial	763,336	81,020		844,356	1,763,589	64,644		1,828,233
. trading	8,082			8,082	89			89
. miscellaneous	19			19				
	771,437	81,020	0	852,457	1,763,678	64,644	0	1,828,322

(1) *Not including the caption "Advances".*

ACCOUNTS RECEIVABLES AND LIABILITIES AT SEPTEMBER 30, 2004 - GEOGRAPHICAL AREA (CUSTOMER/SUPPLIER LOCATION) (in thousands of euro)

	Italy	Other EU countries	Rest of Europe	North America	Central and South America	Other areas	TOTAL
Accounts receivable in long-term investments							
. subsidiaries	—	71,380	—	—	—	—	**71,380**
. affiliated companies	40,753	2,252	—	—	—	—	**43,005**
. others	103,706	—	—	—	—	—	**103,706**
Total	144,459	73,632	—	—	—	—	**218,091**
Accounts receivable in current assets (*)							
. customers	3,333,996	79,524	399	2,558	5,174	914	**3,422,565**
. subsidiaries	1,909,838	10,578	15	—	202	1,252	**1,921,885**
. affiliated companies	103,083	—	243	—	80	—	**103,406**
. taxes receivable	44,419	—	—	—	407	—	**44,826**
. others	620,407	35	—	—	2,722	—	**623,164**
	6,011,743	90,137	657	2,558	8,585	2,166	**6,115,846**
LIABILITIES							
. Debentures	8,760,489	3,900,000	—	—	—	—	**12,660,489**
. Convertible debentures	2,827,904	—	—	—	—	—	**2,827,904**
. Due to banks	721,967	165,413	—	—	—	—	**887,380**
. Due to other lenders	665,308	—	—	—	—	—	**665,308**
. Advances	28,603	—	—	—	—	—	**28,603**
. Accounts payable to suppliers	1,343,997	42,065	—	2,012	1,475	479	**1,390,028**
. Accounts payable to subsidiaries	1,799,460	16,203,324	—	—	—	—	**18,002,784**
. Accounts payable to affiliated companies	95,688	—	—	—	—	—	**95,688**
. Taxes payable	624,074	—	—	—	22	—	**624,096**
. Contributions to pension and social security security institutions	574,584	—	—	—	6	—	**574,590**
. Other liabilities	1,362,978	—	—	—	—	—	**1,362,978**
Total	18,805,052	20,310,802	0	2,012	1,503	479	**39,119,848**

REVENUES 9 MONTHS TO SEPTEMBER 30, 2004 - GEOGRAPHICAL AREA (CUSTOMER LOCATION)

	Italy	Other EU countries	Rest of Europe	North America	Central and South America	Other areas	TOTAL
SALES AND SERVICE REVENUES	11,729,124	59,084	435	2,268	2,088	170	11,793,169

(*) *Not including the caption "Deferred tax assets".*

STATEMENTS OF CASH FLOWS

	(in thousands of euro)		9 months to 9/30/2004	9 months to 9/30/2003
A.	**NET FINANCIAL INDEBTEDNESS, AT BEGINNING OF PERIOD**		**(35,326,677)**	**(30,622,646)**
	Net financial indebtedness, at beginning of period of merged company TILAB		—	(169,196)
B.	**ADJUSTED NET FINANCIAL INDEBTEDNESS, AT BEGINNING OF PERIOD**		**(35,326,677)**	**(30,791,842)**
	Operating income		3,256,088	3,169,275
	Depreciation of fixed assets and amortization of intangible assets		2,003,278	2,108,942
	Investments in fixed assets and intangible assets(1)		(1,493,713)	(1,891,206)
	Proceeds from disposal of intangible assets and fixed assets		5,371	314,784
	Change in operating working capital and other changes		11,418	(4,759)
C.	**FREE CASH FLOWs FROM OPERATIONS**		**3,782,442**	**3,668,816**
	Investments in long-term investments(1)		(1,616,407)	(6,491,593)
	Proceeds from sale/redemption value of other intangible assets, fixed assets and long- term investments		2,042,811	3,016,155
	Change in non-operating working capital and other changes(2)		602,819	(3,842,192)
D.			**1,029,223**	**(7,317,630)**
E.	**NET CASH FLOWS BEFORE DISTRIBUTION OF INCOME/RESERVES AND CONTRIBUTIONS BY SHAREHOLDERS**	**(C+D)**	**4,811,665**	**(3,648,814)**
F.	**DISTRIBUTION OF INCOME/RESERVES**		**(1,740,058)**	**(793,524)**
G.	**CONTRIBUTIONS BY SHAREHOLDERS/ WITHDRAWALS**		**14,410**	**1,579**
H.	**CHANGE IN NET FINANCIAL INDEBTEDNESS**	**(E+F+G)**	**3,086,017**	**(4,440,759)**
I.	**NET FINANCIAL INDEBTEDNESS, AT END OF PERIOD**	**(A+H)**	**(32,240,660)**	**(35,232,601)**

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

(in thousands of euro)

Increase (decrease) in medium/long-term debt	8,263,303	(1,672,544)
Increase (decrease) in short-term borrowings	(11,349,320)	6,282,499
Total	**(3,086,017)**	**4,609,955**

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

(in thousands of euro)

Industrial investments:	1,493,713	1,891,206
- *intangible assets*	*688,179*	*435,704*
- *fixed assets*	*805,534*	*1,455,502*
Investment in long-term investments	1,616,407	6,491,593
CASH USED FOR INVESTMENTS	**3,110,120**	**8,382,799**

(2) The caption can be analyzed as follows:

(in thousands of euro)

Net financial income (expense)	(1,293,356)	(1,959,579)
Receipt of dividends	1,322,519	438,000
Utilization of risk reserve for early exercise of JP Morgan put option		(1,941,843)
Payment of income taxes(3)	940,000	(90,000)
Extraordinary items and other	(366,344)	(288,770)
CHANGE IN NON-OPERATING WORKING CAPITAL AND OTHER CHANGES	**602,819**	**(3,842,192)**

(3) This is a positive figure at September 30, 2004 as a result of the collection of a tax credit sold to TIM (euro 1,103,000 thousand).

ANNEX V

TIM S.p.A. Interim Financial Statements at September 30, 2004

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BALANCE SHEETS		September 30, 2004			December 31, 2003			September 30, 2003	
(in thousands of euro)									
ASSETS									
RECEIVABLES FROM SHAREHOLDERS FOR CAPITAL CONTRIBUTIONS									
INTANGIBLE ASSETS, FIXED ASSETS AND LONG-TERM INVESTMENTS			—			—			—
. INTANGIBLE ASSETS									
.. Start-up and expansion costs		948			3,791			4,739	
.. Research, development and advertising costs		—			—			—	
.. Industrial patents and intellectual property rights		547,898			527,835			356,914	
.. Concessions, licenses, trademarks and similar rights		2,330,012			2,189,858			2,220,351	
.. Goodwill		19,166			—			—	
.. Work in progress and advances		154,375			179,429			132,883	
.. Other intangibles		56,942			43,264			31,832	
			3,109,341			2,944,177			2,746,719
. FIXED ASSETS									
.. Land and buildings		11,190			12,128			12,494	
.. Plant and machinery		1,596,584			1,428,098			1,396,296	
.. Manufacturing and distribution equipment		26,415			23,391			18,446	
.. Other fixed assets		204,286			205,663			213,547	
.. Construction in progress and advances		186,939			438,615			245,109	
			2,025,414			2,107,895			1,885,892
. LONG-TERM INVESTMENTS									
.. Equity investments in:									
... subsidiaries		4,262,737			3,964,877			3,689,275	
... affiliated companies		41			1,469			1,495	
... other companies		601			536			535	
total		4,263,379			3,966,882			3,691,305	
.. Advances on future capital contributions		319,543			120,940			232,082	
.. Accounts receivable	(*)			(*)			(*)		
... other receivables	2,726	22,112		1,679	17,681		1,459	17,116	
.. Other securities		1,273			2,972			3,093	
			4,606,307			4,108,475			3,943,596
TOTAL INTANGIBLE ASSETS, FIXED ASSETS AND LONG-TERM INVESTMENTS			9,741,062			9,160,547			8,576,207
CURRENT ASSETS									
. INVENTORIES									
.. Finished goods and merchandise: merchandise			38,075			20,288			36,906
. ACCOUNTS RECEIVABLE	(* *)			(* *)			(* *)		
.. trade accounts receivable	—	1,058,487		—	1,082,551		—	947,254	
.. from subsidiaries	—	41,258		—	32,037		—	35,155	
.. from affiliated companies	—	1,652		—	234		—	10,654	
.. from parent companies	—	673,734		—	1,651,479		—	1,456,469	
.. taxes receivable	—	8,981		—	7,389		—	13,333	
.. deferred tax assets	482,488	992,537		609,009	1,038,520		714,818	1,141,598	
.. other receivables									
..... Government and other public entities for grants and subsidies	—	12,526		—	12,570		—	15,572	
..... other receivables	—	340,298		—	484,475		—	384,588	
			3,129,473			4,309,255			4,004,623
. SHORT-TERM FINANCIAL ASSETS									
.. Treasury stock (for a total par value of euro 53,870.10)		3,939			3,913			3,666	
			3,939			3,913			3,666
. LIQUID ASSETS									
.. Bank and postal accounts		1,909			3,046			8,299	
.. Cash and valuables on hand		495			312			282	
			2,404			3,358			8,581
TOTAL CURRENT ASSETS			3,173,891			4,336,814			4,053,776
ACCRUED INCOME AND PREPAID EXPENSES	(* *)			(* *)			(* *)		
... Accrued income and other prepaid expenses	2,645	64,285		—	43,760		—	40,827	
			64,285			43,760			40,827
TOTAL ASSETS			12,979,238			13,541,121			12,670,810

(*) Amounts due within 12 months

(**) Amounts due beyond 12 months

BALANCE SHEETS	September 30, 2004			December 31, 2003			September 30, 2003		
(in thousands of euro)									
LIABILITIES AND SHAREHOLDERS' EQUITY									
SHAREHOLDERS' EQUITY									
. SHARE CAPITAL			513,964			513,964			513,964
. ADDITIONAL PAID-IN CAPITAL			5,525,626			5,525,626			5,525,626
. LEGAL RESERVE			103,942			103,942			103,942
. RESERVE FOR TREASURY STOCK IN PORTFOLIO			3,939			3,913			3,666
. MISCELLANEOUS RESERVES:									
.. Reserve for capital grants (under D.P.R. No. 917/1986, art. 55)		14,681			14,681			14,681	
.. Special reserve		86,242			113,579			113,826	
.. Reserve Law 342/2000, art. 14		303,827			303,827			303,827	
.. Reserve for accelerated depreciation		150,000			—			—	
.. Merger surplus reserve		53,783			53,783			53,783	
			608,533			485,870			486,117
. RETAINED EARNINGS			—			1,331			1,331
. NET INCOME			2,142,811			2,321,624			1,846,360
			8,898,815			8,956,270			8,481,006
RESERVES FOR RISKS AND CHARGES									
.. Reserve for pensions and similar obligations		1,676			1,676			1,676	
.. Reserve for taxes, reserve for deferred taxes		777,561			—			679,088	
.. Other reserves		526,412			658,127			699,804	
			1,305,649			659,803			1,380,568
RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES			104,196			87,926			88,188
LIABILITIES	(* *)			(* *)			(* *)		
.. Due to banks	—	198		—	19		—	0	
.. Due to other lenders	—	—		—	1,637		—	22,746	
.. Trade accounts payable	—	1,626,258		—	1,888,242		—	1,334,023	
.. Accounts payable to subsidiaries	—	2,689		—	655		—	4,302	
.. Accounts payable to affiliated companies	—	3,369		—	3,536		—	2,728	
.. Accounts payable to parent companies	—	403,471		—	398,448		—	459,948	
.. Taxes payable	—	68,090		—	845,732		—	107,206	
.. Contributions to pension and social security institutions	1,283	11,709		1,275	19,917		2,338	11,171	
.. Other liabilities	—	535,940		—	666,692		—	752,365	
	1,283		2,651,724	1,275		3,824,878	2,338		2,694,489
ACCRUED EXPENSES AND DEFERRED INCOME	(* *)			(* *)			(* *)		
... Accrued expenses and other deferred income	6,139	18,854		—	12,244		—	26,559	
			18,854			12,244			26,559
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY			12,979,238			13,541,121			12,670,810

(* *) Amounts due beyond 12 months

MEMORANDUM ACCOUNTS (in thousands of euro)	September 30, 2004			December 31, 2003			September 30, 2003		
GUARANTEES PROVIDED									
. Sureties									
.. on behalf of affiliated companies	169,253			209,166			183,938		
.. on behalf of parent companies	—			—			—		
.. on behalf of others	28,645			27,020			24,391		
		197,898			236,186			208,329	
. Other									
.. on behalf of subsidiaries	355,249			425,828			5,388		
.. on behalf of affiliated companies	456,780			453,167			—		
.. on behalf of others	51,000			51,000			51,000		
		863,029			929,995			56,388	
			1,060,927			1,166,181			264,717
COLLATERAL PROVIDED									
. For own obligations, excluding liabilities		—			—			1,549	
. For liabilities recorded in the balance sheet		—			—			—	
			—			—			1,549
PURCHASES AND SALES COMMITMENTS			987			6,189			9,417
OTHER MEMORANDUM ACCOUNTS			—			—			2,251
TOTAL			1,061,914			1,172,370			277,934

STATEMENTS OF INCOME			9 months to September 30, 2004			9 months to September 30, 2003			Year 2003
(in thousands of euro)									
PRODUCTION VALUE									
. Sales and service revenues			7,381,031			6,979,951			9,468,629
. Increases in capitalized internal construction costs			26,095			—			—
. Other revenues and income									
.. operating grants		203			28			28	
.. other		22,899			21,940			31,126	
			23,102			21,968			31,154
			7,430,228			7,001,919			9,499,783
PRODUCTION COSTS									
. Raw materials, supplies and merchandise			466,464			382,856			592,803
. Services			2,171,115			2,061,244			2,819,682
. Use of property not owned			371,087			403,774			569,185
. Personnel costs:									
.. wages and salaries		244,563			236,662			315,038	
.. social security contributions		76,659			73,668			98,855	
.. termination indemnities		16,195			15,236			20,003	
.. other costs		6,810			5,280			7,410	
			344,227			330,846			441,306
. Amortization, depreciation and writedowns									
.. amortization of intangible assets		371,950			301,936			424,123	
.. depreciation of fixed assets		461,648			486,045			658,859	
.. writedowns of receivables included in current assets and liquid assets		29,876			32,120			66,299	
			863,474			820,101			1,149,281
. Changes in inventories of raw materials, supplies and merchandise			(17,787)			(1,261)			15,357
. Provisions for risks			—			—			—
. Other provisions			2,738			11,054			14,851
. Miscellaneous operating costs									
.. losses		387			1,130			1,463	
.. TLC operating fees		2,558			3,814			5,035	
.. other miscellaneous costs		25,036			19,032			27,846	
			27,981			23,976			34,344
			(4,229,299)			(4,032,590)			(5,636,809)
OPERATING INCOME			3,200,929			2,969,329			3,862,974
FINANCIAL INCOME AND EXPENSE									
. Other financial income from									
.. accounts receivable included in long-term investments									
... other	194			246			343		
		194			246			343	
.. securities, other than equity investments, included in long-term investments		4			77			102	
.. other income									
... interest and fees from subsidiaries	351			—			—		
... interest and fees from affiliated companies	—			—			2		
... interest and fees from parent companies	29,714			8,069			17,812		
... interest and fees from others and miscellaneous income	555			2,352			2,246		
		30,620			10,421			20,060	
			30,818			10,744			20,505
. Interests and other financial expenses									
.. interest and fees paid to subsidiaries		—			1,623			1,623	
.. interest and fees paid to parent companies		1,346			5,326			5,810	
.. interest and fees paid to others and miscellaneous expenses		4,477			7,172			10,558	
			(5,823)			(14,121)			(17,991)
. Foreign exchange gains and losses		(161)			3,159			1,043	
			(161)			3,159			1,043
TOTAL FINANCIAL INCOME AND EXPENSE			24,834			(218)			3,557

STATEMENTS OF INCOME	9 months to September 30, 2004		9 months to September 30, 2003		Year 2003	
(in thousands of euro)						
VALUE ADJUSTMENTS TO FINANCIAL ASSETS						
. Upward adjustments						
.. of equity investments	31		—		—	
.. of securities, other than equity investments, included in current assets	26		—		—	
		57		—		—
. Writedowns						
.. of equity investments	—		4,494		4,520	
.. securities, other than equity investments, included in long-term investments	—		1,563		1,836	
.. of securities, other than equity investments, included in current assets	—		619		372	
		—		6,676		6,728
TOTAL VALUE ADJUSTMENTS TO FINANCIAL ASSETS		57		(6,676)		(6,728)
EXTRAORDINARY INCOME AND EXPENSE						
. Income						
.. elimination of tax interference	241,702		—		—	
.. miscellaneous	9,439		622,885		646,610	
		251,141		622,885		646,610
. Expense						
.. prior years' taxes	(92,413)		(7,665)		(7,670)	
.. provisions and writedowns to equity investments	—		(478,000)		(618,000)	
.. miscellaneous	(8,737)		(18,295)		(29,119)	
		(101,150)		(503,960)		(654,789)
TOTAL EXTRAORDINARY INCOME AND EXPENSE		149,991		118,925		(8,179)
INCOME BEFORE TAXES		3,375,811		3,081,360		3,851,624
. Income taxes, current and deferred		1,233,000		1,235,000		1,530,000
NET INCOME		2,142,811		1,846,360		2,321,624

NOTES TO THE FINANCIAL STATEMENTS

INTRODUCTION

The interim financial statements for the nine months ended September 30, 2004 of TIM S.p.A. have been prepared in accordance with the provisions of the Italian Civil Code pertaining to statutory financial statements and with the changes and additions introduced by the reform of corporate law pursuant to Legislative Decree No. 6 dated January 17, 2003, as amended, art. 81 of Consob Resolution No. 11971 dated May 14, 1999 and the relevant Annex 3C-bis and subsequent changes and additions.

Appropriate reclassifications have been made to the data relating to prior periods, where necessary, for purposes of comparison with the interim financial statements for the nine months ended September 30, 2004.

The statement of cash flows is attached to these interim financial statements (Annex 5).

All amounts are expressed in thousands of euros, unless otherwise indicated.

Summary of significant accounting policies

The accounting policies adopted in the preparation of the interim financial statements for the nine months ended September 30, 2004, taking into account the adjustments required by the nature of interim financial reporting, have been applied on a basis consistent with those of the annual financial statements, with the exception of income taxes for the period.

Intangible assets

Intangible assets are stated at purchase or production cost and are systematically amortized each year on the basis of their estimated residual period of benefit.

Appropriate writedowns are made when the investments are considered unlikely to be fully recovered and their cost is written down to market value or, in the event of sale, to realizable value. In subsequent financial statements, the lower value will not be maintained in cases in which the reasons for the writedown cease to exist.

The amortization policy is described in the following paragraphs.

Start-up and expansion costs: these are amortized over a period not exceeding five years beginning from the year in which the costs are incurred. With reference to the provisions of art. 2426, paragraph 5, of the Italian Civil Code, a statement is made to the effect that the amount of available reserves exceeds the value of unamortized intangible assets.

Industrial patents and intellectual property rights: these are amortized according to their estimated useful life on a five-year basis or on a three-year basis in the case of software, beginning from the time the cost is incurred.

Concessions, licenses, trademarks and similar rights: these are amortized according to their residual period of utilization.

Goodwill: this refers to the purchase of the Information Technology business segment from IT Telecom S.p.A. and is amortized over three years.

Other intangibles: these refer to leasehold improvements and are amortized over five years.

Work in progress: this is stated at the direct amount of costs incurred for the purchase of assets, services rendered by third parties and miscellaneous expenses.

Fixed assets

Fixed assets are stated at purchase or production cost and depreciated systematically on the basis of their residual useful life according to the following criteria. The cost of assets transferred by Telecom Italia at the time of the demerger included inflation adjustments made pursuant to special laws on assets existing at December 31, 1981 (Law No. 576 dated December 2, 1975 and Law No. 72 dated March 19, 1983) as well as mandatory revaluations of properties (purchased by December 31, 1990 and shown in the balance sheet at December 31, 1991) pursuant to Law No. 413 dated December 30, 1991.

Fixed assets are depreciated each year using the straight-line method at rates determined on the basis of their estimated remaining useful life.

Ordinary maintenance expenses are entirely charged to the statement of income in the year incurred.

Mobile radio equipment owned by the company or leased to customers is fully depreciated in the year of purchase, given the low per unit cost and short useful life.

Construction in progress: this is stated at the amount of direct costs incurred for the purchase of assets, third-party services and miscellaneous expenses.

Long-term investments

- *Equity investments:* long-term equity investments are stated at purchase or subscription cost, applying the criterion of weighted average cost per movement, if any. For companies that present performance such as to assume a permanent impairment in value, the amount is adjusted – through specific writedowns – up to the value attributable to the equity investments. Losses in value exceeding the corresponding carrying value are shown in the Reserves for risks and charges.

  Writedowns to equity investments are not maintained in successive years if the conditions generating them cease to exist.

  The cost of equity investments in foreign companies has been converted to euros at the exchange rate prevailing at the time of acquisition or subscription.
- *Other securities other than equity investments:* if acquired with the intention of keeping them in portfolio until maturity, such securities are recorded in long-term investments at purchase cost adjusted by the pertinent portion referring to the difference between purchase cost and reimbursement value.

Inventories

Inventories are stated at the lower of realizable value and purchase cost, determined using the weighted average cost method. Merchandise exceeding foreseeable commercial requirements and slow-moving or obsolete inventories are written down to estimated realizable value.

Accounts receivable and liabilities

Accounts receivables included in long-term investments and current assets are stated at estimated realizable value.

Liabilities are shown at nominal value.

Accounts receivable due from the Company's dealers are subject to sale without recourse to factoring companies (within pre-set limits). When each receivable sold becomes due, the factoring company pays the Company the nominal value of such accounts receivable, net of amounts due to dealers for services rendered. The Company has not issued any guarantees for these transactions.

Transactions in foreign currency

Monetary assets and liabilities are accounted for at the exchange rate as of the transaction date and updated to the exchange rates prevailing at period-end, taking into account hedging contracts. Unrealized positive and negative and differences arising from recording foreign currency assets and liabilities at the exchange rates at the transaction date and at the period end date are recorded in the statement of income and any unrealized net exchange gain is set aside in a specific reserve until realization.

Treasury stock

Treasury stock is recorded in current assets as it is available for sale, and has been purchased on the market in execution of the resolutions passed by the Shareholders' Meetings of June 15, 1999 and April 12, 2000. These shares are shown at the lower of cost (calculated as the weighted average for each movement) and market value. A specific equity reserve has been recorded in Shareholders' equity under liabilities for the same amount as the treasury stock booked under assets.

Accruals and deferrals

These items are recorded on the accrual basis.

Reserves for risks and charges

Reserve for taxes and reserve for deferred taxes: this includes income taxes for the period calculated on the basis of the best possible estimate using available information and on a reasonable projection of performance for the year up to the end of the tax period. It also includes deferred taxes, net of deferred tax assets, whenever the conditions exist, deriving from temporary differences between the values attributed to assets and liabilities for accounting purposes and the value attributed to the same assets and liabilities for tax purposes.

Deferred tax assets which cannot be set off against deferred tax liabilities are booked in Current assets under Deferred tax assets.

In keeping with the principle of prudence, deferred tax assets are not booked unless there is reasonable certainty of the existence of sufficient taxable income in future years when the temporary differences reverse.

No deferred taxes are set aside on tax suspension reserves unless transactions for their distribution or utilization are expected to be entered into and the distribution or utilization will give rise to taxation.

Other reserves: these reserves relate primarily to provisions to cover expenses of certain or likely existence whose amount or date of occurrence could, however, not be determined at the end of the period.

Reserve for employee termination indemnities

The reserve for employee termination indemnities, recorded net of advances paid, is determined based on the provisions of art. 2120 of the Italian Civil Code, Law No. 297 of May 29, 1982 calling for mandatory cost-of-living adjustments, and also on collective bargaining agreements. The reserve is adjusted to the liability maturing at the end of the period for personnel in force at that date. Other receivables in Long-term investments include receivables for taxes paid in advance on employees termination indemnities as set forth by Law No. 662 dated December 23, 1996, and subsequent changes and additions.

Revenues and expenses

Revenues and expenses are recorded on an accrual basis.

In particular, activation fees are recognized when the contract is signed, in that they are associated with the activation expenses. As for telecommunications services, "traffic revenues" include amounts invoiced by the Company to its customers and payable to other domestic and foreign wireline and mobile operators.

Grants

Operating grants and grants for plant installations are recorded in "Other revenues and income" in the accounting period in which the paperwork documenting the grants is received, or in the period in which the respective costs are incurred, provided that the certainty of payment is confirmed by established procedures.

Specifically, grants for plant installations are recorded under Deferred income and credited to the statement of income in relation to the depreciation taken on the assets to which the grants refer.

Leased assets

Capital goods acquired under leasing agreements are recognized in the financial statements by a method consistent with current legislation, which requires that leasing payments be recorded as operating costs by the lessee.

Income taxes

Current income taxes are computed on the basis of a realistic estimate of the income tax charge according to the tax laws in force; in interim financial statements, the related income tax liability is recorded in the reserve for taxes and deferred taxes.

Deferred income taxes are calculated according to the policy described in the paragraph on Reserves for risks and charges.

Memorandum accounts

"Guarantees provided" are shown at an amount equal to the obligations guaranteed net of any counter-guarantees received in order to reduce the risk and potential exposure in relation to the guaranteed party.

"Purchases and sales commitments" which do not fall under the normal operating cycle refer to contracts whose performance is deferred and for which the Company has obligations to third parties and vice versa from the time the contracts are signed.

Commitments are valued on the basis of contracts outstanding at period-end. With regard to specific commitments, lease obligations include future lease payments plus the purchase option.

****

Disclosure regarding related party transactions and, in particular, transactions with subsidiaries, affiliated companies and parent companies and companies controlled by the latter is provided in the applicable principal balance sheet and statement of income captions. Such disclosure is considered exhaustive with regard to the requirements of art. 2428 of the Italian Civil Code, Consob communication No. 97001574 dated February 20, 1997, No. 98015375 dated February 27, 1998 and No. 2064231 dated September 30, 2002 and art. 150, first paragraph, of Legislative Decree No. 58/1998.

All transactions entered into with such companies have been concluded on the basis of normal market conditions or specific provisions of the law.

BALANCE SHEETS - ASSETS

ASSETS **euro 9,741,062 thousand**
(euro 9,160,547 thousand at December 31, 2003)

Intangible assets, fixed assets and long-term investments increased by euro 580,515 thousand compared to December 31, 2003.

INTANGIBLE ASSETS **euro 3,109,341 thousand**
(euro 2,944,177 thousand at December 31, 2003)

Intangible assets increased by euro 165,164 thousand compared to December 31, 2003. The increase is due to additions during the period (euro 295,412 thousand) and the writeback of the value of the UMTS license (euro 241,702 thousand) which became necessary as a result of the changes introduced by the reform of corporate law (Legislative Decree No. 6/2003) which, overall, are higher than the amortization charge for the period (euro 371,950 thousand).

An analysis of the composition and the changes in intangible assets during the first nine months of the year is presented in the following tables, with a separate indication of writedowns.

	12/31/2003				
	Cost		Accumulated amortization		
(in thousands of euro)	Gross value	Writedowns	Gross value	Writedowns	Total
Start-up and expansion costs	34,348	(15,397)	(23,687)	8,527	**3,791**
Research, development and advertising costs	27,940	(27,940)	(15,472)	15,472	**—**
Industrial patents and intellectual property rights	1,950,092	(7,537)	(1,420,663)	5,943	**527,835**
Concessions, licenses, trademarks and similar rights	2,441,070	(7,272)	(245,616)	1,676	**2,189,858**
Goodwill	2,061	(2,061)	(1,188)	1,188	**—**
Work in progress and advances	179,691	(262)	—	—	**179,429**
Other intangibles	243,196	(75,254)	(146,315)	21,637	**43,264**
Total	**4,878,398**	**(135,723)**	**(1,852,941)**	**54,443**	**2,944,177**

	Changes during the period				
(in thousands of euro)	Additions	Reclassifications	Sales/ Retirements/ Other movements	Amortization	Total
Start-up and expansion costs	—	—	—	(2,843)	**(2,843)**
Research, development and advertising costs	—	—	—	—	**—**
Industrial patents and intellectual property rights	150,776	120,453	—	(251,166)	**20,063**
Concessions, licenses, trademarks and similar rights	—	241,702	—	(101,548)	**140,154**
Goodwill	23,000	—	—	(3,834)	**19,166**
Work in progress and advances	106,212	(131,266)	—	—	**(25,054)**
Other intangibles	15,424	10,813	—	(12,559)	**13,678**
Total	**295,412**	**241,702**	**—**	**(371,950)**	**165,164**

(in thousands of euro)	9/30/2004 Cost Gross value	Cost Writedowns	Accumulated amortization Gross value	Accumulated amortization Writedowns	Total
Start-up and expansion costs	34,348	(15,397)	(26,530)	8,527	**948**
Research, development and advertising costs	27,940	(27,940)	(15,472)	15,472	**—**
Industrial patents and intellectual property rights	2,221,321	(7,537)	(1,671,829)	5,943	**547,898**
Concessions, licenses, trademarks and similar rights	2,441,070	(7,272)	(105,462)	1,676	**2,330,012**
Goodwill	25,061	(2,061)	(5,022)	1,188	**19,166**
Work in progress and advances	154,637	(262)	—	—	**154,375**
Other intangibles	269,433	(75,254)	(158,874)	21,637	**56,942**
Total	**5,173,810**	**(135,723)**	**(1,983,189)**	**54,443**	**3,109,341**

The most important item in *Intangible assets* is the caption *Concessions, licenses, trademarks and similar rights* which comprises the value of the UMTS license, purchased at the end of 2000 and booked for a cost of euro 2,417,018 thousand, equal to the bid price at auction.

Amortization of the license commenced in January 2002 – although its commercial use began during 2004 – so as not to compromise the tax benefit connected with deductibility.

Beginning from the first half of 2004, in compliance with the changes in the law introduced by Legislative Decree No. 6/2003 which imposes the neutralization of any tax interference existing in the financial statements, and taking into account the recent indications provided by agencies and regulators, the amortization taken on the UMTS license up to December 31, 2003 (euro 241,702 thousand) was written back with a contra-entry to extraordinary income.

The relative charge for deferred taxes was recorded in the Reserve for deferred taxes (euro 91,242 thousand) with a contra-entry to extraordinary expenses.

The amortization of the UMTS license is calculated on the basis of the remaining period of utilization of the license, which is deemed to represent, at this time, the economic life of the asset; amortization began in January 2004 in view of the fact that the service was already operational and used by a pool of experimental users.

The following tables provides a summary of the effects of the elimination of tax interference on the result for the first nine months of 2004 and shareholders' equity at September 30, 2003.

(in thousands of euro)	9 months to 9/30/2004 Income for the period	9 months to 9/30/2003 Income for the period	Shareholders' equity
Amounts before elimination of tax interference	**1,992,351**	**1,846,360**	**6,634,646**
Tax interference, gross of deferred taxes	241,702	93,055	120,851
Related deferred taxes	(91,242)	(35,122)	(49,247)
Total tax interference, net of deferred taxes	150,460	57,933	71,604
Amounts after elimination of tax interference	**2,142,811**	**1,904,293**	**6,706,250**

Additions during the period total euro 295,412 thousand and largely refer to software. Part of this amount, for euro 79 thousand, comes from the acquisition of the business segment for innovative service using IP networks from IT Telecom S.p.A.; the acquisition was finalized on April 1, 2004. The sales price agreed by the parties was euro 23 million, which was also based on an outside appraisal conducted by Milestone Advisory House S.p.A. of Milan. This amount was posted by TIM in *Goodwill* and is being amortized over the estimated residual life of three years, starting on April 1, 2004. This value is deemed to reflect the fair value of the intangible asset at September 30, 2004.

Some of the additions during the period, totaling euro 66,473 thousand, refer to transactions with related parties, mainly IT Telecom S.p.A.

FIXED ASSETS **euro 2,025,414 thousand**
(euro 2,107,895 thousand at December 31, 2003)

Fixed assets decreased by euro 82,481 thousand owing to additions during the period (euro 409,986 thousand) that were lower than the depreciation charge (euro 491,060 thousand) and the net value of fixed asset disposals (euro 1,407 thousand).

An analysis of the composition and the changes in fixed assets during the first nine months of the year is presented in the following tables, with a separate indication of writedowns and upward adjustments.

	12/31/2003					
	Cost			Accumulated depreciation		
(in thousands of euro)	Gross value	Writedowns	Upward adjustments	Gross value	Writedowns	Total
Land and buildings						
- non-industrial	*601*	—	*13*	—	—	*614*
- industrial	*37,664*	*(9,682)*	*1,984*	*(20,064)*	*1,612*	*11,514*
Total land and buildings	38,265	(9,682)	1,997	(20,064)	1,612	**12,128**
Plant and machinery	5,570,951	(84,218)	344	(4,077,484)	18,505	**1,428,098**
Manufacturing and distribution equipment	98,566	(5,131)	2	(71,699)	1,653	**23,391**
Other fixed assets	620,148	(6,710)	7	(410,017)	2,235	**205,663**
Construction in progress and advances	440,531	(1,916)	—	—	—	**438,615**
Total	**6,768,461**	**(107,657)**	**2,350**	**(4,579,264)**	**24,005**	**2,107,895**

	Changes during the period				
(in thousands of euro)	Additions	Reclassifications	Sales/ Retirements/ Other movements	Depreciation	Total
Land and buildings					
- non-industrial	—	—	—	—	—
- industrial	—	—	*0*	*(938)*	*(938)*
Total land and buildings	—	—	0	(938)	**(938)**
Plant and machinery	258,825	335,031	(1,331)	(424,039)	**168,486**
Manufacturing and distribution equipment	12,563	—	—	(9,539)	**3,024**
Other fixed assets	20,319	34,924	(76)	(56,544)	**(1,377)**
Construction in progress and advances	118,279	(369,955)	—	—	**(251,676)**
Total	**409,986**	**—**	**(1,407)**	**491,060**	**82,481**

	9/30/2004					
	Cost			Accumulated depreciation		
(in thousands of euro)	Gross value	Writedowns	Upward adjustments	Gross value	Writedowns	Total
Land and buildings						
- non-industrial	*601*	—	*13*	—	—	***614***
- industrial	*33,067*	*(7,068)*	*1,984*	*(17,407)*	—	***10,576***
Total land and buildings	33,668	(7,068)	1,997	(17,407)	—	**11,190**
Plant and machinery	5,914,422	(81,371)	344	(4,252,469)	15,658	**1,596,584**
Manufacturing and distribution equipment	111,129	(5,131)	2	(81,238)	1,653	**26,415**
Other fixed assets	674,688	(6,710)	7	(465,934)	2,235	**204,286**
Construction in progress and advances	188,855	(1,916)	—	—	—	**186,939**
Total	**6,922,762**	**(102,196)**	**2,350**	**(4,817,048)**	**19,546**	**2,025,414**

Additions during the first nine months of the year, totaling euro 409,986 thousand, largely refer to transmission installations and machinery. Part of the additions referring to the caption *Other fixed assets,* amounting to euro 450 thousand, come from the sale of the business segment by IT Telecom, the seller, to TIM, the buyer, as commented in *Intangible assets.*

Some of the additions during the nine-month period, totaling euro 793 thousand, refer to transactions with related parties, mainly IT Telecom S.p.A.

Details of fixed assets sold/retired/transferred during the period January 1 – September 30, 2004 are provided in the following table.

	Cost			**Accumulated depreciation**		
(in thousands of euro)	**Gross value**	**Writedowns**	**Upward adjustments**	**Gross value**	**Writedowns**	**Total**
Land and buildings						
- *non-industrial*	—	—	—	—	—	—
- *industrial*	*4,597*	*(2,614)*	—	*(3,595)*	*1,612*	*0*
Total land and buildings	4,597	(2,614)	—	(3,595)	1,612	0
Plant and machinery	250,385	(2,847)	—	(249,054)	2,847	**1,331**
Manufacturing and distribution equipment	—	—	—	—	—	**—**
Other fixed assets	703	—	—	(627)	—	**76**
Construction in progress and advances	—	—	—	—	—	**—**
Total	**255,685**	**(5,461)**	**—**	**(253,276)**	**4,459**	**1,407**

In March 2004, TIM contributed the business segment for applications development and maintenance in SAP environment to Societa Consortile Shared Service Center a r.l., acquiring 4.55% of the company, an affiliate of the Telecom Italia Group. The fixed assets sold, the net book value of which totaled euro 15 thousand, referred to the *Other fixed assets* category.

LONG-TERM INVESTMENTS **euro 4,606,307 thousand**
(euro 4,108,475 thousand at December 31, 2003)

Long-term investments increased by euro 497,832 thousand, compared to December 31, 2003, and is detailed as follows:

(in thousands of euro)	9/30/2004	12/31/2003
Equity investments in:		
- subsidiaries	4,262,737	3,964,877
- affiliated companies	41	1,469
- other companies	601	536
	4,263,379	**3,966,882**
Advances on future capital contributions	**319,543**	**120,940**
Accounts receivable:		
- other receivables	22,112	17,681
	341,655	**138,621**
Other securities	**1,273**	**2,972**
Total	**4,606,307**	**4,108,475**

Equity investments **euro 4,263,379 thousand**
(euro 3,966,882 thousand at December 31, 2003)

Subsidiaries euro 4,262,737 thousand
(euro 3,964,877 thousand at December 31, 2003)

Equity investments in subsidiaries refer to the holding in TIM International N.V. The euro 297,860 thousand increase is due to the conversion to share capital of a part of advances on future capital contributions made during the first months of 2004 and of all those booked at December 31, 2003. The carrying value of the subsidiary was thus increased up to euro 8,364,737 thousand, gross of the writedowns made in prior years for euro 4,102,000 thousand.

Affiliated companies euro 41 thousand
(euro 1,469 thousand at December 31, 2003)

Equity investments in affiliated companies decreased by euro 1,428 thousand, compared to December 31, 2003, owing to the sale of the investment in Edotel S.p.A. to Telecom Italia S.p.A. The sale price was equal to the carrying value in the financial statements (euro 1,939 thousand).

Other companies euro 601 thousand
(euro 536 thousand at December 31, 2003)

Equity investments in other companies increased by euro 65 thousand, compared to December 31, 2003, following the acquisition of the investment in *Societa Consortile Shared Service Center a r.l.* The acquisition was part of the deal for the contribution of the business segment commented under fixed assets. The amount corresponds to the value of the business segment conferred and established by the appraiser assigned by the Milan Court.

Advances on future capital contributions **euro 319,543 thousand**
(euro 120,940 at December 31, 2003)

Advances on future capital contributions increased by euro 198,603 thousand compared to the end of the prior year.

These refer to non-interest earning advances for future capital increases paid during the period to TIM International N.V. and not yet converted to share capital.

Such advances are directed toward providing support for the development of the TIM Group abroad, principally in South America. Advances on future capital contributions at December 31, 2003 and a part of the advances made during 2004 (for a total of euro 177,400 thousand) have been converted, for euro 297,860 thousand, to share capital following the resolution passed by the Shareholders' Meeting of the subsidiary on April 29, 2004.

(in thousands of euro)	12/31/2003	Advances	Reimbursements	Other changes	9/30/2004
Equity investments in subsidiaries					
TIM International N.V.	120,460	496,943	—	(297,860)	319,543
Equity investments in affiliated companies					
Edotel S.p.A.	480	—	—	(480)	—
Total	**120,940**	**496,943**	**—**	**(298,340)**	**319,543**

Details of changes during the period in equity investments and advances on future capital contributions, as well as the list of equity investments held by TIM S.p.A., are listed at the end of these Notes in Annex 1.

Accounts receivable **euro 22,112 thousand**
(euro 17,681 thousand at December 31, 2003)

Accounts receivable increased by euro 4,431 thousand compared to December 31, 2003. They refer to:

- loans granted to employees for euro 21,230 thousand;
- tax credits on advances made from employee termination indemnities (revalued by euro 12 thousand pursuant to Law No. 662/1996, and subsequent changes and integrations) for euro 882 thousand. The upward adjustment has been booked in financial income.

(in thousands of euro)	12/31/2003	Changes during the period: Disbursements	Reimbursements	Other changes	9/30/2004
Other receivables	17,681	4,036	—	395	22,112
Total	**17,681**	**4,036**	**—**	**395**	**22,112**

A breakdown of accounts receivable falling due within and beyond five years is presented in these Notes in Annex 2.

Securities **euro 1,273 thousand**
(euro 2,972 thousand at December 31, 2003)

Securities decreased by euro 1,699 thousand compared to December 31, 2003. They refer to an investment in the Saturn Venture Partners LLC closed-end investment fund.

Government securities recorded in the financial statements at December 31, 2003 for euro 1,550 thousand became due in the early months of 2004.

CURRENT ASSETS **euro 3,173,891 thousand**
(euro 4,336,814 thousand at December 31, 2003)

INVENTORIES **euro 38,075 thousand**
(euro 20,288 thousand at December 31, 2003)

Merchandise **euro 38,075 thousand**
(euro 20,288 thousand at December 31, 2003)

Period-end inventories consisted of the following:

- euro 36,933 thousand of mobile radio equipment and relevant accessories (net of an inventory writedown of euro 448 thousand);
- euro 1,590 thousand of equipment acquired following finalization of the sale of the business segment by Wind S.p.A. to TIM which gave rise, in the previous year, to the acquisition of assets related to the "Core Network" of ex-Blu S.p.A., part of which could not be used by the TIM network and were thus resold.

ACCOUNTS RECEIVABLE **euro 3,129,473 thousand**
(euro 4,309,255 thousand at December 31, 2003)

Accounts receivable decreased by euro 1,179,782 thousand compared to December 31, 2003.

The table below provides details, for each accounts receivable category, of beginning and ending balances as well as changes during the period.

		Changes during the period			
(in thousands of euro)	**12/31/2003**	**Utilizations**	**Provisions**	**Other changes**	**9/30/2004**
Trade accounts receivable	1,193,551	—	—	(4,064)	1,189,487
- allowance for doubtful accounts	(111,000)	9,876	(29,876)	—	(131,000)
Total trade accounts receivable	**1,082,551**	**9,876**	**(29,876)**	**(4,064)**	***1,058,487***
Accounts receivable from subsidiaries	32,037	—	—	9,221	41,258
Accounts receivable from affiliated companies	11,387	—	—	(9,691)	1,696
- allowance for doubtful accounts	(11,153)	11,109	—	—	(44)
Total accounts receivable from affiliated companies	**234**	**11,109**	**—**	**(9,691)**	**1,652**
Accounts receivables from parent companies	**1,651,479**	**—**	**—**	**(977,745)**	**673,734**
Taxes receivable	**7,389**	**—**	**—**	**1,592**	**8,981**
Deferred tax assets	**1,038,520**	**—**	**—**	**(45,983)**	**992,537**
Other receivables					
Government and other public entities for grants and subsidies	12,570	—	—	(44)	12,526
Other receivables	484,475	—	—	(144,177)	340,298
Total other receivables	**497,045**	**—**	**—**	**(144,221)**	**352,824**
Total	**4,309,255**	**20,985**	**(29,876)**	**(1,170,891)**	**3,129,473**

Trade accounts receivable, gross of the relative allowance account, totals euro 1,189,487 thousand, for a decrease of euro 4,064 thousand compared to December 31, 2003.

Starting in the first half of 2004, trade accounts receivable sold to factoring companies and not yet due are recorded in *other receivables*, consistent with the Group's classification policy; up to December 31, 2003, such receivables had been classified in *trade accounts receivable*. Receivables with factoring companies total euro 146,808 thousand at September 30, 2004. Appropriate reclassifications were also made to the balances at September 30, 2003 and December 31, 2003 (euro 178,875 thousand and euro 266,267 thousand, respectively), for purposes of comparison.

The allowance for doubtful receivables at September 30, 2004 amounts to euro 131,000 thousand, after utilization of euro 9,876 thousand and provisions of euro 29,876 thousand.

Accounts receivable arising from trade transactions with related parties total euro 242,321 thousand and mainly refer to Telecom Italia Sparkle S.p.A.

Accounts receivable from subsidiaries increased by euro 9,221 thousand, compared to December 31, 2003, and mainly refer to trade transactions (euro 31,377 thousand) principally in connection with traffic revenues.

Accounts receivable from affiliated companies, gross of the relative allowance account, amount to euro 1,696 thousand, for a decrease of euro 9,691 thousand compared to December 31, 2003. During the first few months of the year, part of the trade accounts receivable due from Is TIM (subsequently merged with the Turkish mobile operator Aycell in TT&TIM, now AVEA I.H.A.S.), equal to euro 11,109 thousand - covered by the allowance for doubtful receivables at December 31, 2003 – was sold to the subsidiary TIM International N.V. at net book value.

The balance of accounts receivable from affiliated companies at the end of the period consists of euro 66 thousand of financial receivables, euro 141 thousand of trade receivables (also principally for traffic revenues) and euro 1,445 thousand of other receivables.

Accounts receivable from parent companies decreased by euro 977,745 thousand, compared to December 31, 2003, and include the balance on the correspondence current account (euro 497,870 thousand, a decrease of euro 942,591 thousand), trade accounts receivable (euro 174,207 thousand) and other receivables (euro 1,657 thousand). The correspondence current account represents almost all of the financial resources of TIM S.p.A. at September 30, 2004.

Deferred tax assets amount to euro 992,537 thousand and are presented net of the reserve for deferred taxes totaling euro 51,993 thousand.

The gross amount of deferred tax assets mainly refers to the portion of the writedowns made to the carrying value of the subsidiary TIM International N.V. in 2002 and 2003 which will become deductible in future years.

Other receivables are detailed in the following table.

(in thousands of euro)	**9/30/2004**	**12/31/2003**	**Changes**
Government and other public entities for grants and subsidies	12,526	12,570	(44)
Accounts receivable from factoring companies	146,808	266,267	(119,459)
Receipts from factoring companies in transit	59,803	107,332	(47,529)
Other receipts in transit	803	2,415	(1,612)
Employee-related receivables	5,549	3,961	1,588
Other receivables	127,335	104,500	22,835
Total	**352,824**	**497,045**	**(144,221)**

During the first nine months of the year, TIM sold trade accounts receivable without recourse to factoring companies within pre-fixed limits for euro 2,359 million.

Accounts receivable from related parties amount to euro 137,220 thousand and principally refer to the company Intesa Mediofactoring S.p.A.

A breakdown of accounts receivable, accrued income and prepaid expenses by maturity and type is given at the end of these notes in Annex 2.

SHORT-TERM FINANCIAL ASSETS **euro 3,939 thousand**
(euro 3,913 thousand at December 31, 2003)

Treasury stock

Treasury stock refers to 897,835 TIM ordinary shares purchased in 2000, in execution of the resolutions passed by the Shareholders' Meetings of June 15, 1999 and April 12, 2000, for subsequent sale to dealers. This treasury stock, representing the shares remaining after the expiration of the offer to the dealers, was upwardly adjusted to market value by euro 26 thousand. There were no new purchases or sales of treasury stock during the nine-month period.

LIQUID ASSETS **euro 2,404 thousand**
(euro 3,358 thousand at December 31, 2003)

Liquid assets decreased by euro 954 thousand compared to December 31, 2003. Liquid assets include bank and postal accounts for euro 1,909 thousand (a reduction of euro 1,137 thousand) and cash and valuables on hand for euro 495 thousand.

Related party transactions, consisting of liquid assets on the current account, total euro 1,775 thousand and chiefly refer to Banca Intesa group companies.

ACCRUED INCOME AND PREPAID EXPENSES **euro 64,285 thousand**
(euro 43,760 thousand at December 31, 2003)

Accrued income and prepaid expenses increased by euro 20,525 thousand compared to December 31, 2003.

Accrued income totals euro 5,100 thousand (euro 1,858 thousand at December 31, 2003) and are mainly financial in nature.

Related party transactions total euro 5,064 thousand and principally refer to Telecom Italia S.p.A.

Prepaid expenses amount to euro 59,185 thousand (euro 41,902 thousand at December 31, 2003) and include euro 22,651 thousand referring to October line leases charged by Telecom Italia S.p.A., euro 21,464 thousand for the reversal of property lease advance payments and related shared expenses and euro 5,184 thousand for sponsorship expenses referring to the last quarter of the year.

Related party transactions amount to euro 25,799 thousand and principally refer to Telecom Italia S.p.A.

BALANCE SHEETS - LIABILITIES AND SHAREHOLDERS' EQUITY

SHAREHOLDERS' EQUITY **euro 8,898,815 thousand**
(euro 8,956,270 thousand at December 31, 2003)

Shareholders' equity decreased by euro 57,455 thousand compared to December 31, 2003.

The following table shows the individual components of Shareholders' equity and the relative changes during the period.

SHAREHOLDERS' EQUITY

		Changes during the period		
(in thousands of euro)	**Balance 12/31/2003**	**Appropriation of 2003 net income**	**Other changes**	**Balance 9/30/2004**
Share capital	513,964	—	—	513,964
Additional paid-in capital	5,525,626	—	—	5,525,626
Legal reserve	103,942	—	—	103,942
Reserve for treasury stock in portfolio	3,913	—	26	3,939
Other reserves:				
Reserve Law No. 342/2000, art. 14	303,827	—	—	303,827
Reserve for accelerated depreciation	—	103,414	46,586	150,000
Special reserve	113,579	17,944	(45,281)	86,242
Reserve for capital grants	14,681	—	—	14,681
Merger surplus reserve	53,783	—	—	53,783
Retained earnings	1,331	—	(1,331)	—
Net income	2,321,624	(2,321,624)	2,142,811	2,142,811
Total shareholders' equity	**8,956,270**	**(2,200,266)**	**2,142,811**	**8,898,815**

There were no changes in *share capital* during the period. Share capital amounts to euro 513,964,432.74 and consists of 8,434,004,716 ordinary shares and 132,069,163 savings shares, each with a par value of euro 0.06.

The *Reserve for treasury stock in portfolio* increased by euro 26 thousand, compared to December 31, 2003, following adjustment of the carrying value of treasury shares booked in Current assets; the *special reserve* also decreased by the same amount.

The *Reserve for accelerated depreciation* was set up, ex art. 67 paragraph 3 of D.P.R. No. 917/1986 (text prior to the changes set forth in Legislative Decree No. 344/2003), by an appropriation of 2003 profits for euro 103,414 thousand and by a transfer from the special reserve for euro 46,586 thousand, as voted by the Shareholders' Meeting which approved the 2003 financial statements. At the end of the year, the *Reserve for accelerated depreciation* will be reclassified to special reserve, not being necessary the separate indication in the balance sheet, in accordance to art. 109, paragraph 4, T.U.I.R., furthermore remaining the total tax suspension (as more highlighted in table of the restrictions of a tax nature regarding share capital and reserves).

The *Special reserve,* besides the changes described previously, increased by euro 17,944 thousand, being the difference between the maximum dividends voted on 2003 net income and the dividends actually paid to the shareholders. Such difference was caused by the failure to fully subscribe to the portion of the share capital increases available for subscription and the existence of treasury stock in portfolio. The special reserve also increased by euro 1,331 thousand as a result of the transfer of retained earnings appropriated in 2002, as voted by the Shareholders' Meeting which approved the 2003 financial statements.

Retained earnings decreased by euro 1,331 thousand as a result of previously described transfer to the Special reserve.

In order to complete disclosure on the amounts and the composition of Shareholders' equity, details of the nature of the individual equity reserves and the portions that are subject to restrictions for statutory purposes are described in the following table.

(in thousands of euro)	Balance 9/30/2004	Amount subject to restrictions	Amount not subject to restrictions
Capital reserves			
Additional paid-in capital	5,525,626	—	5,525,626
Legal reserve	103,942	102,793	1,149
Merger surplus reserve	53,783	—	53,783
Total capital reserves	**5,683,351**	**102,793**	**5,580,558**
Income reserves			
Reserve for treasury stock in portfolio	3,939	3,939	—
Reserve Law No. 342/2000, art. 14	303,827	444	303,383
Special reserve	86,242	79,515	6,727
Reserve for accelerated depreciation	150,000	—	150,000
Reserve for capital grants	14,681	—	14,681
Total income reserves	**558,689**	**83,898**	**474,791**
Total reserves in shareholders' equity	**6,242,040**	**186,691**	**6,055,349**

The entire amount of *additional paid-in capital* is available for distribution owing to the fact that the legal reserve is higher than one-fifth of share capital.

The *legal reserve* is available for an amount of euro 1,149 thousand, that is, for the amount which exceeds the amount restricted as per art. 2430 of the Italian Civil Code.

The *merger surplus reserve*, generated in 2002 following the merger of Blu S.p.A. in TIM, corresponds to the difference between the carrying value of the cancelled shares and the underlying share of net equity of the merged company. The entire amount is available for distribution.

The *reserve for treasury stock in portfolio* is not a distributable reserve, as provided by art. 2357-ter of the Italian Civil Code.

The *reserve Law No. 342/2000, art. 14 of* and the *special reserve* are not available for distribution in part (respectively, for euro 444 thousand and euro 78,567 thousand), given that these amounts have been set aside to guarantee the capital stated as the source of financing to fund specific investment programs under Law No. 488/92.

The special reserve is also unavailable for distribution – as per art. 2426 of the Italian Civil Code – for a further amount equal to the residual value of the start-up and expansion costs recorded in assets (euro 948 thousand).

Lastly, investment programs under Law No. 488/1992 are underway for a total of euro 139,500 thousand for which a request has been filed to obtain benefits; should the benefits in question be awarded, the Company is obliged to set up a guarantee with its own equity for a total amount of euro 103,015 thousand, as a result of which the *reserve for accelerated depreciation* will be restricted for the same amount, as voted by the Shareholders' Meeting for the approval of the financial statements.

Restrictions of a tax nature regarding share capital and reserves at September 30, 2004 are as follows:

(in thousands of euro)	Balance 9/30/2004	Amount liened for tax purposes
Share capital	**513,964**	**100,347**
Reserve Law No. 342/2000, art. 14	303,827	303,827
Reserve for accelerated depreciation	150,000	150,000
Reserve for capital grants	14,681	14,681
Total reserves	**468,508**	**468,508**
Total	**982,472**	**568,855**

The *reserve Law* No. 342/2000, art. 14, set up in 2001 to adjust the fiscal values of certain depreciable assets to the higher values shown in the financial statements is still covered by tax relief arrangements. As provided by law, the distribution of this reserve would be taxable to TIM.

The entire *reserve for capital grants* is covered by tax relief arrangements. This reserve was attributed prorated to TIM in 1995 at the time of the partial demerger of Telecom Italia to TIM.

Tax-deferred *share capital* amounts to euro 100,347 thousand and refers to the attribution of several inflation reserves to TIM dating back to the foregoing demerger.

As set forth in the new art. 109, paragraph 4, T.U.I.R., whenever, after a distribution of profits or reserves, the residual reserves in shareholders' equity (other than the legal reserve) are lower than the amount of the previously-mentioned adjustment of the UMTS license (equal to euro 150,460 thousand, net of the related reserve for deferred taxes), the difference distributed would be subject to taxation. In the same way, as already mentioned, the registered amount in the r*eserve for accelerated depreciation* is now submitted to the same suspension regime. At the end of the year the r*eserve for accelerated depreciation* will be reclassified to special reserve.

RESERVES FOR RISKS AND CHARGES **euro 1,305,649 thousand**
(euro 659,803 thousand at December 31, 2003)

Reserves for risks and charges increased by euro 645,846 thousand compared to December 31, 2003. The composition and changes in these reserves are summarized in the following table.

		Changes during the period					
(in thousands of euro)	**12/31/2003**	**Provisions**	**Utilizations**	**Released to income**	**Reclassifications/ Other changes**	**Total changes**	**9/30/2004**
For pensions and similar obligations							
For agents retirement indemnity......	1,676	—	—	—	—	—	1,676
	1,676	**—**	**—**	**—**	**—**	**—**	**1,676**
Reserve for taxes, reserve for deferred taxes							
Reserve for taxes..................	—	1,233,000	—	—	(550,826)	682,174	682,174
Reserve for deferred taxes...........	0	—	—	—	95,387	95,387	95,387
	0	**1,233,000**	**—**	**—**	**(455,439)**	**777,561**	**777,561**
Other reserves:							
Reserve for technological upgrading.......................	290,222	—	(131,205)	—	—	(131,205)	159,017
Reserve for regulatory framework expenses........................	114,191	3,675	—	—	—	3,675	117,866
Other reserves	253,714	2,345	(7,030)	—	500	(4,185)	249,529
	658,127	**6,020**	**(138,235)**	**—**	**500**	**(131,715)**	**526,412**
Total	**659,803**	**1,239,020**	**(138,235)**	**—**	**(454,939)**	**645,846**	**1,305,649**

• *Reserve for pensions and similar obligations* **euro 1,676 thousand**
(euro 1,676 thousand at December 31, 2003)

There were no changes during the period.

• *Reserve for taxes, reserve for deferred taxes* **euro 777,561 thousand**
(euro 0 thousand at December 31, 2003)

The reserves for taxes and for deferred taxes increased by euro 777,561 thousand compared to December 31, 2003.

The *reserve for taxes* includes the provision for income taxes referring to the first nine months of the year, net of taxes receivable from the Financial Administration for advances paid during the period and shown in the column *Other changes*.

The reserve for deferred taxes is recorded net of deferred tax assets of euro 51,993 thousand, described in the note on *Accounts receivable*. The gross amount of deferred tax liabilities principally refers to accelerated depreciation relating to the year 2003, recorded solely for tax purposes (euro 55,875 thousand), and the writeback of depreciation taken on the UMTS license up to December 31, 2003 (euro 91,242 thousand).

• *Other reserves* **euro 526,412 thousand**
(euro 658,127 thousand at December 31, 2003)

The *reserve for technological upgrading* totaling euro 159,017 thousand was utilized for euro 131,205 thousand during the period to cover depreciation on analog equipment and installations and other operating costs regarding TACS service, nonrecurring expenses relating to specific actions taken to shift the clientele to third-generation technology, as well as expenses to upgrade pre-existing network equipment and the implementation of the Edge platform.

The *reserve* for *regulatory framework expenses* (euro 117,866 thousand) includes the estimate of probable future charges relating to TIM's general obligations towards agencies and regulators in accordance with specific laws affecting the industry. A provision of euro 3,675 thousand was set aside during the period to free up frequencies (1800 MHz band) for the years 2003 and, prorata, 2004.

Sundry reserves also include the reserve for guarantees, the reserve for expenses connected with the sale of BLU (a reserve set up in the 2002 financial statements), the reserve for premium operations and prize contests and the reserve for employee reductions. Utilizations during the first nine months of the year mainly regard the reserve for premium operations and prize contests (euro 4,267 thousand). Movements due to other changes refer to the *reserve for corporate restructuring* as a result of the acquisition of the business segment from the company IT Telecom S.p.A. during the period and previously described in the note on *Fixed assets*. The remaining euro 39 thousand refers to the utilization of the reserve for litigation with employees.

RESERVE FOR EMPLOYEE TERMINATION INDEMNITIES **euro 104,196 thousand**
(euro 87,926 thousand at December 31, 2003)

The reserve for employee termination indemnities increased by euro 16,270 thousand, compared to December 31, 2003, and presented the following changes during the period:

(in thousands of euro)	
Balance at 12/31/2003	**87,926**
Changes during the period:	
Provisions charged to income for amounts to fund employee termination indemnities accrued in favor of employees during the year plus the fixed and variable cost-of-living adjustments required under Law No. 297/1982	16,195
Utilizations for:	
- Indemnities paid to employees who took retirement or resigned during the period	(1,843)
- advances pursuant to Law No. 297/1982	(1,228)
- pension funds	(4,522)
- substitute tax on the revaluation of the reserve C25	(16)
Total utilizations	*(7,609)*
Transfers to/from other Group companies and other changes	*7,684*
Balance as of 9/30/2004	**104,196**

LIABILITIES **euro 2,651,724 thousand**
(euro 3,824,878 thousand at December 31, 2003)

Liabilities decreased by euro 1,173,154 thousand compared to December 31, 2003. Details are as follows.

	9/30/2004			12/31/2003		
(in thousands of euro)	Financial	Trade and other accounts payable	Total	Financial	Trade and other accounts payable	Total
Due to banks	198	—	198	19	—	19
Due to other lenders	—	—	—	1,637	—	1,637
Trade accounts payable	—	1,626,258	1,626,258	—	1,888,242	1,888,242
Accounts payable to subsidiaries	—	2,689	2,689	—	655	655
Accounts payable to affiliated companies	—	3,369	3,369	—	3,536	3,536
Accounts payable to parent companies	—	403,471	403,471	—	398,448	398,448
Taxes payable	—	68,090	68,090	25,271	820,461	845,732
Contributions to pension and social security institutions	—	11,709	11,709	—	19,917	19,917
Other liabilities	—	535,940	535,940	—	666,692	666,692
Total	198	2,651,526	**2,651,724**	26,927	3,797,951	**3,824,878**

Due to banks are represented by bank overdrafts.

Due to other lenders at December 31, 2003 include a short-term loan due to IBM ITALIA Servizi Finanziari S.p.A. for the assignment of accounts payable for euro 1,637 thousand, the last installment of which was paid during the first half of the current year.

Trade accounts payable decreased by euro 261,984 thousand compared to December 31, 2003. A portion of this amount, equal to euro 273,576 thousand, refers to related party transactions, including those with IT Telecom S.p.A., Telecom Italia Sparkle S.p.A. and Telemedia Applicazioni S.p.A.

Accounts payable to subsidiaries and accounts payable to affiliated companies increased by euro 2,034 thousand and decreased by euro 167 thousand, respectively, compared to December 31, 2003. Such accounts payable refer mainly to liabilities arising from traffic effected by TIM users on the network of Group companies.

Accounts payable to parent companies increased by euro 5,023 thousand compared to December 31, 2003. Other accounts payable increased by euro 9,393 thousand and amount to euro 217,972 thousand. They primarily represent VAT payable (booked in this caption following use of the Group's VAT settlement system for euro 211,780 thousand). Trade accounts payable total euro 185,499 thousand and decreased by euro 4,370 thousand compared to December 31, 2003.

Taxes payable primarily represent the liability for the government concession tax on mobile radio utilities (euro 53,821 thousand).

Details of *other liabilities* are as follows:

(in thousands of euro)	9/30/2004	12/31/2003	Change
Customer-related items:			
advance payments on conversations	52,697	58,287	(5,590)
prepaid traffic	282,795	358,638	(75,843)
subscription charges invoiced and referring to subsequent periods	4,406	23,554	(19,148)
other	45,569	45,121	448
Total customer-related items	**385,467**	**485,600**	**(100,133)**
Employee-related items	**121,270**	**107,600**	**13,670**
Dividends payable to shareholders	**6,698**	**5,481**	**1,217**
Other	**22,505**	**68,011**	**(45,506)**
Total	**535,940**	**666,692**	**(130,752)**

Related party transactions regarding other liabilities amount to euro 1,072 thousand and entirely refer to those with IT Telecom S.p.A.

A breakdown of liabilities, accrued expenses and deferred income by maturity and type is presented at the end of these Notes in Annex 3.

ACCRUED EXPENSES AND DEFERRED INCOME **euro 18,854 thousand**
(euro 12,244 thousand at December 31, 2003)

Accrued expenses and deferred income increased by euro 6,610 thousand compared to December 31, 2003.

Accrued expenses amount to euro 327 thousand (euro 648 thousand at December 31, 2003) and almost entirely refer to production costs (euro 306 thousand).

Related party transactions regarding accrued expenses total euro 195 thousand and relate entirely to Telecom Italia S.p.A.

Deferred income totals euro 18,527 thousand (euro 11,596 thousand at December 31, 2003) and mainly includes grants for plant installations referring to future years (euro 6,467 thousand) and subscriber fees collected but referring to the month of October 2004 (euro 11,519 thousand).

MEMORANDUM ACCOUNTS

Memorandum accounts total euro 1,061,914 thousand and can be analyzed as follows:

(in thousands of euro)	9/30/2004	12/31/2003
Guarantees provided	1,060,927	1,166,181
Purchases and sales commitments	987	6,189
Total	**1,061,914**	**1,172,370**

Guarantees provided amount to euro 1,060,927 thousand and decreased by euro 105,254 thousand compared to December 31, 2003.

At the end of last year and following the actions taken to rationalize the guarantee structure within the Telecom Italia Group, TIM signed an Indemnity Agreement on behalf of Telecom Italia S.p.A. and Telecom Italia Finance S.A. for the guarantees issued by TIM International N.V. in the interests of its foreign subsidiaries. For the renewal and the re-negotiation of certain loan contracts during the first nine months of 2004 and which previously fell under the scope of the above Indemnity Agreement, TIM assumed the role of the ultimate guarantor for the Parent Company, replacing the Dutch subsidiary, for this purpose.

Guarantees provided are detailed as follows:

- euro 355,249 thousand on behalf of subsidiaries;
- euro 626,033 thousand on behalf of affiliated companies;
- euro 28,645 thousand on behalf of others for premium operations and prize contests sponsored by TIM S.p.A. and rental contracts;
- euro 51,000 thousand with respect to a surety policy issued by RAS S.p.A. on December 9, 2002 and counter-guaranteed by TIM S.p.A. on behalf of the Financial Administration – Revenue Service – VAT Office of Naples following the VAT refund request filed by Blu S.p.A. with these offices.

Purchases and sales commitments total euro 987 thousand and decreased by euro 5,202 thousand compared to the end of the prior year. They refer to scheduled future payments for the management of the equity investments that are currently part of the Saturn Venture Partners LLC closed-end investment fund.

The following should also be mentioned:

- third-party shares on deposit with the Company amount to euro 5,529 thousand and refer to TIM shares;
- accounts receivable sold as part of regular factoring transactions – which exceeded the limits prefixed by the counterpart – amount to approximately euro 38 million;
- in 2001, TIM issued letters of patronage on behalf of its subsidiaries to financial companies and suppliers, mainly for investments to be made in future years. TIM, under these letters of patronage, guarantees financial support to its indirect subsidiaries should they fail to meet commitments with their own resources.

As the sponsor of the credit facility disbursed to Digitel, TIM S.p.A. signed the following:

- a “Sponsor Contingent Capital Contribution Agreement”. At September 30, 2004, this agreement calls for TIM S.p.A.’s commitment, through TIM International N.V., to increase share capital or make subordinated loans equal to any EBITDA loss resulting from six-month reports prepared for this purpose compared to a parameter-based business plan in the event that a pre-established “debt/ contributed equity” ratio arises at the same time;
- a “Performance Support Conditional Guarantee Agreement”. This agreement calls for TIM S.p.A.’s commitment to guarantee to service Digitel’s debt in the event of a significant EBITDA loss (in excess of 20%);

- a guarantee to lenders in the event of bankruptcy filed by third parties, for a period of four years from the closing date, which will cease after this time only if Digitel's debt/EBITDA ratio is less than or equal to 2.5 to 1.TIM's maximum overall commitment can be estimated at USD 222 million, plus any interest and accessory charges (reduced by the guarantees already provided in the Performance Support Conditional Guarantee).

  TIM S.p.A.'s direct estimated commitment is significantly lower than the maximum theoretical amount, considering that Digitel has infragroup lines of credit for about USD 115 million million that help reduce the risk of bankruptcy and there are mechanisms in place that limit TIM's intervention, as provided by the Sponsor Contingent Capital Contribution Agreement. Given the current difficulty in determining this commitment, no memorandum account has been recorded;
- Company assets held by third parties total euro 5,817 thousand;
- the Company received third-party guarantees amounting to euro 176,263 thousand and collateral totaling euro 4,135 thousand.

* * *

With reference to the operations off-balance sheet, at September 30, 2004 turn on in being three Currency Forward contracts for the amount of USD 12,000 thousand (euro 9,795 thousand) with expiry date as of December 31,2004.

* * *

Tax audit on BLU incorporated company is running. At the moment, significant reliefs have not emerged.

STATEMENTS OF INCOME

PRODUCTION VALUE **euro 7,430,228 thousand**
(euro 7,001,919 thousand for the first nine months of 2003)

Production value includes the following:

SALES AND SERVICE REVENUES **euro 7,381,031 thousand**
(euro 6,979,951 thousand for the first nine months of 2003)

A breakdown of sales and service revenues is set out in the table below.

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Sales			
Telephone products and accessories	351,204	267,967	83,237
Services			
Traffic revenues			
- outgoing traffic	3,201,256	3,182,064	19,192
- incoming traffic	1,688,253	1,670,428	17,825
- roaming traffic	532,918	485,973	46,945
Value-added service revenues	927,331	742,681	184,650
Subscription charges, maintenance and rentals	99,995	121,169	(21,174)
Fees to activate service and takeovers	7,880	10,429	(2,549)
Prepaid service recharges	470,534	417,065	53,469
Other revenues			
- revenues from other operators	10,272	12,239	(1,967)
- other miscellaneous income	91,388	69,936	21,452
Total service revenues	**7,029,827**	**6,711,984**	**317,843**
Sales and service revenues	**7,381,031**	**6,979,951**	**401,080**

A breakdown of revenues by geographical area is set out in the table below.

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Italy	**6,647,385**	**6,288,626**	**358,759**
Rest of Europe	**503,718**	**484,772**	**18,946**
North America	**24,608**	**22,820**	**1,788**
Rest of the world:			
South America	43,845	33,529	10,316
Africa	64,623	57,474	7,149
Asia	56,025	54,000	2,025
Oceania	40,827	38,730	2,097
Total Rest of the world	**205,320**	**183,733**	**21,587**
	7,381,031	**6,979,951**	**401,080**

The amounts for "Europe", "North America", and "Other countries" are almost entirely attributable to revenues generated by traffic outgoing from or incoming to those geographical regions.

Service revenues (representing 95.2% of total revenues) grew by 4.7%. The main sources of revenues are those connected with traffic and Added-Value Services, totaling 86% of revenues overall.

Traffic income increased by 1.6% compared to the corresponding period of 2003 whereas Value-added Services revenues rose by 24.9%; Short Message Services (outgoing from and incoming to the TIM network) account for the most important components of revenues.

Revenues generated by related party transactions total euro 856,898 thousand, chiefly with Telecom Italia S.p.A. and Telecom Italia Sparkle S.p.A.

INCREASES IN CAPITALIZED INTERNAL CONSTRUCTION COSTS **euro 26,095 thousand**
(euro - for the first nine months of 2003)

Following the reorganization of activities in the Information Technology sector – mainly as a result of the previously-mentioned acquisition of a business segment from IT Telecom S.p.A. – part of the IT activities carried out internally by the Company have been capitalized starting from the current year.

OTHER REVENUES AND INCOME **euro 23,102 thousand**
(euro 21,968 thousand for the first nine months of 2003)

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Operating grants	203	28	175
Grants for plant installations	1,030	945	85
Other:			
Expense reimbursements	6,918	7,088	(170)
Late payment fees	1,050	4,903	(3,853)
Gains on the sale/transfer of fixed assets	1,483	703	780
Sundry	12,418	8,301	4,117
Total other	*21,869*	*20,995*	*874*
Total	**23,102**	**21,968**	**1,134**

Operating grants refer to projects funded by the European Commission under the Fifth Framework Program.

Grants for plant installations include the grants referring to the period on projects funded by Law No. 488/1992 (euro 1,000 thousand), Law No. 341/1995 (euro 5 thousand) and the Ascoli Piceno Territorial Agreement (euro 25 thousand).

Expense reimbursements mainly refer to reimbursements for costs pertaining to personnel (euro 2,670 thousand) and recoveries for guarantees on radio mobile equipment (euro 1,922 thousand).

Revenues generated by related party transactions total euro 2,617 thousand, mainly with AVEA I.H.A.S.

PRODUCTION COSTS **euro 4,229,299 thousand**
(euro 4,032,590 thousand for the first nine months of 2003)

RAW MATERIALS, SUPPLIES AND MERCHANDISE **euro 466,464 thousand**
(euro 382,856 thousand for the first nine months of 2003)

Raw materials, supplies and merchandise increased by euro 83,608 thousand compared to the corresponding period of 2003. They mainly include purchases of mobile communications equipment and related accessories and, to a lesser extent, other goods necessary for company operations.

SERVICES **euro 2,171,115 thousand**
(euro 2,061,244 thousand for the first nine months of 2003)

Services increased by euro 109,871 thousand compared to the first nine months of 2003. Details are as follows:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Amounts due to other operators	1,176,761	1,119,522	57,239
Marketing and advertising services	451,088	433,895	17,193
Professional and other fees	139,917	133,496	6,421
Administrative and general services	105,248	89,891	15,357
Management of buildings and plant	95,455	90,755	4,700
Data processing	55,916	50,819	5,097
Maintenance costs	47,329	41,342	5,987
Studies and research	37,292	35,239	2,053
Employee-related expenses	34,535	28,423	6,112
Telecommunications	27,574	37,862	(10,288)
Total	**2,171,115**	**2,061,244**	**109,871**

Services include euro 428,618 thousand of costs for the purchase of services from related parties, specifically Telecom Italia S.p.A. and Telecom Italia Sparkle S.p.A.

USE OF PROPERTY NOT OWNED **euro 371,087 thousand**
(euro 403,774 thousand for the first nine months of 2003)

Costs for use of property not owned decreased by euro 32,687 thousand compared to the first nine months of 2003.

These costs refer to rental, hire and leasing expenses for the period. They comprise, besides property rentals (euro 140,904 thousand), the hire of equipment (euro 23,046 thousand), leasing payments (euro 2,737 thousand) and line lease costs connected with the use of direct connections and accesses to the wireline network of Telecom Italia S.p.A. (euro 204,400 thousand).

Costs generated by related party transactions amount to euro 230,078 thousand and mainly refer to transactions with Telecom Italia S.p.A.

Details are as follows:

(in thousands of euro)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Rentals	345,304	375,338	(30,034)
Hires	23,046	22,386	660
Lease installments	2,737	6,050	(3,313)
Other	—	—	—
Total	**371,087**	**403,774**	(32,687)

PERSONNEL COSTS **euro 344,227 thousand**
(euro 330,846 thousand for the first nine months of 2003)

The average equivalent number of employees at September 30, 2004 is 9,310.

The breakdown of employees by professional category is shown in the following table:

(average equivalent number)	9 months to 9/30/2004	9 months to 9/30/2003	Change
Executives	230	223	7
Middle management	563	446	117
Office staff	8,501	8,508	(7)
Workers	16	20	(4)
Total	**9,310**	**9,197**	**113**

AMORTIZATION, DEPRECIATION AND WRITEDOWNS **euro 863,474 thousand**
(euro 820,101 thousand for the first nine months of 2003)

Amortization of intangible assets **euro 371,950 thousand**
(euro 301,936 thousand for the first nine months of 2003)

Additional details on the components of this caption are presented in the note on *Intangible Assets*.

Depreciation of fixed assets **euro 461,648 thousand**
(euro 486,045 thousand for the first nine months of 2003)

A portion of the depreciation expense on the plants used for the TACS services for the first nine months of 2004, totaling euro 7,414 thousand, was taken from the Reserve for technological upgrading. Euro 21,998 thousand of the reserve was also used to cover the residual depreciation in respect of a part of the network equipment not compatible with the Edge platform that was removed from the production plan.

Additional details on the components of this caption are presented in the note on *Fixed Assets.*

CATEGORIES OF ASSETS GROUPED ACCORDING TO CORRESPONDING ASSET ITEMS

	(Rate %)
Buildings	6 - 10
Plant and machinery	8 - 20
Industrial and distribution equipment	25
Other fixed assets	12 - 25

Writedowns of receivables, included in current assets and liquid assets **euro 29,876 thousand**
(euro 32,120 thousand for the first nine months of 2003)

This amount refers to provisions to the Allowance for doubtful accounts for trade accounts receivable from customers and is calculated so as to adjust these receivables to estimated realizable value.

CHANGES IN INVENTORIES OF RAW MATERIALS, SUPPLIES AND MERCHANDISE **- euro 17,787 thousand**
(- euro 1,261 thousand for the first nine months of 2003)

The changes refer mainly to mobile radio transmission equipment and accessories.

OTHER PROVISIONS **euro 2,738 thousand**
(euro 11,054 thousand for the first nine months of 2003)

Other provisions refer to amounts set aside in the Reserve for premium operations and prize contests (euro 1,163 thousand) and the Reserve for regulatory framework expenses (euro 1,575 thousand).

With regard to the Reserve for regulatory framework expenses, the total provision set aside in the reserve during the period for the expenses to free up the frequencies amount to euro 3,675 thousand, of which euro 1,575 thousand relates to the portion for the first nine months of 2004 and euro 2,100 thousand to the portion for the year 2003 which was not booked in the relevant financial statements since the amount could not be estimated at the date of their preparation. The portion relating to 2003 was recorded in *Extraordinary expense*.

MISCELLANEOUS OPERATING COSTS **euro 27,981 thousand**
(euro 23,976 thousand for the first nine months of 2003)

(in thousands of euro)	**9 months to 9/30/2004**	**9 months to 9/30/2003**	**Change**
Losses on sales/writeoffs/transfers of fixed assets	387	1,130	(743)
TLC operating fee	2,558	3,814	(1,256)
Other sundry costs:			
Universal Service	8,766	9,273	(507)
Other taxes and duties	7,965	5,420	2,545
Association dues	2,169	1,636	533
Other costs	6,136	2,703	3,433
Total other sundry costs	25,036	19,032	6,004
Total	27,981	23,976	4,005

TLC operating fees, totaling euro 2,558 thousand, include the estimate of the fee for the operation of the regulatory body (M.D. dated July 16, 1999) and the portion referring to the annual fees established by Legislative Decree No. 259 dated August 1, 2003 for the first nine months of 2004.

Costs generated by related party transactions total euro 298 thousand and mainly refer to Telecom Italia S.p.A.

FINANCIAL INCOME AND EXPENSE **euro 24,834 thousand**
(- euro 218 thousand for the first nine months of 2003)

Financial income and expense increased overall by euro 25,052 thousand compared to the first nine months of 2003. Details are as follows:

(in thousands of euro)		9 months to 9/30/2004	9 months to 9/30/2003	Change
Other financial income	(A)	30,818	10,744	20,074
Interest and other financial expense	(B)	(5,823)	(14,121)	8,298
Foreign exchange gains and losses	(C)	(161)	3,159	(3,320)
Total	**(A+B+C)**	**24,834**	**(218)**	**25,052**

Other financial income includes the following:

(in thousands of euro)	9 months to 9/30/2004			9 months to 9/30/2003	Change
	Included in long-term investments	Included in current assets	Total		
Other financial income from accounts receivable from others	194	—	194	246	(52)
Other financial income from securities, other than equity investments	4	—	4	77	(73)
Other income:					
- interest and fees from parent companies	—	29,714	29,714	8,069	21,645
- interest and fees from subsidiaries	—	351	351	—	351
- interest and fees from others and miscellaneous income	—	555	555	2,352	(1,797)
Total other income	*—*	*30,620*	*30,620*	*10,421*	*20,199*
Total	**198**	**30,620**	**30,818**	**10,744**	**20,074**

Other financial income from accounts receivable included in long-term investments from others of euro 194 thousand refers in interest earned on loans granted to personnel.

Other financial income from securities, other than equity investments, included in long-term investments refers to interest earned during the period on government securities which fell due during the period.

Interest and fees from parent companies consist mainly of interest earned on the current account with Telecom Italia S.p.A.

Interest and other financial expense include the following:

(in thousands of euro)	1.1 - 30.9.2004			1.1 - 30.9.2003	Change
	Medium/long-term debt	Short-term borrowings	Total		
Interest and fees paid to subsidiaries	—	—	—	1,623	(1,623)
Interest and fees paid to parent companies	—	1,346	1,346	5,326	(3,980)
Interest and fees paid to others and miscellaneous expenses	—	4,477	4,477	7,172	(2,695)
Total	**—**	**5,823**	**5,823**	**14,121**	**(8,298)**

Interest and fees paid to others and miscellaneous expenses include, among other things, expenses connected with the payment of taxes on an installment basis and discounts for spot-cash payments.

Foreign exchange gains amount to euro 1,137 thousand; *foreign exchange losses* total euro 1,298 thousand.

The possible net profit on evaluation changes will be object, in the financial statements of the year, of a provision in a specific not available equity reserve until its realization.

VALUE ADJUSTMENTS TO FINANCIAL ASSETS **euro 57 thousand**
(- euro 6,676 thousand for the first nine months of 2003)

Value adjustments to financial assets include:

- euro 26 thousand for the upward adjustment of treasury stock booked in current assets;
- euro 31 thousand for the writeback of the carrying value of the investment in the affiliated company Edotel S.p.A.

EXTRAORDINARY INCOME AND EXPENSE **euro 149,991 thousand**
(euro 118,925 thousand for the first nine months of 2003)

Extraordinary income amounts to euro 251,141 thousand (euro 622,885 thousand for the first nine months of 2003). It mainly refers to income from the elimination of tax interference (prior period fiscal amortization of the UMTS license) for euro 241,702 thousand.

Extraordinary expense amounts to euro 101,150 thousand (euro 503,960 thousand for the first nine months of 2003).

The most important item refers to *prior years' taxes* for a total of euro 92,413 thousand; this caption includes the effect of the elimination of tax interference (euro 91,242 thousand) for the cancellation of the prior period amortization of the UMTS license.

Extraordinary expense also includes euro 2,100 thousand relating to the provision for the year 2003 to the Reserve for regulatory framework expenses and euro 750 thousand for the provision to the Reserve for employee reductions. Expenses regarding the portion of principal and interest connected with Law No. 58/1992 amount to euro 914 thousand.

Costs arising from transactions with related parties total euro 1,522 thousand and refer entirely to Telecom Italia S.p.A.

INCOME TAXES, CURRENT AND DEFERRED **euro 1,233,000 thousand**
(euro 1,235,000 thousand for the first nine months of 2003)

Current taxes and deferred taxes refer to the first nine months of 2004 and have been calculated by applying the tax rate for the period to the pretax profit.

OTHER INFORMATION

ANNEX 1

EQUITY INVESTMENTS IN LONG-TERM INVESTMENTS AT 12/31/2003

(in thousands of euros)	Cost	Upward adjustments	Writedowns	Carrying value
TIM International N.V.	8,066,877	—	(4,102,000)	3,964,877
Total subsidiaries	**8,066,877**	**—**	**(4,102,000)**	**3,964,877**
Equity investments in affiliated companies				
Iridium Italia S.p.A.	904	—	(904)	—
Edotel S.p.A.	6,038	—	(4,610)	1,428
Cons. Scuola Superiore Alta Formaz. Univ. Federico II.	26	—	—	26
Consorzio Energia Gruppo Telecom Italia	5	—	—	5
Telenergia S.r.l.	10	—	—	10
Total affiliated companies	**6,983**	**—**	**(5,514)**	**1,469**
Equity investments in other companies				
Telecom Italia Audit S.c.r.l.	500	—	—	500
Conai - Consorzio Nazionale Imballaggi	1	—	—	1
Consorzio Cefriel	33	—	—	33
Idroenergia s.c.r.l.	1	—	—	1
ABI Lab	1	—	—	1
Shared Service Center S.c.r.l.	—	—	—	—
Total other companies	**536**	**—**	**—**	**536**
Advances on future capital contributions				
TIM International N.V.	120,460	—	—	120,460
Edotel S.p.A.	480	—	—	480
Total advances on future capital contributions	**120,940**	**—**	**—**	**120,940**

	CHANGES DURING THE PERIOD				
	Purchases/ Subscriptions	Reclassification/ Sales	Writedowns/ Writebacks	Capital replenishments	Total changes
Equity investments in subsidiaries					
TIM International N.V.	—	297,860	—	—	297,860
Total subsidiaries	**—**	**297,860**	**—**	**—**	**297,860**
Equity investments in affiliated companies					
Iridium Italia S.p.A.	—	—	—	—	—
Edotel S.p.A	—	(1,459)	31	—	(1,428)
Cons. Scuola Superiore Alta Formaz. Univ. Federico II	—	—	—	—	—
Consorzio Energia Gruppo Telecom Italia	—	—	—	—	—
Telenergia S.r.l..	—	—	—	—	—
Total affiliated companies	**—**	**(1,459)**	**31**	**—**	**(1,428)**
Equity investments in other companies					
Telecom Italia Audit S.c.r.l.	—	—	—	—	—
Conai - Consorzio Nazionale Imballaggi	—	—	—	—	—
Consorzio Cefriel	—	—	—	—	—
Idroenergia s.c.r.l..	—	—	—	—	—
ABI Lab	—	—	—	—	—
Shared Service Center S.c.r.l..	65	—	—	—	65
Total other companies	**65**	**—**	**—**	**—**	**65**
Advances on future capital contributions					
TIM International N.V.	496,943	(297,860)	—	—	199,083
Edotel S.p.A.	—	(480)	—	—	(480)
Total advances on future capital contributions	**496,943**	**(298,340)**	**—**	**—**	**198,603**

EQUITY INVESTMENTS IN LONG-TERM INVESTMENTS AT 9/30/2004

	Cost	Upward adjustments	Writedowns	Carrying value
Equity investments in subsidiaries				
TIM International N.V.	8,364,737	—	(4,102,000)	4,262,737
Total subsidiaries	**8,364,737**	**—**	**(4,102,000)**	**4,262,737**
Equity investments in affiliated companies				
Iridium Italia S.p.A.	904	—	(904)	—
Edotel S.p.A.	4,579	—	(4,579)	—
Cons. Scuola Superiore Alta Formaz. Univ. Federico II.	26	—	—	26
Consorzio Energia Gruppo Telecom Italia	5	—	—	5
Telenergia S.r.l.	10	—	—	10
Total affiliated companies	**5,524**	**—**	**(5,483)**	**41**
Equity investments in other companies				
Telecom Italia Audit S.c.r.l.	500	—	—	500
Conai - Consorzio Nazionale Imballaggi	1	—	—	1
Consorzio Cefriel	33	—	—	33
Idroenergia s.c.r.l.	1	—	—	1
ABI Lab	1	—	—	1
Shared Service Center S.c.r.l.	65	—	—	65
Total other companies	**601**	**—**	**—**	**601**
Advances on future capital contributions				
TIM International N.V.	319,543	—	—	319,543
Edotel S.p.A.	—	—	—	—
Total advances on future capital contributions	**319,543**	**—**	**—**	**319,543**

ANNEX 2

ACCOUNTS RECEIVABLE, ACCRUED INCOME AND PREPAID EXPENSES BY MATURITY AND TYPE

(in thousands of euros)	9/30/2004 Amounts due (*)				12/31/2003 Amounts due (**)			
	Within one year	From two to five years	Beyond five years	Total	Within one year	From two to five years	Beyond five years	Total
Accounts receivables in long-term investments								
From others								
employees	1,945	5,593	13,692	21,230	825	4,749	11,253	16,827
miscellaneous	781	101	—	882	854	—	—	854
Total accounts receivables in long-term investments	**2,726**	**5,694**	**13,692**	**22,112**	**1,679**	**4,749**	**11,253**	**17,681**
Accounts receivable in current assets								
Other financial receivables from								
parent companies	497,870	—	—	497,870	1,440,461	—	—	1,440,461
subsidiaries	166			166	—	—	—	—
affiliated companies	66	—	—	66	66	—	—	66
	498,102	**—**	**—**	**498,102**	**1,440,527**	**—**	**—**	**1,440,527**
Trade accounts receivable from								
customers	1,058,487	—	—	1,058,487	1,082,551	—	—	1,082,551
parent companies	174,207	—	—	174,207	208,557	—	—	208,557
subsidiaries	31,377	—	—	31,377	22,457	—	—	22,457
affiliated companies	141	—	—	141	141	—	—	141
others	803	—	—	803	2,415	—	—	2,415
	1,265,015	**—**	**—**	**1,265,015**	**1,316,121**	**—**	**—**	**1,316,121**
Other accounts receivable from								
parent companies	1,657	—	—	1,657	2,461	—	—	2,461
subsidiaries	9,715	—	—	9,715	9,580	—	—	9,580
affiliated companies	1,445	—	—	1,445	27	—	—	27
others	871,051	246,920	235,568	1,353,539	931,530	609,009	—	1,540,539
	883,868	**246,920**	**235,568**	**1,366,356**	**943,598**	**609,009**	**—**	**1,552,607**
Total accounts receivable in current assets	**2,646,985**	**246,920**	**235,568**	**3,129,473**	**3,700,246**	**609,009**	**—**	**4,309,255**
Accrued income and prepaid expenses								
Accrued income								
financial	5,064	—	—	5,064	1,822	—	—	1,822
Trade	36	—	—	36	36	—	—	36
Prepaid expenses								
financial	—	—	—	—	295	—	—	295
trade	56,540	2,645	—	59,185	41,607	—	—	41,607
Total accrued income and prepaid expenses	**61,640**	**2,645**	**—**	**64,285**	**43,760**	**—**	**—**	**43,760**

(*) All periods subsequent to 9/30/2004.

(**) All periods subsequent to 12/31/2003.

ANNEX 3

LIABILITIES, ACCRUED EXPENSES AND DEFERRED INCOME BY MATURITY AND TYPE

	9/30/2004 Amounts due (*)				12/31/2003 Amounts due (**)			
(in thousands of euros)	Within one year	From two to five years	Beyond five years	Total	Within one year	From two to five years	Beyond five years	Total
Short-term borrowings								
Due to banks	198	—	—	198	19	—	—	19
Due to other lenders	—	—	—	—	1,637	—	—	1,637
Taxes payable	—	—	—	—	25,271	—	—	25,271
	198	**—**	**—**	**198**	**26,927**	**—**	**—**	**26,927**
Trade accounts payable								
Accounts payable to suppliers	1,626,258	—	—	1,626,258	1,888,242	—	—	1,888,242
Accounts payable to subsidiaries	2,601	—	—	2,601	567	—	—	567
Accounts payable to affiliated companies	2,736	—	—	2,736	2,903	—	—	2,903
Accounts payable to parent companies	185,499	—	—	185,499	189,869	—	—	189,869
	1,817,094	**—**	**—**	**1,817,094**	**2,081,581**	**—**	**—**	**2,081,581**
Other payables								
Accounts payable to subsidiaries	88	—	—	88	88	—	—	88
Accounts payable to affiliated companies	633	—	—	633	633	—	—	633
Accounts payable to parent companies	217,972	—	—	217,972	208,579	—	—	208,579
Taxes payable	68,090	—	—	68,090	820,461	—	—	820,461
Contributions to pension and social security institutions	10,426	1,200	83	11,709	18,642	1,196	79	19,917
Other liabilities	535,940	—	—	535,940	666,692	—	—	666,692
	833,149	**1,200**	**83**	**834,432**	**1,715,095**	**1,196**	**79**	**1,716,370**
Total liabilities	**2,650,441**	**1,200**	**83**	**2,651,724**	**3,823,603**	**1,196**	**79**	**3,824,878**
Accrued expenses and deferred income								
Accrued expenses								
Financial	21	—	—	21	212	—	—	212
Trade	306	—	—	306	436	—	—	436
Other	—	—	—	—	—	—	—	—
Deferred income								
Financial	541	—	—	541	513	—	—	513
Trade	11,847	4,289	1,850	17,986	4,944	4,289	1,850	11,083
Total accrued expenses and deferred income	**12,715**	**4,289**	**1,850**	**18,854**	**6,105**	**4,289**	**1,850**	**12,244**

(*) *All periods subsequent to 9/30/2004.*

(**) *All periods subsequent to 12/31/2003.*

ANNEX 4

ACCOUNTS RECEIVABLE, LIABILITIES AND REVENUES BY GEOGRAPHICAL AREA

(in thousands of euros)	Italy	Other EU countries	Rest of Europe	North America	Central and South America	Other areas	TOTAL
Accounts receivable in long-term investments							
. subsidiaries	—	—	—	—	—	—	—
. affiliated companies	—	—	—	—	—	—	**—**
. others	22,112	—	—	—	—	—	**22,112**
Total	**22,112**	**—**	**—**	**—**	**—**	**—**	**22,112**
Accounts receivable in current assets							
. customers	1,090,728	41,306	16,120	16,261	14,362	10,710	**1,189,487**
. subsidiaries	—	26,098	—	—	15,160	—	**41,258**
. affiliated companies	233	—	1,463	—	—	—	**1,696**
. taxes receivable	8,981	—	—	—	—	—	**8,981**
. deferred tax assets	992,537	—	—	—	—	—	**992,537**
. others	352,824	—	—	—	—	—	**352,824**
Total	**2,445,303**	**67,404**	**17,583**	**16,261**	**29,522**	**10,710**	**2,586,783**
LIABILITIES							
. Debentures	—	—	—	—	—	—	**—**
. Convertible debentures	—	—	—	—	—	—	**—**
. Due to banks	198	—	—	—	—	—	**198**
. Due to other lenders	—	—	—	—	—	—	**—**
. Advances	—	—	—	—	—	—	**—**
. Accounts payable to suppliers	1,324,323	96,378	2,686	7,989	1,347	9,965	**1,442,688**
. Accounts payable to subsidiaries	—	2,251	—	—	438	—	**2,689**
. Accounts payable to affiliated companies	—	3,100	269	—	—	—	**3,369**
. Taxes payable	68,090	—	—	—	—	—	**68,090**
. Contributions to pension and social security institutions	11,709	—	—	—	—	—	**11,709**
. Other liabilities	535,940	—	—	—	—	—	**535,940**
Total	**1,940,260**	**101,729**	**2,955**	**7,989**	**1,785**	**9,965**	**2,064,683**
SALES AND SERVICE REVENUES	**6,647,385**	**355,217**	**148,501**	**24,608**	**43,845**	**161,475**	**7,381,031**

ANNEX 5

STATEMENTS OF CASH FLOWS

(in thousands of euro)			9 months to 9/30/2004	9 months to 9/30/2003
A.	**NET FINANCIAL LIQUIDITY (INDEBTEDNESS), AT BEGINNING OF PERIOD**		**1,418,350**	**(1,491,660)**
	Operating income		3,200,929	2,969,329
	Depreciation of fixed assets and amortization of intangible assets		833,598	787,981
	Investments in fixed assets and intangible assets		(704,869)	(473,734)
	Proceeds from disposal of intangible assets and fixed assets		1,572	30,521
	Change in operating working capital and other changes		(293,147)	94,528
B.	**FREE CASH FLOWS FROM OPERATIONS**		**3,038,083**	**3,408,625**
	Investments in long-term investments(1)		(504,860)	(235,049)
	Proceeds from sale/redemption value of other intangible assets, fixed assets and long-term investments		7,761	2,436
	Change in non-operating working capital and other changes(2)		(1,254,259)	(198,831)
C.			**(1,751,358)**	**(431,444)**
D.	**NET CASH FLOWS BEFORE DISTRIBUTION OF INCOME/RESERVES AND CONTRIBUTIONS BY SHAREHOLDERS**	**(B+C)**	**1,286,725**	**2,977,181**
E.	**DISTRIBUTION OF INCOME/RESERVES**		**(2,200,265)**	**(410,144)**
F.	**CONTRIBUTIONS BY SHAREHOLDERS**			
G.	**CHANGE IN NET FINANCIAL LIQUIDITY (INDEBTEDNESS)**	**(D+E+F)**	**(913,540)**	**2,567,037**
H.	**NET FINANCIAL LIQUIDITY (INDEBTEDNESS), AT END OF PERIOD**	**(A+G)**	**504,810**	**1,075,377**

Note:
The value of the investments of the first nine months of 2004 is exposed net of company branches acquisitions/ assignments effects.