TELECOM ITALIA S P A
Form 20-F
April 16, 2013
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 20-F

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

x **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the fiscal year ended: December 31, 2012

OR

¨ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**
For the transition period from N/A to N/A

OR

¨ **SHELL COMPANY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

Date of event requiring this shell company report

Commission file number 1-13882

Telecom Italia S.p.A.

(Exact name of Registrant as specified in its charter)

Italy

(Jurisdiction of incorporation or organization)

Piazza degli Affari 2, 20123 Milan, Italy

(Address of principal executive offices)

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(Name, Telephone, E-mail and/or Facsimile number and Address of Company Contact Person)

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

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

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

None

(Title of Class)

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

None

(Title of Class)

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock

as of the close of the period covered by the annual report.

Ordinary Shares 13,254,622,987

Savings Shares 6,026,120,661

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act Yes x No ¨

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934. Yes ¨ No x

Note Checking the box above will not relieve any registrant required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934 from their obligations under those Sections.

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ¨ No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer ¨ Non-accelerated filer ¨

Indicate by check mark which basis of accounting the registrant has used to prepare the financial statement included in this filing:

U.S. GAAP ¨ International Financial Reporting Standards as issued by the International Accounting Standards Board x Other ¨

If Other has been checked in response to the previous question indicate by check mark which financial statement item the registrant has elected to follow Item 17 ¨ Item 18 ¨

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

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

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INTRODUCTION

Telecom Italia S.p.A. is incorporated as a joint stock company under the laws of Italy. As used in this Annual Report, unless the context otherwise requires, the term Company means Telecom Italia S.p.A. the operating company for fixed and mobile telecommunications services in Italy and the holding company for various businesses, principally telecommunications, and the terms we , us and our refers to the Company, and, as applicable, the Company and its consolidated subsidiaries.

Unless otherwise indicated, the financial information contained in this Annual Report has been prepared in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board (designated as **IFRS**).

Unless otherwise indicated, any reference in this Annual Report to Consolidated Financial Statements is to the Consolidated Financial Statements for the year ended December 31, 2012 of the Telecom Italia Group (including the notes thereto) included elsewhere herein.

Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995.

The Private Securities Litigation Reform Act of 1995 provides a safe harbor for forward-looking statements. This Annual Report contains certain forward-looking statements.

Forward-looking statements are statements that are not historical facts and can be identified by the use of forward-looking terminology such as believes, may, is expected to, will, will continue, should, seeks or anticipates or similar expressions or the negative thereof or oth terminology, or by the forward-looking nature of discussions of strategy, plans or intentions.

The forward-looking statements in this Annual Report include, but are not limited to, the discussion of the changing dynamics of the telecommunications marketplace, including the continuing developments in competition in all aspects of our businesses from new competitors and from new and enhanced technologies, our outlook for growth in the telecommunications industry both within and outside of Italy, including our outlook regarding developments in the telecommunications industry, and certain trends we have identified in our core markets, including regulatory developments.

Such statements include, but are not limited to, statements under the following headings: (i) Item 3. Key Information 3.1 Risk Factors , (ii) Item 4. Information on the Telecom Italia Group 4.1 Business 4.1.7 Updated Strategy , (iii) Item 4. Information on the Telecom Italia Group 4.3 Regulation , (iv) Item 5. Operating and Financial Review and Prospects , (v) Item 8. Financial Information 8.2 Legal Proceedings and (vi) Item 11 Quantitative and Qualitative Disclosures About Market Risks , including statements regarding the likely effect of matters discussed therein.

Actual results may differ materially from those projected or implied in the forward-looking statements. Such forward-looking information is based on certain key assumptions which we believe to be reasonable but forward-looking information by its nature involves risks and uncertainties, which are outside our control, that could significantly affect expected results.

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

- our ability to successfully implement our strategy over the 2013-2015 period;

- our ability to successfully achieve our debt reduction and other targets;

- the increasing competition from global and local OTT (Over The Top) players (operators offering contents and services on the internet without owning its own proprietary telecommunications network infrastructure);

- the continuing impact of increased competition in our markets, including competition from established domestic competitors and global and regional alliances formed by other telecommunications operators in our core Italian domestic fixed-line and wireless markets and our other principal markets;

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- the continuing effects of the global economic crisis in the principal markets in which we operate, including, in particular, our core Italian market;
- our ability to introduce new services to stimulate increased usage of our fixed and wireless networks to offset declines in the traditional voice business mainly due to the continuing impact of regulatory required price reductions, market share loss and pricing pressures generally;
- our ability to successfully implement our internet and broadband strategy;
- the impact of regulatory decisions and changes in the regulatory environment in Italy and other countries in which we operate, including recent changes to allowable charges for data and voice roaming;
- the impact of economic development generally on our international business and on our foreign investments and capital expenditures;
- as our services are technology-intensive, our ability to develop new technologies in order to avoid our services becoming non-competitive;
- the impact of political developments in Italy and other countries in which we operate;
- the impact of fluctuations in currency exchange and interest rates;
- our ability to build up our business in adjacent markets and in international markets (particularly in Brazil and Argentina), due to our specialist and technical resources;
- our ability to achieve the expected return on the investments and capital expenditures we have made and continue to make (such as those in Brazil and Argentina);
- the amount and timing of any future impairment charges for our authorizations, goodwill or other assets; and
- the outcome of litigation, disputes and investigations in which we are involved or may become involved.

The foregoing factors should not be construed as exhaustive. Due to such uncertainties and risks, readers are cautioned not to place undue reliance on such forward-looking statements, which speak only as of the date hereof. We undertake no obligation to release publicly the result of any revisions to these forward-looking statements which may be made to reflect events or circumstances after the date hereof, including, without limitation, changes in our business or acquisition strategy or planned capital expenditures, or to reflect the occurrence of unanticipated events.

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KEY DEFINITIONS

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

EU	means the European Union.
IASB	means the International Accounting Standards Board.
IFRS	means International Financial Reporting Standards issued by the IASB. IFRS also include all effective International Accounting Standards (**IAS**) and all Interpretations issued by the IFRS Interpretations committee (formerly called International Financial Reporting Interpretations Committee IFRIC), comprising those previously issued by the Standing Interpretations Committee (**SIC**).
Ordinary Shares	means the Ordinary Shares, 0.55 euros par value each, of Telecom Italia.
Parent, Telecom Italia and Company	means Telecom Italia S.p.A..
Savings Shares	means the Savings Shares, 0.55 euros par value each, of Telecom Italia.
Telecom Italia Group and Group	means the Company and its consolidated subsidiaries.

In addition to the foregoing terms, certain technical telecommunication terms relating to our businesses are defined in the glossary of this Annual Report (see Item 4. Information on the Telecom Italia Group 4.5 Glossary of Selected Telecommunications Terms).

In addition, we use the measure Accesses when considering certain statistical and other data for our domestic Italian business. Access refers to a connection to any of the telecommunications services offered by the Group in Italy. We present our customer base using this model because the integration of telecommunications services in bundled service packages has changed the way residential and corporate customers contract for our services. Because a single customer may contract for multiple services, we believe it is more accurate to count the number of accesses, or services a customer has contracted for, as opposed to only counting the number of our customers. For example, a customer that has fixed line telephony service and broadband service represents two accesses rather than a single customer. The following are the main categories of accesses:

- Fixed Telephony accesses: includes PSTN lines (public switched telephone network), ISDN lines (integrated services digital network) and circuits. For purposes of calculating our number of fixed line accesses, we multiply our lines to service as follows: PSTN (×1); basic ISDN (×2); primary ISDN (× between 20 and 30 as an average);

- Internet and data accesses: includes broadband accesses (wholesale ADSL and retail ADSL lines), narrowband accesses (internet service through the PSTN) and other accesses (unbundled local loops, circuits and other business data accesses including WiFi and fiber optic cable);

- IP TV (Internet Protocol TV);

- Mobile accesses: number of lines;

- Unbundled local loop: includes accesses to both ends of the copper local loop leased to other operators to provide voice and DSL services (fully unbundled loop, fully UL) or only DSL service (shared unbundled loop, shared UL);

- Wholesale ADSL: means wholesale asymmetrical digital subscriber line; and

- Other: includes other circuits for other operators.

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Item 1. Identity of Directors, Senior Management and Advisers /

Item 2. Offer Statistics and Expected Timetable

PART I

Item 1. IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not Applicable

Item 2. OFFER STATISTICS AND EXPECTED TIMETABLE

Not Applicable

Item 3. KEY INFORMATION

3.1 RISK FACTORS

In addition to the other information contained in this Annual Report, investors should carefully consider the risks described below before making any investment decision. The risks described below are not the only ones we face. Additional risks not known to us or that we currently deem immaterial may also impair our business and results of operations. Our business, financial condition, results of operations and cash flows could be materially adversely affected by any of these risks, and investors could lose all or part of their investment.

Risks Related To The Telecom Italia Group

Our business will be adversely affected if we are unable to successfully implement our strategic objectives. Factors beyond our control may prevent us from successfully implementing our strategy.

On February 8, 2013, we presented our updated 2013 2015 business and strategic plan (the **2013-2015 Plan**). The 2013-2015 Plan sets out our primary strategic objective as well as a number of strategic priorities to achieve this objective over the next three years:

- continued deleveraging to reduce our net financial debt, through:
  - focus on strategic markets Italy, Brazil and Argentina with the goal of stabilizing consolidated revenues through the contribution from Latin America;
  - technological developments in fixed-line telephony and mobile telephony in Italy, mobile telephony in Brazil and network capacity in Argentina to take advantage of growing demand for data;
  - extension and acceleration of our cost reduction policy in order to contribute to the financing of the above mentioned technological developments;
  - sustainable shareholder remuneration. We announced our intention to revise our dividend policy in order to bring it into line with the continuing policy of deleveraging the Group.

Our ability to implement and achieve these strategic objective and priorities may be influenced by certain factors, including factors outside of our control, such as:

- regulatory decisions and changes in the regulatory environment in Italy, Brazil and Argentina or in the other countries in which we operate;

- increasing number of competitors in our principal markets which could cause us to lose further market share;

- increasing and stronger market competition in our principal markets with a consequent decline in the prices of services;

- increasing competition from global and local OTT (Over The Top) players (operators offering content and services on the internet without owning its own proprietary telecommunications network infrastructure);

- the success of disruptive new technologies which could cause significant reductions in revenues from fixed and mobile telephony;

- the continuing effects of the weak global economy, in particular continuing weak gross domestic product (GDP) growth in Italy and in the other markets in which we operate, including the effects on our customers and their ability to purchase or continue to purchase our services;

- the effect of exchange rate fluctuations, particularly in Brazil and Argentina, on our operating revenues, margins and financial management;

- our ability to strengthen our competitive position in Italy and in international markets, particularly in Brazil and Argentina;

- our ability to develop and introduce new technologies which are attractive in our principal markets, to manage innovation, to supply value added services and to increase the use of our fixed and mobile networks;

- our ability to manage and reduce costs;

- our ability to refinance existing indebtedness when due in the capital and bank markets which remain volatile and subject to disruption;

· any difficulties which we may encounter in our supply and procurement processes, including as a result of the insolvency or financial weaknesses of our suppliers; and

· the costs we may incur due to unexpected events, in particular where our insurance is not sufficient to cover such costs.

As a result of these uncertainties there can be no assurance that the business and strategic objectives identified by our management can effectively be attained in the manner and within the time-frames described. Furthermore, if we are unable to attain our strategic priorities, our goodwill may be further impaired which could result in further significant write-offs.

The global economic crisis and the continuing weakness of the Italian economy over the past several years has adversely affected our business and continuing global economic weakness and volatility in the Eurozone could further adversely affect our business and therefore have a negative impact on our operating results and financial condition.

Since the modest recovery in GDP in Italy in 2010 and 2011 following sharp declines that were triggered by the global financial crisis, GDP declined in 2012, with a negative growth of -2.4%. The continuing weakness of the Italian economy is attributable in part to fiscal tightening (a mix of spending cuts and tax increases), aimed at reinforcing the multi-year budget deficit reduction plan and balancing the structural deficit by 2013; this process is expected to continue under the Fiscal Compact rules. This fiscal policy should result in structural adjustments and sustainability in the long term, but it has contributed to the weakness in domestic demand experienced by the Italian market during 2012, which is expected to continue for the coming years.

Weakness in the Italian economy, our core market and, in particular, low or negative GDP growth and increasing levels of unemployment, has had and, if such economic weakness persists, may continue to have a direct negative impact on the spending patterns of customers, both in terms of the products and services they subscribe for and the extent to which they use such products and services. During periods of deteriorating economic conditions and high unemployment, retail customers generally have less discretionary income with which to purchase products and services. Our consumer segments are most directly impacted by a reduction in discretionary income, and as a result of continued economic weakness in Italy, it may be more difficult for us to attract new customers, or retain existing customers, and our revenues and Average Revenue Per User (**ARPU**), particularly in consumer segments, may continue to decline.

Additionally, our business and corporate customers are also affected by general economic conditions and consumer spending, and therefore an extended recession, or public perception of declining economic conditions, is and could continue to substantially decrease telecommunications and IT expenditures among our business and corporate customers, which would in turn adversely affect our revenues in our business and corporate segments. In addition to the economic weakness, the competitive environment is expected to continue to place downward pressure in telecommunications service prices leading to a negative impact on our domestic revenues.

The continuing global economic weakness could also adversely affect our businesses in our principal international markets of Brazil and Argentina which may also have a negative impact on our operating results and financial condition.

If we fail to successfully implement our plans to improve efficiency and optimize expenditures, our results of operations and financial condition could be adversely affected.

[1] The Fiscal Compact is an intergovernmental treaty introduced as a new and stricter version of the previous Stability and Growth Pact. The treaty entered into force on January 1, 2013 for those Member States of the European Union which had completed ratification prior to this date. Under the Fiscal Compact, ratifying Member States are required to have enacted laws requiring their national budgets to be in balance or in surplus within the treaty s definition within one year after the Fiscal Compact enters into force for them. The laws must also provide for a self-correcting mechanism to prevent their breach. The treaty defines a balanced budget as a general budget deficit less than 3.0 per cent. of the GDP, and a structural deficit of less than 1.0 per cent. of GDP if the debt level is below 60 per cent. or else it shall be below 0.5 per cent. of GDP.

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Item 3. Key Information **Risk Factors**

Our leverage is such that deterioration in cash flow can change the expectations of our ability to repay our debt and the inability to reduce our debt could have a material adverse effect on our business. Continuing volatility in the international credit markets may limit our ability to refinance our financial debt.

Our consolidated gross financial debt was 40,181 million euros at December 31, 2012 compared with 41,951 million euros at December 31, 2011. Our consolidated net financial debt was 29,053 million euros at December 31, 2012 compared with 30,819 million euros at December 31, 2011. Our high leverage has been a factor in our strategic decisions for a number of years and the reduction of our leverage remains a key strategic objective. As a result, however, we are reliant on cost cutting and free cash flow to finance critical technology improvements and upgrades to our network.

Due to the competitive environment and continuing weak economic conditions, there could be deterioration in our income statement and statement of financial position measures used by investors and rating agencies in determining our credit quality. Ratios derived from these same separate income statement and statement of financial position measures are used by the rating agencies, such as Moody s, S&P and Fitch, which base their ratings on our ability to repay our debt.

Although rating downgrades do not have an immediate impact on outstanding debt, except for outstanding debt instruments that specifically contemplate ratings in order to determine interest expense, or on its relative cost to us, downgrades could lead to a greater risk with respect to refinancing existing debt or higher refinancing costs.

Factors which are beyond our control such as deterioration in performance by the telecommunications sector, unfavorable fluctuations in interest rates and/or exchange rates, further disruptions in the capital markets, particularly debt capital markets, and, in a broader sense, deterioration in general economic conditions at the sovereign level as a result of the continuing effects of the economic and financial crisis could have a significant effect on our ability to reduce our debt, or our ability to refinance existing debt through further access to the financial markets. As a result of the reduction of debt being a key element of our strategy, the failure to reduce debt could be viewed negatively and adversely affect our credit ratings.

The management and further development of our business will require us to make significant further capital and other investments. If we are unable to finance our capital investment as described above, we may therefore need to incur additional debt in order to finance such investment. Our future results of operations may be influenced by our ability to enter into such transactions, which in turn will be determined by market conditions and factors that are outside our control. In addition, if such transactions increase our leverage it could adversely affect our credit ratings.

We are continuously involved in disputes and litigation with regulators, competition authorities, competitors and other parties and are the subject of a number of investigations by judicial authorities. The ultimate outcome of such proceedings is generally uncertain. If any of these matters are resolved against us, they could, individually or in the aggregate, have a material adverse effect on our results of operations, financial condition and cash flows in any particular period.

We are subject to numerous risks relating to legal, tax, competition and regulatory proceedings in which it is currently a party or which could develop in the future. We are also the subject of a number of investigations by judicial authorities. Such proceedings and investigations are inherently unpredictable. Legal, tax, competition and regulatory proceedings and investigations in which we are, or may become, involved (or settlements thereof) may, individually or in the aggregate, have a material adverse effect on our results of operations and/or financial condition and cash flows in any particular period. Furthermore, our involvement in such proceedings and investigations may adversely affect our reputation.

Operational risks could adversely affect our reputation and our profitability.

We face numerous operational risks inherent in our business, including those resulting from inadequate internal and external processes, fraud, employee errors or misconduct, failure to comply with applicable laws, failure to document transactions properly, loss or disclosure of critical or commercially sensitive data or personally identifiable information or systems failures. These events can result in direct or indirect losses and adverse legal and regulatory proceedings, and harm our reputation and operational effectiveness.

We have in place risk management practices designed to detect, manage and monitor at a senior level the evolution of these operational risks. However, there is no guarantee that these measures will be successful in effectively controlling the operational risks that we face and such failures could have a material adverse effect on our results of operations and could harm our reputation.

Risks associated with Telecom Italia s ownership chain.

Telco S.p.A. (**Telco**) a company in which interests are held by the Generali group (**Generali**) (30.58 per cent.), Intesa Sanpaolo S.p.A. (**Intesa Sanpaolo**) (11.62 per cent.), Mediobanca S.p.A. (**Mediobanca**) (11.62 per cent.), and Telefónica S.A. (**Telefónica**) (46.18 per cent.) is Telecom Italia s largest shareholder, holding an interest of approximately 22.38 per cent. of the voting rights.

On February 29, 2012, Telefónica, Intesa Sanpaolo, Mediobanca, and Generali entered into a renewal agreement (the **2012 Shareholders Agreement**) in which they agreed to enter into a new shareholders agreement for a period of three years on the same terms and conditions set out in the original shareholders agreement dated as of April 28, 2007, as subsequently amended and supplemented. Please see Item 7 Major Shareholders and Related-Party Transactions 7.1 Major Shareholders 7.1.1 Shareholders Agreements .

The 2012 Shareholders Agreement sets out the criteria for drawing up the list of candidates for the appointment of the Board of Directors of Telecom Italia:

- Telefónica, insofar as it holds at least 30 per cent. of Telco s share capital, will be entitled to designate two candidates; and

- the other shareholders of Telco, as they hold the absolute majority of its share capital, have the right to designate the other members on the list, of which three candidates would be appointed unanimously and the others on a proportional basis.

Based on the foregoing, Telco may exert a significant influence on all matters to be decided by a vote of shareholders, including appointment of directors. In the shareholders meeting held on April 12, 2011, 12 out of 15 Board members were elected from a list proposed by Telco, while the remaining three Directors were elected from a list proposed by a group of asset management companies and international institutional investors. In principle, the interests of Telco in deciding shareholder matters could be different from the interests of Telecom Italia s other ordinary shareholders, and it is possible that certain decisions could be taken that may be influenced by the needs of Telco.

In addition, Telefónica is the largest shareholder of Telco. Presently, Telefónica and its associated companies (the **Telefónica Group**) and the Telecom Italia Group are direct competitors outside of their respective domestic markets, including Brazil and Argentina; nevertheless, the 2012 Shareholders Agreement provides that the Telecom Italia Group and the Telefónica Group will be managed autonomously and independently. The 2012 Shareholders Agreement provides, among other things, that the directors designated by Telefónica in Telco and Telecom Italia shall be directed by Telefónica to neither participate nor vote at Board of Directors meetings which discuss matters relating to companies of the Telecom Italia Group in countries where the Telefónica Group and the Telecom Italia Group compete. Specific additional matters have been agreed with respect to the Telecom Italia Group s operations in Brazil and Argentina. The presence of Telefónica in Telco could, however, result in legal or regulatory proceedings or affect regulatory decisions in countries where the Telecom Italia Group may wish to operate if the Telefónica Group is also an operator or competitor in such jurisdictions. For further information, please see Item 7 Major Shareholders and Related-Party Transactions 7.1 Major Shareholders 7.1.1 Shareholders Agreements and Item 10. Additional Information 10.1 Corporate Governance . See also

Note Contingent liabilities, other information, commitments and guarantees of the Notes to the Consolidated Financial Statements included elsewhere herein.

Telco is a holding company and the sole operating company in which it has an interest is Telecom Italia. Therefore, should Telco be unable to obtain funding from its shareholders, present or future, or from other sources, its cash flows would be entirely dependent upon the dividends paid on the Telecom Italia shares for its funding needs.

The Italian State, through the Treasury, is in a position to exert certain powers with respect to Telecom Italia.

Although no shareholder is in a position to prevent a takeover of Telecom Italia, the Italian State, through the Treasury, is in a position to exert certain powers with respect to Telecom Italia through the exercise of the special powers included in Telecom Italia s bylaws pursuant to compulsory legal provisions.

On March 26, 2009, the European Court of Justice (the **ECJ**) declared that Italy, through the special powers, failed to comply with its obligations under the EC Treaty. According to the ECJ s ruling, the alleged infringement of the EC Treaty arose due to the applicable Italian legal provisions not making sufficiently clear the conditions for the exercise of the Treasury s special powers, so that investors would not be in a position to know in what situations the powers will be used. Through a decree passed on May 20, 2010, the Italian Government amended the criteria under which it may exercise such special powers although the ruling by the ECJ did not have any immediate or direct impact on Telecom Italia s bylaws.

In May 2012 regulations relating to the special powers on share ownership in the sectors of defense and national security, and regarding activities of strategic importance in the energy, transport and communication sectors were published and became effective. The regulations provide that, at the moment the Prime Ministerial implementing decrees come into force with respect to *the networks and systems, goods and relationships of strategic importance for the communications* [ ] *sector* , the clauses in the Company s bylaws on special powers will cease to have effect and will be replaced by these regulations. In brief, the new regulations will provide:

- the Italian Government with the authority to impose conditions and possibly to oppose the purchase, for any reason whatever, by non-EU citizens, of controlling shareholdings in companies which hold strategic assets identified in the regulations. For non-EU citizens, any right to purchase will be permitted solely on condition of reciprocity with the purchaser s home jurisdiction;

- a power of veto granted to the Italian Government (including through prescriptions or conditions) on any resolution, act or transaction which has the effect of modifying the ownership, control or availability of strategic assets or changing their use, including resolutions of merger, demerger, transfer of registered office abroad, transfer of the company or business units which contain the strategic assets or their assignment by way of guarantee, amendment to company s bylaws purpose, company dissolution or amendment in bylaws provisions relating to limitations on voting rights.

The exercise of such powers, or the right or ability to exercise such powers, could make a change of control transaction with respect to Telecom Italia (whether by merger or otherwise) more difficult to achieve, if at all, or discourage certain bidders from making an offer relating to a change of control that could otherwise be beneficial to shareholders.

For further information, please see Item 7 Major Shareholders and Related-Party Transactions 7.1 Major Shareholders 7.1.3 Continuing Relationship with the Italian Treasury .

System failures could result in reduced user traffic and reduced revenue and could harm our reputation.

Our success largely depends on the continued and uninterrupted performance of our information technology, network systems and of certain hardware and datacenters that we manage for our clients. Our technical infrastructure (including our network infrastructure for fixed-line and mobile telecommunications services) is vulnerable to damage or interruption from information and telecommunication technology failures, power loss, floods, windstorms, fires, terrorism, intentional wrongdoing, human error and similar events. Unanticipated problems at our facilities, system failures, hardware or software failures, computer viruses or hacker attacks could affect the quality of our services and cause service interruptions. Any of these occurrences could result in reduced user traffic and reduced revenue and could negatively affect our levels of customer satisfaction and harm our reputation.

Our business depends on the upgrading of our existing networks.

We must continue to maintain, improve and upgrade our existing networks in a timely and satisfactory manner in order to retain and expand our customer base in each of our markets. A reliable and high quality network is necessary to manage churn by sustaining our customer base, to maintain strong customer brands and reputation and to satisfy regulatory requirements, including minimum service requirements. The maintenance and improvement of our existing networks depends on our ability to:

- upgrade the functionality of our networks to offer increasingly customized services to our customers;
- increase coverage in some of our markets;
- expand and maintain customer service, network management and administrative systems;
- expand the capacity of our existing fixed copper and mobile networks to cope with increased bandwidth usage; and
- upgrade older systems and networks to adapt them to new technologies.

In addition, due to rapid changes in the telecommunications industry, our network investments may prove to be inadequate or may be superseded by new technological changes. Our network investments may also be limited by market uptake and customer acceptance. If we fail to make adequate capital expenditures or investments, or to properly and efficiently allocate such expenditures or investments, the performance of our networks, both in real terms and in relative terms as compared to our competitors, could suffer, resulting in lower customer satisfaction, diminution of brand strength and increased churn.

Many of these tasks are not entirely under our control and may be affected by applicable regulation. If we fail to maintain, improve or upgrade our networks, our services and products may be less attractive to new customers and we may lose existing customers to competitors, which could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to The Telecommunications Industry and Financial Markets

The value of our operations and investments may be adversely affected by political and economic developments in Italy or other countries. Continuing global economic weakness could reduce purchases of our products and services and adversely affect our results of operations, cash flows and financial condition.

Our business is dependent to a large degree on general economic conditions in Italy and in our other principal markets, Brazil and Argentina, including levels of interest rates, inflation, taxes and general business conditions. A significant deterioration in economic conditions could adversely affect our business and results of operations. The weak economic conditions of the last several years have had an adverse impact on our business, particularly in Italy.

The economic recession that the Italian market has been experiencing in recent years have weighed, and may continue to weigh heavily, on the development prospects of our domestic market.

Continuing uncertainty about global economic conditions poses a significant risk as consumers and businesses postpone spending in response to tighter credit, negative financial news (including high levels of unemployment) or declines in income or asset values, which could have a material negative effect on the demand for our products and services. Economic difficulties in the credit markets and other economic conditions may reduce the demand for or the timing of purchases of our products and services. A loss of customers or a reduction in purchases by our current customers could have a material adverse effect on our financial condition, results of operations and cash flow and may negatively affect our ability to meet our targets. Other factors that could influence customer demand include access to credit, consumer confidence and other macroeconomic factors.

We may also be adversely affected by political developments in Italy and in the countries where we have made significant investments. Certain of these countries have political and legal systems that are less predictable than in Western Europe.

Political or economic upheaval or changes in laws or in their application in the countries outside Italy where we have significant investments may harm the operations of the companies in which we have invested and impair the value of these investments.

In particular, in recent years the Argentine Government has taken several actions to re-nationalize concessions and public service companies that were privatized in the 1990 s, such as Aguas Argentinas S.A. and Aerolíneas Argentinas S.A. Additionally, in May 2012, Law No. 26,741, established the expropriation of the 51% of the capital stock of YPF S.A. and the 51% of the capital stock of YPF GAS S.A., which were directly or indirectly owned by Repsol YPF S.A. (**Repsol**). To date, the Argentine Government has not compensated any of the expropriated investors. These actions had a negative effect on the market. We cannot provide any assurance that similar actions of the Argentine Government will not be extended to other private companies or other sectors in the near future.

In the past, the Argentine Government has imposed a number of monetary and currency exchange control measures, including temporary restrictions on the free availability of funds deposited with banks and restrictions or limitations on the access to foreign exchange markets and transfers of funds abroad, including for purposes of paying principal and interest on debt, trade liabilities to foreign suppliers and dividend payments to foreign shareholders. Between the end of 2001 and 2002, the Argentine Government implemented a unified exchange market (Mercado Único y Libre de Cambios **MULC**) with significant regulations and restrictions for the purchase and transfer of foreign currency.

Since late 2011 the Argentine Government implemented a series of measures aimed to increase controls on the foreign trade and capital flows. To that effect, certain measures were implemented to control and limit the purchase of foreign currency, such as the prior approval of the Administración Federal de Ingresos Públicos (Argentine Federal Tax Authority **AFIP**) for any purchase of foreign currency made by private companies and individuals for saving purposes. In addition, the Banco Central de la Republica Argentina (**BCRA**) expanded the controls and measures to make payments abroad accessing the local foreign exchange market, regarding trade payables and financial debt, and also established demanding procedures that must be met to pay certain trade payables with related parties. Although there are no regulations that prohibit making dividend payment to foreign shareholders, in practice authorities have substantially limited any purchase of foreign currency to pay dividends since these exchange controls were implemented. There can be no assurance that the BCRA or other government agencies will not increase controls and restrictions for making payments to foreign creditors, dividend payments to foreign shareholders, which would limit our ability to comply in a timely manner with payments related to our liabilities to foreign creditors or non-resident shareholders.

Pursuing the same objective, in October 2011 Decree No. 1,722 eliminated an exception for oil, gas and mining companies, and thus requires these companies to liquidate all their export receipts in the local foreign exchange market. Moreover, in October 2011 the National Insurance Bureau issued Resolution No. 36,162 imposing the obligation for insurance companies to repatriate all investments and liquid assets allocated outside Argentina. We cannot ensure that similar measures will not be implemented for other private companies or other sectors in the future.

In addition, starting in February 2012, all import operations of goods and services must be filed and approved in advance by AFIP. Such procedure could negatively affect the provision of imported products and services within our Argentinean supply chain.

Since we operate in a heavily regulated industry, regulatory decisions and changes in the regulatory environment could materially adversely affect our business.

Our fixed and mobile telecommunications operations, as well as our broadband services and television broadcasting businesses, are subject to regulatory requirements in Italy and our international operations are subject to regulation in their host countries. In Italy, we are the only operator subject to universal service obligations, which requires us to provide fixed line public voice telecommunications services in non-profitable areas. As a member of the EU, Italy has adapted its telecommunications regulatory framework to the legislative and regulatory framework established by the EU for the regulation of the European telecommunications market. The last review of the EU common regulatory framework was approved at the end of 2009 and has been transposed in Italy in 2012.

In compliance with the regulatory framework the Italian regulator responsible for the regulation of the telecommunications, radio and television broadcasting sectors (**AGCom**) has to identify operators with significant market power (**SMP**) based on market analyses in relevant retail and wholesale markets, identified

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in an EC Recommendation. The framework established criteria and procedures for identifying remedies applicable to operators with SMP in various markets. An operator designated by a national authority as having SMP will be subject to a set of obligations necessary to safeguard competition. AGCom s regulatory approach is mainly focused on the regulation of our wholesale business, while the regulation of retail markets is being gradually withdrawn.

Regulatory uncertainty and regulatory changes imposed on us can have an adverse effect on our revenues as well as making it difficult to make important decisions on investments. In September 2012 AGCom launched the third round of market analysis which should have set wholesale access fees for LLU, WLR and Bitstream services on the copper and fiber-based networks for the 2013-2015 period. However, AGCom decided to set the fees for the above mentioned copper-based access services only for the year 2013 while postponing the decision regarding the fees for the 2014-2016 period. This approach has created uncertainty because the 2013 fees have been fixed without a market analysis and for the following 2014-2016 period only the range of the final year (2016) access charges has been submitted for public consultation.

In addition the Council of State (*Consiglio di Stato)* published two judgments on both fixed and mobile termination rates: the first judgment upheld the complaint filed by Fastweb (one of Telecom Italia s main competitors in the fixed line market) and revoked the symmetry of 2012 Time Division Multiplexing (TDM) fixed termination tariffs among operators; the second one upheld the complaint filed by H3G (the fourth mobile operator in Italy) and revoked the decrease on termination fees on the H3G network in the period November 2008-June 2009. As a result, Telecom Italia s costs for fixed and/or mobile termination services could be expected to increase.

The regulatory framework of the Next Generation Access Network (NGAN) is not yet completely defined. Proceedings to establish NGAN regulation with a view to introducing: 1) a cost model for the pricing of passive and active wholesale services and the definition of the so-called NGAN competitive areas where the price of fiber-based bitstream and virtual access services are not subject to the cost orientation obligation; 2) the perspective enforcement of symmetric obligations on all operators, for the access to fiber vertical wiring and to building connection segments; and 3) potential amendments to the regulation of the copper sub-loop unbundling service in light of the possible introduction of the vectoring technology on Fiber to the Cabinet -Very High- Speed Digital Subscriber Line (FTTCab-VDSL) accesses. As Next Generation Access will require significant investments, the regulatory approach regarding the obligations which could be imposed on us could have an adverse effect on our cash flows and financial condition potentially hampering future investments.

On April 4, 2012, the Italian Parliament approved a law mandating AGCom to impose on us the obligation to separately offer our ancillary services (activation and maintenance) for the LLU lines so that they might be provided also by third parties. However, in July 2012, the EU Commission formally opened an infringement procedure against Italy, in relation to the possible breach of the EU regulatory framework stating the principle of independence and autonomy of national authorities by the above mentioned law. From a technical point of view granting the possibility for third parties to manage the maintenance of the incumbent s network may cause serious negative effects on the quality of the service, on the security and integrity of the network as well as on the efficient deployment of the infrastructure to the detriment of end-users. In February 2013 the EU Commission issued a reasoned opinion concluding that the Italian Government has infringed the European legislation. As a consequence, the Italian Government was required to change the law within two months and therefore the law aimed at the transposition in the Italian framework of the EU rules (Legge Comunitaria 2013), preliminarily discussed in March 2013, includes a specific provision aimed at withdrawing the obligation for AGCom to impose on Telecom Italia the disaggregated offer of its LLU ancillary services. The formal approval of this law by the Italian Parliament will end the infringement procedure by the European Commission.

Our Brazilian and Argentinean Business Units are subject to extensive regulation in their respective countries. Our international operations, therefore, confront similar regulatory issues as we face in Italy, including the possibility for regulators to impose obligations and conditions on how we operate our businesses in these countries as well as taking decisions that can have an adverse effect on our results, including setting, and in particular, reducing the rates we can charge or, as is the case in Argentina, freezing, since 2002, the rates we can charge for basic fixed line telephony services. As a result, the decisions of regulators or the implementation of new regulations in Brazil and Argentina, and the costs of our compliance with any such decisions or new regulations, may limit our flexibility in responding to market conditions, competition and changes in our cost base which could individually or in the aggregate, have a material adverse effect on our business and results of operations.

For example, in 2012 the Argentine Government cancelled the auction for the 850 MHz and 1900 MHz spectrum bands that were returned by Telefónica Móviles Argentina S.A. These spectrum bands were returned due to the spectrum cap restrictions of 50 MHz.

In December 2012 the Argentine President announced the launching of a new state owned mobile company branded libre.ar . The government s dual-role, as both regulator and competitor, opens several risks to our Argentine mobile business including possible adverse changes in the regulatory framework and the current market rules. The lack of allocation of additional frequency bands is negatively affecting the quality of service of all the Argentinean mobile operators. It could also adversely affect our mobile competitive position and may require higher capital expenditures to continue providing high quality mobile services to our customers.

In Brazil we operate under authorizations granted by the Brazilian Government. As a result, we are obliged to maintain minimum quality and service standards. Our failure to comply with all the requirements imposed by Anatel and by the Brazilian Government may result in the imposition of fines or other government actions, including the suspension of the service commercialization for a given period.

Due to the continuous evolution of the regulatory regime affecting various parts of our business in Italy and in our international operations, we are unable to clearly predict the impact of any proposed or potential changes in the regulatory environment in which we operate both in Italy and internationally. Regulations in the telecommunications industry are constantly changing to adapt to new competition and technology. Changes in laws, regulation or government policy could adversely affect our business and competitiveness. In particular, our ability to compete effectively in our existing or new markets could be adversely affected if regulators decide to expand the restrictions and obligations to which it is subject or extend them to new services and markets. Finally, decisions by regulators regarding the granting, amendment or renewal of our authorizations, or those of third parties, could adversely affect our future operations in Italy and in other countries where it operates.

There is also a general risk related to the possible imposition of fines by the competent authorities for violations of regulations to which we are subject.

For further information regarding the matters discussed above and other aspects of the regulatory environments in which Telecom Italia Group s businesses operates, see Item 4.3. Regulation .

We operate under authorizations granted by government authorities.

Many of our activities require authorizations from governmental authorities. These authorizations specify the types of services the operating company holding such authorization may provide. The continued existence and terms of our authorizations are subject to review by regulatory authorities and to interpretation, modification or termination by these authorities. Although authorization renewal is not usually guaranteed, most authorizations do address the renewal process and terms that, however, may be affected by political and regulatory factors.

Many of these authorizations are revocable for public interest reasons. The rules of some of the regulatory authorities with jurisdiction over our operating companies require us to meet specified network build-out requirements and schedules. In particular, our existing authorizations typically require us to satisfy certain obligations, including minimum specified quality, service and coverage conditions. Failure to comply with these obligations could result in the imposition of fines or even in the revocation or forfeiture of the authorization. In addition, the need to meet scheduled deadlines may require us to expend more resources than otherwise budgeted for a particular network build-out.

Additional authorizations may also need to be obtained if we expand our services into new product areas, and such authorizations may be related to auctions (such as the assignment or the right of use of spectrum) or otherwise prove expensive or require significant cash outlays, or have certain terms and conditions, such as requirements related to coverage and pricing, with which we may not have previously had to comply. If we are unable to obtain such authorizations within the expected timeframe, at a commercially acceptable cost, or at all, or if the authorizations includes onerous conditions, it could have a material adverse effect on our business, financial condition and results of operations.

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The Pesification and freezing of rates may continue to adversely affect Telecom Argentina s revenues.

In accordance with the Argentine Public Emergency Law, in January 2002, rates for Basic telephone services and long distance services were converted to Argentine pesos and fixed at an exchange rate of P$1.00=US$1.00 (the Pesification). The rates that Telecom Argentina may charge in the future will be determined by negotiations between Telecom Argentina and the Argentine Government.

In March 2006, Telecom Argentina executed a Letter of Understanding (the **2006 Letter of Understanding**) with the Argentine Government pursuant to which Telecom Argentina will be permitted to raise certain rates and incorporate certain modifications to the current regulatory framework.

The 2006 Letter of Understanding contemplated the signing and effectiveness of the Minutes of Agreement of the Renegotiation upon the fulfillment of certain necessary steps, which as of the date of this Annual Report have yet to occur. Although Telecom Argentina expects such fulfillment to occur, we cannot guarantee if or when this will happen. We are unable to predict the outcome of the negotiations with regard to further rate increases and the rate scheme which will be applied in the future. Moreover, Telecom Argentina is unable to predict whether the Argentine Government will impose additional conditions or requirements, and if these conditions or requirements are imposed, whether Telecom Argentina will be able to satisfy them.

In addition, in early 2013 the Argentine Government adopted certain initiatives in order to reduce current inflation rates, including price agreements with certain non-regulated sectors such as supermarkets and retailers. In this context and considering the increasing demands of service quality improvements that all Argentine mobile operators are facing, our mobile subsidiary Personal decided not to implement the rate increases announced in the fourth quarter of 2012 (to be effective as from March 2013) for postpaid and cuentas claras customers. Although mobile telephony is a non-rate regulated industry, we cannot predict whether current or new factors including governmental initiatives in order to reduce inflation rates would negatively impact Personal s ability to apply rate increases, thus negatively affecting the profit margins and the level of requested funds for capital expenditures to maintain or increase the quality of the service.

Rate restrictions for regulated services of Telecom Argentina may continue for a number of years and may continue affecting revenues from fixed line and other services. In a high inflation environment this may continue to significantly affect Telecom Argentina s financial results.

Strong competition in Italy or other countries may reduce our core market share for telecommunications services and may cause reductions in prices and margins thereby having a material adverse effect on our results of operations and financial condition.

Strong competition exists in all of the principal telecommunications business areas in Italy in which we operate, including, most significantly, the fixed-line and mobile voice telecommunications and broadband businesses. Competition has been intense since the liberalization of the Italian telecommunications market in 1998 and there is now entrenched competition from international operators who have been present in the Italian market for some time and direct competition with our fixed-line and mobile telephony businesses and for broadband services.

As of the date of this Annual Report, there are a number of significant competitors offering fixed-line and broadband services and three operators (in addition to us) offering mobile services in the Italian domestic market. In addition, some virtual mobile operators have been operating in the Italian mobile market since 2007 as a result of commercial agreements reached with operators of mobile networks, some of which originated from fixed line operators.

Moreover, convergence enables lateral competition from IT, Media and Devices/Consumer Electronic players. This competition may further increase due to the consolidation and globalization of the telecommunications industry in Europe, including Italy, and elsewhere. We face competition from international competitors who have entered local markets to compete with existing operators as well as from local operators, each of which has increased the direct competition we face in our Italian domestic fixed-line, mobile telephony and broadband businesses.

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Competition in our principal lines of business has led, and could lead, to:

- price and margin erosion for our products and services;
- a loss of market share in our core markets;
- loss of existing or prospective customers and greater difficulty in retaining existing customers;
- obsolescence of existing technologies and more rapid deployment of new technologies;
- an increase in costs and payback period related to investments in new technologies that are necessary to retain customers and market share; and
- difficulties in reducing debt and funding strategic and technological investments if we cannot generate sufficient profits and cash flow.

Although we have taken a number of steps to realize additional efficiencies and to rebalance revenue mix through the continuing introduction of innovative and value added services, if any or all of the events described above should occur, the impact of such factors could have a material adverse effect on our results of operations and financial condition.

In addition to competitive pressures, as a result of the increasing substitution of data services in place of traditional voice and SMS communications, our traditional voice and SMS markets also have been decreasing and are expected to continue to decrease due to increasing competition from alternative modes of telecommunications.

We face increasing competition from non-traditional data services on new voice and messaging over the internet technologies, in particular over-the-top (OTT) applications, such as Skype, Google Talk, FaceTime and WhatsApp. These applications are often free of charge, other than for data usage, accessible via smartphones, tablets and computers and allow their users to have access to potentially unlimited messaging and voice services over the internet, bypassing more expensive traditional voice and messaging services such as short message service (SMS) which have historically been a source of significant revenues for fixed and mobile network operators such as us. With the growing share of smartphones, tablets and computers in Italy as well as our international markets of Brazil and Argentina, an increasing number of customers are using OTT applications services in substitution for traditional voice or SMS communications.

Historically, we have generated a substantial portion of our revenues from voice and SMS services, particularly in our mobile business in Italy, and the substitution of data services for these traditional voice and SMS volumes has had and is likely to continue to have a negative impact on our revenues and profitability. As a result of these and other factors, we face a mobile market in which price pressure has been increasing.

All mobile network operators, including ourselves, are currently competing with OTT application providers who leverage on existing infrastructures and who generally do not operate capital-intensive business models associated with traditional mobile network operators like us. OTT application service providers have recently become more sophisticated competitors, and technological developments have led to a significant improvement in the quality of service, in particular speech quality, delivered via data communications applications such as OTT. In addition, players with strong brand capability and financial strengths, such as Apple, Google and Microsoft, have turned their attention to the provision of OTT application services. In the long term, if non-traditional mobile voice and data services or similar services continue to increase in popularity, as they are expected to do, and if we and other mobile network operators are not able to address this competition, this could contribute to further declines in ARPU and lower margins across many of our products and services, thereby having a material adverse effect on our business, results of operations, financial condition and prospects.

Our business and our revenues may be negatively affected if we are unable to continue the introduction of new services, stimulating increased usage of our fixed and wireless networks.

The maturity of telecommunications markets (particularly in our core Italian market) and the rapidly changing competitive landscape (for example, the rise of global platform/networks of organizations (an ecosystem) delivering a specific product or service through both competition and cooperation) have resulted in a continuous erosion in traditional service revenues for telecommunications operators.

In this context, our strategy has led to integration of our core offering portfolio with new services outside traditional telecommunications domains (eg. Cloud Services, Digital Media, M2M services), which are able to generate new revenue streams and at the same time stimulate increased usage of our fixed and wireless networks. A deep knowledge of customers needs and preferences, the ability to respond rapidly to their changes and a thorough understanding of the specialized needs of certain industries are particularly important for exploiting such opportunities.

Failing to exploit these business opportunities and to identify an appropriate role in the relative ecosystems may have a material adverse effect on our revenue streams.

Continuing rapid changes in technologies could increase competition, reduce usage of traditional services or require us to make substantial additional investments.

Many of the services we offer are technology-intensive and the development or acceptance of new technologies may render such services non-competitive, replace such services or reduce prices for such services. Our markets are characterized by rapid and significant changes in technology, customer demand and behavior, and, as a result feature a constantly changing competitive environment. In addition, as the convergence of services accelerates, we make and will have to make substantial additional investments in new technologies to remain competitive. The new technologies we choose may prove to be commercially unsuccessful. Moreover, we may not receive the necessary authorizations to provide services based on new technologies in Italy or abroad, or may be negatively impacted by unfavorable regulation regarding the usage of these technologies. Furthermore, our most significant competitors in the future may be new entrants to our markets who do not have to maintain an installed base of older equipment.

As a result, if we are unable to effectively anticipate, react to or access technological changes in our telecommunications markets we could lose customers, fail to attract new customers or incur substantial costs in order to maintain our customer base or to maintain revenues from such customer base, all of which could have a material adverse effect on our business, financial condition and results of operations.

The mobile communications markets have matured and competition has increased.

Although mobile communications markets have reached maturity levels in our domestic market in the voice services segment, the mobile broadband business continues to grow. However such change has had an adverse effect on revenues from our mobile services.

The evolution of the mobile telecommunications markets in which we operate will depend on a number of factors, many of which are outside our control. These factors include:

- the activities of our competitors;

- competitive pressures and regulations applicable to retail and wholesale prices;

- the development and introduction of new and alternative technologies for mobile telecommunications products and services and their attractiveness to our customers; and

- the success of new disruptive or substitute technologies.

In addition, as our core domestic Italian market has become increasingly saturated there is a growing focus on customer retention. Such focus could result in increased expenses to retain customer loyalty or, if we are unable to satisfactorily offer better value to our customers, our market share and revenues could decline. The main mobile competitors in Italy, including us, suffered higher levels of churn in 2012 than we had experienced in recent years. Such a high level of churn is indicative of the intense competition in this market. Furthermore, during the first months of 2013 we have experienced a significant deterioration in the Italian mobile market, with a strong increase in the level of competition and nearly unprecedented price pressure in comparison with prior periods; a continuation of such price pressure could have an adverse effect on our current and future revenues and results of operations.

If the mobile telecommunications markets in which we operate perform worse than expected, or if we are unable to retain our existing customers or stimulate increases in customer usage, our financial condition and results of operations may be harmed. In particular, our goodwill may be further impaired which could result in further significant write-offs.

We may be adversely affected if we fail to successfully implement our Internet and broadband strategy.

The continuing development of Internet and broadband services is an important part of our strategic objectives and means to increase the use of our networks in Italy and abroad. Our strategy includes the development of broadband and value added services in order to offset the decline of traditional voice services. Our ability to successfully implement this strategy may be affected if:

- Internet usage in Italy continues to grow more slowly than anticipated, for reasons such as changes in Internet users preferences or lower than expected penetration rate growth for PCs, tablets, smartphones and other Internet connected devices;
- broadband penetration does not grow as we expect;
- competition increases, for reasons such as the entry of new competitors (telcos, OTT players or players from adjacent markets), consolidation in the industry or technological developments introducing new platforms for Internet access and/or Internet distribution or other operators can provide broadband connections superior to those that we can offer; and
- we experience any network interruptions or related problems with network infrastructure.

Any of the above factors may adversely affect the successful implementation of our strategy, our business and results of operations.

Our business may be adversely affected if we fail to successfully implement our Information and Communications Technology (ICT) strategy.

We intend to continue focusing on IT-TLC convergence by addressing the ICT market, offering network and infrastructure management, as well as application management.

Moreover as the use of cloud IT services matures and their adoption grows, we may take advantage of the new cloud opportunities especially in the Business customer segment providing a full range of services (from core Infrastructure to Software as a Service through partners ecosystem) integrated with a wide range of connectivity options and end-to-end SLAs. We expect to experience increasing competition in this market as additional competitors (mainly Telco operators through acquisition and partnership with IT operators) also enter this market.

There is no assurance that the services offered will be successful; as a result our revenues could be negatively affected.

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

The effects of, and any damage caused by, exposure to an electromagnetic field were and are the subject of careful evaluations by the international scientific community, but until now there is no scientific evidence of harmful effects on health. We cannot rule out that exposure to electromagnetic fields or other emissions originating from wireless handsets will not be identified as a health risk in the future.

Our mobile communications business may be harmed as a result of these alleged health risks. For example, the perception of these health risks could result in a lower number of customers, reduced usage per customer or potential consumer liability. In addition, although Italian law already imposes strict limits in relation to transmission equipment, these concerns may cause regulators to impose greater restrictions on the construction of base station towers or other infrastructure, which may hinder the completion of network build-outs and the commercial availability of new services and may require additional investments.

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

In the past, we have made substantial international investments, primarily in U.S. dollars, and have significantly expanded our operations outside of the Euro zone, particularly in Latin America.

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Item 3. Key Information **Risk Factors**

We generally hedge our foreign exchange exposure, but do not cover translation risk relating to our foreign subsidiaries. Movements in exchange rates of the Euro relative to other currencies (in particular the Brazilian Real and Argentine Peso) may adversely affect our consolidated results. In particular, with respect to Argentina, we currently utilize for all purposes the official exchange rate of the Argentine Peso because it is the exchange rate that Telecom Argentina accesses for making payment to foreign creditors and for collections from foreign operators. The increasing restrictions in the exchange rates market increased the gap between the official Peso exchange rate and the implicit exchange rate, reached through the valuation of securities trading in the local market in pesos and the same ones trading in an external market in another currency. Given the economic and political conditions in Argentina, we cannot predict whether, and to what extent, the value of the peso may depreciate against the U.S. dollar, the Euro or other foreign currencies, in such a form that it will capture partially or totally the current gap between the official exchange rate and the implicit exchange rate. A rise in the value of the Euro relative to other currencies in certain countries in which we operate or have made investments will reduce the relative value of the revenues or assets of our operations in those countries and, therefore, may adversely affect our operating results or financial position.

In addition, we have raised, and may raise in an increasing proportion in the future, financing in currencies other than the Euro, principally the U.S. dollar and British pound. In accordance with our risk management policies, we generally hedge the foreign currency risk exposure related to non-Euro denominated liabilities, through cross-currency and interest rate swaps.

Furthermore, we enter into derivative transactions hedging our interest rate exposure to change interest rates in order to manage the volatility of our income statement, while remaining within predefined target levels. However, no assurance can be given that fluctuations in interest rates will not adversely affect our results of operations or cash flows.

Furthermore, an increase of sovereign spreads, and of the default risk it reflects, in the countries where we operate, may affect the value of our assets in such countries.

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Item 3. Key Information **Exchange Rates**

3.2 EXCHANGE RATES

We publish our consolidated financial statements in euros. References to , euro and Euro are to the euro, the single unified currency that was introduced in Italy and 10 other member states of the EU on January 1, 1999. References to U.S. dollars , dollars , U.S.$ or $ are to U.S. dollar the currency of the United States of America.

For convenience only (except where noted otherwise), certain euro figures have been translated into dollars at the rate (the Euro/Dollar Exchange Rate) of 1.00= U.S.$ 1.3186, using the last noon buying rate in The City of New York for cable transfers in foreign currencies as announced by the Federal Reserve Bank of New York for customs purposes (the **Noon Buying Rate**) on December 31, 2012.

These translations should not be construed as a representation that the euro amounts actually represent such dollar amounts or have been or could be converted into dollars at the rate indicated.

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

The following table sets forth for the years 2008 to 2012 and for the beginning of 2013 certain information regarding the Noon Buying Rate for Dollars expressed in U.S.$ per 1.00.

Calendar Period	High	Low	Average(1)	At Period end
2008	1.6010	1.2446	1.4725	1.3919
2009	1.5100	1.2547	1.3936	1.4332
2010	1.4536	1.1959	1.3262	1.3269
2011	1.4875	1.2926	1.3931	1.2973
2012	1.3463	1.2062	1.2859	1.3186
2013 (through April 5, 2013)	1.3692	1.2782	1.3173	1.3027

Monthly Rates	High	Low	Average(1)	At Period end
October 2012	1.3133	1.2876	1.2974	1.2958
November 2012	1.3010	1.2715	1.2837	1.3010
December 2012	1.3260	1.2930	1.3119	1.3186
January 2013	1.3584	1.3047	1.3304	1.3584
February 2013	1.3692	1.3054	1.3347	1.3079
March 2013	1.3098	1.2782	1.2953	1.2816
April 2013 (through April 5, 2013)	1.3027	1.2836	1.2884	1.3027

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

The Ordinary Shares and Savings Shares of Telecom Italia trade on *Mercato Telematico Azionario* (**Telematico**), managed by Borsa Italiana S.p.A. (**Borsa Italiana**) in euro. Fluctuations in the exchange rate between the euro and the U.S. dollar will affect the U.S. dollar equivalent of the euro price of the Ordinary Shares and the Savings Shares and the price of the Ordinary Share American Depositary Shares (**Ordinary Share ADSs**) and the Savings Share American Depositary Shares (**Savings Share ADSs**), on the New York Stock Exchange (**NYSE**). Cash dividends are paid in euro. Exchange rate fluctuations will affect the U.S. dollar amounts received by owners of Ordinary Share ADSs and Savings Share ADSs upon conversion by the Depositary of cash dividends paid in euro on the underlying Ordinary Shares and Savings Shares. See Item 10. Additional Information 10.5 Description of American Depositary Receipts .

3.3 SELECTED FINANCIAL AND STATISTICAL INFORMATION

The selected financial data set forth below is consolidated financial data of the Telecom Italia Group as of and for each of the years ended December 31, 2012, 2011, 2010, 2009 and 2008, which have been extracted or derived, with the exception of amounts presented in U.S. dollars, financial ratios and statistical data, from the Consolidated Financial Statements of the Telecom Italia Group prepared in accordance with IFRS as issued by IASB and which have been audited, with respect to 2012, 2011 and 2010, by the independent auditor PricewaterhouseCoopers S.p.A., which replaced Reconta Ernst & Young S.p.A., as part of the normal required rotation of auditors. 2009 and 2008 were audited by the independent auditor Reconta Ernst & Young S.p.A.

In 2012, the Group applied the accounting policies on a basis consistent with those of the previous years, except for:

- the early adoption, starting from the first half of 2012, of the revised version of IAS 19 (Employee Benefits), whose effects are described in Note Accounting Policies of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report. The early adoption of such amendments resulted in the restatement of the 2011 and 2010 separate consolidated income statements and consolidated statements of comprehensive income;
- the new standards and interpretations adopted by the Group since January 1, 2012 (IAS 12 (Income Taxes) and IFRS 7 (Disclosures Transfers of Financial Assets)), that did not have any effect on the consolidated financial statements at December 31, 2012.

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Item 3. Key Information **Selected Financial And Statistical Information**

The selected financial data below should be read in conjunction with the Consolidated Financial Statements and notes thereto included elsewhere in this Annual Report.

	Year ended December 31						
	2012(*)	**2012(*)**	**2011(*) (Restated)**	**2010(*) (Restated)**	**2010**	**2009**	**2008**
	(millions of U.S. dollars, except percentages, ratios, employees and per share amounts)(1)	**(millions of euros, except percentages, ratios, employees and per share amounts)**					
Separate Consolidated Income Statement Data:							
Revenues	**38,903**	**29,503**	**29,957**	**27,571**	**27,571**	**26,894**	**28,746**
Operating profit (loss)	**2,540**	**1,926**	**(680)**	**5,858**	**5,818**	**5,493**	**5,437**
Profit (loss) before tax from continuing operations	**(58)**	**(44)**	**(2,743)**	**4,128**	**4,132**	**3,339**	**2,894**
Profit (loss) from continuing operations	**(1,686)**	**(1,279)**	**(4,353)**	**3,579**	**3,582**	**2,218**	**2,217**
Profit (loss) from Discontinued operations/Non-current assets held for sale	3	2	(13)	(7)	(7)	(622)	(39)
Profit (loss) for the year	**(1,684)**	**(1,277)**	**(4,366)**	**3,572**	**3,575**	**1,596**	**2,178**
Profit (loss) for the year attributable to owners of the Parent(2)	*(2,145)*	*(1,627)*	*(4,811)*	*3,118*	*3,121*	*1,581*	*2,177*
Capital Expenditures	**6,851**	**5,196**	**6,095**	**4,583**	**4,583**	**4,543**	**5,040**
Financial Ratios:							
Operating profit (loss)/Revenues (ROS)(%)	6.5%	6.5%		21.2%	21.1%	20.4%	18.9%
Ratio of earnings to fixed charges(3)	0.98	0.98	(0.29)	2.84	2.84	2.51	2.21
Employees, average salaried workforce in the Group, including personnel with temporary work contracts:							
Employees (excluding employees relating to the consolidated companies considered as Discontinued operations/Non current assets held for sale) (average number)	78,564	78,564	78,369	70,150	70,150	69,964	73,508
Employees relating to the consolidated companies considered as Discontinued operations/Non current assets held for sale (average number)						2,168	3,277

Basic and Diluted earnings per Share (EPS)(4):							
Ordinary Share	**(0.11)**	**(0.08)**	**(0.25)**	**0.16**	**0.16**	**0.08**	**0.11**
Savings Share	**(0.11)**	**(0.08)**	**(0.25)**	**0.17**	**0.17**	**0.09**	**0.12**
Of which:							
From continuing operations:							
Ordinary Share	*(0.11)*	*(0.08)*	*(0.25)*	*0.16*	*0.16*	*0.11*	*0.11*
Savings Share	*(0.11)*	*(0.08)*	*(0.25)*	*0.17*	*0.17*	*0.12*	*0.12*
From Discontinued operations/Non-current assets held for sale:							
Ordinary Share						*(0.03)*	
Savings Share						*(0.03)*	
Dividends:							
per Ordinary Share(5)	0.026	0.020	0.043	0.058	0.058	0.050	0.050
per Saving Share(5)	0.041	0.031	0.054	0.069	0.069	0.061	0.061

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Item 3. Key Information **Selected Financial And Statistical Information**

	2012 (millions of U.S. dollars, except employees)(1)	2012	As of December 31, 2011	2010	2009	2008
		(millions of euros, except employees)				
Consolidated Statement of Financial Position Data:						
Total assets	**102,264**	**77,555**	**83,886**	**89,040**	**86,267**	**86,223**
Equity:						
Equity attributable to owners of the Parent	25,552	19,378	22,790	28,819	25,952	25,598
Non-controlling interests	4,792	3,634	3,904	3,736	1,168	730
Total Equity	**30,344**	**23,012**	**26,694**	**32,555**	**27,120**	**26,328**
Total Liabilities	**71,920**	**54,543**	**57,192**	**56,485**	**59,147**	**59,895**
Total equity and liabilities	**102,264**	**77,555**	**83,886**	**89,040**	**86,267**	**86,223**
Share capital(6)	**13,982**	**10,604**	**10,604**	**10,600**	**10,585**	**10,591**
Net financial debt(7)	**38,309**	**29,053**	**30,819**	**32,087**	**34,747**	**34,039**
Employees, number in the Group at year-end, including personnel with temporary work contracts:						
Employees (excluding employees relating to the consolidated companies considered as Discontinued operations/Non-current assets held for sale) (number at year-end)	83,184	83,184	84,154	84,200	71,384	75,320
Employees relating to the consolidated companies considered as Discontinued operations/Non-current assets held for sale (number at year-end)					2,205	2,505

	2012	2011	As of December 31, 2010	2009	2008
			(thousands)		
Statistical Data:					
Domestic (Italy) Business Unit					
Physical accesses(8)	21,153	21,712	22,122	22,256	22,289
Of which physical accesses (retail)	*13,978*	*14,652*	*15,351*	*16,097*	*17,352*
Broadband accesses	8,967	9,089	9,058	8,741	8,134
Of which retail broadband accesses	*7,020*	*7,125*	*7,175*	*7,000*	*6,754*
Mobile lines	32,159	32,227	31,018	30,856	34,797
Brazil Business Unit					
Mobile lines	70,362	64,070	51,015	41,102	36,402
Argentina Business Unit					
Fixed-line network connections	4,128	4,141	4,107	4,060	4,010
Broadband accesses	1,629	1,550	1,380	1,214	1,032
Mobile lines	21,276	20,342	18,212	16,281	14,390

(*) Starting from 2012, the Telecom Italia Group has early adopted and retrospectively applied revised IAS 19 (Employee Benefits); therefore, the comparative figures for 2011 and 2010 have been restated on a consistent basis. The adoption of IAS 19 does not have any effect on the Group s statement of financial position other than certain reclassifications under Equity. Further details and the effects on the years ended December 31, 2011 and 2010 are provided in the Note Accounting Policies of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report. 2009 and 2008 data has not been restated for the adoption of IAS 19 as the company considered the impact immaterial.

(1) For the convenience of the reader, Euro amounts for 2012 have been converted into U.S. dollars using the Euro/Dollar Exchange Rate in effect on December 31, 2012, of 1.00 =1.3186 U.S.$.

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Item 3. Key Information	Selected Financial And Statistical Information

(2) For the purposes of IFRS, Parent , as used in this Annual Report, means Telecom Italia S.p.A.

(3) Due to the loss in 2012 and in 2011, the ratio coverage was less than 1:1. The company would have needed to generate additional earnings of 38 million euros in 2012 and 2,704 million euros in 2011 to achieve a coverage of 1:1. For purposes of calculating the ratio of earnings to fixed charges :

- Earnings is calculated by adding:

  profit (loss) before tax from continuing operations;

  fixed charges (as defined below);

  amortization of capitalized interest and debt issue discounts or premiums;

  dividends from associates and joint ventures accounted for using the equity method; and

  share of losses of associates and joint ventures accounted for using the equity method and then subtracting:

  capitalized interest for the applicable period; and

  share of earnings of associates and joint ventures accounted for using the equity method.

- Fixed charges is calculated by adding:

  interest expenses (both expensed and capitalized);

  issue costs and any original debt issue discounts or premiums; and

  an estimate of the interest within rental expense for operating leases.

(4) In accordance with IAS 33 (*Earnings per share*), basic earnings per Ordinary Share is calculated by dividing the Group s profit (loss) available to shareholders by the weighted average number of shares outstanding during the year, excluding treasury shares. Since Telecom Italia has both Ordinary and Savings Shares outstanding, the calculations also take into account the requirement that holders of Savings Shares are entitled to an additional dividend equal to 2% of the par value of shares above dividends paid on the Ordinary Shares.

For the purpose of these calculations, the weighted average number of:

Ordinary Shares was 13,277,621,082 for the year ended December 31, 2012, was 13,264,375,078 for the year ended December 31, 2011, 13,239,883,276 for the year ended December 31, 2010, 13,220,792,908 for the year ended December 31, 2009 and 13,246,643,947 for the year ended December 31, 2008;

Savings Shares was 6,026,120,661 for the years ended December 31, 2012, 2011, 2010, 2009 and 2008.

For diluted earnings per share the weighted average number of shares outstanding is adjusted assuming conversion of all dilutive potential shares. Potential shares are those securities that, if converted into shares, would increase the total number of shares outstanding and reduce the earnings attributable to each share. Potential shares include options, warrants and convertible securities. The Group s profit (loss) is also adjusted to reflect the impact of the conversion of potential shares net of the related tax effects.

(5) Subject to approval, at the Annual Shareholders Meeting to be held on April 17, 2013, Telecom Italia s dividend coupons for the year ended December 31, 2012, will be clipped on April 22, 2013, and will be payable from April 25, 2013.

(6) Share capital represents share capital issued net of the par value of treasury shares.

(7) Net Financial Debt is a Non-GAAP Financial Measure as defined in Item 10(e) of Regulation S-K under the 1934 Act. For further details please see Item 5. Operating and Financial Review and Prospects 5.2 Results of Operations for the Three Years Ended December 31, 2012 5.2.3 Non-GAAP Financial Measures .

(8) Physical accesses include Broadband accesses.

3.4 DIVIDENDS

The determination of our future dividend policy, and the amounts thereof, will depend upon a number of factors, including but not limited to our earnings, financial condition and cash requirements, prospects and such other factors as may be deemed relevant at the time. As part of our 2013-2015 Plan, we announced our intention to reduce our annual dividend beginning in 2012 in order to bring it into line with our strategic priority of continuing to deleverage and reduce our net financial debt. See Item 4 Information on the Telecom Italia Group 4.1.7 Updated Strategy .

The following table sets forth the dividends per Ordinary Share and per Savings Share declared by Telecom Italia with respect to each of the last five fiscal years and the aggregate dividends paid in such years. Actual dividends paid are rounded to the nearest whole cent.

	Dividends on Ordinary Shares			Dividends on Savings Shares		
Year ended December 31,	**Euros per Share**	**U.S. Dollars per Share(1)**	**(millions of euros)**	**Euros per Share**	**U.S. Dollars per Share(1)**	**(millions of euros)**
2008	0.0500	0.0652	667.16	0.0610	0.0796	367.59
2009	0.0500	0.0619	667.16	0.0610	0.0755	367.59
2010	0.0580	0.0846	775.48	0.0690	0.1006	415.80
2011	0.0430	0.0563	575.30	0.0540	0.0707	325.41
2012(2)	0.0200	0.0261	267.59	0.0310	0.0404	186.81

(1) Euro amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on the respective payment dates. For the year ended December 31, 2012, Euro amounts have been translated into U.S. dollars using the Noon Buying Rate in effect on April 5, 2013.

(2) Subject to approval at the Annual Shareholders Meeting to be held on April 17, 2013. Pursuant to Italian Stock Exchange rules, dividends on the Ordinary Shares and the Savings Shares are payable from the fourth trading day after the third Friday of each month, and in any case, at least four business days after the Shareholders Annual Meeting approving the dividends. Telecom Italia s dividend coupons for the year ended December 31, 2012, will be clipped on April 22, 2013, and will be payable from April 25, 2013.

Payment of annual dividends is subject to approval by the holders of Ordinary Shares at the annual general shareholders meeting, which must be held within 180 days after the end of the financial year to which it relates (pursuant to article 18, second paragraph, of the Company s Bylaws). In addition, Article 21 of the Company s Bylaws gives the Board of Directors the power to approve the distribution of interim dividends . Pursuant to Italian law, the distribution may be approved after the final approval of the preceding year s financial statements, and the interim dividends may not exceed the lower of (i) the difference between profits from the preceding fiscal year and amounts required to be attributed to legal and statutory reserves and (ii) available reserves. Once paid in compliance with applicable laws, shareholders cannot be required to repay interim dividends to the Company if the shareholders collected such dividends in good faith. Dividends not collected within five years from the date they become payable will be forfeited in favor of the Company. If profits are not fully distributed, additional reserves are created.

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

Dividends in respect of Ordinary Shares and Savings Shares held with Monte Titoli S.p.A. (**Monte Titoli**) are automatically credited to the accounts of the beneficial owners with the relevant participant of Monte Titoli, without the need for presentation by such beneficial owners of any documentation. See Item 10. Additional Information 10.4 Description of Capital Stock .

Arrangements between Euroclear or Clearstream and Monte Titoli permit the shareholders to collect the dividends through Euroclear or Clearstream. Holders of American Depositary Receipts (**ADRs**) are entitled to receive payments in respect of dividends on the underlying Ordinary Shares and Savings Shares, as the case may be, in accordance with the relevant Deposit Agreement.

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Item 3. Key Information **Dividends**

Dividends payable on the Company s Ordinary Shares and Savings Shares may be subject to deduction of Italian withholding tax. See Item 10. Additional Information 10.6 Taxation . Italian regulations do not contain any specific restrictions on the payment of dividends to non-residents of Italy. See Item 10. Additional Information 10.2 Exchange Controls and Other Limitations Affecting Security Holders .

Pursuant to Italian law, in connection with the payment of dividends, participants of Monte Titoli are required to supply to the Italian tax authorities certain information concerning the identity of non-resident shareholders holding Ordinary Shares or Savings Shares. Shareholders are required to provide their Italian tax identification number, if any, or alternatively, in the case of legal entities, their name, country of establishment and address, or in the case of individuals, their name, address and place and date of birth, or in the case of partnerships, the information required for legal entities and the information required for individuals with respect to one of their representatives. In the case of Ordinary Share ADSs and Savings Share ADSs owned by non-residents in Italy, Telecom Italia understands that the provision of information concerning the Depositary, in its capacity as holder of record of the Ordinary Shares and Savings Shares, as the case may be, will satisfy these requirements.

The Depositary, in accordance with instructions from Telecom Italia, will provide information to beneficial owners of Ordinary Share ADSs and Savings Share ADSs, that are considered U.S. residents for purposes of applicable law. To the extent such owners wish to benefit from reduced withholding tax rates on dividends under an income tax treaty, claims for such benefits must be accompanied by the required information. See Item 10. Additional Information 10.6 Taxation .

Item 4. INFORMATION ON THE TELECOM ITALIA GROUP

4.1 BUSINESS

4.1.1 BACKGROUND

The legal and commercial name of the company is Telecom Italia S.p.A. Telecom Italia is a joint-stock company established under Italian law on October 29, 1908, with registered offices in Milan at Piazza degli Affari 2. The telephone number is +39 (02) 85951. The company is recorded in the Milan Companies Register at number 00488410010, R.E.A. number 1580695, R.A.E.E. number IT08020000000799.

Our Depositary in New York (JP Morgan Chase) is presently located at 4 New York Plaza, New York, New York 10004.

The duration of the company, as stated in the company s Bylaws, extends until December 31, 2100.

On October 25, 2007, Assicurazioni Generali S.p.A. (**Generali**), Sintonia S.A. (**Sintonia**), Intesa Sanpaolo S.p.A. (**Intesa Sanpaolo**), Mediobanca S.p.A. (**Mediobanca**) and Telefónica S.A. (**Telefónica**), through their wholly owned subsidiary Telco S.p.A. (**Telco**), completed the purchase of the entire share capital of Olimpia S.p.A., which held approximately 18% of the share capital, from Pirelli & C. S.p.A. and Sintonia S.p.A.

5.6% of the ordinary share capital of Telecom Italia was contributed on the same date by Mediobanca and companies of the Generali group to Telco. As of October 25, 2007, the total investment held by Telco equaled 23.595% of Telecom Italia s ordinary share capital.

Telco was held by Generali (28.1%), Intesa Sanpaolo (10.6%), Mediobanca (10.6%), Sintonia (8.4%) and Telefónica (42.3%).

On March 20, 2008 Telco acquired a further 121.5 million Ordinary Shares and increased its ownership in Telecom Italia s ordinary share capital to 24.5%.

On December 22, 2009 Telco and Sintonia executed a purchase and sale agreement pursuant to which Sintonia acquired from Telco shares representing approximately 2.06% of Telecom Italia s share capital and Telco voluntarily reduced its share capital by acquiring and cancelling Sintonia s Telco shares and Sintonia left the shareholder group which controls Telco.

On February 29, 2012, Telefónica, Intesa Sanpaolo, Mediobanca and Generali entered into a new shareholders agreement for a period of three years on the same terms and conditions set out in the original Shareholders Agreement dated as of April 28, 2007 as it had been subsequently amended and supplemented (the **2012 Shareholders Agreement**).

Currently Telco interests are held by Generali (30.58%), Intesa Sanpaolo (11.62%), Mediobanca (11.62%) and Telefónica (46.18%). See Item 7. Major Shareholders and Related-Party Transactions for a description of the existing shareholder arrangements.

4.1.2 DEVELOPMENT

On February 8, 2013, Telecom Italia presented its 2013 2015 Plan. The 2013-2015 Plan sets out the primary strategic objective of the Telecom Italia Group over the next three years as well as a number of strategic priorities to achieve this objective. This objective focuses on continued deleveraging to reduce the Telecom Italia Group s net financial debt.

Telecom Italia also announced its intention to revise its dividend policy in order to bring it into line with its primary strategic objective of deleveraging the Group.

For more details, please see 4.1.7 Updated Strategy .

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4.1.3 Business

The Group operates mainly in Europe, South America and the Mediterranean Basin.

The Telecom Italia Group is engaged principally in the communications sector and, particularly, the fixed and mobile national and international telecommunications sector.

The operating segments of the Telecom Italia Group are organized according to the respective geographical location of the telecommunications business (Domestic Italy, Brazil and Argentina) and according to the specific businesses for the other segments.

The principal changes in the scope of consolidation in 2012 are as follows:

- **Matrix Other Operations**: the company was sold on October 31, 2012, and consequently excluded from the consolidation area.

The principal changes in the scope of consolidation in 2011 are as follows:

- companies entering the scope of consolidation:
  - **Tim Fiber Brazil Business Unit**: on October 31, 2011, we acquired a 100% stake in the company Eletropaulo Telecomunicações Ltda and a 98.3% stake in AES Communications Rio de Janeiro S.A., both telecommunications infrastructure operators in the states of São Paolo and Rio de Janeiro, now renamed Tim Fiber SP and Tim Fiber RJ, respectively. The original ownership interest in Tim Fiber RJ was subsequently increased to 99.1% and the remaining 0.9% was the object of a tender offer which was concluded at the end of February 2012 and brought the percentage interest to 99.7%. The acquisitions were carried out through the subsidiary Tim Celular S.A., into which the two companies were recently merged;
  - **4GH group Domestic Business Unit**: on July 27, 2011, the 4G Holding group entered the scope of consolidation (retail sale of telephony products) following the acquisition of 71% of the ordinary shares of 4G Holding S.p.A. which in turn holds 100% of 4G Retail S.r.l.; the two companies merged in 2012;
- companies exiting the scope of consolidation:
  - **Loquendo Domestic Business Unit**: on September 30, 2011, Loquendo S.p.A. was sold and consequently exited the scope of consolidation.

For further details please see Item 5. Operating and Financial Review and Prospects 5.2 Results of Operations for the Three Years Ended December 31, 2012 5.2.2. Reorganization of Business and Note Form, Content and Other General Information of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

Following is a summary description of the Telecom Italia group s principal geographical business areas.

Domestic Business Area

Telecom Italia operates as the consolidated market leader in Italy in providing telephone and data services on fixed-line and mobile networks for final customers (retail) and other operators (wholesale). Furthermore the Telecom Italia Sparkle group operates in the international wholesale sector.

Telecom Italia is one of three mobile operators authorized to provide services using GSM 900 technology in Italy and one of three operators authorized to provide services using GSM 1800 (formerly DCS 1800) technology in Italy. It is also one of four operators holding a UMTS authorization and providing third-generation telephony services in Italyand it is one of the three operators that acquired a 800MHz spectrum in 2011 to provide 4G services.

At December 31, 2012 the Telecom Italia Group had approximately 14.0 million physical accesses (retail) in Italy, a decrease of 0.7 million compared to December 31, 2011. This decrease reflects a market characterized by a continuing trend of customers replacing fixed lines with mobile, resulting in a continuing fall in fixed line

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accesses. The Wholesale customer portfolio in Italy reached approximately 7.2 million accesses for telephone services at December 31, 2012, an increase of approximately 0.1 million compared to December 31, 2011.

The broadband portfolio in Italy was 9.0 million accesses at December 31, 2012 (consisting of approximately 7.0 million retail accesses corresponding to a market share of approximately 52% and 2.0 million wholesale accesses), a decrease of approximately 0.1 million compared to December 31, 2011.

In addition, the Telecom Italia Group had approximately 32.2 million mobile telephone lines at December 31, 2012 in Italy, approximately stable compared to December 31, 2011.

Brazil Business Area

The Telecom Italia Group operates in the mobile and fixed telecommunications sector in Brazil through the Tim Brasil group which offers mobile services using UMTS and GSM technologies. Focus is also on continued 2G and 3G expansion while 4G roll-out begins. Moreover, with the acquisitions of Intelig Telecomunicações, Tim Fiber RJ and Tim Fiber SP, the portfolio of services has been expanded by offering fiber optic data transmission using full IP technology such as DWDM and MPLS and offering residential broadband services.

At December 31, 2012, the Telecom Italia Group had 70.4 million mobile telephone lines in Brazil (64.1 million at December 31, 2011).

Argentina Business Area

The Telecom Italia Group operates in Argentina and Paraguay through the Sofora Telecom Argentina group. In particular, in Argentina it operates in fixed telecommunications through the company Telecom Argentina and in mobile telecommunications through the company Telecom Personal; in Paraguay it operates in mobile telecommunications with the company Núcleo.

At December 31, 2012 the Telecom Italia Group had approximately 4.1 million fixed lines (in Argentina), 21.3 million mobile telephone lines (of which 19.0 million in Argentina and 2.3 million in Paraguay) and 1.6 million broadband accesses.

4.1.4 Disposals and Acquisitions of Significant Equity Investments in 2012

For a description of disposals and acquisitions of significant equity investments in 2012 please see Note Form, Content and Other General Information , Note Investments in Associates and Joint Ventures Accounted for Using the Equity Method and Note Other Investments of the

Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

4.1.5 Recent Developments During 2013

Possible integration with 3 Italia and project for the network separation

On April 11, 2013, the Telecom Italia Board of Directors examined the possible integration with 3 Italia and the progress of the project for the network separation.

Management reported on preliminary contacts with 3 Italia and its ultimate parent company Hutchison Whampoa (**HW**) on a business combination of the company with Telecom Italia, possibly via contribution in kind or merger, which the HW Group has made subject to the acquisition of an additional stake in Telecom Italia, such that the HW Group would become the leading shareholder of the Company.

The Board of Directors established a special committee, chaired by the Chairman of the Board of Directors (Director Franco Bernabè) and composed of the Lead Independent Director (Director Zingales), the Chairman of the Control and Risk Committee (Director Catania) and Directors Linares and Galateri, in order to verify within a short time the Company s interest in carrying on such a transaction.

Moreover, the Board of Directors mandated the management to define the operational process and the feasibility of the structural separation of the access network.

For a description of other recent developments please see Item 8. Financial Information 8.2 Legal Proceedings and Note Events Subsequent to December 31, 2012 of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

4.1.6 Overview of the Telecom Italia Group s Major Business Areas

The following is a chart of the Telecom Italia Group s Business Units as of December 31, 2012:

(*) Main subsidiaries: Telecom Italia S.p.A.; Telenergia S.p.A.; Telecontact Center S.p.A., PAth.Net S.p.A.; HR Services S.r.l. and Shared Service Center S.r.l.(now Telecom Italia Information Technology S.r.l.).

(**) With reference to the sale of La7 S.r.l., please see Note Events subsequent to December 31, 2012 of the Notes to the Consolidated Financial Statements included elsewhere herein.

On October 31, 2012, Telecom Italia S.p.A. completed the sale of its wholly-owned subsidiary, Matrix, to Libero, controlled by Weather Investment II S.à.r.l.. In 2012 Matrix was also moved to Other Operations and was consequently no longer part of Core Domestic in the Domestic Business Unit.

For further details about companies which are part of the various Business Units, please see Note List of companies of the Telecom Italia Group of the Notes to the Consolidated Financial Statements included elsewhere herein.

For the revenues, operating profit (loss), capital expenditures and number of employees of the Telecom Italia Group s Business Units please see Item 5. Operating and financial review and prospects 5.2 Results of operations for the three years ended December 31, 2012 5.2.5 Business unit financial data .

4.1.7 Updated Strategy

Strategic Priorities and Objectives of the 2013-2015 Plan

On February 8, 2013, Telecom Italia presented its updated 2013 2015 Plan. The 2013-2015 Plan sets out the Telecom Italia Group s primary strategic objective as well as a number of strategic priorities to achieve this objective over the next three years:

· continued deleveraging to reduce its net financial debt, through:

focus on strategic markets Italy, Brazil and Argentina with the goal of stabilizing consolidated revenues through the contribution from Latin America;

technological developments in fixed-line telephony and mobile telephony in Italy, mobile telephony in Brazil and network capacity in Argentina to take advantage of growing demand for data;

extension and acceleration of the Group s cost reduction policy in order to contribute to the financing of the above mentioned technological developments;

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sustainable shareholder remuneration. Telecom Italia announced its intention to revise its dividend policy in order to bring it into line with the continuing policy of deleveraging the Group.

Domestic market

In the Domestic market Telecom Italia, leveraging on its fixed and mobile network infrastructure, intends to:

· stabilize revenues;

· defend market share on traditional services through quality of service;

· grow innovative services leveraging on both access and applications services such as Cloud services;

· develop UBB (UltraBroadband) networks taking into account further developments in the regulatory framework and technological changes.

Brazil

Tim Brasil s strategic priorities are to:

· expand its customer base through FMS (Fixed Mobile Substitution);

· pursue high potential in mobile broadband penetration;

· continue network evolution, mainly through the increase of coverage on 3G and the roll out of the 4G network;

· satisfy the growing demand for Internet services, while optimizing capital expenditure.

Argentina

Telecom Argentina Group s strategic priorities are to:

- further build on its market share and its fixed and mobile platforms;
- enlarge its network capacity;
- support premium positioning on mobile to boost value added services revenues;
- fully exploit the high demand for data traffic.

There can be no assurance that these objectives will actually be achieved. See Introduction Cautionary Statement for Purposes of the Safe Harbor Provisions of the United States Private Securities Litigation Reform Act of 1995. .

4.1.8 THE ORGANIZATIONAL STRUCTURE

The following diagram highlights the organizational structure of the Telecom Italia Group as of April 10, 2013:

* * *

Andrea Mangoni will leave the Telecom Italia Group on April 30, 2013.

4.2 BUSINESS UNITS

4.2.1 Domestic

The Domestic Business Unit operates as the consolidated market leader in Italy in providing telephone and data services on fixed-line and mobile networks for final retail voice customers and other wholesale operators. In the international field, the Business Unit develops fiber optic networks for wholesale customers (in Europe, in the Mediterranean and in South America).

On October 31, 2012, Telecom Italia S.p.A. completed the sale of the company Matrix, a wholly-owned subsidiary, to Libero, controlled by Weather Investment II S.à.r.l.. In 2012 Matrix was also moved to Other Operations and was consequently no longer part of Core Domestic in the Domestic Business Unit.

The Domestic Business Unit is organized as follows as of December 31, 2012:

(*) Principal companies: Telecom Italia S.p.A., Telenergia S.p.A., Telecontact Center S.p.A., PAth.Net S.p.A., HR Service Center S.r.l. and Shared Service Center S.r.l. (now Telecom Italia Information Technology S.r.l.).

The principal operating and financial data of the Domestic Business Unit are reported according to two Cash-generating units (**CGU**):

- **Core Domestic**: Core Domestic includes all telecommunications activities within the Italian market. Revenues are divided according to the net contribution of each market segment to the CGU s results, excluding intrasegment transactions. The sales market segments defined on the basis of the customer centric organizational model are as follows:
  - **Consumer**: Consumer comprises the aggregate of voice and internet services and products managed and developed for individuals and families in the fixed and mobile telecommunications markets and public telephony;
  - **Business**: Business comprises the aggregate of voice, data, internet and ICT solutions services and products managed and developed for SMEs (small and medium enterprises) and SOHOs (Small Office Home Office) in the fixed and mobile telecommunications markets;
  - **Top**: Top comprises the aggregate of voice, data, internet and ICT solutions services and products managed and developed for Top, Public Sector, Large Account and Enterprise clientele in the fixed and mobile telecommunications markets;

- **National Wholesale**: National Wholesale consists of the management and development of the portfolio of regulated and unregulated wholesale services for fixed and mobile telecommunications operators in the Italian domestic market;

- **Other** (support structures):

  - Technology & IT: services related to the development, building and operation of network infrastructures, real estate properties and plant engineering, delivery processes and assurance regarding client services in addition to the development and operation of information services;

- Staff & Other: services carried out by Staff functions and other support activities performed by minor companies of the Group also offered to the market and other Business Units.

- **International Wholesale**: International Wholesale includes the activities of the Telecom Italia Sparkle group which operates in the international voice, data and internet services market aimed at fixed and mobile telecommunications operators, ISPs/ASPs (Wholesale market) and multinational companies through its own networks in the European, Mediterranean and South American markets.

v MARKETING CHANNELS AND DISTRIBUTION

As a result of the customer centric approach, Telecom Italia utilizes a sales structure as follows for each of its customer segments:

Distribution

The sales structure is organized according to a vertical, multi-channel approach, in which different types of distribution channels are specialized for different customer segments of the market, based on clusters of customers and services. This approach enhances the focus and customization of our products.

- ***Consumer***

Consumer customers are now managed by several channels focused on volume and value acquisitions, including:

- the *Push Sales Channel* consisting of an outbound telephone channel called Telesales with a network of approximately 18 partners having a total of 2,500 operators supported by 21 employees and the Agent channel made up of sales agents with a network of 40 partners with 700 sales agents assisted by 20 employees. An additional 59 employees support sales in the following Headquarters areas: Development, Coordination and Sales Management;

- the *Pull* channel: consisting of the retail network of shops, dealers, and organized and specialized large-scale distribution, amounting to a total of approximately 6,200 retail points of sale (at December 2012). Points of sale are geographically widespread and of many different types: direct; franchisee; monobrand; multibrand; organized and specialized large-scale distribution.

In addition to these partners, distribution also is done through the *Public Telephone* channel, a network of 17 partners focused on National and International prepaid card services and associated traffic packages.

- ***Business***

The business distribution channels are made up of:

- *BP Business Partner* channel (approximately 80): a network focused on standard offers with about 1,500 agents;
- *VAR Value Added Reseller* channel (approximately 70): a network organized geographically focused on VAS, customized solutions and complex networks (250 agents) and on ICT (200 agents);
- *Outbound Call Center:* 12 partners focused on specific canvass and loyalty activities;
- *Shops*: some specific shops (approximately 3,000) offering business products and assistance (14 Key Account).

- ***TOP***

The Top Customers department is organized in separate units, one dedicated to Private Top Customers (Large Companies, Banks, Insurance, etc), two dedicated to the Public Sector (Public Administration, Health, etc.) and four focused on Strategic, Large and Medium Enterprises. At the end of 2012 around 640 Sales personnel and about 143 Partner (Senior Account channel) had a dedicated portfolio to supervise and develop, supported by structures focused on pre-sales (e.g. offers design) and post sales processes (e.g. assistance). The main activities include:

- offering the whole range of services (fixed and mobile telephone, data, ICT services and products); and
- supporting the customer and providing assistance, when required.

· *National Wholesale Services*

The National Wholesale Services (**NWS**) division manages relationships with approximately 300 other telco operators, who can be both customers and competitors of Telecom Italia. These customers purchase Telecom Italia network and professional services to build services for their own customers.

In order to ensure complete management of the relationship with customers, the NWS Department is organized to cover all stages of the process:

- analysis of technological innovation, for New Products and Service Innovation Marketing;
- analysis of business evolution in wholesale market, for Marketing development;
- definition of the offer for wholesale regulated services, such as Interconnection, Data Services, Access Services; the offer is developed by the marketing group according to conditions and rules set by National and European Authorities;
- sales through direct vendors, which are supported by presales and project managers;
- contracts definition and disputes solution through specialized personnel;
- billing, credit and administrative activities, revenue integrity control; and
- caring and business process reengineering.

The NWS department is set up as an independent department, which allows Telecom Italia, along with other conditions (accounting separation, compliance with the resolutions of the Authorities) to manage transparency and fairness in its relationship with other operators, as well as compliance with all regulatory requirements.

v CUSTOMER AND LINES

The table below sets forth, for the periods indicated, certain statistical data of the Domestic Business Unit:

As of and for the years ended December 31,

	2012	2011	2010
DOMESTIC FIXED			
Physical accesses (thousand)(1)	21,153	21,712	22,122
Of which retail physical accesses (thousand)	*13,978*	*14,652*	*15,351*
Broadband accesses in Italy at year-end (thousand)	8,967	9,089	9,058
Of which retail broadband accesses (thousand)	*7,020*	*7,125*	*7,175*
Network infrastructure in Italy:			
access network in copper (millions of km pair, distribution and connection)	114.5	112.2	111.7
access and carrier network in optical fiber (millions of km fiber)	5.7	4.6	4.3
Network infrastructure abroad:			
European backbone (km of fiber)	55,000	55,000	55,000
Mediterranean (km of submarine cable)	7,500	7,500	7,000
South America (km of fiber)	30,000	30,000	30,000
Atlantic (km of submarine cable)	15,000	15,000	15,000
Total traffic:			
Minutes of traffic on fixed-line network (billions):	101.8	108.9	121.5
Domestic traffic	*85.9*	*93.3*	*104.1*
International traffic	*15.9*	*15.6*	*17.4*
DownStream and UpStream traffic volumes (PBytes):	2,202	1,937	1,647
DOMESTIC MOBILE			
Number of lines at year-end (thousand)	32,159	32,227	31,018
Change in lines (%)	(0.2)	3.9	0.5
Churn rate (%)(2)	26.6	21.9	22.0
Total outgoing traffic per month (millions of minutes)	3,664	3,633	3,305
Total average outgoing and incoming traffic per month (millions of minutes)	4,921	4,843	4,597
Mobile browsing volumes (PBytes)(3)	93.1	75.9	53.0
Average monthly revenues per line(4) (euro)	15.5	17.4	19.7

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(1) Total physical accesses includes broadband accesses.

(2) The data refers to total lines. The churn rate for the whole year represents the number of mobile customers who discontinued service during the period expressed as a percentage of the average number of customers.

(3) National traffic, excluding roaming.

(4) The values are calculated on the basis of revenues from services (including revenues from prepaid cards) as a percentage of the average number of lines.

At December 31, 2012 the Telecom Italia Group had approximately 14.0 million physical accesses (retail) in Italy, a decrease of 0.7 million compared to December 31, 2011. The Wholesale customer portfolio in Italy reached approximately 7.2 million accesses for telephone services at December 31, 2012, an increase of approximately 0.1 million compared to December 31, 2011.

The broadband portfolio in Italy was 9.0 million accesses at December 31, 2012 (consisting of approximately 7.0 million retail accesses corresponding to a market share of approximately 52% and 2.0 million wholesale accesses), a decrease of approximately 0.1 million compared to December 31, 2011.

In addition, the Telecom Italia Group had approximately 32.2 million mobile telephone lines at December 31, 2012 in Italy, stable compared to December 31, 2011.

v **MAIN CHANGES IN THE REGULATORY FRAMEWORK**

For the main regulatory events which occurred in 2012 that may have a significant impact on the operation of the Domestic Business Unit, please see Item 4. Information On The Telecom Italia Group 4.3 Regulation .

v **COMPETITION**

The market

The Italian telecommunications market continues to be highly competitive with significant pricing pressure, which has led to an ongoing decline in the traditional service components, particularly voice service.

In this context, the key element in the evolution of the market continues to be the increased penetration of broadband, particularly mobile, facilitated by the greater penetration of next-generation handsets.

The development of broadband has also led to an evolution of increasing competition, with greater interaction between players of different markets. This has opened the field to competition from non-traditional operators (in particular Over the Top companies OTTs and producers of electronic and consumer devices), as well as given telecommunication operators the opportunity to develop new network based services (mainly in the IT and Media fields).

For the legacy telecommunications operators, in addition to the core competition from the other traditional operators in the sector, there has been increased competition from OTTs and device producers who take advantage of their better understanding of the evolution of consumer trends, consumer electronics and software environments and who operate entirely in the digital world, basing their behavior on competition approaches that are completely different to those of telecommunications operators.

Over time, therefore, the traditional players business models have had to change to meet the challenges from the new entrants and to exploit new opportunities:

· in Media, broadcasters, who are vertically integrated players, continue to dominate the scene; however, with the Web becoming increasingly important as a complementary distribution platform, they are increasingly under pressure from consumer electronics companies and OTTS;

· in Information Technology (where Italy continues to have a level of investment relative to its GDP significantly lower than that of the United States and other European countries), the decline in revenues is driving the various players towards the cloud computing growth oasis as a way of protecting market shares in their respective core businesses. Telecommunications operators are expected to strengthen in this sector, including through partnerships;

- in the Consumer Electronics market, producers can develop services that can be used through the internet, building on handset ownership and management of the user experience, loosening or breaking the relationship between customers and telecommunications operators and competing with the media and OTTs, through games consoles and set-top boxes, for the role of net enabler through the living room screen;

- OTTs have, for some time now, been leading the transformation of the methods of use of telecommunications services (including voice), increasingly integrating them with Media and IT.

Conversely, with regard to the positioning of the telecommunications operators in converging markets, there are a number of aspects at varying levels of development:

- initiatives involving innovative services in the IT market with the expansion of Cloud services for business and consumer customers;

- new wireless applications such as Machine-to-Machine (MTM) and mobile payment;

- significant presence as enablers of online digital content use on the living room screen using OTT TV multidevice solutions.

Competition in Fixed-Line Telecommunications

The fixed-line telecommunications market is characterized by the rapid decline in voice revenues due to reduction in prices and the progressive shift of voice traffic to mobile. In recent years all the operators have attempted to offset this phenomenon by concentrating mainly on the ability to innovate their offering by developing the penetration of ADSL and introducing bundled voice, broadband and services deals (double play), in a highly competitive environment with consequent pricing pressure.

The evolution of the competitive product offering has also been influenced by consolidation, among competitors, of an approach based on the control of infrastructure (above all Local Loop Unbundling LLU). The main fixed operators are now also offering mobile services, as Mobile Virtual Operators (MVOs).

In 2012, the migration of customers from fixed-line to mobile telephony services continued, as well as the migration to alternative communications solutions (Voice Over IP, messaging, e-mail and social network chat) due to the widespread penetration of *personal* computers and tablets. For years, both for retail consumers and small and medium businesses, mature traditional voice services have been replaced by value-added content and services based on the internet protocol. This shift has been facilitated by the use of the internet and changes in user preferences, by the spread of broadband, personal computers and other connected devices, and by the quality of the service.

The competitive scenario in the Italian fixed telecommunications market is characterized by the presence, in addition to Telecom Italia, of a number of operators such as Wind-Infostrada, Fastweb, Vodafone-TeleTu, BT Italia that have different business models focused on different segments of the market.

At the end of 2012, fixed accesses in Italy numbered approximately 21.4 million, slightly (-3.2%) down from 2011 (22.1 million). The growing competition in the access market has led to a gradual reduction in Telecom Italia s market share.

In the broadband market, at December 31, 2012 fixed broadband customers in Italy numbered about 13.6 million with a penetration rate on fixed accesses of about 63%.

The spread of broadband is driven not only by the penetration of personal computers, but also by the growing demand for speed and access to new IP based services (Voice over IP, Content, social networking services, online gaming, IP Centrex, etc.). In 2012, however, the slowdown in growth of the fixed-line broadband market continued, due both to a general tendency of operators to concentrate on the growth of flat-rate plans (dual play) with higher added value and to the continuing weakness of the macroeconomic environment. The decline continued in revenues from the data transmission segment, which suffered the effects of competition that has led to reduction in average prices.

Competition in Mobile Telecommunications

The mobile market, although saturated and mature in its traditional component of voice services, continues to see growth in the number of mobile lines, driven by the increase in multiSIM/multidevice customers and in non-human lines (lines which operate with a SIM card but are not used for voice services such as an Apple iPad) (at December 31, 2012, mobile lines in Italy numbered about 97 million with growth of about 1% over 2011 and with a penetration rate of approximately 159% of the population).

Along with the progressive contraction in traditional service components, such as voice and messaging, which also reflect the increasing spread of communication apps , there has been significant growth in the mobile broadband market, which, in the last few years has been, and in the future will continue to be, the main opportunity for the strategic and commercial growth of the mobile telecom industry. This growth will be facilitated by the launch of Ultra Broadband fourth generation mobile phone systems.

In 2012, the growth in mobile broadband customers continued, both large and small screen, with a high penetration rate on mobile lines as a result of the increasing spread of smartphones and tablets.

Alongside innovative services that have already caught on and are under full-scale development, as in the case of mobile Apps, there are other market environments, associated with the development of mobile broadband, with major potential for growth in the medium term, such as mobile payment.

In the Italian mobile telecommunications market, competition is dominated by Telecom Italia and also by the infrastructured operators (Vodafone, Wind, H3G) which are focused on different segments of the market or have different strategies.

In addition to these operators, the field also includes mobile virtual operators (MVO), of which PosteMobile is the most important player. These operators currently have a limited share of the market, but continue to enjoy significant growth compared to infrastructured operators.

4.2.2 Brazil

The Telecom Italia Group operates in the mobile and fixed telecommunications sector in Brazil through the Tim Brasil group which offers mobile services using UMTS and GSM technologies. Moreover, with the acquisitions of Intelig Telecomunicações, Tim Fiber RJ and Tim Fiber SP (now merged into Tim Celular S.A.), the portfolio of services has been expanded by offering fiber optic data transmission using full IP technology such as DWDM and MPLS and offering residential broadband services.

The Tim Brasil group s services cover an area which includes around 95% of Brazil s urban population. Tim Brasil group has approximately 70.4 million mobile lines which covers each of the Brazilian states and the Federal District. As of December 31, 2012, its combined penetration reached approximately 132.7% of the Brazilian population and our combined market share totaled approximately 26.9%.

Since the Tim Brasil group began operating in the Brazilian market, its intention has been to provide its customers with state-of-the-art technology and services. This goal has been achieved through the offer of edge technology, that has allowed convergence between voice services either mobile or fixed , internet access and data transfer. Management believes this convergence has been made feasible with developments under 3G.

The table below sets forth, for the periods indicated, the number of mobile lines of the Brazil Business Unit:

	As of and for the years ended December 31,		
	2012	2011	2010
Number of lines at year-end (thousands)	70,362	64,070	51,015
MOU (minutes/months) (*)	135.8	128.6	116.0
ARPU (Reais)	19.1	21.4	23.7

(*) Net of visitors.

v **Marketing**

During 2012, Tim Brasil intensified promotional activity on voice plans and further expanded data services.

In the Consumer segment, TIM has continuously developed the Infinity and Liberty concept (prepaid and postpaid, respectively), adding the Plano Controle to its Liberty platform, in order to develop its own prepaid value base upon the migration to a Controle plane, boosting this segment s profitability. The profitability increase is possible because a Controle plan has hybrid characteristics, combining postpaid and prepaid benefits, giving the liberty and convenience of a postpaid plan and also allowing customers to control their expenses, like a prepaid user.

Gross acquisitions in 2012 amounted to 37.4 million new lines compared to 39.6 million new lines in 2011, a decrease of -5.7% over the corresponding period of 2011. Net additions in 2012 amounted to 6.3 million lines compared to 13.1 million lines in 2011, a decrease of -51.8% over the corresponding period of 2011.

In the Business segment, TIM continued to enhance and differentiate its offering, maintaining an emphasis on simplified service and transparency. TIM launched a number of new products and services based on the needs of its business clients and also maintained its focus on the provision of internet solutions, providing companies of all sizes with improved unlimited internet connectivity.

Main Plans marketed are:

- Infinity (Prepaid): customer is charged per call of unlimited duration to TIM numbers and local fixed telephones; for SMS and mobile internet services, clients are charged for day of use, and services are provided unlimitedly;

- Infinity Tri (Prepaid in Rio Grande do Sul): customer of Rio Grande do Sul are charged per day of use for voice (to TIM numbers and local fixed telephones), SMS and mobile internet services;

· Tim Beta (Prepaid): limited segmented plan addressed to young customers, charged per day for voice (to TIM numbers), SMS and mobile internet services;

· Tim Liberty: customer pays a fixed monthly rate; no limits on calls to any TIM number in Brazil, without limitation as to call, or call duration. Also, they may add further benefits to this plan using the Liberty Rádios plan to talk unlimitedly to any radio user (SME), without deduction from its package of minutes; and

· Liberty Controle: for customers that want no limits on calls to TIM numbers in Brazil, keeping bill under total control. Customers pay a fixed rate every month, no limits on calls to TIM numbers, and also receives bonus to use other types of calls/services.

In 2012, TIM improved its Combos offers (including minute package and handset), with focus on handsets that encourage the use of internet and value added services, as Smartphone, modems, and tablets. Combos had strong commercial appeal, either offering handsets or being associating with data offers.

TIM continued to aggressively market itself to larger companies as potential clients, offering, in addition to customized pricing plans, handset options under loan for use contracts.

v DISTRIBUTION

Tim Brasil s services are marketed through the largest distribution network in Brazil, with over 10,000 points of sale, among premium stores and dealers (exclusive or multi-brand), in addition to relying on the distribution capacity of a number of major retail chains. Tim Brasil s prepaid service customers rely, in addition to traditional points of sale, on alternative recharge channels, such as supermarkets and newsstands, totaling about 470,000 points spread all over Brazil. Sales of Tim Brasil s products and services are offered by Tim Brasil s sales personnel, as well as by authorized dealers. Most devices are sold on credit card and in 12 installments.

v MAIN CHANGES IN THE REGULATORY FRAMEWORK

For the main regulatory developments which occurred in 2012 that may have an economic impact on the Brazil Business Unit, please see Item 4. Information On The Telecom Italia Group 4.3 Regulation .

v COMPETITION

At the end of 2012, the Brazilian mobile market reached 261.8 million lines. This is 8.1% more than at the end of 2011 and a penetration of 132.7% of the population (123.9% in 2011). Net total line increases in 2012 was 19.5 million lines, 19.7 million fewer net lines than in 2011.

4.2.3 ARGENTINA

The Telecom Italia Group operates in the fixed and mobile telecommunications sector in Argentina mainly through Telecom Argentina and Telecom Personal (thereafter Personal), respectively, as well as mobile telecommunications operations in Paraguay through Núcleo. In particular, Telecom Argentina is one of the largest private-sector companies in Argentina. Telecom Argentina has a non-expiring license to provide fixed-line telecommunications services and also provides other telephone related services such as international long-distance service, data transmission, IT solutions outsourcing and Internet services. Personal has a non-expiring licence to provide mobile services in Argentina and Núcleo has a renewable license to provide mobile services in Paraguay.

(*) Holding companies.

(**) Non-operating companies.

Telecom Argentina s business strategy is focused on increasing its profitability and maximizing value generation for its customers, shareholders, employees and the broader community it serves. In order to promote the achievement of its goals in a sustainable and consistent manner, the Argentine Business Unit develops business plans according to the market and macroeconomic environment and invests in products and services innovation aimed at improving its customers user experience by adding content, interactivity and convenience to communication.

In **fixed services**, the growth was led by the increase in the Broadband business, as a result of a 5% increase in Internet accesses (reaching 1.6 million accesses as of December 31, 2012) and an 18% increase in the Broadband ARPU (access+ISP) compared to 2011. Fixed lines remained at 4.1 million as of December 31, 2012, the same level as at December 31, 2011.

In the **mobile business**, the Personal customer base increased by 0.8 million in 2012 reaching 19.0 million lines as of December 31, 2012 (of which 33% are postpaid contracts). At the same time, ARPU increased approximately 12% over the prior year. A large part of this growth can be traced to value-added services which, on the whole, accounted for approximately 53% of Personal mobile service revenues in 2012. Additionally, Personal successfully implemented number portability in 2012. Due to, among other things, enhanced retention efforts, number portability has so far not had any significant impact on Telecom Personal s revenues.

In Paraguay, Núcleo s customer base grew by about 7% over the prior year reaching 2.3 million lines at year-end, of which 19% were postpaid.

The table below sets forth certain operating data for the Argentina Business Unit as of and for the years ended December 31, 2012, 2011 and 2010:

	As of and for the years ended December 31,		
	2012	**2011**	**2010**
Number of fixed lines (thousands)	4,128	4,141	4,107
ARBU (Average Revenue Billed per User) (Argentine pesos)	48.2	45.7	42.8
Telecom Personal mobile lines (thousands)	18,975	18,193	16,333
MOU Telecom Personal (minutes/months)	99	99	102
ARPU Telecom Personal (Argentine pesos)	57.7	51.4	44.4
Nucleo mobile lines (thousands)(*)	2,301	2,149	1,878
Broadband accesses (thousands)	1,629	1,550	1,380
ARPU (Argentine pesos)(**)	102.3	87.0	76.1

(*) Wimax lines included.

(**) The calculation method was updated in order to exclude, from the customer base, the internet sticks sold to customers who already have ADSL access.

v **MARKETING**

Fixed Services

The residential fixed line business grew moderately in voice services based on the increase in the sale of subscription plans with monthly charges and the sale of supplementary services. Telecom Argentina has concentrated its efforts on satisfying its customers access demand, and increasing the ARBU (Average Revenue Billed per User). Regarding voice Value-added Services (VAS), focus was placed in the sale of VAS package offers and line maintenance service. Additionally, the portfolio of Aladino handsets was expanded.

In the Internet business, the leadership of the brand Arnet was based on effective communication with differentiated offers by segment and competitive prices. Also, the portfolio of access speeds available to customers was expanded during the year. With respect to VAS on broadband access, during 2012 focus was placed to increase the penetration of VAS by the expansion of the service portfolio such as: offers that combine mail, calls and Internet; Arnet Móvil (which provides access to Internet through the Personal 3G network) and Arnet Play (a video-streaming service for residential customers).

Corporate segment continued its strategy of providing converged solutions that integrate voice, data, Internet, multimedia, ICT, data centers and applications.

Mobile Services

Product and service offers developed during 2012 were focused on increasing customer acquisition and loyalty since the implementation of number portability in March 2012. With respect to high value customers, Personal continued to expand its portfolio of plans, adding a benefit that allows unused minutes during one month to be used in the next month and by launching innovative handsets. Also, Personal continued with the strategy of recharge benefits and differential benefits for members of Club Personal, Personal s loyalty program. Additionally, the benefit Grupo Familiar was launched, which is available for all lines belonging to the same family, by enabling them to talk and send SMS for free between themselves. Finally, Personal continued offering unlimited Internet per day (US$1 per day), a disruptive offer that allowed Personal to be considered as the industry benchmark.

With respect to Núcleo, during 2012 new packaged offers of voice, messages and data for the prepaid segment, and tailored plans for postpaid and Plan Control segments were launched. In addition, Núcleo consolidated its leadership in mobile Internet based on packaged offers for prepaid customers, at competitive prices. At strategic level, Núcleo performed retention and loyalty actions for high value customers, mainly through a major campaign to replace handsets. Finally, in the fourth quarter of 2012 Núcleo focused its actions in connection with the implementation of the number portability, assuming the role of educating the market regarding the benefits of portability.

v **Distribution**

During 2012, Arnet continued with multimedia communication campaigns that further served to strengthen brand positioning. With respect to web sites, their main target was to become a channel for the exploration of Telecom Argentina products and services and for the improvement of the relationship with its customers. The web sites focused on communicating in real time all the brand offers, creating a digital experience with both Arnet (Internet products and services) and Telecom (voice products and services) products, and enriching customer self-management. In this regard, during November 2012 *Mi Cuenta* (My Account) was launched, a web site that allows clients to view information and perform several tasks in a simple way.

During 2012 Personal s sales offices strengthened its model of management, with a focus on client counseling and education based on the sale of value added products, handsets upgrade and improved technology.

In addition, Personal opened new sales offices with a renewed design nationwide and the restyling, expansion and relocation of certain existing offices. The direct sale channel reinforced the comprehensive customer care to high-value customers, while the indirect sale channel Agents continued to increase, mainly based on the sale of VAS and smartphones.

Also, during 2012, Núcleo promoted self-management by its clients through the launch of the web portal My Personal World and by nontraditional channels such as social networks, SMS, chat and email.

v **Main changes in the Regulatory Framework**

For the main regulatory developments on the Argentina Business Unit which occurred in 2012, please see Item 4. Information On The Telecom Italia Group 4.3 Regulation .

v COMPETITION

The telecommunications markets in Argentina and Paraguay continue to show strong demand for new services and higher access speed in a fiercely competitive environment in the different business segments.

Specifically, in the mobile segment in Argentina, Personal is one of three operators offering services at the national level and competes with Claro (America Móvil group) and Movistar (Telefónica group). Following the introduction of number portability in 2012 competition has intensified. The acquisition and retention of high-value customers will continue to be central to Personal s strategy, which intends to lend support to mobile use through the launch of new products and services that not only enable retention of existing customers, but also put Personal in the position of being the preferred operator in the mobile sector in Argentina.

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In Paraguay, Núcleo, operates in a market featuring strong competition, especially since the implementation of number portability in Paraguay in November 2012. Its main competitor is Tigo (Millicom group).

In the broadband segment, the Argentina Business Unit operates through the Arnet brand and its competitors are mainly ADSL Speedy (Telefónica group), Fibertel (Clarín group), which offers broadband access services using cable modems, and Telecentro, which offers triple play plans.

4.2.4 MEDIA

On May 9, 2012 the Board of Directors of Telecom Italia Media approved the decision of the Board of Directors of Telecom Italia S.p.A. to start the process of selling the Media segment. As a result, in May 2012, a corporate restructuring was initiated, which resulted in the establishment of La7 S.r.l., a wholly-owned subsidiary of Telecom Italia Media S.p.A. With effect as of September 1, 2012, the television assets became part of this new company, through the contribution of a business segment by Telecom Italia Media S.p.A.

Following completion of the above restructuring, the Telecom Italia Media group is now organized into the following operating units:

- **La7**: includes the Telecom Italia Media s operations relating to the television broadcasters La7 and La7d and the Multimedia/Web area (La7.it and La7.tv) and is being sold;

- **MTV group**: includes the operations of MTV Italia and its subsidiary MTV Pubblicità relating to the television broadcasters MTV and MTV Music, the 360° Playmaker production unit, the production of multimedia musical platforms and satellite channels, in addition to MTV Mobile and Digital (Web);

- **Network Operator (TIMB)**: includes the operations of Telecom Italia Media Broadcasting relating to managing the digital broadcasting networks of La7 and MTV and the Digital Multiplex channels operated by the Group, in addition to accessory services and radio and television broadcasting platforms offered to Group companies and third parties.

As of December 31, 2012, the Business Unit was organized as follows:

The table below sets forth, for the periods indicated, certain statistical data of the Media Business Unit:

	As of and for the years ended December 31,		
	2012	2011	2010
La7 audience share Free to Air (average during the period, in %)	3.5	3.8	3.1
Gross advertising revenues (millions of euros)	225	242	208

At December 31, 2012, the three Digital Multiplexes of Telecom Italia Media Broadcasting cover 94.9% of the Italian population.

v **MAIN CHANGES IN THE REGULATORY FRAMEWORK**

For the main regulatory events which occurred in 2012 that may have an economic impact on Media Business Unit, please see Item 4. Information On The Telecom Italia Group 4.3 Regulation .

4.2.5 OLIVETTI

The Olivetti group mainly operates in the manufacture of office products and services for Information Technology. It carries out Solution Provider activities to automate processes and business activities for small and medium-size enterprises, large corporations and vertical markets.

The Business Unit s markets are mainly in Europe, Asia and South America.

Effective January 1, 2012, the contact center business and resources of Advalso S.p.A. were sold to Telecontact Center S.p.A. (a subsidiary of Telecom Italia Domestic Business Unit), under the project aimed at unitary management under the control of Telecontact Center of the call center activities conducted in the Telecom Italia Group. Moreover, on June 13, 2012, the shareholders meeting of the subsidiary Olivetti I-Jet S.p.A. approved the wind-up of the company.

As of December 31, 2012, the Olivetti Business Unit was organized as follows (the main companies are indicated):

v **COMPETITION**

Competition continues to have an adverse effect on Olivetti revenues. It resulted in lower prices for many products and services reflecting a market subject to significant price pressure. This is also attributable to customers having reduced their IT budget.

4.2.6 COMPETITION

We face domestic competition in all of our businesses. Competition continues to have an adverse effect on our revenues as it resulted in lower tariffs for many of our products and services as well as the introduction of flat-rate pricing plans which have been used to enhance retention efforts but at the same time reducing revenues from such customers.

For details please see Item 4. Information on the Telecom Italia Group 4.1 Business 4.1.7 Updated Strategy , Item 4. Information on the Telecom Italia Group 4.2.1 Domestic and Item 4. Information on the Telecom Italia Group 4.2.2 Brazil and Item 4. Information on the Telecom Italia Group 4.2.3 Argentina .

4.3 REGULATION

The EU regulatory framework

Telecom Italia s operations in the European Union (**EU**) are subject to the EU framework on telecommunications regulation which includes directives, regulations, recommendations and communications. As such, being a member of the EU, Italy is required to implement the directives issued by the EU. Regulations, however, adopted at the EU level have general application and are binding and directly applicable in each EU Member States without the need of further national implementation. Recommendations and communications, on the other hand, are not legally binding although politically important.

The European Commission began liberalizing the telecommunications market to competition in the late 1980s and early 1990s. In Italy, as well as in all the main EU Member States, liberalization opened up competition of public voice telephony and public network infrastructure in 1998.

The need for a revision of the 1998 framework emerged from the growing convergence between telecommunications, broadcasting and information technology. A new EU Regulatory Framework (consisting of five Directives: the framework; access and interconnection; authorization; the universal service and users rights; privacy and data protection directives) was adopted in 2002, regulating all forms of fixed and wireless telecommunications, data transmission and broadcasting.

A recommendation adopted in February 2003, on relevant product and service markets susceptible of ex ante regulation, completed this set of legal instruments. In December 2007, the European Commission (**EC**) amended this first Recommendation on relevant markets, reducing the previous 18 markets susceptible to ex-ante regulation to 7: retail access at a fixed location (market 1) and, at wholesale level, call origination at a fixed location (market 2); call termination at a fixed location (market 3): wholesale (physical) network infrastructure access (including shared or fully unbundled access) at a fixed location (market 4); wholesale broadband access (market 5); wholesale terminating segments of leased lines (market 6) and voice call termination on mobile networks (market 7).

The EU regulatory framework obliges National Regulatory Authorities (**NRAs** **,** in Italy **AGCom**) to run market analyses before imposing appropriate obligations on individual operators having Significant Market Power (**SMP**) according to specific EU guidelines. A company is deemed to have SMP if, either individually or jointly with others, such company enjoys a position equivalent to dominance, that is to say a position of economic strength providing the company itself with the power to behave, to an appreciable extent, independently of competitors, customers and ultimately consumers. Market shares are normally used as a proxy for market power: while undertakings with market shares of no more than 25% are not likely to enjoy a (single) dominant position, single dominance concerns normally arise in the case of undertakings with market shares of over 40% and market shares in excess of 50 % are in themselves, except in exceptional circumstances, evidence of the existence of a dominant position.

The market analyses carried out by NRAs are subject to the assessment of the EU Commission which, to a certain extent, can challenge the NRAs findings, having a veto power on the definition of the market and on the identification of SMP operators. As per the choice of remedies the EU Commission has no veto power but can raise serious doubts after which the Body of European Regulators for Electronic Communications (**BEREC**) is required to give an opinion. The EU Commission, BEREC and the NRA involved then have to cooperate to find a solution within three months. Neither the Commission nor BEREC are able to make a binding intervention. Should a NRA decide not to amend or withdraw a draft measure after the EU Commissions expresses serious doubts, it shall provide a reasoned justification .

The EU legal framework was revised in November 2007, with the aim of defining a new European regulatory framework for the sector.

The revision of the framework established a set of rules composed of the Better Regulation Directive (Directive 2009/140/EC, amending the Framework , Access and Authorisation directives) and the Citizens Rights Directive (Directive 2009/136/EC amending the Universal Servic E-Privacy directives and the Regulation 2006/2004 on Consumer Protection Cooperation) to be transposed into national laws of the 27 EU Member States by May 25, 2011 and by the Regulation which was directly applicable establishing the new European Telecoms Authority BEREC . The new EU telecoms rules were officially adopted on December 18, 2009.

The revised directives were transposed into the Italian legal framework by means of the *Legge Comunitaria* 2010 which was published in the Italian Official Journal on January 2, 2012; the Italian Government was delegated the authority to adopt (within three months) measures aiming at transposing the revised directives. The Legislative Decrees of May 28, 2012 (n. 69 and 70) transposing the EU 2009 regulatory framework entered into force on June 1, 2012.

Telecommunication Regulatory Framework in Italy

The legal basis for the electronic communications sector in Italy is as follows:

(i) Law 36 of February 22, 2001 aimed at protecting the population from the effects of the exposure to electric, magnetic and electromagnetic fields and Prime Ministerial Decree (Decreto del Presidente del Consiglio dei Ministri DPCM) of July 8, 2003, which sets up Exposure limits, attention values and quality goals to protect the population against electric, magnetic and electromagnetic fields generated by frequencies between 100 KHz and 300 GHz ;

(ii) the Electronic Communications Code (**ECC**), which transposed into national law the EU Access, Authorisation, Framework and Universal Service directives;

(iii) Data Protection Code ;

(iv) the Consolidated Law on Radio-Television containing the principles regulating the organization of radio-television system and its convergence with different means of interpersonal and mass communications;

(v) the Consumer Code ;

(vi) Legislative Decree October 3, 2006, n. 262 which contained Urgent measures regarding tax and financial issues and, partially amended the sanctions regime set by the ECC by introducing further examples of administrative offences, a generalized increase in the fines for each sanction and the elimination of the partial cash settlements of fines;

(vii) Decree Law January 31, 2007, n. 7 containing urgent measures for the protection of consumers, for the promotion of competition, for the development of economic activities. The above mentioned law impacts the electronic communications sector by prohibiting top-up charges and the expiration of phone traffic for prepaid phone cards;

(viii) Legislative Decree May 30, 2008, n. 109 transposing into national law the EU Directive 2006/24/EC on the retention of data generated or processed in connection with the provision of publicly available electronic communications services or of public communications networks;

(ix) Law June 18, 2009, n. 69 providing measures to simplify the procedures for the installation and development of optical fiber networks (Article 1 Broadband);

(x) Decree Law July 6, 2011, n. 98, enacted by Law July 15, 2011, n. 111 further simplifying the procedure for the installation of small mobile equipment (0.5 sq. radiator area) and low power equipment (7 watt);

(xi) the 2011 Budget Law (Law December 13, 2010, n. 220), regulating the procedures for the issue of 800, 1800, 2000 and 2600 MHz frequencies rights of use;

(xii) Decree Law October 18, 2012 n. 179 (enacted by Law December 17, 2012 n. 221) providing for further broadband network funding to cancel the digital divide, measures to accelerate the roll-out of mobile fourth generation networks and administrative simplifications for optical fiber layout;

(xiii) Decree Law February 9, 2012 n. 5 (enacted by Law April 4, 2012 n. 35) imposing on Telecom Italia two further obligations: a) the disaggregation of maintenance costs for lines in unbundling; and b) the possibility for OLOs to buy ancillary services from third parties;

(xiv) the 2013 Budget Law (Legge di Stabilità 2013) modifying art. 96 of the Italian Communication Code regarding mandatory services required by public authorities to telecom operators for crime prevention and punishment purposes.

Furthermore, the ECC confirmed the responsibilities of the Ministry of Communications and of AGCom as set by the previous legislation. In particular:

(i) the Ministry is responsible for postal services, telecommunications, multimedia networks, informatics, telematics, radio and television broadcasts and innovative technologies applied to the communications sector. In May 2008, the functions of the Ministry of Communications and its resources were transferred to the Ministry of Economic Development;

(ii) AGCom is an independent regulatory authority granting fair competition among operators and protecting consumers. It must report on its activities to the Italian Parliament, which set up its powers, defined its bylaws and elected its members.

4.3.1 Telecommunication Regulation in Italy

In July 2008, Telecom Italia proposed to AGCom several undertakings related to its access network (**Undertakings**) aimed at integrating and strengthening the non-discrimination obligations (imposed by AGCom in 2002) amongst Telecom Italia s own retail divisions and other operators in the provision of wholesale access network services.

AGCom approved Telecom Italia s Undertakings, which are divided into 14 main groups and pursue four main goals:

- offering additional guarantees of equal treatment amongst Telecom Italia s commercial divisions and other electronic communications operators (Operators) purchasing wholesale access services from Telecom Italia;
- providing benefits to Operators and final users, through the improvement in the quality of the fixed access network and of related services;
- making the evolution of Telecom Italia s fixed access network more transparent for Operators; and,
- ensuring the maintenance of competitive conditions in the migration towards new generation networks.

Following the AGCom approval of the Undertakings, a number of proceedings which could have resulted in sanctions against Telecom Italia were suspended.

At the beginning of 2008, Telecom Italia created its Open Access department, a separate business unit focusing its activities on the implementing the Undertakings. To ensure equal treatment for its own retail divisions and those of the Operators (internal-external equal treatment), Telecom Italia undertook a set of activities focused on three main areas:

- technical-organizational domain: solutions for the improvement of internal delivery processes and to assure that SMP services were adopted;

- cultural-behavioral domain: a Code of Conduct has been adopted and intensive training activities have been carried out in order to spread the principles of internal-external equal treatment; and,

- economic-regulatory domain: service contracts were drafted and transfer charges adopted to implement equality of economic treatment.

The implementation of the Undertakings, their complexity and their impact on the stakeholders system, required the creation of a governance system. In particular, the following bodies were set up: an independent body (the **Supervisory Board**) and the AGCom Undertakings Monitoring Group for the monitoring of the work in progress (**GMI**) and the Italian Office of Telecommunications Adjudicator (**OTA Italia**), whose mission is to prevent and settle disputes amongst Operators and the **Next Generation Network Committee** submitting possible solutions to technical, organizational and economic issues raised by the transition to the Next Generation Network.

In November 2011, three years after the formalization of the Undertakings AGCom recognised that Telecom Italia had fully implemented all the Undertakings and terminated certain proceedings against Telecom Italia that were suspended following the approval of the Undertakings.

At the end of 2012, 45 Operators had joined in the New Delivery Process (**NDP**) for Bitstream, 17 Operators for Local Loop Unbundling (**LLU** and 12 Operators for Wholesale Line Rental (**WLR**).

GMI continues to monitor the implementation of the Undertakings.

After the AGCom s positive assessment and the notification to the European Commission, the access network operational separation model adopted by Telecom Italia can be considered a new European regulatory model and a viable alternative to the Access Network Functional Separation adopted by British Telecom (Open Reach).

Telecom Italia s Operational Separation model will further continue to ensure quality of treatment (both in economic and technical terms), the promotion of an Equivalence Culture , through personnel formation programs, and transparency to alternative network operators (AltNets) for both Copper and Fiber Access Network.

In July 2012, Telecom Italia submitted to AGCom the undertakings to be applicable to new generation access network services.

Market analyses

Following a first round (2006-2007) and a second round (2008-2009) of market analyses, in December, 2010, AGCom started the third round of market analyses reviewing the mobile termination market to define the relevant market, identifying SMP Operators and setting regulatory obligations on SMP Operators. The final decision was published on November 2011 containing the new glide path for Mobile Termination Rates (MTRs) for the period from July 1, 2012 to July 1, 2013. With respect to fixed markets, the third round of market analysis on wholesale and retail access markets was launched in September 2012.

The main developments regarding markets in the electronic communications sector that occurred in 2012 and in the first quarter of 2013 are described below.

· **Retail-fixed markets**

As a result of the first round of fixed retail market analyses, AGCom identified Telecom Italia as SMP operator and imposed regulatory obligations, including a price cap mechanism and price control.

In particular, the relevant retail fixed regulated markets included: access to the public telephone network provided at a fixed location for residential and business customers (markets 1 and 2); local, national and fixed-mobile services markets retention component only for residential and non-residential customers (markets 3 and 5, removed from the revised 2007 Recommendation); international telephone services, for residential and non-residential customers, provided at a fixed location (markets 4 and 6, removed from the revised 2007 Recommendation); leased lines market (market 7, removed from the revised 2007 Recommendation).

At the end of 2009, AGCom concluded the second round of assessment of **the international calls market** and of the minimum **set leased lines market** and deregulated both markets withdrawing all *ex ante* obligations on Telecom Italia starting from 2010.

In 2010 AGCom concluded the second round of market analysis of the **national retail fixed voice services**. As a consequence, AGCom decided to withdraw all regulatory obligations starting from six months after the publication of its final decision. In the transitional six-month period (until January 12, 2011), AGCom maintained the obligation of prior notification of new tariffs. Since January 12, 2011 Telecom Italia has been allowed to fix retail tariffs without prior notification to or approval by AGCom.

In September 2010, AGCom set new rules for the assessment of Telecom Italia s retail offers, including non-standard offers (public tender and tailored top business offers) and bundles (multiple-play offers). The new **price test methodology** is based on a replicability test developed on the basis of the following key principles: (i) a single replicability test valid for offers commercialized in different (both traditional and innovative) contexts, reference to the most efficient technology and network architecture that could be used by AltNets to replicate Telecom Italia s offers and, hence, to a combination of wholesale inputs (ULL, WLR, bitstream, etc.); (ii) the evaluation of network and downstream AltNets costs on the basis of avoidable or long run incremental costs;

(iii) application of the price test to the whole bundle, taking into account the overall cost of provisioning without considering whether each component of the bundle may be replicated by an alternative operator; (iv) *ad hoc* assessment of offers within tenders, taking into account the most efficient network architecture that could be used by AltNets to compete in a specific context. Following the publication of the AGCom document Circolare Attuativa (July 8, 2011), Telecom Italia asked for its revision. AGCom started a preliminary investigation and, in June 2012, rejected Telecom Italia s requests, stating that its *on-going practice* allowed the resolution of the critical procedural aspects claimed by Telecom Italia.

In 2012, Telecom Italia introduced a set of measures to simplify the tariff structure of the basic offers for both consumer and business customers. The last step of this simplification path is the new pricing schemes that Telecom Italia introduced early in 2013. For business customers, starting from January 1, 2013, the basic offer will consist of a single charge for all national calls, a price reduction for fixed-to-mobile calls and a change in the connection fee. For the consumer customers basic offer, starting from April 1, 2013 Telecom Italia introduced price simplification based on the introduction of a single price for all national and fixed-to-mobile calls, a change in the connection fee and the introduction of a discount equal to 50% for all national calls lasting more than three hours (the pricing is per 60 seconds telephone fees charged in advance). The tables below summarize the standard offers schemes described above:

Business prices (VAT not included)

cent/minut (VAT not included)	Previous prices (until 12/31/2012)	New prices (from 01/01/2013)
Local	1.0	0.0
National	7.0	0.0
Fixed-Mobile (TIM, Vodafone, Wind, Tre, etc.)	8.0	3.0
Set up fee	10.0 cent	20.0 cent

Consumer prices (VAT included)

cent/minut (VAT included)	Previous prices (until 03/31/2013)	New prices (from 04/01/2013)
Local and national	1.90	5.0(*)
Fixed-Mobile (TIM, Vodafone, Wind, Tre, etc.)	9.0	5.0
Set up fee	7.94 cent	5.0 cent

(*) Over 3 hours/ month, 50% discount.

With respect to the **retail access market**, AGCom reduced regulatory constraints removing, starting from 2010, the price cap mechanism used to control residential and business subscriber monthly fees, now subject only to a price test (see above for details), in order to ensure replicability by an efficient operator. At the same time, AGCom maintained the obligation to notify prices and conditions 30 days in advance of the commercial launch (instead of the previous 60 days), but a clause of tacit approval at the end of the notice period was introduced. As for bundling services, the previous prohibition has been withdrawn as a consequence of the increased demand for Telecom Italia s WLR offer.

Starting from April 1, 2013, an increase of the RTG consumers monthly fee entered into force (from 16.6/month, VAT included, to 17.40/month, VAT included) to adjust the fees for inflation; prices of the ISDN monthly fee and of all business connections monthly fees have not been changed. Starting from April 1, 2013, Telecom Italia also introduced a single fee for the resolution of the contract after the first 12 months. This fee applies to all customers (consumer and business), whenever the resolution of the contract is not due to Telecom Italia. Such a fee was reduced from 48.40 or 60.50 VAT included (respectively for the single line/ADSL for anticipated or contextual resolution of the contract fee of both service components) to 34.90 VAT included.

With the aim to ensure the start-up of Telecom Italia s commercial **optical fiber retail offers**, pending the implementation of NGA regulation (see the Wholesale fixed markets paragraph for further details), AGCom authorized (in December 2012) Telecom Italia to launch NGAN retail offers in areas where NGAN services were already offered by other operators. It provided that: (i) the service should be offered only in towns where

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comparable offers by other alternative operators were already in place (Milan, Rome, Turin, Bologna, Genoa, Naples and Bari); (ii) the maximum number of Telecom Italia connectable customers premises should be of 40,000 units; and (iii) wholesale ultra broadband offers shall be provided at prices based on the retail price reduced by a given percentage in the ranges of 20%-30% (*retail minus* approach). After 60 days from the approval of the new NGA wholesale offers, Telecom Italia may launch offers not limited by the above restrictions.

· **Wholesale fixed markets**

The first round of market analyses for fixed wholesale markets was concluded in 2006. In particular, the following markets were analyzed: Call origination (market 8); Call termination (market 9); Transit services (market 10, removed from the revised 2007 Recommendation); Unbundled access (including shared access) to metallic loops and sub-loops for the purpose of providing broadband and voice services (market 11); Broadband access (market 12); Terminating segments of leased lines (market 13) and Trunk segments of leased lines (market 14, removed from the revised Recommendation).

As a result of market analyses, AGCom in 2006 imposed on Telecom Italia, as SMP operator, regulatory measures including price control in the form of a network cap (except for the wholesale broadband access market).

The network cap mechanism was applied to calculate the prices of wholesale call origination, termination and transit services and of unbundled network-access services (i.e. Local Loop Unbundling and Shared Access). This mechanism was also applied to circuits, with the aim of ensuring that cost orientation is used to calculate the prices of the termination and long-distance circuit segments.

Following the conclusion of the second round of market analyses of the **wholesale access market**, in December 2009, AGCom confirmed the current regulatory regime applicable to wholesale access obligations on copper infrastructure (unbundling and *bitstream*), whereas, with regard to price setting, for the period May 1, 2010 to December 31, 2012 a network cap mechanism based on a Bottom-Up Long-Run Incremental Cost (**BU-LRIC**) model was re-introduced. Following the adoption of the above-mentioned cost model, in November 2010 AGCom set new wholesale rates for the following wholesale services: unbundling, bitstream and WLR and the value of weighted average cost of capital (**WACC**) related to wholesale access services to be applied from May 2010 to December 2012. The WACC was set at a value equal to 9.36%. AGCom set the following LLU monthly fees: 8.70/month as of May 1, 2010; 9.02/month as of January 1, 2011; and 9.28/month as of January 1, 2012. The increases in the LLU monthly fee and in other wholesale services for the 2011-2012 periods were, however, conditioned on the assessment, by AGCom, of the parameters related to network quality improvement and to the updating of Telecom Italia s access network. Following evaluation by an external auditor, AGCom s assessments were positive and, therefore, Telecom Italia was allowed to increase the intended wholesale prices.

Referring to the **WLR service**, AGCom required Telecom Italia to provide the service, only in the areas where disaggregated access services are not offered. The price for the service was calculated according to the network cap method, for the period from May 1, 2010 to December 31, 2012, based on a BU-LRIC model (see above), instead of the previous retail-minus regime. However, at the end of May 2012, AGCom approved the 2012 WLR Reference Offer with reference to the technical conditions launching a public consultation at national level on the WLR monthly fee. The above procedure did not imply any market analysis in contrast, according to Telecom Italia, to the regulatory certainty principle. In this procedure, AGCom proposed a monthly rental fee equal to 11.90/month which should be applied from June 1, 2012 *versus* the 12.88/month previously established. The AGCom introduced this reduction on the basis of new market conditions which would make the AltNets retail offers based on WLR (in areas not suitable for LLU) non-profitable. In addition to AGCom failing to utilize proper market analysis in establishing the amendment of the 2012 WLR monthly rental mentioned above, Telecom Italia reiterated to AGCom the non-existence of competitive issues in the areas not suitable for LLU, in the light of the fact that, despite a decline in the fixed line market, the WLR service availability was continuously increasing. At the end of December 2012, AGCom with Decision 643/12/CONS set a monthly rental fee equal to 11.70/month to be applied from June 1, 2012.

In September 2012, AGCom launched the third round of market analysis on wholesale and retail access markets. As a result, a new network cap for wholesale access services over copper was supposed to be set for the 2013-2015 period. However, the decision aimed at defining the new network caps obliged AGCom to impose on Telecom Italia the obligation to breakdown the costs of maintenance services for the supply of LLU lines and the acquisition of maintenance services from third parties. However, AGCom itself underlined within the above decision that the EU Commission had formally opened an infringement procedure against Italy, in relation to the possible breach of the Framework Directive (July 2012) since the abovementioned law violates the autonomy and independence of the National Regulatory Authority. On February 21, 2013, the European Commission issued a reasoned opinion in which it considered this matter the comments received from the Italian Government as unpersuasive. As a consequence, the Italian Government shall, within two months, comply with the EU reasoned opinion and change the law accordingly. The Italian Government preliminarily discussed in March 2013 and is going to approve within the decree law aimed at transposition in the Italian framework the EU rules (Legge Comunitaria 2013) a specific provision aimed at withdrawing the AGCom obligation to impose on Telecom Italia the disaggregated offer for its LLU ancillary services independently of its autonomous decision based on a market analysis procedure. The formal approval of this law by the Italian Parliament is expected to end the infringement procedure by the European Commission.

Pending the conclusion of the third round of market analyses on the wholesale and retail access markets, AGCom extended the economic conditions of the wholesale access services published in the Reference Offers approved for the year 2012(LLU, Bitstream and WLR services).

However, on December 20, 2012, following the request by the European Commission to make the cost positioning between the LLU, WLR and Bitstream fixed line wholesale services consistent, the Authority launched two public consultations on the 2013 pricing of WLR services and of Bitstream services, anticipating the results of the analysis to be carried out during the third round of market analyses in the retail and wholesale access markets up to 2013. In particular, AGCom proposed the reduction of 2013 Naked Bitstream access monthly fee from 19.50 to 17.50 (-10.3%) while confirming the analogue WLR monthly fee (11.70) set for the period June-December 2012. As to LLU, on March 27, 2013 a public consultation was opened aimed at defining 2013 prices. Following the above public consultation the new prices for shared access, sub-loop unbundling as well as a first increase of WACC will also be defined. In particular, AGCom decided for submit for public consultation the following ranges of prices related to the monthly rental fees: 8.62 - 9.25 for LLU (9.28 in 2012), 5.75 - 6.17 for sub-loop unbundling (6.19 in 2012) and 0.79 - 0.96 for shared access (1.35 in 2012), including a WACC value of 9.83% (currently at 9.36%). As a consequence, due to the above, the third round of market analyses on the wholesale access market will focus on setting prices and WACC value for the 2014-2016 period (instead of the 2013-2015 period).

In the meantime (March 25, 2013), the Council of State granted the requests filed by Eutelia and WIND, and issued a decision on the 2010-2012 market analysis setting the fees for WLR and Naked Bitstream services. The Council of State focused on the AGCom decision to anchor the network cap mechanism for the above mentioned fees on a retail minus method rather than on a cost orientation one, stating that the decision lacks proper ground and rationale. AGCom has to issue a new statement; however the new decision may not necessarily be different from the previous one, i.e. AGCom can confirm the previous decision providing a more sound legal and economical ground.

In order to complete the **NGAN set of rules** published, in February 2012, AGCom opened three proceedings aimed at introducing: 1) a cost model for the pricing of passive and active wholesale services and the definition of the so called NGAN competitive areas where price of fiber based bitstream and virtual access services are not subject to the cost orientation obligation; 2) potential regulatory amendments of the copper sub-loop unbundling service in light of the possible introduction of the vectoring technology on Fiber To The Cabinet Very High-speed Digital Subscriber Line (**FTTCab-VDSL**) accesses; and 3) the perspective enforcement of symmetric obligations on all operators, for the access to fiber vertical wiring and to building connection segment. In February 2013, the foregoing proceedings were included in the 3rd round market analysis procedure on wholesale and retail access markets while on March 28, 2013 a new public consultation was opened on symmetric regulation for the access to fiber vertical wiring and to building connection segment.

On February 28, 2013, AGCom approved with modifications Telecom Italia s first NGA Reference Offers for passive infrastructure access and wholesale broadband access. For 2012 AGCom approved, among other things, lower than initially proposed monthly fees for the new local level Ethernet bitstream access product (VULA). In details, the monthly rental for VULA over FTTC (30/3 Mbps, naked access) was set at 21.51 (Telecom Italia s initial proposal 31.01 with a reduction of -31%) and for VULA over FTTH (100/10 Mbps) was set at 24.90 (Telecom

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Italia s initial proposal 38.00 with a reduction of -35%). With respect to the hi-house fiber wiring, actual bottleneck of the NGA distribution network, the monthly rental fee was set at 5.96 compared with the Telecom Italia s proposal equal to 9.50 (with a reduction of -37%).

With respect to **migration between operators**, AGCom revised fixed-line customer migration rules, substantially reducing the processing times (reduced to five days as of March 2010) for the donating operator to verify the recipient s migration request (so called Phase II). Moreover, in cases where migration is not requested, the user will have the right to restore, free of charge, the previous configuration within five working days. Furthermore, in order to prevent the activation of services not requested by retail customers fixed-line operators introduced (starting from February 2011) an individual security code provided to the customer when they sign the contract for the access service. Finally, with Decision 62/11/CIR, published on July 2011, the daily capacity of each operator for the migration order management has been increased by 60%.

The regulatory framework should gradually reduce the above-mentioned timeframe.

With reference to **fixed call termination and origination**, in April 2011, AGCom approved fixed interconnection charges from July 1, 2011 to the end of 2013 (prices provided for call origination were set equal to the ones for call termination). In particular, with respect to fixed termination rates (**FTRs**) of both Telecom Italia and AltNets having SMP, AGCom set 2011 prices at the same level as 2010, therefore maintaining AltNet asymmetric prices equal to Telecom Italia s termination charge for the SGT level. Moreover, AGCom deferred to 2012 the application of symmetric termination fares, equal to Telecom Italia s tariff at local exchange level (**SGU**), among the AltNets and Telecom Italia itself. AGCom, finally, decided that, starting from 2013, only IP termination would be regulated, with a single symmetric tariff for Telecom Italia and for other fixed network operators, resulting from the BU-LRIC model to be developed consistent with EU Recommendation 2009/396/EC on termination rates. In 2012, AGCom, approved Telecom Italia s reference offer for fixed services offered in TDM mode, setting a value of cent 0.272/min for local level (SGU) termination. Moreover, on October 31, 2012, Telecom Italia published its reference offer for the year 2013 for interconnection services in both TDM and IP technology in line with the applicable regulatory framework so that the tariffs for IP termination service were regulated while TDM services were provided on commercial basis. Following a public consultation, in January 2013, AGCom notified to the European Commission the IP interconnection glide path for the 2012 2015 period, setting the origination service trend separated from the termination one; previously a unique value was applicable to both the origination and termination services AGCom proposes to apply a glide path until January 1, 2015 in order to allow operators to reach the efficiency required by the application of the pure LRIC model; only starting from that date will tariffs defined through a pure BU-LRIC model be applied to fixed termination rates. With a letter dated February 7, 2013, the European Commission opened a Phase II investigation into the fixed IP termination rates proposed by the Italian regulator, because the fully cost oriented rate (cent 0.043/min) based on a bottom-up pure long run incremental cost (pure LRIC) model would not be reached before January 1, 2015 contrary to the Commission s guidelines. The Commission s Phase II investigation suspended the adoption of AGCom s draft measure on IP FTRs for three months. In the meantime, due to the delay in setting the technical specifications of IP interconnection the migration towards IP could not be achieved by 2012 as envisaged by AGCom. The specifica tecnica ST769 was published on MiSE s website only on January 8, 2013. As a consequence, the Authority launched a public consultation to set regulated rates for TDM services for the year 2013.

The legal dispute over fixed termination prices asymmetry between Telecom Italia and AltNets for the period June 2010-June 2011 was decided on May 15, 2012. The Third Section of the Council of State admitted the appeals filed by some of the alternative operators and by AGCom against the ruling of the Administrative Court of Lazio which overruled decisions regarding 2010 and 2011 tariffs and overcoming the asymmetries between the reverse termination tariffs applied by AltNets and the ones applied by Telecom Italia. In brief, the Council of State, revising the Administrative Court ruling, agreed with the alternative operators claims that the differences existing between Telecom Italia s network architecture and the alternative architectures, determine different costs. Fastweb recently appealed against the Council of State decision since, in its opinion, the Court did not deal with its appeal against the symmetry of termination rates at local level for the year 2012 and should have cancelled 2012 symmetry. The hearing on the appeal was held on January 25, 2013 and, the Council of State upheld the complaint filed by Fastweb and revoked the application of symmetry of TDM 2012 termination tariffs among operators. Consequently, AGCom with Decision 187/13/CONS restored symmetry at national level (SGT) retroactively for 2012; TI therefore, shall pay to terminate on AltNets networks 0.361 eurocent/min instead of 0.272 eurocent/min.

Concerning **transit services**, in April 2010, AGCom identified two markets: (i) local conveyance and transit market (which includes the single transit service involving only one switch and the transit service between two or more switches located in the same telephone district and the transit services provided jointly with the originating or terminating service) and (ii) national conveyance and transit market (including transit services between two or more switches located in different telephone districts, also when provided jointly with the originating or terminating service). While the regulation for the national conveyance and transit service markets has been withdrawn, AGCom maintained the regulation for the local conveyance and transit market.

Regarding the wholesale markets for **trunk segments of leased lines** and for **terminating segments of leased lines**, AGCom, in January 2010, stated that the market for trunk services was competitive and removed all ex-ante obligations. As to the terminating services market, AGCom identified the following two separate markets: (i) circuits provided between a Telecom Italia node and end user s premises (market A); and (ii) circuits provided between a Telecom Italia node and a mobile operator s base station (market B). AGCom decided to deregulate market B, removing existing ex ante obligations starting from 31 December 2010. AGCom, however, identified Telecom Italia as a SMP in Market A and imposed a network cap for the years 2010-2012.

· **Mobile markets**

In February 2009, AGCom confirmed that the wholesale market for access and call origination on mobile networks should not be subject to ex-ante regulation.

With respect to the wholesale market for voice call termination on mobile networks, AGCom introduced in November 2008 a four year gradual decline in tariffs, setting the Maximum Termination Rate (**MTR**) for each SMP mobile network operator and the elimination of asymmetry enjoyed by the third entrant (WIND) in July 2011 (5.3 eurocents/min) and by the last entrant (H3G) in July 2012 (4.5 eurocents/min).

Following this decision, AGCom developed a new cost model for MTRs taking into account the May 2009 EU Recommendation on the regulation of termination rates. The new cost model was used in the third round of market review in order to update the values of the glide path (multiyear mechanism of price control) set for mobile termination rates.

In November 2011, AGCom published its final decision on wholesale prices for voice call termination on individual mobile networks. The new glide path, based on half-monthly (instead of annual) variations, started from July 1, 2012 and expires on July 1, 2013 with the commencement of a symmetric termination rate for all mobile operators (0.98 eurocents/min).

Mobile networks vocal termination **eurocents/min.**	**Prices applied from 7.1.2011**		**New glide path**	
		from 7.1.2012	**from 1.1.2013**	**from 7.1.2013**
Termination on H3G network	6.3	3.5	1.7	0.98
Termination on Telecom Italia, Vodafone and Wind networks	5.3	2.5	1.5	0.98

AGCom s final decision on wholesale prices was challenged before the Administrative Court by Vod/Win/H3G complaining that it introduced a very steep reduction of MTR; Telecom Italia appealed only against the provision stating that asymmetry for H3G should end as of July 1, 2013. On January 2013, AGCom, after providing evidence of the rationale of the above asymmetry in favor of H3G, following two TAR sentences, confirmed the application of asymmetry to H3G up to June 30, 2013. Telecom Italia has challenged this decision with the Regional Administrative Court of Lazio.

In February 2013, the Council of State, accepted the appeals filed by H3G, revoked the original 2008 decision to reduce certain termination rates due to lack of justification and *ad hoc* proceeding . The Council of State concluded that the termination price decrease introduced by AGCom for H3G in the period November 2008-June 2009 from cent 16.26/min to cent 13.00/min was not legitimate. AGCom has not yet issued any decision following the above judgment.

Concerning the wholesale market for SMS termination, as a consequence of a public consultation concluded in October 2012, AGCom decided not to regulate the above mentioned market because it tends towards competition over time, and therefore the second criterion of the three criteria test for ex ante regulation could not be considered as met. Consequently the SMS termination prices continue to be commercially negotiated on a reciprocity basis among operators.

Mobile number portability (MNP)

On January 7, 2011 AGCom published Decision 147/11/CIR on *Amendment to the regulations on mobile number portability*. The Decision, among other things, provides that:

- MNP should be set up by 8.30 a.m. of the second working day following input of the customer s request in the recipient operator s systems;
- from January 1, 2013, the recipient operator must refund the customer, upon request, in case of delays in the activation of the MNP, for a minimum of 2.5 euros for each working day of delay, up to a maximum of 50 euros. The refund is not due for delays up to two working days; for delays over two working days, the refund calculation takes into account all the days late including the first two; and
- the data of the customers who request the MNP activation is to be treated by the donating operator with confidentiality and used only for the activation of the service.

International roaming

The new roaming Regulation (531/2012, the so called Roaming III Regulation) was approved by the European Parliament and the Council in June 2012 and entered into force on July 1, 2012.

The Roaming III Regulation provides for the following measures applicable to roaming services within the EU (extended to European Economic Area countries):

- transparency measures (such as cut off limit to prevent bill shock and info SMS on the applied retail tariffs) and the adoption of price caps both on voice, SMS and data (retail and wholesale). The retail caps will remain in force until 2017 and the wholesale caps until the expiry of the new regulation in 2022;
- the unbundling/decoupling of the roaming services from the domestic services starting from July 2014 (structural solution). In the unbundling scenario, the customer will buy the roaming services (separately from the domestic services) from an alternative roaming provider (mobile network operator MNO or mobile virtual network operator MVNO/reseller). The definition of the structural solution was delegated to an implementing regulation by the European Commission;

· the obligation to provide wholesale roaming access to MNO/MVNO/resellers at regulated prices.

The agreed price caps are the following:

at wholesale level:

WHOLESALE		**ROAMING III**	
	July 1, 2012	**July 1, 2013**	**July 1, 2014**
voice (cent/min)	14	10	5
sms (cent/sms)	3	2	2
data (cent/MB)	25	15	5

at retail level:

RETAIL		**ROAMING III**	
	July 1, 2012	**July 1, 2013**	**July 1, 2014**
voice out (cent/min)	29	24	19
voice in (cent/min)	8	7	5
sms (cent/sms)	9	8	6
data (cent/MB)	70	45	20

In December 2012 the European Commission published the implementing regulation indicating Single IMSI (International mobile subscriber identity) and LBO (local break out) as the structural solutions to be implemented for decoupling. It remains a high level document which delegates to BEREC the definition of guidelines on the technical elements necessary to enable the separate sale of roaming services and provides for the creation of an Industry Forum to ensure a coordinated approach among market players, BEREC and the Commission.

Such Industry Forum defined the Technical Specifications of the unbundling solution, whose details are being further defined by *ad hoc* technical working groups. The results of the working groups will be used to define detailed implementation guidelines which BEREC is expected to publish by the end of June 2013.

Long Term Evolution (LTE) Frequencies

The so-called digital dividend is the allocation of a portion of the broadcasting frequency band to other telecommunication services. AGCom published guidelines for the frequency national plan aiming at fostering the release of the digital dividend band (as required by the European Commission Recommendation 2009/848/EC of October 28, 2009) at present allocated to a large number of local broadcasters (about 600).

On December 7, 2010, following the approval of the 2011 Financial Bill, ACGom and the Ministry for the Economic Development Communications Department launched the process to award, by means of a tender, radio frequencies rights of use to be assigned to broadband mobile electronic communication services.

On June 10, 2011, AGCom published its decision regulating the procedures aiming at issuing the 800, 1800, 2000 and 2600 MHz frequencies rights of use. Finally, on June 27, 2011, the Ministry for the Economic Development published the Invitation to Tender for the award of the frequencies rights of use.

The minimum tender rates for each frequency lot were as follows:

BAND	**Minimum rate per lot (in euros)**
800 FDD	353,303,732.16
1800 FDD	155,869,293.60
2000 TDD	77,934,646.80
2600 FDD	30,668,726.75
2600 TDD	36,802,472.10

The Ministry for the Economic Development granted Telecom Italia the right to file offers for the use of frequencies.

On October 3, 2011, the Ministry for the Economic Development Communications Department awarded Telecom Italia two 2x5 MHz standard blocks at 800 MHz each, a 2x5 MHz block at 1800 MHz and three 2x5 MHz standard blocks at 2600 MHz each. Telecom Italia s total investment amounts to 1.223 million euro, net of a 38 million euros discount due to Telecom Italia s commitment to implement the new networks using more than 50% environmental sustainable equipment. Given this discount, a specific credit guarantee was set up.

On November 3, 2011, Telecom Italia made a payment of 767 million euros for the award of the above-mentioned frequency blocks and established a five-year guarantee of the remaining 456 million euros to be paid.

The rights of use, formally awarded by the Ministry on October 3, 2011, were allocated on February 2012.

The 2600 MHz band can be used starting from January 1, 2013; at the beginning of January 2013, the Ministry communicated that the 800 MHz band is also available to be used.

Quality of services of broadband internet access at fixed location

Since November 2008, the operators have been required to provide information about the service level of internet access services at a fixed location:

· operators must state their minimum standards of service quality (including the minimum connection speed) and other information about the characteristics of the access. Subscribers can terminate their contract if the quality of their connection is below the claimed minimum standards;

· operators shall undertake statistical measurements at regional level (for example speed data transmission; delay; rate of packet loss). At present, this activity has been taken in 15 regions and will be gradually extended to all 20 Italian regions.

Since the autumn of 2010, customers have been able to measure the quality of their broadband connections.

AGCom has also introduced a *super-partes* agency verifying operators measurements.

Quality of services of broadband internet access within mobile network

In February 2011, the NRA launched a working group with operators to measure the quality of data service provided by mobile networks.

The working group developed drive test campaigns to be performed every six months in the main cities of all Italian regions. In the June October 2012 period an experimental campaign was conducted aiming at refining the data gathering process. Currently the first campaign is in progress and the results will be available by September.

Universal Service

The Universal Service is a minimum set of services of a certain quality, which shall be made available to all customers, regardless of their geographical location and shall be offered at a reasonable price, taking into account the specific national conditions,. To date, Telecom Italia is the only operator with the obligation of providing the Universal Service (**USO**) throughout Italy.

A fund, set up by the Ministry of Communications, is used to contribute to finance the net cost for the provision of Universal Service. All the main companies in the sector including Telecom Italia contribute to the above fund.

The net cost of providing the Universal Service is calculated as the difference between the company s net cost when it is subject to the obligation of providing the Universal Service and the net cost of the same operation should the obligation not exist. It is AGCom s responsibility to verify the net cost of the Universal Service.

In March 2008, AGCom published a Decision introducing a new method of calculating the net cost based on historical cost accounting (the previous was based on current cost accounting) in order to reduce the net cost for the provision of Universal Service. Such a calculation affects credits related to the Universal Service net cost for the years 2004, 2005 and 2006 which have been re-calculated and submitted to AGCom under the new methodology.

With Decision 153/11/CIR, AGCom assessed the 2004 net cost for universal service. The Authority decided the applicability of the sharing mechanism and assessed the net cost for the year 2004 was 25.9 million euros. The contribution rate due by other operators (Vodafone, Wind and Fasteweb, Teletu Italia and BT) amounts to 8.7 million euros.

With Decision 139/12/CIR AGCOM completed the process for the evaluation of the 2005 net cost of universal service. The Authority established the applicability of the sharing mechanism and determined the net cost for the year 2005 in total 25.6 million euros. The contribution rate due by other operators (Vodafone, Wind and Fastweb, Italy TeleTu and BT) amounted to 10.3 million euros.

Net costs calculations for the years 2006, 2007, 2008, 2009, 2010, 2011 and 2012 have been submitted by Telecom Italia to AGCom. At present the independent auditor appointed by AGCom is verifying 2006 calculations.

In September 2011, with Decisions 106, 107, 108 and 109/11/CIR, AGCom confirmed the amounts to be paid by Vodafone for the years 1999-2003. Vodafone filed new appeals against those decisions with the Council of State (Consiglio di Stato) and with the Administrative Court of Lazio. The sums in discussion (except for the amount for 2001 which is not the subject of appeal) amounted to approximately 37 million euros.

With Decision 153/11/CIR AGCom completed the 2004 US net cost evaluation process. Vodafone and Fastweb filed an appeal with the administrative regional court. The date of the hearings to deal with the merits have not been fixed yet.

Public Telephony

In April 2010 AGCom confirmed that the criteria regarding the distribution of public telephones on the national territory was no longer consistent with current social needs and removed quantitative obligations for Telecom Italia. As a result, Telecom Italia was authorized to remove public telephones after consultation with local municipalities and interested citizens. Since 2010, approximately 25,000 public telephones have been removed. At the end of 2012 the total number of public telephones in place amounted to around 90,000.

Accounting separation and fixed network cost accounting

SMP operators are required to have a transparent accounting system as to their costs. These operators shall provide AGCom annually with both a description and a report on their cost accounting system to assess their compliance with the requirements of the electronic telecommunications regulatory framework. Moreover, SMP fixed and mobile operators must keep a separate accounting system separating the activities in each of the relevant wholesale and retail markets defined by AGCom according to the periodic market analyses.

The rules on regulatory accounting in Italy are set in accordance with EC Recommendations, particularly with Recommendation on Cost Accounting and Accounting Separation , issued on September 2005.

Changes in the regulation on cost accounting and accounting separation follow detailed rules set out in periodical market analyses.

The weighted average cost of capital employed was set by the AGCom at 9.36% nominal pre-tax in December 2010; Telecom Italia stated that this underestimated the cost and caused regulated service s costs to be undervalued and asked that the decision be reviewed.

Since 2008 the regulatory asset base includes Telecom Italia s goodwill which amounts (according to the 2012 statement of financial position) to 30.6 billion euros (approximately 45.8% of the total assets).

Since the services provided by Telecom Italia are capital intensive, decisions related to the perimeter and the cost of capital are absolutely material: as a matter of fact, according to the regulatory accounting for 2010 (the last published) the average employed capital for the sole regulated wholesale services amounts to approximately 11 billion euros. As a consequence, increasing WACC by 1% would increase by 110 million euros the reference cost base for the calculation of prices for wholesale services.

During the first half of 2012, the independent auditors appointed by AGCom to review Telecom Italia s accounting separation of the fixed network services for the year 2010 completed their audit and delivered the requested audit reports to AGCom. Reports of the auditors are approved by means of an AGCom decision; regulatory accounts and accounting methodology are also published by Telecom Italia on its website.

The regulatory accounting report for the year 2011 was produced during 2012 and delivered to AGCom in January 2013 meeting AGCom s final approval (December 2012) of new accounting rules regarding internal contracts, transfer charges and further reporting requirements aimed at complying with the equivalence principle.

At present, Telecom Italia is fully compliant with its regulatory accounting obligations.

Accounting separation and mobile network cost accounting

In connection with AGCom s second round of market analyses concerning the market for the termination of voice calls on individual mobile networks , AGCom requested SMP operators to produce economic and quantitative data related to regulatory accounting methodologies for the purpose of setting new network cap values. Consultation on the main assumptions of Mobile LRIC model was closed in November 2010.

During 2011, AGCom started a new round of market analyses and stated a new glide path for MTRs for the 2012-2015 period. AGCom also:

(A) updated the glide path in three steps: 07/01/2012, 01/01/2013 and 07/01/2013 in order to speed up the process towards symmetric rates; and

(B) clarified the rules to be applied for regulatory accounting.

During 2012:

- auditing activities regarding accounts at historical costs for the year 2010 ended in March 2012;
- reports of the auditor were published by AGCom on December 2012;
- regulatory accounting report for the year 2011 was delivered to AGCom in January 2013, in compliance with AGCom s Decisions.

At present, Telecom Italia is fully compliant with its regulatory accounting obligations.

AGCom 2011-2012 fee

In January 2011, AGCom carried out an assessment of the compliance by Telecom Italia and all other telecommunications companies with respect to their obligation to pay annual fees to the Authority for the years 2006 through 2010. On March 1, 2011, AGCom notified Telecom Italia that the Company had not fully paid its operating expenses due for the relevant periods, listing additional accounting items which, in its opinion, should have been included in the cost basis used to make the calculation. Telecom Italia was therefore required by AGCom to pay an extra sum for amounts not paid in the five years 2006-2010. Telecom Italia appealed this decision with the Lazio Regional Administrative Court which suspended the terms of the payment until the end of the proceeding.

On March 3, 2011, AGCom published its decision on the payment of the annual fee for the year 2011 with which the Authority raised the contribution share from 1.5 to 1.8 of 2009 communications sector revenues. On April 30, 2011, Telecom Italia paid (with reservation) an amount equal to 24.2 million euros, calculated consistently with the reasoning on which it calculated its fees for the 2006-2010 period and, at the same time, contested the 2011 decision with the Lazio Regional Administrative Court in relation both to the increase in the level of the contribution and to the broadening of the accounting items to be considered in the cost basis.

With respect to the two appeals filed by the Company, two orders were published by the II Section of the Lazio Regional Administrative Court in December 2011. These orders suspended the above-mentioned rulings and referred to the EU Court of Justice a preliminary question, i.e. the assessment of AGCom s national financing system consistency with the principles deriving from the EU sectorial Directives. This decision is pending.

On March 28, 2012, AGCom published its decision on the payment of the fee for the year 2012 (Decision 650/11/CONS), setting the calculation methodology on 2.0 of 2010 revenues of the communications sector. On April 30, 2012, Telecom Italia paid (with reservation) an amount equal to 23.0 million euros and challenged Decision 650/11/CONS before the Regional Administrative Court of Lazio.

Broadband and digital divide

Over the last few years, AGCom introduced several measures aimed at endorsing the development of fixed and mobile broadband through the provision of simplified procedures to deploy the relevant networks.

Particularly important in this respect were laws introducing:

- a lighter authorization procedure for the deployment of broadband mobile equipment; and,
- simplified rules for the use of innovative digging techniques (mini-trench) for the deployment of optical fiber equipment.

In 2010 the simplification process also affected the authorization procedure for the deployment of electronic communication equipment in protected areas. Since half of Italy is considered as a protected area (*area di conservazione*), provisions aiming at accelerating digging authorizations are important levers for broadband expansion throughout the country.

In 2011 new laws were implemented to simplify the administrative procedure for the expansion of small mobile equipment (0.5 sq. area) and of low power equipment (7 watt). The deployment of mobile equipment falling within the above-mentioned thresholds was actually exempted from the DIA regime (*Denuncia di Inizio Attività* Commencement Notice) previously provided for by the Electronic Communications Code and subject to a simple notification, to be made at the time of commencement of the works.

Further important measures to promote the development of fixed and mobile networks were recently introduced by means of art. 14 of the Decree Law. 179/2012 Further urgent measures for the economic development of the Country) enacted by Law 221/2012. Particularly regarding the deployment of optical fiber and cables the measures provide for:

- reducing the terms already established by the Code of the Electronic Communications for the release of authorizations to dig (copper and fibre both) by reducing the period of the administrative procedure through introduction of the tacit approval principle;
- modifying the rules of the roads (Codice della Strada) introducing the use of techniques aimed at limiting the environmental impact by reducing the depth of excavations; and
- established that telecommunication operators can access common parts of buildings also without the consent of the condominium in order to lay optical fiber.

With reference to the diffusion of the mobile digital technologies, art. 14 modified the criteria for calculation of electromagnetic field allowing a better use of the electromagnetic power available. The implementation of this rule is subject to the adoption of a further regulation which is, at present, under discussion.

The new law also improved the simplification introduced by the L. 211/11 granting the possibility to install equipment up to 10 watts after the provision to City Hall and Arpa of a mere self-certification of activation.

4.3.2 Privacy and Data Protection

Telecom Italia must comply with Italy s Personal Data Protection Code (Legislative Decree June 30, 2003 n. 196, hereinafter as Privacy Code), which came into force on January 1, 2004.

The Privacy Code is divided into three parts: (1) general data protection principles; (2) additional measures applicable to organizations in certain areas, including telecommunications services; and (3) sanctions and remedies.

The Privacy Code applies to all data processing within Italy and also affects organizations not being based in Italy but using equipment located in Italy, such as computer-based systems.

According to the Code, personal data shall be processed lawfully and fairly, retained accurately and up to date and must not be excessive or stored for a longer period than needed. Therefore, information systems shall be configured in order to minimize the use of personal data.

The data subject (any natural person that is the subject of the personal data) and the subscriber (any natural or legal person who or which is party to a contract with the provider of publicly available electronic communications services, or is the recipient of such services by means of pre-paid cards) shall receive preliminary information on the purposes and modalities of data processing. Consent of the data subject is necessary to process personal data, except in specific cases (i.e. obligations imposed by law or by a contract with the data subject). Furthermore, the data subject has the right to access his/her personal data and to obtain information on the purposes and methods of the processing.

Italy s Privacy Provisions Related to Specific Processing Operations in the Electronic Communications Sector

With respect to data retention, communications service providers (**CSPs**) are allowed to retain traffic data for a six-month period in order to deal with disputes over billing and subscriber services. CSPs are also required to retain telephone and electronic communications traffic data for the purpose of detecting and preventing crimes. At present, data retention terms for crime prevention and prosecution are: 24 months for telephony traffic (fixed and mobile); 12 months for electronic communications traffic; and 30 days for unsuccessful call attempts.

Traffic data must be kept and controlled in compliance with general provisions issued by the Italian Data Protection Authority (**Garante per la protezione dei dati personali**), which requires electronic communication operators to adopt strict security measures.

Customer profiling in the electronic communications sector is regulated by the Italian Data Protection Authority. CSPs must obtain the consent of the data subject for profiling based on individual and detailed personal data, while prior approval of the Italian Data Protection Authority is needed to process aggregated personal data without the data subject s consent.

Concerning direct marketing activities, the general rule is the **opt-in system** . Nevertheless Privacy Code also allows the processing of personal data obtained from directories of subscribers, in order to carry out operator-assisted telephone calls for commercial purposes; such processing is possible unless the entity entered its respective telephone numbers in a public opt-out register , which came into force on February 1, 2011.

At present, OTT players are benefitting from current regulation. This is especially true with regards to privacy legislation: indeed, differently from telecom operators, OTTs, in particular from the USA, have significantly fewer constraints in collecting personal data and using it for marketing purposes. Such a situation provides OTTs with an important competitive advantage over Telco operators.

Recent amendments

Legislative decrees that transposed the EU 2009 regulatory framework into Italian law, including the revised e-Privacy Directive, entered into force on June 1, 2012.

The two decrees amended the Privacy Code and the Electronic Communications Code.

These amendments set out that storing information, or accessing information already stored in the terminal equipment of subscriber/user (i.e. by cookies) shall only be permitted on condition that the subscriber/user has given his consent. Such a consent shall be obtained by means of simplified arrangements not yet defined by the Italian Data Protection Authority (DPA). Such simplified arrangements will result from the outcome of a public consultation (closed last March, 19 2013), taking into account the proposals put forward by consumer associations and other stakeholders (i.e. industry associations involved). Consent may be given through the use of specific computer programs or devices which may be easily managed by the users.

Cookies are exempted from the requirement of informed consent, if they satisfy one of the following criteria: i) are used exclusively for the purpose of carrying out the transmission of a communication on an electronic communications network; ii) are strictly necessary to the provider of an information society service that has been explicitly requested by the subscriber/user to provide the above service.

The Privacy Code requires providers of publicly available electronic communications services to adopt technical and organizational measures that are adequate in the light of the existing risk, in order to safeguard the security of their services and to take measures when breaches of personal data occur. Such measures must protect personal data against the risk of their accidental or unlawful destruction or loss and of unauthorized access to the data or of processing operations that are either unlawful or inconsistent with the purposes for which the data have been collected.

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Item 4. Information On The Telecom Italia Group **Regulation**

Under the Privacy Code, in case of a personal data breach , (i.e., a security breach leading, accidentally or not, to the destruction, loss, alteration, unauthorized disclosure of or access to personal data transmitted, stored or otherwise processed in the context of the provision of a publicly available communications service) the provider shall inform without delay the Italian Data Protection Authority (currently the Italian Data Protection Authority specified the term in 24 hours for the first communication and in 3 days for the communication of further details on the personal data breach). Moreover, where the breach is likely to adversely affect the personal data or privacy of a subscriber or other individuals, the provider must also inform them without delay.

According to new article 70 of the amended Communications Code regarding the information that should be included in the contract at the user s request, the provider shall include information on:

· any procedures put in place to measure and shape traffic in a network in compliance with the right of protection of personal data of the user so as to avoid saturation of the network; and

· on how those procedures could impact service quality.

4.3.3 Antitrust in Italy

Legislation on competition

Telecom Italia is subject to Italian competition law.

Law October 10, 1990 n. 287 (Provisions aiming at protecting competition and the market) set up the *Autorità Garante della Concorrenza e del Mercato*, or Antitrust Authority .

The Antitrust Authority is responsible for:

(i) applying Law 287/1990 and supervising: (a) restrictive agreements; (b) abuses of a dominant position; and (c) concentrations of enterprises;

(ii) applying, whenever the necessary conditions are met, the relevant EU provisions (i.e., Articles 101 and 102 of the Treaty on the Functioning of the European Union);

(iii) applying Legislative Decree September 6, 2005 n. 206 concerning unfair commercial practices; and,

(iv) monitoring conflicts of interest in the case of individuals holding government positions.

In addition, the Antitrust Authority may (i) adopt interim measures; and (ii) enforce commitments binding upon the proposing parties in order to dispel identified anticompetitive concerns closing the investigation without any finding of a violation.

Antitrust Proceedings

For a discussion of the significant antitrust proceedings to which the Telecom Italia Group is a party please see Note Contingent Liabilities, Other Information, Commitments and Guarantees of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report .

4.3.4 ANTITRUST ISSUES AT THE EUROPEAN LEVEL

Legislation on competition

Telecom Italia is subject to the European competition law. European competition policy was developed from the three central rules set out in the Treaty on the Functioning of the European Union:

1. agreements between two or more independent market operators which restrict competition are prohibited by Article 101 of the Treaty on the Functioning of the European Union (TFEU or Treaty)). This provision covers both horizontal agreements (between actual or potential competitors operating at the same level of the supply chain) and vertical agreements (between firms operating at different levels, i.e. agreement between a manufacturer and its distributor). Only limited exceptions are foreseen in the general prohibition. The most flagrant example of illegal conduct infringing Article 101 is the creation of a cartel between competitors (which may involve price-fixing and/or market sharing).

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Item 4. Information On The Telecom Italia Group **Regulation**

2. Article 102 of the Treaty prohibits firms holding a dominant position on a determined market to abuse that position, for example by charging unfair prices, by limiting production, or by refusing to innovate to the prejudice of consumers.

3. State aid distorting competition and trade within the EU are prohibited (art. 107 of the Treaty). State aid is defined as an advantage in any form whatsoever conferred on a selective basis to undertakings by national public authorities. Therefore, subsidies granted to individuals or general measures open to all enterprises are not covered by Article 107 of the Treaty and do not constitute State aid. Furthermore, the EC Treaty provides that in some circumstances, government interventions are necessary for a well-functioning and equitable economy stating some exceptions and sector specific rules . The Guidelines for the application of State aid rules in relation to rapid deployment of broadband networks state that public funding of broadband projects is not considered state aid if one of three possible exemption routes is used: a) the public authority invests under the same conditions that would be applied to a private investor (MEIP principle); b) the public contribution is limited to the compensation of the provision of a service of general economic interest (SGEI principle); c) it meets certain conditions (promoting the economic development of underdeveloped areas, promoting the execution of an important project of common European interest or to remedy a serious disturbance in the economy of a Member State, facilitating the development of certain activities or areas, promoting culture and heritage conservation.

The Commission is empowered by the Treaty to apply these prohibition rules and holds a number of investigative powers to that end (e.g. inspection at business and non-business premises, written requests for information, etc.). It may also impose fines on undertakings which violate the EU antitrust rules. The main rules on procedures are set out in Council Regulation (EC) 1/2003.

Since May 1, 2004 all National Competition Authorities have also been empowered to fully apply EU Antitrust rules (i.e. Articles 101 and 102 of the TFEU) in order to ensure that competition is not distorted or restricted. National courts may also apply these provisions in order to protect the individual rights conferred on citizens by the Treaty.

State aids rules, on the contrary, can only be applied by the European Commission.

As part of the overall enforcement of EU competition law, the Commission has also developed and implemented a policy on the application of EU competition law to actions for damages before national courts. It also cooperates with national courts in order to ensure the coherent application of the EU competition rules within the Member States.

Main Antitrust proceedings pending in front of the European Commission

On February 2011, Telecom Italia and the Autonomous province of Trento (**PAT**) signed a MoU to establish a Public-Private Partnership for NGAN (fiber optics) deployment in the Trentino region (around 150,000 households). The Public-Private Partnership is based on a market-driven approach (no state aid) and should allow a shorter time to deployment for the Trentino region an area where only one broadband network operator is present). The project foresees the participation of PAT, Telecom Italia and other industrial partners. A newly established corporation (Newco) (the Trentino NGN Joint Venture) will deploy a fiber network (dark fiber) based on a FTTH 3-GPON architecture and will sell accesses to any Telco/ISP operator based on equivalence principles. Telecom Italia will confer network assets useful for NGAN deployment and will have the possibility to acquire a majority stake or 100% stake of Newco by exercising a call option awarded to it by a shareholders agreement that will govern the public-private partnership.

On July 25, 2012, the European Commission opened an investigation aiming at assessing compliance of the Trentino NGN Joint Venture with European rules on State aid.

The proceeding is aimed at assessing the compliance of the project with the MEIP principle as was in the intentions of the parties. The parties, in fact, have not notified it as State aid nor are interested in an assessment concluding that the project results in State aid compatible with EU rules. The purpose of the investigation is to assess whether there is State aid (Phase I) and, in case it is concluded that there is State aid, whether such aid is compatible with the relevant EU Rules (Phase II).

The parties are not interested in going to Phase II, therefore either the Commission states that the project is MEIP compliant (thus no State aid) in which case the proceedings stop physiologically at Phase I; or, the Commission considers that the project is not MEIP compliant thus implying State aids. In this latter case the Commission should normally go to Phase II but this would not happen in this case because the parties would withdraw the project before the conclusion of Phase I.

Accordingly, if the Commission concludes that the project complies with the MEI principle, it will close the investigation and declare that there is no State aid.

If, on the other hand, the European Commission assessment recognizes the existence of an economic advantage for Telecom Italia and, hence, State aid, it would normally further evaluate whether the aid is compatible with the internal market. In this case, if the Commission concludes that there is State aid the parties will withdraw the project. This has little impact on the business of Telecom Italia as a whole as the project is a pilot which could be replicated in case of positive outcome but would not have negative consequences in case of withdrawal.

PAT submitted its brief on the Commission s assessment on November 22, 2012. Telecom Italia requested an extension of the deadline and submitted its brief on December 3, 2012. Telecom Italia explained its position to the Commission in an ad hoc meeting on December 5, 2012.

PAT has subsequently had access to the complainants objections on the Commission s assessment on January 29, 2013. PAT filed with the Commission its reply to the latter objections on March 1, 2013. The parties are confident that their submissions will dispel the Commission s concerns and will be available to provide any further information and/or clarification on this issue, being also available to discuss with the Commission possible modifications of the project to overcome Commission s eventual residual doubts on the applicability of the MEIP principle.

4.3.5 TELECOMMUNICATION REGULATORY FRAMEWORK IN BRAZIL

Telecom Italia Group s operations in Brazil are subject to the 1997 General Law on Telecommunications (Lei Geral de Telecomunicações **LGT**) and to a comprehensive regulatory framework for the provision of telecommunications services adopted by the Regulatory Agency for Telecommunications Agência Nacional de Telecomunicações (**ANATEL**).

ANATEL is responsible for the regulation and implementation of national policies in matter of telecommunications. It is a quasi-independent body (the relationship with the Ministry of Communication is institutional, but not hierarchical) enjoying financial and operational autonomy and a wide range of functions and powers, to ensure competition and to avoid concentration of services. The board members have a fixed term, are selected and appointed by the President under approval by the Senate.

ANATEL has the power to impose restrictions, limitations or conditions on concessions, permits or authorizations. ANATEL has the authority to propose and issue legally binding regulations on telecommunications service providers. The rules issued by ANATEL are subject to periodic updates. Any proposed regulation or action by ANATEL is subject to a period of public consultation, which may include public hearings, and can be challenged in Brazilian courts.

ANATEL privatized the former public monopolistic operator and progressively opened the market to competition, in addition to promoting universal access to basic telecommunications services.

With regard to the operational activity of TIM, Intelig and TIM Fiber, ANATEL developed regulations for mobile communication services (**SMP** Personal Mobile Services), fixed communications services (**STFC**) and data transmission and multimedia services (**SCM**).

In October 2008, ANATEL approved the proposed General Update Plan in Telecommunications Regulation (**PGR**) aiming at planning the actions to be promoted by ANATEL for the next ten years, in order to update the regulation of telecommunications in Brazil. Implementation of the Local Loop Unbundling and Virtual Mobile Operators were included in the expected short-term actions by the PGR.

Number portability was introduced in Brazil beginning in September 2008 and became fully operational in March 2009.

The exploitation of mobile services by Mobile Virtual Operators, based on commercial agreements between established operators and virtual operators was introduced in 2010.

Authorizations

ANATEL carried out the privatization of the former public monopoly operator and gradually opened the sector to competition, in addition to fostering universal access to basic telecom services. According to the General Telecommunications Law and to the regulations issued by ANATEL, licenses to provide telecommunications services are granted either under the public regime, by means of a Concession or a Permission, or under the private regime, by means of an Authorization. Only certain fixed-line service providers are currently operating under the public regime (Telefónica, Embratel and Oi, commonly referred to as Concessionaires). All the other telecommunications services providers in Brazil are currently operating under the private regime, including all the mobile and data service providers.

Since the launch of GSM mobile services in 2002, four main players operate in the mobile market (Claro, Vivo, Oi and TIM) and compete nationwide. Third generation mobile services deployment started in 2008 while the deployment of fourth generation mobile services started in 2012.

The authorizations for fixed and mobile services give the Telecom Italia Group (which operate under the brand names TIM, TIM Fiber and Intelig) coverage of the entire Brazil allowing to provide fixed, mobile, long distance and multimedia services.

According to Brazilian law, Internet access is considered a value-added service, and providers of Internet services are not considered to be telecommunications operators. The rules require that all telecommunications services operators allow network access to any interested party to provide value-added services, without discrimination, unless technically impossible. The voice service providers can also provide value-added service through their own networks.

Interconnection rules

Telecommunication operators must publish a public interconnection offer highlighting both economic and technical conditions and are subject to the General Interconnection Regulatory Framework enforced by ANATEL in 2005.

The interconnection charges for fixed network (**TU-RL**) amount to a percentage of retail prices for the incumbent operators. Alternative operators (including TIM) can apply asymmetrical interconnection rates exceeding up to 20% the one applied by the incumbents.

The values of mobile interconnection rates (**VU-M**) are freely negotiated by operators. The National Regulatory Authority has, however, arbitration power in case of disagreement being able to determine a reference value according to criterion set up by regulation.

Interconnection agreements are subject to prior approval by ANATEL.

National Broadband Plan

In May 2010, the Brazilian government approved a National Broadband Program to extend national broadband coverage by 2014. The plan includes the reactivation of Telebras, responsible for managing and operating a national fiber network, and a new framework aimed at reducing the wholesale connectivity price and consequently allowing a more affordable price of entry level broadband residential connections.

Other measures in the plan are represented by fiscal incentives to induce the operators to offer broadband access to low income families, public investments in research and financial support to national industries.

Main regulatory developments

Fixed Termination Rates

In May 2012, ANATEL approved a new regulation on fixed termination rates setting local interconnection rates in case of a traffic unbalance of at least 75% of traffic exchanged amongst fixed network operators. Fixed networks will only remunerate each other when there is a 75%-25% imbalance of interconnection traffic (previously, it was 55% versus 45%). Below that threshold a system of bill and keep applies.

ANATEL also decided that starting from January 2014, the Bill and Keep system will generally apply, i.e., all operators take rights of tariffs generated on their networks, and no interconnection remuneration will be in place.

Leased Lines

In May 2012, ANATEL approved new regulations on Wholesale Leased Lines (EILD).

Operators holding a significant market power are obliged to provide EILD at a reference price 30% lower than the one previously practiced. The provision of special Leased Lines, at a higher price than the standard lines, should be amply justified and limited to requests requiring larger investments or, only in case of copper lines, when the premises are located far from the central offices. Existing contracts shall be adapted to the new ANATEL provisions.

Suspension of new sales because of alleged service complaints

In July 2012 ANATEL suspended the sales of new mobile plans by the three main carriers in certain states, because of alleged consumer complaints about dropped calls and spotty coverage, ANATEL imposed the suspension of new sales in various states to Oi (in 5 states), TIM (19 states) and America Movil SA s Brazilian unit Claro (3 states). Together, the three companies represent about 70% of Brazil s mobile market.

The suspension was an unusually strong sanction and one of the toughest measures ever taken by ANATEL.

The companies had 30 days to present investment plans to regulators showing how they ll improve service. Only after plans approval, sales were resumed.

The operators committed themselves to invest in improving the quality level of mobile services in the next two years. The plans submitted by the operators cover all states and the Federal District, and include investments in network improvements, improved customer service and reduced service interruptions. The providers showed improvement proposals detailed state by state, including measures to ensure quality of service and networks.

As a consequence, in August 2012 ANATEL lifted the ban on new sales of mobile phone plans for the three carriers, considering satisfactory the investment plans to ensure better service and coverage.

In February 2013 ANATEL released the first quarterly review of the National Action Plan to Improve the Provision of Personal Mobile Service. The above review includes the assessment of the first three months of long-term plans submitted by providers to ANATEL to improve services. The evaluation will be continuous over two years.

The report was released after detailed analysis of the results presented between August and October last year.

Assignment of frequencies in the 2.5GHz and 450MHz bands

In June 2012, the auction for the allocation of radio frequencies in the 2.5GHz band was held. Together with the 2.5GHz frequencies, enabling 4G/LTE applications, a portion of frequencies in the range of 450MHz was assigned.

Since no bidder was interested in separately acquiring frequencies in the 450MHz band, because of the lack of standards and the burdensome coverage obligations, frequencies were then assigned, along with coverage obligations, to the 2.5GHz frequency winners.

TIM Brasil was awarded a 10MHz block of national spectrum and 6 regional licenses in the 2.5GHz band bidding approximately 148 million euros.

Telefónica Brazil (Vivo) was the largest bidder in the auction, agreeing to pay approximately 407 million euros for 20MHz of national 2.5GHz spectrum.

Claro was awarded 20 MHz and 19 regional licenses *vis-à-vis* a fee of approximately 383 million euros.

Oi, part-owned by Portugal Telecom, was awarded a 10MHz block of national spectrum along with 11 regional licenses bidding approximately 154 million euros.

Coverage obligations:

- 450MHz: by December 31, 2015, rural areas within 30 km from the City Hall covered with voice and data services;
- 2.5 GHz: by December 31, 2016, gradual coverage by means of 4G services of the cities with more than 100,000 inhabitants (starting from the cities involved in the 2014 FIFA World Cup).

Cost models implementation

In 2005, ANATEL issued a ruling for Accounting Separation and Cost Accounting , introducing on license holders and groups holding Significant Market Power in the offering of fixed and/or mobile network interconnection and wholesale leased lines (*Exploração Industrial De Linha Dedicada* **EILD**) the obligation to present the Accounting Separation and Allocation Document (*Documento de Separação e Alocação de Contas* **DSAC**). Starting from 2006 (for fixed operators) and 2008 (for mobile operators), operators (TIM included) are providing ANATEL with the requested information.

In August 2011, ANATEL launched a project called Modelo de Custos , setting up a consortium of consultants (Advisia, Analysys Mason, Grant Thornton) in charge of developing, within two years, the cost model for fixed and mobile networks for communications services.

Between July and August 2012, ANATEL held a public consultation on the conceptual approach and recommendations for the construction of the Long Run Incremental Cost model for fixed and mobile networks.

By 2014, when the cost model will be available, ANATEL should have an instrument for the effective application of the obligation of cost orientation for the development of regulated wholesale services.

General Competition Plan (PGMC)

In November 2012, ANATEL published the General Competition Target Plan (PGMC), introducing tools for market analysis, for the identification of operators with market power and for the consequent imposition of asymmetric measures.

The approval of the PGMC represents a milestone in the development of the Brazilian regulation, which is gradually evolving towards a model based on market analysis and towards the application of ex ante regulatory obligations in presence of obstacles to the competition development.

The decision opens significant market power operators fixed networks to unbundling and wholesale broadband access, and improves transparency measures by the creation of a Supervisory Board to ensure the respect of the wholesale service quality levels.

Fixed networks in fiber optics will benefit from a regulatory holiday of nine years, which will have to be confirmed in four years, when PGMC will be revised.

In each market, ANATEL imposed a set of asymmetrical obligations to operators having significant market power.

The most important measure imposed in the fixed access market is the further opening of wholesale fixed networks through the introduction of access obligations on copper networks (eg, Leased Lines, bitstream unbundling) for the vertically integrated, fixed operators having significant market power: Oi, Telefónica and Telmex.

TIM Brasil was appointed as significant market power operator in the wholesale markets of mobile termination, national roaming and the access to ducts and trenches. The measures applied to the significant market power operator in those markets, include:

- a glide path on mobile termination rates for the 2013-2015 period, based on a price cap system, with a decrease of almost 50% in the next three years;
- the obligation to offer the service of national roaming to operators not having significant market power: regional licensed CTBC and Sercomtel and national licensed Nextel.

The obligation to offer the access to own ducts and trenches.

Mobile interconnection rate glide path

As a result of the November 2012 decision by ANATEL on market analysis (PGMC), the full billing of the exchanged traffic was maintained amongst the undertakings considered as having significant market power in the market of mobile interconnection (Claro, Oi, TIM and Vivo), whereas the partial bill and keep will be applied amongst operators being designated as having significant market power and operators not designated (Sercomtel, CTBC and Nextel).

The imbalance between incoming and outgoing traffic over which the termination fee will be paid amongst operators being designated as having significant market power and operators not being designated will be 80% from January 2013 to February 2015. From that date, it will decline to 60% until February 2016, when the full billing methodology will be applied again.

ANATEL also modified the October 2011 glide path to be applied to the reference value of the mobile termination for calls coming from the fixed networks.

As a result, the expected reduction of MTR, from February 2013, R$0,37/min (approximately 0.14/min) to R$0.34R/min (approximately 0.13/min) was confirmed: the successive reductions for 2014 and 2015 have been increased: R$0.25R/min (approximately 0.1/min) in 2014 and R$0.17/min (approximately 0.07/min) in 2015. From 2016, the values will be cost-oriented and, according to the statement by the ANATEL rapporteur, should converge to approximately R$$0.10/min (approximately 0.04/min).

Proposal on new allocation of the 700 MHz band

A public consultation proposed by ANATEL on the new allocation of the 700 MHz band was held from February 21 to April 14, 2013. The draft Regulation on Conditions for Use of Radio Frequencies concerns the allocation of the range of frequency from 698MHz to 806MHz (the so called 700 MHz band), allowing the allocation of the band for the provision of fourth generation telecommunication services and high speed internet.

Currently, the 700 MHz band is used for broadcasting. The new destination will be possible due to the transition from analogue TV to digital TV, which allows greater density in the frequency range dedicated to broadcasting, freeing up more space for the provision of telecommunications services.

The decision should be approved and released in the first half of 2013. The auction for the allocation of the frequencies to the mobile operators is expected by the first half of 2014.

4.3.6 Telecommunication Regulatory Framework in Argentina

Telecom Argentina and Telecom Personal operate in a regulated industry. Regulation not only covers rates and service conditions, but also the terms under which various licensing and technical requirements are imposed.

Telecom Argentina s and Telecom Personal s activities are supervised and controlled by the *Comisión Nacional de Comunicaciones* (**CNC**), a governmental agency under the supervision of *Secretaría de Comunicaciones* (**SECOM**), which is embodied within the Ministry of Federal Planning, Public Investments & Services. The SECOM develops, enforces and implements policies which are applicable to telecommunications services, reviews the applicable legal regulatory framework, approves major technical plans and resolves administrative appeals filed against CNC resolutions.

The Argentinean regulatory framework is mainly featured by:

- the Privatization Regulations, including the List of Conditions and the Transfer Agreement;
- the Licenses granted to Telecom Argentina and its subsidiaries;
- the Agreements on Rates; and
- various governmental decrees, including Decree n. 764/00, establishing the regulatory framework for licenses, interconnection, universal service and radio spectrum management, Public emergency law (law n. 25561) dated January 6, 2002 (regarding, among others, rules freezing fixed telephony rates).

Regulatory Authorities abroad

Núcleo, Telecom Personal s Paraguayan controlled company, is supervised by *Comisión Nacional de Telecomunicaciones* (**CONATEL**) the National Communications Commission of Paraguay.

Telecom Argentina USA, Telecom Argentina s subsidiary, is supervised by the Federal Communications Commission (**FCC**).

Authorizations

In March 1998, the Argentinean government issued the Decree n. 264/98, introducing a plan for the liberalisation of the Argentinean telecommunications industry.

This Decree provided for the extension of the period of exclusivity with respect to the provision of Basic telephone services until sometime between October 8, 1999, and November 8, 1999, depending on the particular region. The Plan also provided for: (i) the liberalization of public telephone services and (ii) the liberalization of telephone service in rural areas. In addition, the Plan contemplated that in January 1999, data transmission services within the countries included in Mercosur would be open to competition, subject to some conditions established therein.

Finally, the full liberalization of local, domestic and international long-distance services took place in November 2000 under Decree n. 764/00. By means of this Decree a new general regulation for full liberalization of telecommunication services was established, with the approval of new rules for licenses, interconnection, Universal Services and radio- frequencies spectrum control, allowing each new licensed company to launch its services in November 2000.

This Decree established a new Regulation of Licenses based on a single nationwide license for the provision of all telecommunication services to the public, including fixed-line, wireless, national and international services. It also established a new Interconnection Regulation that includes the obligation to give transparent networks interconnection and to publish a Reference Interconnection Offer (**RIO**) including the infrastructure elements and services that the dominant operator is required to provide. The commercial conditions for interconnection are defined by free agreement between the parts, while costs for basic interconnection elements are established in this regulation.

The main licensees providing local and/or fixed long-distance telephone services in Argentina are, among others, Telmex, Global Crossing, Comsat, IPlan, Telephone2, Telefónica de Argentina and Telecom Argentina.

Telecom Argentina has been granted non-expiring licenses to provide the following services in Argentina: Local fixed telephony; Public telephony; Domestic and international long-distance telephony; Domestic and international point-to-point link services; Domestic and international telex services; Value added services, data transmission, videoconferencing and broadcasting signal transport services; and Internet access.

Telecom Personal, the affiliated company dedicated to mobile services under the brand Personal, has been granted a non-exclusive and non-expiring license to provide mobile telecommunication services.

Núcleo, in Paraguay, has been granted a renewable five-year period license to provide mobile telecommunication services in Paraguay as well as Personal Communications Services (**PCS**) and Internet access in specific areas of the country.

The freezing of rates for fixed telephony

The Price Cap regime was the methodology originally applied to calculate changes in Telecom Argentina s basic services rates.

Following the 2001 economic crisis, the Public Emergency Law 25561 froze, from January 2002, all tariffs for fixed telephony services (provided under a concession regime by Telecom Argentina and Telefónica de Argentina), and explicitly prohibited rate adjustments. In accordance with this Law, in January 2002, rates for Basic telephone services and long-distance services were converted to pesos and fixed at an exchange rate of P$1.00=US$1.00. The rates Telecom Argentina may charge in the future will be determined by negotiations between Telecom Argentina and the Argentine government.

In accordance with the abovementioned Public Emergency Law, a Renegotiation Unit (**UNIREN**) was created, with the task to renegotiate the rates of all public services.

In May 2004 a Memorandum of Understanding (**MoU**) between the Government and each operator was agreed; the MoU maintained till December 2004 the same tariff level, and granted the continuity of other contractual rights.

In March 2006, Telecom Argentina executed a Letter of Understanding (the Letter of Understanding 2006) with the Argentine government pursuant to which Telecom Argentina will be permitted to raise the termination charge for international incoming calls, increase the time bands for peak-hour rates applied to local and domestic long-distance calls and incorporate certain modifications to the current regulatory framework.

The Letter of Understanding 2006 contemplated the signing and effectiveness of the Minutes of Agreement of the Renegotiation upon the fulfillment of certain necessary administrative steps.

As of the date of this Annual Report, such fulfillment has yet to occur, and the Public Emergency Law has been subsequently extended through December 31, 2013. Also, the freeze of regulated rates still remain in force. Therefore, the Price Cap regime is suspended and it is unknown if and when it will come back into effect or be replaced by other rate regulation procedures.

Universal Service (SU) Regulation

The obligation to pay contributions to the SU has been in force since January 2001 by the regulation approved by Decree 764/00 but could not be implemented.

The SU regime created by Decree No. 764/00 was modified in April 2008 by Decree 558/08. In defining SU the new regulation established two categories: (a) areas with uncovered or unsatisfied needs and (b) customer groups with unsatisfied needs. It also determined that the Secretary of Communication (SC) would have exclusive responsibility for the issuance of general and specific resolutions regarding the new regulation, as well as for its interpretation and application.

The new regime established that the SC will review SU programs which were established under the previous regulation, granting the continuity of SU programs already being administered and implementing programs that had been under review. The financing of SU ongoing programs which were recognized as such will be determined by the SC, whereas telecommunications providers appointed to participate in future SU Programs will be selected by competitive bidding.

The Decree requires telecommunications service providers to contribute 1% of their revenues (from telecommunication services, net of taxes) to the SU Fund and keeps the pay or play mechanism for compliance with the mandatory monthly contribution to the US Fund or, to claim the correspondent receivable, as the case may be.

On November 11, 2010, the SC issued Resolution No. 154/10 adopting the methodology for the deposit of the SU contributions to the trustee s escrow account. The Resolution includes several provisions related to the determination of the contributions that correspond to the periods before and after Decree No. 588/08 was issued. It also states that telecommunication providers may discount the amounts incurred in the implementation of the SU Initial Programs from the contributions to the SU Fund until the SC determines if those Initial Programs qualify as such. However, if as a result of the SC s verification some amounts are not recognized as Initial Programs, those amounts would have to be contributed into the SU Fund or would have to be allocated to develop US projects previously approved by the SC.

On January 26, 2011, the SC issued Resolution No. 9/11 establishing the Infrastructure and Equipment Program. The Resolution provides that telecommunication service providers can contribute to the projects in this program only the amounts corresponding to their pending SU contributions under Decree No. 764/00, before the effective date of Decree No. 558/08.

Incumbent operators have not yet received any set-offs for the services rendered under the SU regime since 2001, and the resolution by the SC of the appeals filed by Telecom Argentina are still pending.

In compliance with Resolution No. 154/10 Telecom Personal contributes to the SU Fund monthly.

In March 2011, Personal submitted to the SC an investment project, pursuant to SC Resolution No. 9/11, for the development of network infrastructure in locations in the Northern Region of Argentina with no mobile coverage. This program is still pending the approval of the SC.

Argentina Conectada Plan

In October 2010, the Government approved the Plan *Argentina Conectada* setting up a commission for the coordination of various initiatives to promote digital inclusion and broadband connectivity throughout the country.

The objectives of the plan are:

- the extension of broadband services to the majority of the country s locations by 2015;
-

the deployment and management by Arsat (public operator that so far has offered satellite services) of a new backbone network, renting fiber from existing operators or by sharing agreements (swaps) of optical fiber;

· the allocation of public funds of approximately 8 billion pesos (about 1.4 billion euro) within 3 years;

· the financing of broad band connectivity in schools and libraries through the Universal Service Fund.

Main regulatory developments

Spectrum

In May 2011 a tender for the allocation of frequencies in the 1900 band (called PCS) and 850 MHz bands (i.e. SRCM) was published. The frequencies were returned by Movistar (Telefónica Group), following the merger with Bell South in 2005 which resulted in it exceeding the limit of 50MHz (spectrum cap) applicable in each region (North, South, Greater Buenos Aires).

Personal took part in the spectrum auction process and expected to acquire additional spectrum to complete its Spectrum cap throughout Argentina, but, on September 5, 2012, SC notified Personal Resolution No. 71, by which, as provided for in Article 10 of the List of Conditions, the auction approved by SC Resolution No. 57/11 was canceled for reasons of opportunity, merit and convenience of the Argentine Government.

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Later in December 2012 two presidential decrees regarding spectrum were issued (decree 2426 and 2427), whose application will result in:

the direct allocation to the state-owned company ARSAT of the frequencies that should be awarded, by means of a mandate to the NRA (SECOM);

the creation of the virtual mobile operator commercial concept;

the allocation of the 700MHz (698MHz to 806MHz) and AWS (Advanced Wireless Services 1710-1755 MHz uplink, 2110-2155MHz downlink) bands to mobile telecommunication terrestrial services;

the declaration of public interest of the Federal Wireless Network), managed by the Ministry of Federal Planning, Public Investment and Services, to be executed through ARSAT, under the National Telecommunication Plan Argentina Conectada , which provides the infrastructure necessary for this purpose, according to the general guidelines established in the Decree s Annex;

the instruction to the Ministerio de Planificación Federal (Ministry of Federal Planning) being the majority shareholder of AR-SAT, to adopt the necessary actions and the business decisions of its responsibility for the execution and delivery of the services required as a result of the development the federal wireless network.

Also, on December 21, 2012, SC published in the Official Bulletin the Resolution No. 222/09 which assigned ARSAT the telecommunication services license authorizing the state company to provide any kind of telecommunication services with or without owned infrastructure. It also provided the authorization for the provision of value-added services, data transmission and transportation of audio and video signals.

By Resolution No. 9/13, published on February 7, 2013, the SC granted ARSAT the registration of Mobile Services and National and International Long Distance Services and the Provision of Telecommunication Facilities.

Mobile Number Portability Implementation

Mobile number portability was implemented from March 2012; a new Data Base Administrator (ABD) was set up to track the number portability.

Portability of mobile numbers are to be completed within 10 working days.

4.3.7 BROADCASTING REGULATORY FRAMEWORK IN ITALY

Consolidated Act on Broadcasting (Legislative Decree 177, July 31, 2005) and Legislative Decree 44, March 15, 2010

Broadcasting activity in Italy is mainly regulated by the Consolidated Act on Broadcasting (Legislative Decree July 31, 2005 n. 177), amended by Legislative Decree March 15, 2010 n. 44 (**Decree 44/10**), implementing the Audio Visual Media Services (**AVMS**) Directive, which entered into force on March 30, 2010.

Decree 44/10 introduced changes in the audio-visual legislation in the areas of advertising and product placement, promotion of European works, short extracts rights, protection of minors, and extends regulation to non-linear audio-visual services.

AGCom implemented the new rules through regulation, including the adjustment of authorizations already released prior to these new rules.

On June 30, 2011, AGCom approved a new regulation (Decision 353/11/CONS) for digital terrestrial broadcasting activities (both concerning network operators and content providers).

Logical Channel Numbering (LCN) Plan

On August 31, 2012, the State Council issued four judgments canceling the Automatic Numbering Plan and, in particular, the assignment to La7 and to MTV of respectively numbers 7 and 8. The State Council objected to the assignment of numbering 8 to MTV, considering the latter not a generalist but a thematic channel. There were no objections to La7 retaining its number 7.

With a resolution published in October 2012, AGCom launched a public consultation for the new numbering plan together with a new survey on users habits. As a consequence of the above public consultation, with a Resolution adopted on March 21, 2013 AGCom confirmed the assignment of the numbers 7, 8, and 9 to generalist channels defined as former analogic channels with programming and informative obligations (Decision 237/13/CONS). Such a decision leaves to La7 and MTV numbers 7 and 8 on the TV remote control.

The Switch off completion

As of July 4, 2012, the process of switch-off (complete move to digital broadcasting) across the country was completed.

Digitalization of broadcasting networks and frequencies

In response to the infringement procedure 2005/5086 filed by the EC against Italy, in June 2008 the Government passed Law n. 101, replacing the special licensing regime for digital terrestrial network operators with an authorization regime compliant with the Code of Electronic Communications and the EU Directives.

As a consequence, the licenses granted have been converted to general authorizations lasting 20 years.

The European Commission approved the changes introduced by Law 101/08, but asked more spectrum resources to be assigned to new entrants (the Digital Dividend). In response to these further requests, AGCom set up the criteria for the complete digital conversion of the television terrestrial networks.

AGCom established the National Plan of Assignment of the Frequencies (PNAF) which will provide for 21 national Digital Video Broadcasting-Terrestrial (DVB-T) networks with 80% coverage of national territory and 4 Digital Video Broadcasting- Handheld (DVB-H) national Networks. Out of the 25 networks, 5 DVBT and 1 DVBH will constitute the Digital Dividend to be assigned on the basis of competitive bidding procedures.

The Ministry for Economic Development Communication Department assigned to the Telecom Italia Media group only 3 DVB-T Networks (out of the 4 Networks managed by the Group). Telecom Italia Media group appealed against this decision in order to safeguard its interests.

Concerning the Digital Dividend, in November 2010 AGCom issued a Decision on the criteria to be adopted in the tenders for the assignment of the Digital Dividend based on a beauty contest with notice published in August 2011.

In December 16, 2011, the new Government suspended the Beauty Contest procedure and canceled it in April 2012.

On April 16, 2012, the Government approved a provision establishing that frequencies will be assigned by the Ministry for the Economic Development through a bidding auction within 120 days from the approval of such provision, on the basis of criteria defined by the Italian Authority. The provision was approved on May 2, 2012.

Telecom Italia Media group participated in the public consultation on the Regulation for the competitive procedure for the assignment of frequencies economic, which ended December 17, 2012 through TIMB, the network operator.

Following the scheme in consultation, 3 lots of frequencies below 700 MHz (LOTS L) should be assigned for a period of 20 years as well as 3 lots of frequencies above 700 MHz (LOTS U) expiring on December 31, 2017. The starting price of the bid is not defined.

TIMB is excluded from participating to the bid for LOTS L, having been treated as RAI and Mediaset, the incumbent operators on the Italian TV market.

PNAF and digital dividend for mobile services

In order to assign the frequencies in the digital switch off areas and for the DVB-T Digital Dividend AGCom issued a decision enforcing the National Plan of Assignment of the Frequencies.

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Furthermore, this decision provided a Digital Dividend for mobile service in the band 790-862 MHz (channels 61-69 Ultra High Frequency UHF) after the switch off of analogue broadcasting. The Italian Budget Law established that those frequencies, previously assigned to local televisions, should be used for mobile services. The tender took place in the summer 2011, with 4 billion euro revenues.

At the end of 2012 channels 61-69 were released by local broadcasters and assigned to mobile services. 175 million euros have been allocated to compensate local broadcasters current assignee of channel 61-69 in Piemonte, Lombardia, Veneto, Trentino Alto Adige, Friuli Venezia Giulia, Emilia Romagna, Lazio and Campania.

4.4 DISCLOSURE PURSUANT TO SECTION 219 OF THE IRAN THREAT REDUCTION AND SYRIA HUMAN RIGHTS ACT OF 2012 (ITRSHRA)

Section 219 of the Iran Threat Reduction and Syria Human Rights Act of 2012 added Section 13(r) to the Exchange Act. Section 13(r) requires an issuer to disclose in its annual or quarterly reports filed with the SEC whether the issuer or any of its affiliates has knowingly engaged in certain activities, transactions or dealings with the Government of Iran, relating to Iran or with designated natural persons or entities involved in terrorism or the proliferation of weapons of mass destruction during the period covered by the annual or quarterly report. Disclosure is required even when the activities were conducted outside the United States by non-U.S. entities and even when such activities were conducted in compliance with applicable law.

In accordance with our Code of Ethics and Conduct, we seek to comply with all applicable international trade laws including applicable sanctions and embargoes.

Activities relating to Iran

The only activities we have that, to our knowledge, relate in any way to Iran are:

i. roaming agreements with the following Iran mobile phone operators: Taliya, KFZO TKC (formerly Payam Kish), Irancell (MTN) and Mobile Company of Iran (MCI) (formerly TCI);

ii. commercial relationship for the delivery of traffic from Iran to our networks and from our networks to Iran (**International Carrier Agreements**). To this end, our subsidiary Telecom Italia Sparkle S.p.A. (**TI Sparkle**) directly and through its subsidiaries entered into agreements with Telecommunication Infrastructure Company (TIC) in Iran.

Roaming agreements

We operate one of the largest mobile network in Italy. Through our foreign subsidiaries, we also have large mobile operations in Brazil (Tim Participações S.A. by means of its subsidiary TIM Celular S.A.) and Argentina (Telecom Argentina S.A. by means of its subsidiary Telecom Personal S.A.).

It is pursuant to roaming agreements that a mobile customer is able to use his or her mobile phone on a network different from such mobile subscriber s home network. The following is the definition of roaming that we provide in the glossary of this Annual Report (see 4.5 Glossary of Selected Telecommunications Terms):

Roaming: *A function that enables wireless subscribers to use the service on networks of operators other than the one with which they signed their initial contract. The roaming service is active when wireless is used in a foreign country (included in GSM network).*

Like all major mobile networks, in response to the competition and customers demands, Telecom Italia, Tim Participações S.A. and Telecom Argentina S.A. have entered into roaming agreements with many foreign mobile networks, so as to allow their customers to make and receive calls abroad.

Roaming agreements are, including those relating to Iran, on standard terms and conditions. In fact, entering into roaming agreements is an activity carried out in the ordinary course of business by a mobile network operator.

Roaming agreements are, generally, reciprocal. Pursuant to a roaming agreement our mobile customers may, when in a foreign country covered by the network (the **Foreign Network**) of an operator with which we have a roaming agreement, make and receive calls on their mobile using such operator s network. Likewise, when a customer of such Foreign Network is in Italy (or Brazil or Argentina), such customer may make and receive calls using our networks or the networks of other mobile operators in Italy (or Brazil or Argentina) if this foreign Network has International Roaming Agreement with other Italian (or Brazilian or Argentine) Operators.

The calls made and received by our customers who use the services of the Foreign Network are billed by the Foreign Network to us at the roaming rate agreed upon in the applicable roaming agreement. Then, we will bill our end customers according to the specific tariff plan of the subscription they have signed with us. Likewise, we bill the Foreign Network at the roaming rate agreed upon in the applicable roaming agreement. The Foreign Network will bill its clients for the calls made and received using our networks according to their specific offer to their customer base. Roaming contracts do not, generally, contemplate other fees or disbursements.

In 2012, the impact on net profit (loss) arising from such Roaming contracts is analyzed as follows:

- our total revenues from roaming agreements with Iranian networks were approximately 330 thousand euros (of which 322 thousand euros recorded by Telecom Italia S.p.A.);

- our total charges from roaming agreements with Iranian networks were approximately 319 thousand euros (of which 296 thousand euros recorded by Telecom Italia S.p.A.).

The purpose of all of these roaming agreements is to provide our customers with coverage in areas where we do not own networks. For that purpose, we intend to continue maintaining these agreements.

International Carrier Agreements

As a rule in the modern telecommunication business, when traffic from a specific network is placed to or transported through a network of ours, we receive a fee from the incoming network. Likewise, when traffic coming from a network of ours is placed to or transported through another network, we owe a fee to such network.

In 2012, the impact on net profit (loss) arising from the above International Carrier Agreements is analyzed as follows:

- our total revenues from traffic from networks located in Iran to our networks were approximately 9.3 million euros; and

- our total charges from traffic to networks in Iran from our networks were approximately 0.4 million euros.

The purpose of this agreement is to allow exchange of international traffic. Consequently, we intend to continue maintaining this agreement.

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Furthermore, in 2012 our subsidiary Olivetti I-Jet in liquidation recorded 2,500 euros for the sale of a printer together with the related print heads.

All such amounts of revenues and charges are deminimis with respect to our consolidated revenues and operating expenses, respectively.

4.5 GLOSSARY OF SELECTED TELECOMMUNICATIONS TERMS

The following explanations are not intended as technical definitions, but to assist the general reader to understand certain terms as used in this Annual Report.

2G (second-generation Mobile System). Second-generation protocols using digital encoding and including GSM, D-AMPS (TDMA) and CDMA. 2G networks are in current use all over Europe and other parts of the world. These protocols support high bit rate voice and limited data communications. 2G networks technology offer auxiliary services such as data, fax and SMS. Most 2G protocols offer different levels of encryption.

3G (third-generation Mobile System). Third-generation wireless service, designed to provide high data speeds, always-on data access, and greater voice capacity. 3G networks allow the transfer of both voice data services (telephony, messaging) and non-voice data (such as downloading Internet information, exchanging email, and instant messaging). The high data speeds, measured in Mbps, are significantly higher than 2G and, 3G networks technology enable full motion video, high-speed internet access and video-conferencing. 3G technology standards include UMTS, based on WCDMA technology (quite often the two terms are used interchangeably) and CDMA2000.

Access charge. Amount charged per minute by national operators for the use of their network by operators of other networks. Also known as an interconnection charge .

ADSL (Asymmetric Digital Subscriber Line). A modem technology which converts existing twisted-pair telephone lines into access paths for multimedia and high-speed data communications. ADSL can receive Mbps and transmit over 832 Kbps in both directions. Such rates expand existing access capacity by a factor of 50 or more without new cabling.

Analog. A transmission which is not digital, e.g., the representation of voice, video or other not in digital form.

ANOs (Alternative Network Operators). Companies other than the incumbent operator which operate telecommunications systems in a national market.

Backbone. Portion of telecommunication network with the highest traffic intensity and from which the connections for services in the local areas depart.

Bitstream. Wholesale broadband access service which consists of supplying an access to XDSL Telecom Italia network and transmission capacity to the network of another Operator.

Broadband services. Services characterized by a transmission speed of 2 Mbit/s or more. According to international standards, these services are divided into two categories: (i) Interactive services, including videotelephone/videoconferencing (both point-to-point and multipoint); videomonitoring; interconnection of local networks; file transfer; CAD; highspeed fax; e-mail for moving images or mixed documents; broadband videotex; Video on demand; retrieval of sound programs or fixed and moving images; and (ii) Broadcast services, such as sound programs, television programs (including high-definition TV and pay TV) and selective document acquisition.

Broadcast. Simultaneous transmission of information to all nodes and terminal equipment of a network.

BSC (Base Station Controller). Interface with the MSC switching exchange. Has the task of supervising and controlling radio resources, both during the phase when a call is being set up and during the maintenance phase.

BSS (Business Support System). The system used by network operators to manage business operations such as billing, sales management, customer-service management and customer databases. A type of Operations Support System (OSS).

BTS (Base Transceiver Station). Radio base station which sends the GSM radio signal via the antenna to cover an area (cell) and coordinates one or more radio transceivers (TRX).

Bundle. Commercial offer including different telecommunication services (voice, broadband internet, IPTV, other) by an operator under the same brand. *Bundle Dual Play* offer includes fixed telecommunication services and broadband internet; *bundle Triple Play* offer is the bundle dual play integrated with IPTV; *bundle Quadruple Play* offer is the bundle triple play integrated with mobile telecommunication services.

Carrier. Company that makes available the physical telecommunication network.

CDMA (Code Division Multiple Access). A digital wireless technology used in radio communication for transmission between a mobile phone and a radio base station. CDMA was developed by Qualcomm, and commercially introduced in 1995. It enables the simultaneous transmission and reception of several messages, each of which has a coded identity to distinguish it from the other messages.

Cell. Geographical portion of the territory illuminated by a BTS: 900MHz / 1800MHz.

Cellular. A technique used in mobile radio technology to use the same spectrum of frequencies in one network multiple times. Low power radio transmitters are used to cover a cell (i.e., a limited area) so that the frequencies in use can be reused without interference for other parts of the network.

Channel. The portion of a communications system that connects a source to one or more destinations. Also called circuit, line, link or path.

Closed User Group. A group of telecommunications users that share a longstanding economic interest. This definition has arisen in a regulatory context; it permits the partial liberalization of some telecommunications services.

Community. A group of customers who have subscribed to specific offers which include special pricing for traffic towards other customers of the same telco.

D-AMPS (Digital-Advanced Mobile Phone Service). It is a digital version of AMPS (Advanced Mobile Phone Service), the original analog standard for cellular telephone service in the United States.

DCS 1800 (Digital Communication System). A derivative of the GSM cellular mobile telephone standard. 1800 refers to the frequency used of 1800 MHz. DCS 1800 is the European PCN standard.

Digital. A mode of representing a physical variable such as speech using digits 0 and 1 only. The digits are transmitted in binary form as a series of pulses. Digital networks are rapidly replacing the older analog ones. They allow for higher capacity and higher flexibility through the use of computer-related technology for the transmission and manipulation of telephone calls. Digital systems offer lower noise interference and can incorporate encryption as a protection from external interference.

Digital divide. The gap between people with effective access to digital and information technology and those with very limited or no access at all. The term encompasses among others: gaps in ownership of or regular access to a computer, internet access today primarily broadband, and related skills.

Digital Terrestrial TV. Digital Terrestrial Television Broadcasting is a new type of broadcasting technology that provides a more effective way of transmitting television services using a digital system instead of the existing analogue system.

DSL Network (Digital Subscriber Line Network). A network built on existing telephone lines with DSL technology devices which use sophisticated modulation schemes to pack data onto copper wires for connections from a telephone switching station to a home or office.

DSLAM (Digital Subscriber Line Access Multiplexer). The DSLAM denotes telecommunications equipment able to process digital signals of various clients and multiply them in a data link to the nodes of the Internet.

DVB H (Digital Video Broadcasting Handheld). DVB H technology combines digital video with the Internet Protocol (IP): contents are subdivided into packets using the same basic technology employed by the Internet. The use of IP technology allows the transmission of TV and radio programs, web pages, music and video games to smartphones/PDA s.

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DWDM (Dense Wavelength Division Multiplexing). This is a technology for multiplying and transmitting different wavelengths along a single optical fiber contemporaneously.

EDGE (Enhanced Data for GSM Evolution). This is a powerful technology that increases the data transmission rate of the GPRS standard from rates of 30-40 kbit/s to more than 100 kbit/s and even up to 200 kbit/s with optimal radio conditions.

Exchange. See Switch.

FTT HOME, FTT CURB, FTT (*Fiber to the* **).** It is the term used to indicate any network architecture that uses fiber optic cables in partial or total substitution of traditional copper cables used in telecommunications networks. The various technological solutions differ in the point of the distribution network where the fiber connection is made, with respect to the end-user s location. In the case of **FTT Curb** (Fibre to the Curb) the fiber connection reaches the equipment (distribution cabinet) located on the pavement, from where copper connections are run to the customer; in the case of **FTTHome** (Fibre to the Home), the fiber connection terminates inside the customer premises.

Gateway. A connection between the LANs and WANs of one or more suppliers. Can also mean the access nodes to international networks of various kinds.

GGSN (**Gateway GPRS Support Node**). Junction connecting an external packed network or GPRS system of a different mobile network.

GPON (Gigabit capable Passive Optical Network). A passive optical network (PON) is a network architecture that brings fiber cabling and signals to the home using a point-to-multipoint scheme that enables a single optical fiber to serve multiple premises.

GRX (GPRS Roaming eXchange for Mobile Operators). The GRX service allows Mobile Operators to interconnect GPRS networks around the world and offer global GPRS roaming coverage.

GSM (Global System for Mobile Communication). A standard for digital cellular telephony used in the world and working on 900MHz and 1800MHz band.

HDSL (High-bit-rate Digital Subscriber Line). Technology for business customers which allows the provision of local loop circuits at higher speeds and lower cost than through conventional means.

Home Access Gateway Access Gateway Home gateway Residential Gateway. A residential gateway is a home networking device, used as a gateway to connect devices in the home to the Internet or other WAN.

HSDPA (High-Speed Downlink Packet Access/UMTS Hi Speed Universal Mobile Telecommunications System). UMTS evolution allows broadband connections up to 3.6 Mbps.

HLR (Home Location Register). Database where are recorded the customer data.

Kvar (kilovolt amperes reactive). Reactive energy: measurement system, expressed in kilovolt, of power losses in an AC electrical system.

ICT (Information and communication(s) technology). Broad area concerned with information technology, telecommunications networking and services and other aspects of managing and processing information, especially in large organizations.

IEEE (Institute of Electrical and Electronics Engineers). An organization of engineers, scientists and students involved in electrical, electronics and related fields. IEEE also functions as a publishing house and standards body.

IMSI (International Mobile Subscriber Identity). The International Mobile Subscriber Identity is a unique identification associated with all cellular networks. It is stored as a 64 bit field and is sent by the phone to the network.

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Interactive. Allowing the user to change some aspect of the program.

Internet. The world s best-known data network. Initially used by the U.S. Department of Defense, the Internet now provides an interface for networks based on different technologies (LANs, WANs, data networks, etc.), but which use the TCP/IP protocol platform.

Internet Protocol TV or IPTV. The service provides the distribution of television channels over Internet connections using the IP protocol. More than just duplicating a distribution means, IPTV enables interactive services so that the viewer can interact with the show as it is broadcast.

IP (Internet Protocol). A set of communications protocols for exchanging data over the Internet.

IP/MPLS (Internet Protocol/Multi Protocol Labeling Switching). A packet switching protocol to optimize network behaviors of mapping Layer3 (IP) end-to-end data flow to Layer2 traffic between adjacent network nodes.

IPTV (Internet Protocol Television). A system that utilises the Internet Protocol infrastructure to transmit digital television content over a network and deliver it via a broadband Internet connection.

ISDN (Integrated Services Digital Network). A system in which several services (e.g., speech and data) may be simultaneously transmitted end to end in digital form.

ISPs (Internet Service Provider). A vendor who provides access to the Internet and World Wide Web.

ITU (International Telecommunication Union). The worldwide policy, spectrum regulation and standardization body in telecommunication operating under the auspices of the United Nations.

LAN (Local Area Network). A private network that covers a local geographic area and provides public telecommunications services as well as interconnection between personal computers.

LLU (Local Loop Unbundling). System through which OLO can rent the last mile of local loop, connecting to their equipments.

Local Loop. Copper wire-couple, through which the telephone connection reaches users; it is the foundation of traditional telephone lines and it is often called last mile .

LTE (Long Term Evolution). Represents the fourth generation (4G) mobile phone systems. LTE belongs to the standard 3GPP (Third Generation Partnership Project) and it is the latest evolution of GSM / UMTS / HSPA standard. LTE offers a higher spectral efficiency in bits per Hertz and download bandwidth up to 150 Mbit / s per cell reducing the latency time. LTE enabled services that require high interactivity (eg, gaming, video conferencing). A further development of LTE, called LTE Advanced , will perform bitrates even higher.

MGCP (Media Gateway Control Protocol). An Internet Engineering Task Force (IETF) signaling protocol proposal allowing a bridge between classic telephone networks and Internet (i.e., IP-based) infrastructures.

MEMS (Micro-Electro-Mechanical Systems). MEMS are miniaturized devices ranging in size from a few micrometers to a few millimeters, which execute one or more monitoring, processing or actuation functions by deploying a combination of electronic, mechanical, optical, chemical or biological components integrated on a usually silicon hybrid circuit.

MGW (Media GateWay). Junction for the connections which carry user traffic.

MPLS (Multi Protocol Label Switching). A packet switching protocol to optimize network behaviors of mapping Layer3 end-to-end data flow to Layer2 traffic between adjacent network nodes.

MS SPRING. A form of traffic protection mechanism for the equipment.

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MSC (Mobile Switching Center). Executes functions such as controlling calls, switching traffic, taxation, controlling network interfaces and acts as an interface with other networks.

MSP. The name of a general purpose programmable switch made by Redcom Laboratories.

Multimedia. A service involving two or more communications media (e.g., voice, video, text, etc.) and hybrid products created through their interaction.

MVNO. (Mobile Virtual Network Operator). MVNO Is a wireless communications services provider that does not own the radio spectrum or wireless network infrastructure over which the MVNO provides services to its customers.

Network. An interconnected collection of elements. In a telephone network, these consist of switches connected to each other and to customer equipment. The transmission equipment may be based on fibre optic or metallic cable or point to point radio connections.

NGAN (New Generation Access Network). New generation network access that can be realized with different technological solutions, typically fiber optic and VDSL pairs.

NGNs (Non-Geographic Numbers). The non-geographic numbers are unique as they are by definition not associated with any particular geographic location (*e.g.* premium rate services, toll free, directory assistance services).

NGN2 (Next Generation Network). New generation network created by Telecom Italia to meet the demands of corporates, public administrations and citizens. The new network architecture guarantees an infrastructure designed to face multiple offers by increasing customisation levels and bandwidth availability, removing bandwidth limits and providing an impressive capacity along with a wide selection of access systems.

Node. Topological network junction, commonly a switching center or station.

Node B (counterpart of BTS in GSM). This is the Radio Base Station in UMTS technology which, via an antenna, sends the UMTS radio signal which creates the coverage of the cell (typically 3 for Node B). It also performs functions which are strictly associated with managing the radio connection.

OLOs (Other Licensed Operators). Companies other than the incumbent operator which operate telecommunications systems in a national market.

Optical fiber. Thin glass, silica or plastic wires, building the interstructure base for data transmission. An optical fiber cable contains several individual fibers, and each of them is capable of driving a signal (light impulse) at illimited bandwidth. Optical fibers are usually employed for long-distance communication: they can transfer heavy data loads, and the signal reaches the recipient, protected from possible disturbances along the way. The driving capacity of optical fibers is higher than the traditional cable ones.

OSS (Operations Support System). Methods and procedures (whether mechanized or not) which directly support the daily operation of the telecommunications infrastructure.

OTT (Over the Top) players. Operators offering contents and services on the internet without owning the proprietary TLC network infrastructure.

Outsourcing. Hiring outsiders to perform various telecommunications services, which may include planning, construction, or hosting of a network or specific equipment belonging to a company, and, ultimately, the management of entire telecommunications systems. Value-added applications may also be provided in various sectors.

Packet-Switched Services. Data services based on parceling or breaking the data stream into packets and switching the individual packets. Information transmitted (whether voice or data) is segmented into cells of a standardized length, which are then transmitted independently of one another, allowing maximization of available capacity and usage of single transmission path for multiple communications. The cells are then reassembled upon reaching their destination.

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Pay-Per-View or PPV. A system by which the viewer pays to see a single program (such as a sporting event, film or concert) at the moment at which it is transmitted or broadcast.

Pay TV. Paid-for TV channels. To receive Pay TV or Pay-Per-View programs, a decoder must be connected to the television set, and a conditional access system.

PCS. Personal communications services.

PDA (Personal Digital Assistant). A handheld computer with a memory size up to several megabytes and a touch-sensitive screen, often using a stylus to input data. The PDA is mainly used for calendar, address book and memoranda functions, but can incorporate advanced office or multimedia functions such as voice calls, messaging, video, mp3 player, etc.

Penetration. The measurement of the take-up of services. As of any date, the penetration is calculated by dividing the number of subscribers by the population to which the service is available and multiplying the quotient by 100.

Platform. The total input, including hardware, software, operating equipment and procedures, for producing (production platform) or managing (management platform) a particular service (service platform).

POP (Point Of Presence). Internet provider locations for network connection, often through dial-up phone lines. When a Pop is within a specific local area, users can connect to the Internet by dialing a local phone number.

POTS (Plain Old Telephone Service). Refers to the basic telephony service (homes use) supplying standard, single-line telephones, fixed-line services and access to public voice telephony network. In contrast, telephone services based on digital communications lines, such as ISDN, are not POTS. The main distinctions between POTS and non-POTS services are speed and bandwidth. POTS is generally restricted to about 52 Kbps.

PSTN (Public Switched Telephone Network). The public telephone network delivering the basic telephone service and, in certain circumstances, more advanced services.

RNC (Radio Network Controller counterpart of BSC in GSM). Supervises and controls radio resources, both during the phase of setting up the call, and during the maintenance phase (for example, handover between different cells). Furthermore, it handles connectivity from and towards: Node B, MSC*, and other RNC.

Roaming. A function that enables wireless subscribers to use the service on networks of operators other than the one with which they signed their initial contract. The roaming service is active when wireless is used in a foreign country (included in GSM network).

RTG. Is the network of the world s public circuit-switched telephone networks in much the same way that the Internet is the network of the world s public IP-based packet-switched networks.

SDH Standard (Synchronous Digital Hierarchy). The European standard for high-speed digital transmission.

Service Provider. The party that provides end users and content providers with a range of services, including a proprietary, exclusive or third-party service center.

SGT (Transit exchange interconnection level for telephone traffic). Transit Exchange for telephone traffic carriage, routing and transmission.

SGU (Local exchange interconnection level for telephone traffic). Local Exchange for telephone traffic carriage, routing and transmission.

Shared Access. Methods of shared access, through the user s duplex cable, with another TLC service provider. This method permits the retention of voice telephony from Telecom Italia (or other operators) alongside ADSL on the proprietary network of the shared access operator, that is, not passing through the Telecom Italia networks but travelling directly along the operator s channels at the substation.

SME. The small- and medium-size enterprise market which consists of businesses having between 3 and 50 employees.

SMS (Short Message Service). Short text messages that can be received and sent through GSM-network connected cellular phones. The maximum text length is 160 alpha-numerical characters.

SNCP. A form of traffic protection mechanism for the equipment.

SOHO. The small office/home office market which consists of businesses that use telephone lines to connect to the Internet, as opposed to dedicated lines, and is made up of small businesses, generally with one or two employees, and businesses conducted out of the home.

Switch. These are used to set up and route telephone calls either to the number called or to the next switch among the path. They may also record information for billing and control purposes.

Synchronous. Type of data transmission in which there is permanent synchronization between the transmitter and the receiver.

TDMA (Time Division Multiple Access). A technology for digital transmission of radio signals between, for example, a mobile phone and a radio base station. TDMA breaks signals into sequential pieces of defined length, places each piece into an information conduit at specific intervals and then reconstructs the pieces at the end of the conduit.

TRX. Radio transceivers located in BTS.

ULL (Unbundling Local Loop). System through which ANO can rent the last mile of local loop, connecting to their equipments.

UMTS (Universal Mobile Telecommunications System). Third-generation mobile communication standard. It s constituted by a broadband system in which data travel at 2Mb-per-second, communication is faster, quality is better and multimedia contents can travel trough the Net.

UMTS Cell. Geographical portion of the territory illuminated by a Node B.

UMTS Channels. These enable all the customers of the cell to access both the CS (Circuit Switched) services and the PS (Packet Switched) services of UMTS technology.

Unbundling. A process which allows telephone carriers (other than Telecom Italia) to lease the last part of the telephone loop, that is to say, the copper wire-cable, connecting Telecom Italia central station to the user s home, disconnecting the user from Telecom terminals and connecting him/her to the telephone carrier s terminals.

Universal service. The obligation to supply basic service to all users throughout the national territory at reasonable prices.

VAS (Value Added Services). Value Added Services provide a higher level of functionality than the basic transmission services offered by a telecommunications network for the transfer of information among its terminals, which include wired or wireless switched-circuit analog voice communications; direct unrestricted digital point-to-point service at 9,600 bit/s; packet switching (virtual call); direct broadband analog transmission of TV signals, and supplementary services, such as closed user groups; call waiting; collect calls; call forwarding, and identification of number called. Value Added Services performed by the network, the terminals or the specialized centers include message handling services (MHS) (which can be used, among other things, for commercial documents in predetermined formats); electronic directories listing users, network addressees and terminals; e-mail; fax; teletex; videotex and videotelephone. Value Added Services could include also value added voice telephony services such as Freephone or Premium Rate Services.

VDSL (Very-high-data-rate Digital Subscriber Line). Access technology that allows providers to give clients, by means of an apparatus installed in their homes, access to voice and TV services on the traditional telephone line with a speeds of up to 100 Mbps in downstream (VDSL2).

VOD (Video On Demand). TV-programme supply on user s request, with payment of a fee for each purchased programme (a movie, a soccer match, etc). Broadcast in a special method for cable and satellite TV.

VoIP (Voice Over IP). Transmission of voice communications over Internet Protocol (IP) data networks, such as IP-based LANs, intranets or the Internet.

VPN (Virtual Private Network). A network designed for a business or government agency, using the infrastructures of a carrier and providing customized services, and which operates in such a manner as to appear dedicated to the user thereof.

WAN (Wide Area Network). A private network that covers a wide geographic area using public telecommunications services.

WI-FI. A service for wireless Internet connection and high speed access.

WLL (Wireless Local Loop). The means of configuring a local loop without the use of wiring.

Wi Max (Worldwide Interoperability for Microwave Access). The Wi MAX is a technology that allows wireless access to broadband telecommunications networks. It is defined by the Wi MAX Forum, a global consortium formed by major companies in the field of fixed and mobile telecommunications which has the purpose to develop, test and promote the interoperability of systems based on IEEE 802.16-2004 standards for fixed access and IEEE.802.16e-2005 for fixed and mobile access.

WLR (Wholesale Line Rental). The WLR Service consists in the resale to wholesale of the basic telephony services and advanced ISDN associated with the fees paid by certified residential and non-residential customers of Telecom Italia s public telephone network.

XDSL (Digital Subscriber Line). It is a technology that makes use of standard telephone lines and it includes different categories including: ADSL Asymmetric DSL, HDSL High-data-rate DSL and VDSL, Very high bit rate DSL. This technology uses a digital signal with a very high frequency in order to increase the data transfer rate.

4.6 DESCRIPTION OF PROPERTY, PLANT AND EQUIPMENT

GENERAL

As of December 31, 2012 and 2011, property, plant and equipment owned and leased are detailed as follows:

	As of December 31, 2012				As of December 31, 2011			
	Owned	Leased	Total property, plant and equipment	% of total property, plant and equipment	Owned	Leased	Total property, plant and equipment	% of total property, plant and equipment
	(millions of euros, except percentage)							
Land	232		232	1.5	235		235	1.5
Civil and industrial buildings	698	972	1,670	10.8	795	1,042	1,837	11.5
Plant and equipment	11,837		11,837	76.5	12,108		12,108	75.7
Manufacturing and distribution equipment	39		39	0.3	32		32	0.2
Other	677	17	694	4.5	724	16	740	4.6
Construction in progress and advance payments	982	25	1,007	6.5	1,005	36	1,041	6.5
Total	**14,465**	**1,014**	**15,479**	**100.0**	**14,899**	**1,094**	**15,993**	**100.0**

The principal categories of our equipment are exchanges and transmission equipment, cable networks, base stations for cellular networks and equipment for radio communications. There are no encumbrances that may affect our utilization of our property or equipment.

Real Estate (Land, Civil and Industrial Buildings)

As of December 31, 2012, the Company owned many buildings located throughout Italy. Specialized buildings for telecommunications services account for the majority of properties both in number and book value. Such buildings house mainly exchange equipment and transmission equipment, and are used as part of our continuing telecommunications operations. General purpose properties consist chiefly of offices, depots and computer centers.

Network Infrastructure (Plant and Equipment)

The Telecom Italia Group network infrastructure includes the domestic and international fixed network, the domestic mobile network, the Brazilian mobile network and the Argentinean and Paraguayan Networks. See -4.5 Glossary of Selected Telecommunications Terms , for definitions of the technical terms used in this section.

Domestic Fixed Network

General. Our domestic fixed voice network consists of 611 main local switches. Concerning the OLO interconnection, each local switch belongs to only one of the 33 gateway areas. Each local switch is physically interconnected to 2 out of 24 (12 pairs) Backbone Nodes (**BBN**).

The fixed long-distance transmission network (Arianna SDH and Phoenix) routes 4,819 VC-4, supports also 93 optical channels 2.5 Gbps point to point and more than 620 optical channels 10 Gbps point to point (also called lambdas from the greek letter l used for wavelength in physics).

In terms of cable infrastructures, the fixed network includes 114.5 million km of copper pairs, mainly in the distribution network and also 5.7 million km of fiber, both in access and trunk network.

Fiber optic cables significantly increase network capacity and make it possible to offer hi-tech services based on the simultaneous transmission of various types of signal, such as voice, data and video.

At December 31, 2012, the domestic fixed network had the following figures:

Central Offices	approximately 10,400
Switching areas	611
Gateway areas (TDM)	33
Aggregation areas	12
Copper network	114.5 million kilometers-pair
Fiber optic access/carrier network	5.74 million kilometers-fiber
Long Distance VC4	4,819
Long Distance Lambda	93 at 2.5 Gbps more than 627 at 10 Gbps
BroadBand/ADSL network	9,135 Central Offices covered
Main PoP data networks	32

TRANSMISSIONS. The Synchronous Digital Hierarchy (**SDH**) transmission systems operates on fiber optics from 155 Mbit/sec up to 10 Gbit/sec.

The nationwide network (Long distance) has been continuously upgraded during 2012. It is based on SDH and optical DWDM technology (Dense Wavelength Division Multiplexing) and still represents the Telecom Italia high capacity transport network.

In order to save fibers usage, DWDM systems have been implemented to multiply, by a factor of 12 up to 96, the available optical fiber band and the current transmission capacity, thus increasing the total transport capacity.

OPB (Optical Packet Backbone). In 2012 Telecom Italia continued to introduce in the data backbone the Terarouter technology, deployed in the majority of the 32 PoPs of the network (in 2013 all the POPs will be updated). At the end of 2012 OPB network had Terarouter nodes in the following PoPs: two Centro Stella PoPs in Rome, two Centro Stella in Milan (Inner Core PoPs) and twenty-eight OPB PoPs located in Naples, Turin, Florence, Palermo, Bari, Bologna, Brescia, Padua, Catania, Nola, Venice, Pisa, Ancona, Taranto, Modena, Verona, Catanzaro, Rimini, Bolzano, Perugia, Pescara, Alessandria, Savona, Bergamo, Cagliari, Genova, Trieste and Como (Outer Core PoPs).

The OPB network support:

· Internet traffic of residential, business and Wholesale customers;

· VPN traffic (Virtual Private Network) of business customers;

· Voice traffic;

· Video traffic related to IPTV services;

· Mobile data traffic.

OPM (Optical Packet Metro). At the end of 2012 OPM network consisted of 30 metro-regional networks to collect traffic to and from customers through IP DSLAM to supply IPTV and xDSL services. The OPM supports also the services based on Gigabit Ethernet technology (the Ethernity, Hyperway, Gigabusiness and GEA services on GBE optical access). At the end of 2012 Gigabit Ethernet Access was available in 59 towns in Italy. Moreover the OPM network is used for backhauling UMTS and LTE access Nodes.

Broadband/xDSL network. Telecom Italia s broadband network offers hi-tech telecommunications services and multimedia applications. In 2012, the xDSL commercial services for residential and business customers (retail and wholesale) have been extended to 7,351 towns, including S. Marino (compared to 7,241 at the end of 2011). At the end of 2012 9,135 local switching areas were covered by ADSL technology (compared to 9,002 at the end of 2011, consolidated data).

NGAN (Next Generation Access Network). In 2012 Telecom Italia continued to deploy its NGAN based on optical fiber cables. The NGAN deployment is based on FTTH (Fiber To The Home) and FTTCab (Fiber To The Cabinet) architecture. Up to now FTTH have been utilized for deployment in Milan while FTTCab in all other cities.

FTTCab uses fiber to the street cabinets equipped with VDSL2 cards.

By the end of 2012 about 2,300,000 households had been passed in the following cities: Ancona, Bari, Bergamo, Bologna, Brescia, Brindisi, Catania, Catanzaro, Como, Firenze, Forlì, Genova, L Aquila, Milano, Monza, Napoli, Padova, Palermo, Perugia, Pisa, Prato, Reggio Emilia, Roma, Taranto, Torino, Treviso, Udine, Varese, Venezia, Verona, Vicenza.

Telecom Italia normally installs new optical cables; in Milan Telecom Italia has also acquired the right of use (IRU approach) for 15 years on fiber optics owned by Metroweb (a utility that already owns a widespread optical access network in Milan).

Domestic Mobile Network

The domestic mobile network consists of:

- GSM network (2G: second generation network);
- UMTS network (3G: third generation network);
- LTE network.

On December 31, 2012 Telecom Italia domestic mobile network had the following figures:

GSM/EDGE network

- 16,778 BTS (Base Transceiver Station) GSM radio station (15,298 BTS at the end of 2011) +9.7%;
  - 1,435 of them are µBTS;
- 807,664 radio channels (784,056 at the end of 2011) +3%;
- 280 BSC (Base Station Controller) (382 at the end of 2011), -27% due to the adoption of new generation more performing equipments;

- GSM Core Network: 10 Transit Exchange and 13 Gateways.

UMTS/HSPA network

- 13,643 node B UMTS radio base station (12,943 node B at the end of 2011) +5.4%;
- 2,017,232 radio channels (1,958,944 radio channels at the end of 2011) +2.98%;
- 117 RNC (Radio Network Controller) +8 new RNC compared to total at the end of 2011;
- GSM/UMTS Core Network: 67 MSC-server; 110 MGW; 42 HLR (Home Location Register); 23 GGSN; 47 SGSN.

In 2012 Telecom Italia continued the implementation plan to distribute the High Speed Downlink Packet Access (**HSDPA**) and the High Speed Uplink Packet Access (**HSUPA**); these systems aim to increase the overall data transmission speed offered by UMTS.

In particular the deployment of **HSDPA at 42 Mbit/s** reached the coverage level of the 20% of the resident population.

LTE network

After an auction, in September 2011, additional frequency blocks on 800 MHz, 1800 MHz and 2600 MHz were acquired by Telecom Italia.

The three bands will be used for LTE deployment to provide ultrabroadband services to mobile customers.

As of the date of this Annual Report, the LTE network covers the major Italian cities.

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International Fixed Network

Telecom Italia Sparkle provides voice, IP and data connectivity services to national and international wholesale customers and to multinational corporates relying on an international network made of a proprietary cross-border backbone and bilateral connections.

The coverage of the Mediterranean and of Central and South America is provided by the interconnection with Lan Med Nautilus regional backbones.

Telecom Italia Sparkle international backbone spans 450,000 km covering all of the major regions worldwide and connects over 500 international voice operators.

The cross-border backbone integrates 4 regional networks:

· Europe (**PEB**);

· Latin America backbone;

· Mediterranean basin backbone;

· USA backbone.

In detail:

· **PEB (Pan European Backbone)**. Proprietary fiber optic network spanning the main European countries: Italy, France, United Kingdom, Netherlands, Belgium, Germany, Switzerland, Austria, Spain, Czech Republic, Slovakia and Romania. The overall length is 55,000 km.

· **Latin American backbone**. High-capacity backbone based on fiber optic ring networks, both terrestrial and submarine, with an overall length of 30,000 km, including the Miami-New York section. The ring has a capacity up to 1.8 Tbit/sec and has automatic optical traffic protection connecting the main cities of South and Central America to North America.

· **Mediterranean backbone**. Submarine ring network with a highly reliable configuration, a total length of 7,500 km and a design capacity close to 4.5 Tbit/sec connecting the main markets of the Mediterranean area: Italy, Greece, Cyprus, Turkey and Israel. Currently, the main landing points are Catania, Athens, Chania-Crete, Haifa, Tel Aviv and Istanbul.

- **USA backbone**. Proprietary high capacity terrestrial backbone with POPs in: Newark, New York, Miami, Ashburn, Atlanta, Chicago, Palo Alto, Los Angeles and Dallas.

The services supplied include Voice, IP and Managed Bandwidth in Europe and in the USA, Managed Bandwidth and IP in the Mediterranean and in South America.

Telecom Italia Sparkle s network is an integrated multi-service backbone based on an IP-MPLS core handling differentiated classes of services. The transport layer is based over DWDM with 10, 40 and 100 Gbit/s optical lambdas while voice services are provided by Class 4 switches.

Traffic protection is implemented by MS SPRING (Multiplex Section Shared Protection Ring), SNCP (Sub Network Connection Protection), OTN (Optical Transport Network), MSP 1+1 (Multi Section Protection) and meshed technologies.

In 2012 capacity upgrades were carried out on the international backbone in order to cope with increasing IP and Managed Bandwidth sales.

In order to support the Internet traffic increase, all of the major IP PoPs were upgraded and a new fiber optic metro ring was built in Amsterdam connecting the Pan European backbone to the Evoswitch telehouse with the aim to interconnect with major content providers.

In Paris a new POP in the Equinix telehouse along with a new router in the Courbevoie POP were made available in order to extend the coverage of the MEF (Metro Ethernet Forum) compliant Ethernet services and to support the sales growth.

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In the Milan POP additional new generation IP cards were added in the existing Terabit Routers multi-chassis architecture in order to strongly increase the number of 10Gbit/s links handled.

IP architecture was deeply reviewed in the Frankfurt POP connecting local edge routers to the IP-MPLS core in the Milan PoP in order to optimize traffic routing and the expenditures for additional upgrades.

In the Pan European backbone major activities were carried out also on the transport network: the OTN technology was extended to all of the main POPs (London, Frankfurt, Amsterdam, Paris, Marseille). As regards the SDH and metro DWDM platforms, outdated equipment was decommissioned in order to reduce operation and maintenance costs and capital expenditures for new upgrades.

With reference to submarine cables, additional capacity on IMEWE and SMW-4 was delivered by the cable consortia while the Mestre-Umagcable linking Italy to Croatia underwent a 20Gbit/s upgrade.

In the USA backbone, outdated routers were replaced by advanced Ethernet equipment in order to strongly increase the IP traffic that can be handled and provide MEF compliant services and traffic protection technologies. The new IP equipment is now available in New York, Ashburn, Miami, Dallas, Atlanta and Los Angeles. A backbone capacity upgrade among the New York, Newark and Miami POPs was also completed.

In Singapore, the capacity on the fiber backhaul linking the POP to the Sea-Me-We3 and Sea-Me-We4 landing station in Tuas was expanded. A new advanced Ethernet router was introduced replacing an SDH router in order to address the increasing demand for Ethernet services. Backbone upgrades were also carried out on the Singapore-Hong Kong-Palo Alto route adding a new 10Gbit/s link while capacity between Singapore and Los Angeles was groomed replacing the existing 2,5Gbit/s links with a single 10Gbit/s trunk.

In the Djibouti IP POP which is managed through the partnership with a local operator, access capacity was nearly doubled in order to keep up with increasing sales to regional customers.

As for mobile services, a new SBC (Session Border Controller) equipment was deployed in the Newark POP for the IPX interconnections. SBC equipment handle inter-alia VoIP (Voice over IP) traffic allowing an improved interworking among all the interconnected networks and an end-to-end monitoring of the Quality of Service.

Outdated DNS servers for GRX (GPRS Roaming eXchange) and IPX services were replaced and SS7 and SIGTRAN (Signaling over IP protocol) signaling networks were upgraded. New capabilities mainly for Mobile number portability management were deployed in the SMS Hub and SMS Transit platforms.

With reference to voice services, a new hub was deployed in Milan for the management of the remote DCMEs (Digital Multiplex Compression Equipment) installed in the far end voice operators premises. The pre-paid traffic platform was upgraded in terms of number of concurrent calls that can be handled. In addition, a new software release was uploaded in the Softswitches and SBC s in order to increase traffic filtering and routing capabilities.

As regards the service offer for multinational corporates, a new access layer for MEF compliant Carrier Ethernet services was deployed in all of the major POPS: Milan, Frankfurt, Paris, London, Hong Kong, Chicago, Newark, Miami, Bucharest, Singapore and Dubai. In Dubai a new POP was opened partnering with a local operator in order to offer both Ethernet over SDH (EoSDH) and Ethernet over MPLS (EoMPLS) services. New EoSDH equipment were deployed also in Catania for the interconnection with LANMED backbone and in a customer s site in Rome. A new IPsec router was added in the Newark POP. Access capacity was also increased in Frankfurt, Prague and Milan to cope with sales growth.

Mediterranean Backbone

In 2012 a new IP POP was deployed in Sofia along with a fiber optic link connecting Istanbul and Sofia. Major upgrades were also completed on the express Tel Aviv-Cyprus fiber (+200Gbit/s), on the Catania-Istanbul fiber (+100Gbit/s) and on the Italy-Greece-Israel Omnibus fiber (+250Gbit/s) of the MED cable.

Latin American Backbone

In 2012 40Gbit/s DWDM platform were deployed on the SAC ring along with the existing 10Gbit/s platform. Upgrades were also completed on the MAC (40Gbit/s), Cooks (30Gbit/s) and TAC (70Gbit/s) network segments.

Brazilian Network

Telecom Italia Group s principal properties in Brazil consist of transmission equipment, switching equipment, which connect calls to and from customers, and radio base stations, which comprise certain signal transmission and reception equipment covering a defined area. At our radio base stations we have also installed antennas and certain equipment to connect these antennas with our switching equipment.

As of December 31, 2012, we had 118 mobile switches for voice capacity, 212 thousand TRXs, 8,256 Node B and approximately 39,000 kilometers in fiber optic cable networks (of which 11,500 in metropolitan areas and 27,400 for Long Distance coverage). We generally lease or buy the sites where our mobile telecommunications network equipment is installed.

Tim Brasil plans to invest up to 11 billion Brazilian reais in capital expenditures, in accordance with its industrial plan for the years 2013-2015.

Argentinean and Paraguayan Network

Telecom Italia Group s operation in Argentina is carried out in two major areas. Voice, data and Internet services (provided through Telecom Argentina) and mobile services (provided through Personal). In Paraguay, there is only a mobile operation (through Núcleo).

In connection with providing the above services, the major fixed assets owned by these companies are comprised of outside plant (external wiring), urban and regional fiber links to a modern internet connection and to connect major telecommunication buildings and mobile sites, access facilities (radio base stations) for the mobile system, switching equipment to connect calls to and from fixed and mobile customers, transmission equipment to interconnect all switching equipment and IP network to carry all data traffic. The transmission and IP facilities are used by both areas, mobile and fixed . It is also remarkable the importance of the software and computing equipment that support both the operation and administration of fixed and mobile businesses.

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Item 4A. Unresolved Staff Comments

Item 4A. UNRESOLVED STAFF COMMENTS

None.

Item 5. OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read in conjunction with the Consolidated Financial Statements included elsewhere in this Annual Report. Such financial statements have been prepared in accordance with IFRS as issued by the IASB.

5.1 CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analyses of our financial condition and results of operations is based upon our Consolidated Financial Statements, which have been prepared in accordance with IFRS as issued by the IASB (designated as **IFRS**). Our reported financial condition and results of operations as reported under IFRS are based on the application of accounting methods which involve the use of subjective assumptions and estimates that underlie the preparation of our financial statements. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily available. Actual results could differ, even significantly, from these estimates owing to possible changes in the factors considered in the determination of such estimates. Estimates are reviewed periodically.

In the absence of a Standard or an Interpretation that specifically applies to a particular transaction, management carefully considers subjective valuation techniques and uses its judgment as to the accounting methods to adopt with a view to providing financial statements which faithfully represent the economic substance of the transactions, are neutral, prepared on a prudent basis and complete in all material respects and in accordance with IFRS.

Since our selection and application of accounting policies involve judgments and other assumptions affecting the application of those policies, reported results are sensitive to changes in conditions or assumptions of management and these are factors to be considered when reading our Consolidated Financial Statements. We believe the critical accounting policies described below involve the most significant subjective assumptions and estimates used in the preparation of our Consolidated Financial Statements under IFRS.

Revenue recognition

Revenues are recognized to the extent that it is probable that economic benefits will flow to the Group and their amount can be measured reliably. Revenues are stated net of discounts, allowances, and returns.

· *Revenues from services rendered*

Revenues from services rendered are recognized in the separate consolidated income statement according to the stage of completion of the service and only when the outcome of the service rendered can be estimated reliably.

Traffic revenues from interconnection and roaming are reported gross of the amounts due to other TLC operators.

Revenues for delivering information or other content are recognized when the information or content is delivered to the customer. In the event that the Group is acting as agent, only the commission received from the content provider is recognized as revenue.

Revenues from the activation of telephone services (as well as the related costs) are deferred over the expected duration of the relationship with the customer (generally 8 years for retail customers and 3 years for wholesale customers). In particular, costs from the activation of telephone services are deferred taking also into account the reasonable expectations of cash flows arising from these services. To determine the expected duration of the relationship with customers we perform an analysis of our historical customer relationship trends.

Revenues from prepaid traffic are recorded on the basis of the minutes used at the contract price per minute. Deferred revenues for unused minutes are recorded in Trade and miscellaneous payables and other current liabilities in the consolidated statement of financial position.

· *Revenues from sales and bundled offerings*

Revenues from sales (telephone and other equipment) are recognized when the significant risks and rewards of ownership are transferred to the buyer.

For offerings which include the sale of mobile handsets and service contracts, we recognize revenues related to the sale of the handset when it is delivered to the final customer whereas traffic revenues are recorded on the basis of the minutes used; the related subscriber acquisition costs, including handset subsidies and sales commissions, are expensed as incurred. The revenues allocated to the handset sale are limited to the contract amount that is not contingent upon the rendering of telecommunication services, i.e. the residual of the amount paid by the customer exceeding the services value. The determination of fair values in the telecommunications business is complex, because some of the components are price-sensitive and, thus, volatile in a competitive marketplace.

A small portion of our bundled offerings in the mobile and broadband businesses are contracts with a minimum contractual period between 12 and 30 months which include an enforced termination penalty. For these contracts, the subscriber acquisition costs are capitalized under Intangible assets with a finite useful life if the conditions for capitalization as described in the related accounting policy are met.

· *Revenues on construction contracts*

Revenues on construction contracts are recognized based on the stage of completion (percentage of completion method).

Revenue recognition is subject to estimation in respect of the expected duration of customer relationships, the estimate of relative fair values and estimates of discounts, returns and allowances. Revisions to such estimates may significantly affect our future operating results.

Allowance for doubtful accounts

Management maintains an allowance for doubtful accounts to account for estimated losses resulting from the inability of our customers to make required payments. Management bases its estimates on the ageing of our accounts receivable balances and our historical write-off experience with similar receivables, customer credit-worthiness and changes in our customer payment history when evaluating the adequacy of our allowance for doubtful accounts. If the financial condition of our customers were to deteriorate, our actual write-offs might be higher than we estimate.

Accounting for tangible and intangible non-current assets

Accounting for tangible and intangible non-current assets involves the use of estimates for determining fair value at the acquisition date in the case of assets acquired in a business combination and the expected useful lives of assets with a finite useful life. The determination of the fair values of assets, as well as the useful lives of the assets is based on management s judgment. Changes in the economic conditions of the markets in which we operate, technology and competitive forces could significantly affect the estimated useful lives of these assets and may lead to a difference in the timing and amount of depreciation and amortization expense.

Acquisition accounting, goodwill and purchase price allocation

We have entered into certain acquisitions and in the future may make further acquisitions. The calculation of the purchase price, and the subsequent allocation of that purchase price to the fair value of the assets acquired and liabilities assumed, is critical due to the long-term impact on the separate consolidated income statement.

Under IFRS, we are required to perform a purchase price allocation and, consequently, as part of that allocation, all consideration, including the fair value of exchanged shares, shall be valued. When equity instruments are issued as part of the consideration, under IFRS we measure them at their fair value as of the date of exchange.

The purchase price is then allocated to the fair value of the assets acquired and liabilities assumed.

The purchase price allocation requires that all assets and liabilities be recorded at fair values which requires significant estimates and judgments to be made. A change in any of these estimates or judgments could change the amount allocated to the assets and liabilities. The resulting change in the purchase price allocation to assets or liabilities has a direct impact on the final amount of the purchase price that is allocated to goodwill.

If actual results differ from these estimates, or we adjust the estimated useful economic lives in future periods, operating results could be significantly affected by these estimates and judgments which involve:

- the definition of the purchase price;
- the identification of the assets acquired and liabilities assumed in the acquisition;
- the valuation of these assets and liabilities in the purchase price allocation; and
- the assessment of whether selected assets have a finite or indefinite useful life.

These could have a significant impact on both the level of total goodwill and ultimately on the separate consolidated income statement.

Accounting for transactions involving interests in group companies

We have entered into certain transactions involving interests in Group companies, and in the future we may make further similar transactions.

Under IAS 27, changes in a parent s ownership interest in a subsidiary that do not result in a loss of control are accounted for as equity transactions (i.e. transactions with owners in their capacity as owners). In such circumstances the carrying amounts of the controlling and non-controlling interests shall be adjusted to reflect the changes in their relative interests in the subsidiary. Any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received shall be recognized directly in equity and attributed to the owners of the parent.

Impairment of assets

The determination of impairment of intangible and tangible assets involves the use of estimates that include, but are not limited to, the cause, timing and amount of the impairment.

- ***Goodwill.*** Goodwill is tested for impairment at least annually or more frequently whenever events or changes in circumstances indicate that goodwill may be impaired, as set forth in IAS 36 (*Impairment of Assets*); however, when the conditions that gave rise to an impairment loss no longer exist, the original amount of goodwill is not reinstated.

The test is generally conducted at the end of every year so the date of testing is the year-end closing date of the financial statements. Goodwill acquired and allocated during the year is tested for impairment at the end of the year in which the acquisition and allocation took place.

To test for impairment, goodwill is allocated, at the date of acquisition, to each cash-generating unit or groups of cash-generating units which is expected to benefit from the acquisition.

Allocation is made to the lowest level at which goodwill is monitored for management purposes and that lowest level is not larger than the operating segment determined in accordance with IFRS 8 (*Operating Segments*).

If the carrying amount of the cash-generating unit (or group of cash-generating units) exceeds the recoverable amount, an impairment loss is recognized in the separate consolidated income statement. The impairment loss is first recognized as a deduction of the carrying amount of goodwill allocated to the cash-generating unit (or group of cash-generating units) and then only applied to the other assets of the cash-generating unit in proportion to their carrying amount, up to the recoverable amount of the assets with a finite useful life. The recoverable amount of a cash-generating unit (or group of cash-generating units) to which goodwill is allocated is the higher of fair value less costs to sell and its value in use.

In calculating the value in use, the estimated future cash flows are discounted to present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. The future cash flows are those arising from an explicit time horizon between three and five years as well as those extrapolated to estimate the terminal value. The long-term growth rate used to estimate the terminal value of the cash-generating unit (or group of cash-generating units) is assumed not to be higher than the average long-term growth rate of the segment, country or market in which the cash-generating unit (or group of cash-generating units) operates.

The value in use of a cash-generating unit which operates in a foreign currency is estimated in the local currency by discounting cash flows to their present value on the basis of an appropriate rate for that currency. The present value obtained is translated to Euro at the spot rate on the date of the impairment test (in the case of the Telecom Italia Group, the date of the financial statements).

Future cash flows are estimated by referring to the current operating conditions of the cash generating unit (or group of cash-generating units) and, therefore, do not include either benefits originating from future restructuring for which the entity is not yet committed, or future investments for the improvement or optimization of the cash-generating unit.

For the purpose of calculating impairment, the carrying amount of the cash-generating unit is established based on the same criteria used to determine the recoverable amount of the cash-generating unit, excluding surplus assets (that is, financial assets, deferred tax assets and net non-current assets held for sale) and includes the goodwill attributable to non-controlling interests.

After conducting the goodwill impairment test for the cash-generating unit (or groups of cash-generating units), a second level of impairment testing is carried out which includes the corporate assets which do not generate positive cash flows and which cannot be allocated by a reasonable and consistent criterion to the single units. At this second level, the total recoverable amount of all cash-generating units (or groups of cash-generating units) is compared to the carrying amount of all cash-generating units (or groups of cash-generating units), including also those cash-generating units to which no goodwill was allocated, and the corporate assets.

See Note Goodwill of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

- ***Intangible and tangible assets with a finite useful life***. At every annual or interim closing date, the Group assesses whether there are any indications of impairment of intangible and tangible assets with a finite useful life. Both internal and external sources of information are used for this purpose. Internal sources include obsolescence or physical damage, and significant changes in the use of the asset and the economic performance of the asset compared to estimated performance. External sources include the market value of the asset, changes in technology, markets or laws, increases in market interest rates and the cost of capital used to evaluate investments, and an excess of the carrying amount of the net assets of the Group over market capitalization. When indicators of impairment exist, the carrying amount of the assets is reduced to the recoverable amount. The recoverable amount of an asset is the higher of fair value less costs to sell and its value in use. In calculating the value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where it is not possible to estimate the recoverable amount of an individual asset, we estimate the recoverable amount of the cash-generating unit to which the asset belongs. Impairment losses are recognized in the separate consolidated income statement. When the conditions that gave rise to an impairment loss no longer exist, the carrying amount of the asset or cash-generating unit is increased to the revised estimate of its recoverable amount, up to the carrying amount that would have been recorded had no impairment loss been recognized. The reversal of an impairment loss is recognized as income in the separate consolidated income statement.

The identification of impairment indicators, the estimation of future cash flows and the determination of fair values of assets or groups of assets (or cash-generating units) require management to make significant judgments concerning the identification and validation of impairment indicators, expected cash flows, applicable discount rates, useful lives and residual values. These estimates can have a material impact on fair value and the amount of any write-downs.

Financial assets

Financial assets include in particular investments, some of which are publicly traded and have highly volatile share prices. Generally, an impairment charge is recorded when an investment s carrying amount exceeds the present value of its estimated future cash flows. The calculation of the present value of estimated future cash flows and the determination of whether an impairment is other than temporary involve judgments and rely heavily on assessments by management regarding the future development and prospects of the investee company. In determining value, quoted market prices are used, if available, or other valuation methodologies. To determine whether an impairment is other than temporary, we consider the ability and intent to hold the investment for a reasonable period of time to ascertain whether a forecasted recovery of fair value exceeds the carrying amount, including an assessment of factors such as the length of time and magnitude of the excess of carrying value over market value, the forecasted results of the investee company, the regional economic environment and state of the industry. Future adverse changes in market conditions, particularly a downturn in the telecommunications industry, or poor operating results could result in losses or an inability to recover the carrying amount of the investment, which could result in impairment charges.

Derivative financial instruments

Telecom Italia enters into several different types of derivative contracts in order to manage its exposure to exchange rate and interest rate risks and to diversify the parameters of debt so that costs and volatility can be reduced to within pre-established operational limits. The changes in the fair value of derivatives which do not qualify for hedge accounting, fair value hedge derivatives and the ineffective portion of cash flow hedge derivatives are recognized in the separate consolidated income statement in the period of change. The gain or loss on the effective portion of qualifying cash flow hedges is recognized directly in a specific equity reserve. The cumulative gain or loss is removed from equity and recognized in the separate consolidated income statement at the same time the hedged transaction affects the separate consolidated income statement. The assessment of the fair value of a derivative contract requires the use of quoted market prices, banker price quotations, price quotations for similar instruments traded in different markets and, where applicable, pricing models. Pricing models and their underlying assumptions impact the amount and timing of unrealized gains and losses recognized. We rely on these pricing models when external fair values are unavailable. The estimates regarding future prices require estimating several factors, including interest rates, currency values and cash flows. Prices realized in the future could differ from these estimates, therefore producing different financial results.

Provision for employee severance indemnity

Employee severance indemnity, mandatory for Italian companies pursuant to art. 2120 of the Italian Civil Code, is a deferred compensation and is based on the employees years of service and the compensation earned by the employee during the service period.

Under IAS 19 (*Employee Benefits*), the employee severance indemnity is considered a Defined benefit plan , except when employees, starting from the year 2007, choose to direct their accruing indemnity portions to supplementary pension funds or to the Treasury Fund managed by the Italian Social Security Institute (INPS); in such case the employee severance indemnity is classified as a Defined contribution plan .

The obligation for the employee severance indemnity classified as a defined benefit plan is determined in accordance with actuarial methods. In the event that changes in assumptions are required, the future amounts of the post employment benefit may be materially affected.

Provisions and contingent liabilities

We exercise considerable judgment in determining our exposure to and recognizing provisions for contingent liabilities related to pending litigations or other outstanding claims subject to negotiated settlement, mediation, arbitration or government regulation as well as other contingent liabilities.

Judgment is necessary in assessing the likelihood that a pending claim will succeed or a liability will arise and to quantify the possible range of the final settlement. Provisions are recorded for liabilities when losses are considered probable and can be reasonably estimated. Because of the inherent uncertainties in making such judgments, actual losses may be different from the originally estimated provision. Significant estimates are involved in the determination of provisions related to taxes, environmental liabilities, our workforce reduction initiative and litigation risks. These estimates are subject to change as new information becomes available, primarily with the support of internal specialists or outside consultants, such as actuaries or legal counsel. Adjustments to loss provisions may significantly affect future operating results.

Income tax expense

The Group calculates income tax expense in each of the tax jurisdictions in which it operates. This process involves a jurisdiction-by-jurisdiction calculation of the current tax charge and an assessment of temporary differences resulting from the different treatment of certain items for consolidated financial and tax reporting purposes. Temporary differences result in the recognition of deferred tax assets or liabilities in the consolidated financial statements. Deferred tax assets are recognized to the extent that their realization is probable. The realization of deferred tax assets depends, among other things, on the company s ability to generate sufficient taxable income in future years and the reversal of taxable temporary differences, taking into account any restrictions on the carry-forward of tax losses. Various factors are used to assess the probability of the future realization of deferred tax assets, including future reversals of existing taxable temporary differences, past operating results, operational plans, loss carry-forward periods, and tax planning strategies. If actual results differ from these estimates or, if these estimates must be adjusted in future periods, the financial position and results of operations may be affected. In the event of a change in the assessment of future utilization of deferred tax assets, the recognized deferred tax assets must be increased or decreased, as the case may be, and the consequent effects recognized in the separate consolidated income statement.

5.2 RESULTS OF OPERATIONS FOR THE THREE YEARS ENDED DECEMBER 31, 2012

5.2.1 SIGNIFICANT TRENDS IMPACTING OUR CORE BUSINESSES

Increased competition continues to have a significant impact on the development of our business. Key trends affecting our core businesses are:

Domestic Business Unit

Telecommunications are strengthening their central role in society, driven by the growing importance of broadband, both fixed and mobile. The ongoing convergence of telecommunications, Information Technology, Media and Consumer Electronics has led to greater competition and faster innovation, thus increasing the industry s complexity. These macro factors have, and continue to have, a material impact on how we plan for, and manage our business.

In the Italian telecommunications market there has been a reduction in consumer and business customers spending on both fixed and mobile services, driven by a decline of traditional voice services, only partially offset by the growth of new Broadband services.

The main strategic priorities and objectives of Telecom Italia in the Domestic market are to:

- stabilize revenues;
- defend market share on traditional services through quality of service;
- grow innovative services leveraging on both access and applications services such as cloud services; and
- develop UBB (UltraBroadband) networks taking into account further developments in the regulatory framework and technological changes.

Brazil Business Unit

Growth in the Brazilian telecommunications market is driven by mobile. Significant trends include acceleration of fixed to mobile substitution and the further development of broadband.

Mobile broadband represents in Brazil a competitive alternative to fixed broadband, considering the country s geography and fixed network characteristics.

In light of these market trends, TIM Brasil s main strategic priorities and objectives are to:

- expand its customer base through fixed to mobile substitution;
- pursue high potential in mobile broadband penetration;
- continue network evolution, mainly through the increase of coverage on 3G and the roll out of the 4G network;
- satisfy the growing demand for Internet services, while optimizing capital expenditure.

Argentina Business Unit

With respect to the telecommunications market in Argentina, growth is expected to be driven by fixed broadband and VAS, and mobile Internet and VAS.

Argentina s strategic priorities are to:

- further build on its market share and its fixed and mobile platforms;
- enlarge its network capacity;
- support premium positioning on mobile to boost value added services revenues;
- fully exploit the high demand for data traffic.

5.2.2 Business Segments

The Telecom Italia Group reports its financial results on basis of the following operating segments:

- **Domestic**: includes operations in Italy for voice and data services on fixed and mobile networks for final customers (retail) and other operators (wholesale), the operations of the Telecom Italia Sparkle group (International wholesale) as well as the related support activities;
- **Brazil**: includes mobile (TIM Celular) and fixed (TIM Celular and Intelig) telecommunications operations in Brazil;
- **Argentina**: includes fixed (Telecom Argentina) and mobile (Telecom Personal in Argentina and Núcleo in Paraguay) telecommunications operations;
- **Media**: includes television network operations and management;
- **Olivetti**: includes manufacture of office products and services for Information Technology. It carries out Solution Provider activities to automate processes and business activities for small and medium-size enterprises, large corporations and vertical markets;
- **Other Operations**: includes finance companies and other minor companies not strictly related to the core business of the Telecom Italia Group.

The principal changes in the scope of consolidation in 2012 are as follows:

- **Matrix Other Operations**: the company was sold on October 31, 2012, and consequently excluded from the consolidation area as of such date.

The principal changes in the scope of consolidation in 2011 are as follows:

- companies entering the scope of consolidation:
  - **Tim Fiber Brazil Business Unit**: on October 31, 2011, we acquired a 100% stake in the company Eletropaulo Telecomunicações Ltda and a 98.3% stake in AES Communications Rio de Janeiro S.A., both telecommunications infrastructure operators in the states of São Paolo and Rio de Janeiro, now renamed Tim Fiber SP and Tim Fiber RJ, respectively. As a result of certain further transactions, the original ownership interest in Tim Fiber RJ was subsequently increased to 99.7%. The acquisitions were carried out through the subsidiary Tim Celular S.A., into which the two companies were recently merged;

  - **4GH group Domestic Business Unit**: on July 27, 2011, the 4G Holding group entered the scope of consolidation (retail sale of telephony products) following the acquisition of 71% of the ordinary shares of 4G Holding S.p.A. which in turn holds 100% of 4G Retail S.r.l.; the two companies merged in 2012;

- companies exiting the scope of consolidation:

  - **Loquendo Domestic Business Unit**: on September 30, 2011, Loquendo S.p.A. was sold and consequently exited the scope of consolidation.

For a description of certain of these businesses, see Item 4. Information on the Telecom Italia Group 4.2 Business Units .

For purposes of the following discussion selected financial data of each Business Unit has been provided for 2012, 2011, and 2010 consistent with the structure of each Business Unit at December 31, 2012.

5.2.3 NON-GAAP FINANCIAL MEASURES

In this Annual Report on Form 20-F, in addition to figures presented in accordance with IFRS as issued by IASB, we disclose figures derived from IFRS that are non-GAAP financial measures (**Non-GAAP Measures**).

Such financial data is considered Non-GAAP financial measures as defined in Item 10(e) of Regulation S-K under the 1934 Act.

In this Annual Report the Non-GAAP Measure used relate to Net Financial Debt.

Net Financial Debt is a Non-GAAP financial measure as defined in Item 10(e) of Regulation S-K under the 1934 Act, but is widely used in Italy by financial institutions to assess liquidity and the adequacy of a company s financial structure. We believe that Net Financial Debt provides an accurate indicator of our ability to meet our financial obligations (represented by gross debt) by our available liquidity, represented by the other items shown in the reconciliation table. Net Financial Debt allows us to show investors the trend in our net financial condition over the periods presented. The limitation on the use of Net Financial Debt is that it effectively assumes that gross debt can be reduced by our cash and other liquid assets. In fact, it is unlikely that we would use all of our liquid assets to reduce our gross debt all at once, as such assets must also be available to pay employees, suppliers, and taxes, and to meet other operating needs and capital expenditure requirements. Net Financial Debt and its ratio to equity (including Non-controlling Interest), or leverage, are used to evaluate our financial structure in terms of sufficiency and cost of capital, level of debt, debt rating and funding cost, and whether our financial structure is adequate to achieve our business plan and our financial targets. Our management believes that our financial structure is sufficient to achieve our business plan and financial targets. Our management monitors the Net Financial Debt and leverage or similar measures as reported by other telecommunications operators in Italy and outside Italy, and by other major listed companies in Italy, in order to assess our liquidity and financial structure relative to such companies. We also monitor the trends in our Net Financial Debt and leverage in order to optimize the use of internally generated funds versus funds from third parties. Net Financial Debt is reported in our Italian Annual Report to shareholders and is used in presentations to investors and analysts. Net Financial Debt is calculated as follows:

	As of December 31,	
	2012	**2011**
	(millions of euros)	
Non-current financial liabilities	34,091	35,860
Current financial liabilities	6,150	6,091
Gross financial debt (A)	**40,241**	**41,951**
Non-current financial assets (B)	**(2,496)**	**(2,949)**
Current financial assets:		
Securities other than investments (current assets)	(754)	(1,007)
Financial receivables and other current financial assets	(502)	(462)
Cash and cash equivalents	(7,436)	(6,714)
Total current financial assets (C)	**(8,692)**	**(8,183)**
Financial assets (D=B+C)	**(11,188)**	**(11,132)**
Net financial debt (A+D)	**29,053**	**30,819**

5.2.4 Overview of 2012 Results of Operations

In 2012, the following characterized the results in our domestic market:

- in the **Domestic Fixed Telecommunications Service Business**, service revenues posted a -3.8% year on year result, a modest decline compared to the previous year. The continuing erosion of the access market, the decrease in market share (674 thousand fixed line losses in 2012 compared to 699 thousand fixed line losses in 2011 and 746 thousand fixed line losses in 2010) and lower traditional services demand and prices (both voice and data, especially in the Business segment) continued in 2012. The line loss was due to, apart from churn in favor of OLOs, disconnection of fixed lines without migration to other operators (a trend that is currently observed e.g. with respect to second homes or clients who abandon their landline and use their mobile phone only). On the revenue side these dynamics are partially offset by actions aimed to preserve the value of our customer base focused on the upselling of high value solutions, especially in the Broadband area;

- the **Domestic Mobile Telecommunications Service Business**, is still characterized by aggressive and competitive behavior that has resulted in a decrease in prices, especially for traditional services (voice and data). This dynamic, in combination with the sharp reduction in mobile termination rates

(MTR) (from 5.3 euro cent to 2.5 euro cent) and the EU price cap on mobile data resulted in a drop of service revenues (-9.0% vs. -8.7% in 2011), only partially offset by the solid growth of mobile internet and by the sales of tablets and smartphones.

In 2012, the following characterized the results in our international markets:

· **Brazil**. Tim Brasil s customer base grew in 2012 by 9.8% compared to 2011 (adding 6.3 million new customers); its market share expanded to 26.9% from 26.5% in 2011. Based on value market share (share in service revenues) Tim Brasil was the second largest Brazilian mobile operator. The company also recorded growth in its pre-paid segment increasing 8.9% year over year (reaching 59.7 million customers), while the post-paid clients increased 15.2% year over year (totaling 10.7 million subscribers).

Tim Brasil continued to focus on growth and profitability, through cost discipline and initiatives to increase revenue from value-added services, increase traffic volumes/usage and network service quality. In particular, revenues from services increased in 2012 by 6.9% compared to 2011 and revenues from handsets grew in 2012 by 35.3% compared to 2011, reflecting the company s strategy of market penetration with high-end handsets (smartphones/webphones and tablets) as a lever to grow mobile data services.

On the cost side, Tim Brasil adopted a disciplined approach to client acquisition, credit analysis and operating expenses.

· **Argentina**. In the Fixed Business growth was mainly due to the increase in the broadband business. The leadership of the brand Arnet was based on effective communication with a differentiated offer by segment and competitive pricing. The broadband accesses increased by more than 5% over the prior year reaching 1.6 million accesses as of December 31, 2012. The ARPU increased by 17.6% over the prior year reaching 102.3 Argentine Pesos.

Rates for regulated voice services continued to be affected by the freezing of rates established by the Public Emergency Law enacted in January 2002. During 2012, the lines in service remained broadly stable at 4.1 million lines as of December 31, 2012. The ARBU (Average Revenue Billed per User) increased by more than 5% over the prior year as a result of the increase in value-added services and the penetration of traffic plans.

In the Mobile Business Telecom Personal s customer portfolio increased by 0.8 million customers (+4.3% over the prior year), reaching 19 million lines as of December 31, 2012, of which 33% were post-paid customers.

At the same time, ARPU improved approximately by 12% over the prior year. A large part of this growth can be traced to value-added services (including SMS text messaging and the mobile internet service) which accounted for approximately 53% of mobile services revenues in 2012.

In Paraguay, the Núcleo customer base grew by about 7% over the prior year and at the end of 2012 Núcleo reached 2.3 million lines, of which 19% were postpaid. During the fourth quarter of 2012, Núcleo focused its efforts on the introduction of Mobile number portability (**MNP**), which took place on November 30, seeking to inform the market on the MNP benefits.

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The following table sets forth our consolidated income statement for the years ended December 31, 2012, 2011 and 2010.

Starting from the first half of 2012 the Telecom Italia Group early adopted and retrospectively applied the revised version of IAS 19 (*Employee Benefits*). Accordingly, the comparative figures of 2011 and 2010 have been restated on a consistent basis.

	Year ended December 31,		
	2012	2011 (Restated)	2010 (Restated)
	(millions of euros)		
Revenues	29,503	29,957	27,571
Other income	298	299	255
Total operating revenues and other income	**29,801**	**30,256**	**27,826**
Acquisition of goods and services	(12,948)	(12,859)	(11,383)
Employee benefits expenses	(3,919)	(3,992)	(3,981)
Other operating expenses	(1,882)	(1,859)	(1,422)
Change in inventories	12	56	(135)
Internally generated assets	581	569	547
Depreciation and amortization	(5,340)	(5,496)	(5,542)
Gains (losses) on disposals of non-current assets	53	3	11
Impairment reversals (losses) on non-current assets	(4,432)	(7,358)	(63)
Operating profit (loss)	**1,926**	**(680)**	**5,858**
Share of profits (losses) of associates and joint ventures accounted for using the equity method	(6)	(39)	99
Other income (expenses) from investments	2	16	289
Finance income	2,082	2,464	3,081
Finance expenses	(4,048)	(4,504)	(5,199)
Profit (loss) before tax from continuing operations	**(44)**	**(2,743)**	**4,128**
Income tax expense	(1,235)	(1,610)	(549)
Profit (loss) from continuing operations	**(1,279)**	**(4,353)**	**3,579**
Profit (loss) from Discontinued operations/Non-current assets held for sale	2	(13)	(7)
Profit (loss) for the year	**(1,277)**	**(4,366)**	**3,572**
Attributable to:			
Owners of the Parent	*(1,627)*	*(4,811)*	*3,118*
Non-controlling interests	*350*	*445*	*454*

5.2.5 Business Unit Financial Data

As from the first half of 2012 the Telecom Italia Group early adopted and retrospectively applied the revised version of IAS 19 (*Employee Benefits*). Accordingly, the comparative figures of 2011 and 2010 for the Business Units have been restated on a consistent basis.

On October 31, 2012, Telecom Italia S.p.A. completed the sale of its wholly-owned subsidiary Matrix, to Libero, controlled by Weather Investment II S.à.r.l.. In 2012 Matrix was also moved to Other Operations and was consequently no longer part of Core Domestic in the Domestic Business Unit. Accordingly, the comparative figures of 2011 and 2010 have been restated on a consistent basis.

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The table below sets forth revenues, operating profit (loss), capital expenditures and number of employees by Business Units, for the periods indicated.

		Domestic	Brazil	Argentina(1)	Media	Olivetti	Other Operations	Adjustments and eliminations	Consolidated Total
		(millions of euros, except number of employees)							
Revenues(2)	2012	17,884	7,477	3,784	222	280	62	(206)	29,503
	2011	18,991	7,343	3,220	238	343	119	(297)	29,957
	2010	20,025	6,199	798	258	391	205	(305)	27,571
Operating profit (loss)	2012	1,078	966	214	(263)	(65)	(3)	(1)	1,926
	2011	(1,996)	984	509	(88)	(43)	(37)	(9)	(680)
	2010	5,197	685	110	(92)	(24)	(34)	16	5,858
Capital expenditures on an accrual basis	2012	3,072	1,500	557	57	3	7		5,196
	2011	4,185	1,290	556	61	5	16	(18)	6,095
	2010	3,087	1,216	188	67	5	23	(3)	4,583
Number of employees at year-end(3)	2012	53,224	11,622	16,803	735	778	22		83,184
	2011	55,047	10,539	16,350	765	1,075	378		84,154
	2010	56,106	10,114	15,650	777	1,090	463		84,200

(1) In the scope of consolidation since October 13, 2010.

(2) Revenues are total revenues of the various business units of the Telecom Italia Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(3) The number of employees at year-end excludes employees relating to the consolidated companies considered as Discontinued operations/Non-current assets held for sale, and includes personnel with temporary work contracts.

5.2.6 Year Ended December 31, 2012 Compared With Year Ended December 31, 2011

v **REVENUES**

Revenues amounted to 29,503 million euros in 2012, a decrease of 454 million euros, or 1.5%, compared to 29,957 million euros in 2011.

The table below sets forth for the periods indicated gross revenues by Business Unit and consolidated revenues.

	Year ended December 31, 2012		2011		Changes	
	Revenues(1) (a)	% of Consolidated revenues	Revenues(1) (b)	% of Consolidated revenues	(a-b)	%
	(millions of euros, except percentages)					
Domestic	17,884	60.6	18,991	63.4	(1,107)	(5.8)
Core Domestic	*16,933*	*57.4*	*18,082*	*60.4*	*(1,149)*	*(6.4)*
International Wholesale	*1,393*	*4.7*	*1,393*	*4.6*		
Brazil	7,477	25.3	7,343	24.5	134	1.8
Argentina	3,784	12.8	3,220	10.7	564	17.5
Media, Olivetti and Other Operations(2)	564	1.9	700	2.3	(136)	
Adjustments and eliminations	*(206)*	*(0.6)*	*(297)*	*(0.9)*	*91*	
Total Revenues	**29,503**	**100.0**	**29,957**	**100.0**	**(454)**	**(1.5)**

(1) Revenues are total revenues of the various business units of the Telecom Italia Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(2) The Other Operations of the Telecom Italia Group consist of the financial companies and other minor companies not associated with the core business of the Telecom Italia Group.

The **Domestic Business Unit** (divided into Core Domestic and International Wholesale) reported a decline of 1,107 million euros (-5.8%) in revenues in 2012, compared to 2011.

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This decrease is partly attributable to the entry into force, in July 2012, of the new mobile termination rates (MTR), which reduced these rates by 53% (from 5.3 to 2.5 eurocents), representing a sharp decrease compared to the tariffs in effect for full year 2011.

The performance of the domestic market was also affected by the macroeconomic environment and continuing competitive pressures.

In particular:

- revenues from services were 17,077 million euros in 2012, down -5.6% compared to 2011. Specifically, revenues from services in the Mobile business decreased by 9.0% compared to 2011. The Fixed-line business revenues from services declined 496 million euros (-3.8% compared with 2011). The decrease in revenues in the mobile market was mainly due to the dilution of the ARPU on traditional services such as voice and text messaging and to the above-mentioned reduction of MTR tariffs (-286 million euros), which decrease was only partly offset by the growth of users and mobile internet. With respect to the fixed line market, the reduction is mainly attributable to the above-mentioned decrease in access lines and the contraction of prices and revenues from traditional services, both voice and data, in particular in the TOP Client segment;

- product revenues of 807 million euros were 93 million euros (-10.3%) lower compared to 2011. The growth in Mobile devices, driven by a greater commercial push on mobile internet-enabled devices was more than offset by the sharp decline in Fixed-line products, attributable to a contraction of the market, but also to a more selective commercial strategy to defend the profit base.

With respect to the **Brazil Business Unit**, revenues grew by 1.8% in 2012 compared to the prior year. Revenues from services continued their positive trend, driven by the growth of the customer base (reaching approximately 70.4 million lines at December 31, 2012, up 9.8% compared to December 31, 2011). Handset revenues also increased compared to 2011.

With respect to the **Argentina Business Unit**, revenues increased 17.5% compared to 2011 (+564 million euros).

For a more detailed analysis of revenue performance by individual Business Units, reference should be made to Item 4. Information On The Telecom Italia Group 4.2 Business Units .

v **OTHER INCOME**

The following table sets forth other income for the years ended December 31, 2012 and 2011:

	Year ended December 31,

	2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of euros, except percentages)			
Late payment fees charged for telephone services	69	71	(2)	(2.8)
Recovery of employee benefit expenses, purchases and services rendered	36	36		
Capital and operating grants	18	24	(6)	(25.0)
Damage compensation, penalties and sundry recoveries	53	36	17	47.2
Other income	122	132	(10)	(7.6)
Total other income	**298**	**299**	**(1)**	**(0.3)**

v **Operating Expenses**

Our operating expenses amounted to 27,875 million euros in 2012, a decrease of 3,061 million euros, or 9.9% compared to 30,936 million euros in 2011. Operating expenses declined primarily as a result of the reduced impairment losses on non-current assets which decreased from 7,358 million euros in 2011 to 4,432 million euros in 2012. The components of our operating expenses include the following:

· **Acquisition of goods and services** amounted to 12,948 million euros in 2012, an increase of 89 million euros compared to 2011 (12,859 million euros). The increase is largely due to the increase in the commercial

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and technical costs of the Argentina Business Unit (+300 million euros, including a negative exchange rate effect of 24 million euros) and the Brazil Business Unit (+109 million euros, including a negative exchange rate effect of 320 million euros), needed to support the growth of the customer base, voice and data traffic volumes, sales of mobile internet-enabled devices and, consequently revenues in Latin America. Offsetting these increases, the domestic business reduced acquisitions of goods and services by 345 million euros compared to 2011, partly attributable to a decrease in the portion of revenues to be paid to other operators, related to the reduction in mobile termination rates.

The following table sets forth the acquisition of goods and services for the years ended December 31, 2012 and 2011:

	Year ended December 31,			
	2012	**2011**	**Changes**	
	(a)	**(b)**	**(a-b)**	**%**
	(millions of euros, except percentages)			
Purchase of goods	2,610	2,525	85	3.4
Portion of revenues to be paid to other operators and interconnection costs	4,018	4,232	(214)	(5.1)
Commercial and advertising costs	2,154	2,259	(105)	(4.6)
Power, maintenance and outsourced services	1,847	1,618	229	14.2
Rent and leases	666	647	19	2.9
Other service expenses	1,653	1,578	75	4.8
Total acquisition of goods and services	**12,948**	**12,859**	**89**	**0.7**
% on Revenues	*43.9*	*42.9*		

· **Employee benefits expenses**

The following table sets forth employee benefits expenses for the years ended December 31, 2012 and 2011:

	Year ended December 31,			
	2012	**2011**	**Changes**	
	(a)	**(b)**	**(a-b)**	**%**
	(millions of euros, except percentages)			
Employee benefits expenses Italian companies:				
Ordinary employee expenses and costs	2,945	3,144	(199)	(6.3)
Corporate restructuring expenses	8	12	(4)	(33.3)
Total employee benefits expenses Italy	**2,953**	**3,156**	**(203)**	**(6.4)**
Employee benefits expenses Outside Italy				
Ordinary employee expenses and costs	949	836	113	13.5
Corporate restructuring expenses	17		17	
Total employee benefits expenses Outside Italy	**966**	**836**	**130**	**15.6**

Total employee benefits expenses	**3,919**	**3,992**	**(73)**	**(1.8)**
% on Revenues	*13.3*	*13.3*		

Employee benefits expenses were 3,919 million euros in 2012 compared to 3,992 million euros in 2011, a decrease of 73 million euros. The change was affected by:

· the reduction of 203 million euros in the Italian component of employee benefits expenses, mainly due to the reduction in ordinary employee benefits expenses, resulting from the decrease in the average salaried workforce of 1,214 compared to 2011, and from restructuring expenses that were 4 million euros lower (8 million euros in 2012; 12 million euros in 2011). In 2012, these expenses derive from the balance between the provision charge of 15 million euros for Olivetti I-Jet (resulting from the agreements signed with the trade unions of the company put into liquidation in June 2012 a decline of 1.8%) and the use of a total of

7 million euros from the remaining provision for mobility under Law 223/91 by Telecom Italia S.p.A. (6 million euros), and by TI Sparkle and TI Information Technology (1 million euros). In 2011 the provision for mobility under Law 223/91, relating to the agreements signed in 2010 with the trade unions of the Parent Telecom Italia S.p.A. and of TI Information Technology, was adjusted by a total of 12 million euros;

· the increase of 130 million euros in the foreign component of employee benefits expenses, due to the increase of 1,409 in the average salaried workforce, relating to the Brazil Business Unit and the Argentina Business Unit. In addition there was an increase of 17 million euros in restructuring expenses, related to the provision charge of the Argentina Business Unit (15 million euros) and Olivetti Engineering S.A., a subsidiary of Olivetti I-Jet (2 million euros).

The Group s average salaried workforce for the periods indicated was as follows:

	Year ended December 31,			
	2012 (a)	2011 (b)	Changes (a-b)	%
	(full time equivalent units, except percentages)			
Average salaried workforce Italy	52,347	53,561	(1,214)	(2.3)
Average salaried workforce Foreign	26,217	24,808	1,409	5.7
Total average salaried workforce(1)	**78,564**	**78,369**	**195**	**0.2**

(1) Includes the average employees with temp work contracts: 61 in 2012 (58 in Italy and 3 outside Italy). In 2011 the headcount was 87 (75 in Italy and 12 outside Italy).

Group s employees at December 31, 2012 and 2011 were as follows:

	As of December 31,			
	2012 (a)	2011 (b)	Changes (a-b)	%
	(units, except percentages)			
Employees Italy	54,419	56,878	(2,459)	(4.3)
Employees Foreign	28,765	27,276	1,489	5.5
Total Employees(1)	**83,184**	**84,154**	**(970)**	**(1.2)**

(1) Includes employees with temporary work contracts: 43 units at December 31, 2012 and 42 units at December 31, 2011.

· **Other operating expenses**

The following tables sets forth other operating expenses for the years ended December 31, 2012 and 2011.

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages)			
Writedowns and expenses in connection with credit management	548	533	15	2.8
Accruals to provisions	214	128	86	67.2
Indirect duties and taxes	391	349	42	12.0
TLC operating fees	621	675	(54)	(8.0)
Penalties, compensation and administrative sanctions	29	41	(12)	(29.3)
Association dues and fees, donations, scholarships and traineeships	25	23	2	8.7
Sundry expenses	54	110	(56)	(50.9)
Total other operating expenses	**1,882**	**1,859**	**23**	**1.2**
% on Revenues	*6.4*	*6.2*		

Other operating expenses in 2012 are substantially in line with 2011.

The decreases for the Domestic Business Unit (-70 million euros) and the Brazil Business Unit (-28 million euros, including a negative exchange rate effect of 54 million euros) are substantially offset by the increases for the other Business Units, primarily the Argentina Business Unit (+76 million euros, including a negative exchange rate effect of 6 million euros). In particular:

- writedowns and expenses in connection with credit management (548 million euros; 533 million euros in 2011) consist of 370 million euros (389 million euros in 2011) relating to the Domestic Business Unit, 100 million euros (unchanged compared to 2011) relating to the Brazil Business Unit and 47 million euros (29 million euros in 2011) relating to the Argentina Business Unit;
- accruals to provisions (214 million euros; 128 million euros in 2011) consist of 91 million euros (60 million euros in 2011) relating to the Brazil Business Unit, 92 million euros (50 million euros in 2011) relating to the Domestic Business Unit and 17 million euros (unchanged compared to 2011) relating to the Argentina Business Unit;
- TLC operating fees (621 million euros; 675 million euros in 2011) consist of 487 million euros (554 million euros in 2011) relating to the Brazil Business Unit, 73 million euros (61 million euros in 2011) relating to the Argentina Business Unit and 59 million euros (58 million euros in 2011) relating to the Domestic Business Unit.

- **Depreciation and Amortization**

The following table sets forth depreciation and amortization for the years ended December 31, 2012 and 2011.

	Year ended December 31,			
	2012	**2011**	**Changes**	
	(a)	**(b)**	**(a-b)**	**%**
	(millions of euros, except percentages)			
Amortization of intangible assets with a finite useful life	2,212	2,163	49	2.3
Depreciation of tangible assets owned and leased	3,128	3,333	(205)	(6.2)
Total depreciation and amortization	**5,340**	**5,496**	**(156)**	**(2.8)**
% on Revenues	*18.1*	*18.3*		

The decrease in depreciation and amortization charges is mainly attributable to the Domestic Business Unit (-305 million euros) principally due to lower amounts of depreciable or amortizable assets. This decrease was offset by the increase in depreciation and amortization charges of the Argentina Business Unit (+130 million euros), partly due to the reduction in the useful lives of Customer Relationships which resulted in an increase of 66 million euros in amortization charges.

- **Gains (losses) on disposals of non-current assets**

In 2012, gains on disposals of non-current assets were 53 million euros and included the gain, net of the incidental expenses of 49 million euros, in connection with the completion of the sale of Matrix on October 31, 2012, as well as net gains on non-current assets mainly relating to the Domestic Business Unit.

In 2011, net gains on disposals of non-current assets amounted to 3 million euros and included the gain of 35 million euros, net of the related incidental expenses, realized on the sale of Loquendo at the end of September 2011 and the net losses from the disposal of tangible assets, mainly of the Parent, for the replacement and subsequent disposal of dedicated mobile telephony plant.

· **Net impairment losses on non-current assets**

Net impairment losses on non-current assets were 4,432 million euros in 2012 (7,358 million euros in 2011) and are attributable to the annual impairment test conducted for the annual financial statements. Specifically, this item refers to:

4,016 million euros of the impairment loss is due to the Core Domestic Cash-generating Unit in the **Domestic Business Unit**. This was a further write down to the goodwill write down of 7,307 million euros in 2011;

a total impairment of non-current assets and goodwill of 157 million euros in the **Media Business Unit**, established following the impairment test process and also taking account of the prospective sale of the investee La7 S.r.l. Specifically, the amount of impairment loss relating solely to the goodwill of the Media Business Unit was 105 million euros, while the remainder relates to non-current assets. This goodwill was previously written down by 57 million euros in 2011;

a total impairment loss of 253 million euros on Intangible assets and Goodwill in the **Argentina Business Unit**, recognized at the time control was acquired by the Telecom Italia Group. In detail, the amount of the impairment loss on Goodwill was 168 million euros, while the remaining portion (85 million euros) related to the impairment loss on Customer relationships.

Further details are provided in the Note Goodwill of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

v **OPERATING PROFIT (loss)**

Operating profit was 1,926 million euros in 2012 (operating loss of 680 million euros in 2011).

The operating profit was adversely affected by the impact of the impairment charge of 4,426 million euros in 2012 (7,364 million euros in 2011 and resulted in an operating loss for that period).

v **SHARE OF PROFITS (LOSSES) OF ASSOCIATES AND JOINT VENTURES ACCOUNTED FOR USING THE EQUITY METHOD**

The Share of profits (losses) of associates and joint ventures accounted for using the equity method was a loss of 6 million euros in 2012, and mainly related to Tiglio I S.r.l.

In 2011 this was a loss of 39 million euros, due to the writedown of the entire investment in the Italtel Group.

v **OTHER INCOME (EXPENSES) FROM INVESTMENTS**

In 2012 other income (expenses) from investments shows a net income of 2 million euros.

In 2011, the income balance of Other income (expenses) from investments was 16 million euros and referred to the gain (17 million euros) on the sale of the entire 27% investment in the Cuban operator EtecSA.

v **Finance Income (Expenses)**

Finance income (expenses) was a net expense of 1,966 million euros (a net expense of 2,040 million euros in 2011), an improvement of 74 million euros. This decrease was mainly due to the positive change in the value of several hedging derivatives, attributable to market fluctuations linked to currency translation. These changes, which are unrealized accounting changes, do not result in any actual monetary settlement. Other positive effects derive from the higher capitalization of finance expenses relating to the purchase of rights to use LTE mobile telephony frequency bands, by the Domestic Business Unit.

For further details about finance income and finance expenses, please see Note Finance income and Finance expenses , of the Notes to the Consolidated Financial Statements included elsewhere in this Annual Report.

v **Income Tax Expense**

Income tax expense was 1,235 million euros, a decrease of 375 million euros compared to 2011. This item also includes 319 million euros relating to the recognition of the credit for the refund receivables for years prior to 2012, following the entry into force of Decree Law 16/2012, which enabled a request for a refund of IRES tax for the IRAP tax calculated on the cost of labor. Net of this effect, income tax decreased by 56 million euros compared to 2011, mainly as a result of the reduction in the tax base of the Parent Telecom Italia.

v PROFIT (LOSS) FROM DISCONTINUED OPERATIONS/NON-CURRENT ASSETS HELD FOR SALE

In 2012, the balance was a profit of 2 million euros, while in 2011 was a loss of 13 million euros and included profits and losses incurred in connection with sales transactions of prior years.

5.2.7 RESULTS OF OPERATIONS OF BUSINESS UNITS FOR THE YEAR ENDED DECEMBER 31, 2012 COMPARED WITH THE YEAR ENDED DECEMBER 31, 2011

v DOMESTIC

On October 31, 2012, Telecom Italia S.p.A. completed the sale of the company Matrix, a wholly-owned subsidiary, to Libero, controlled by Weather Investment II S.à.r.l.. In 2012 Matrix was also moved to Other Operations and was consequently no longer part of Core Domestic in the Domestic Business Unit. Accordingly, the comparative figures of 2011 have been restated on a consistent basis.

The following table sets forth, certain financial and other data for the Domestic Business Unit for the years ended December 31, 2012 and 2011.

	Year ended December 31,			
	2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of euros, except percentages and employees)			
Revenues	17,884	18,991	(1,107)	(5.8)
Operating profit (loss)	1,078	(1,996)	3,074	
% of Revenues	*6.0*			
Employees at year-end (units)(*)	53,224	55,047	(1,823)	(3.3)

(*) The 1,823 headcount change includes the effects resulting from the acquisition, as of January 1, 2012, of the Contact Center business and the related 249 staff from the company Advalso of the Olivetti Business Unit.

Revenues

Revenues decreased by 1,107 million euros, or 5.8%, from 18,991 million euros in 2011 to 17,884 million euros in 2012.

Such decrease was due in part to the continuing weak economy and a market characterized by sharp price reductions on traditional services and tough competition.

The decrease was primarily attributable to the decline in revenues on traditional services as well as the decline in revenues due to the new mobile termination rates (MTR) which reduced these rates by 53% (from 5.3 to 2.5 euro cents) and a Europe-wide cap on the price of roaming traffic. These decreases were only partly offset by the growth in innovative services, especially fixed-line broadband and mobile internet.

The following table sets forth the Domestic Business Unit s revenues by market segment for the years ended December 31, 2012 and 2011.

· **Core Domestic**

	Year ended December 31,			
	2012	**2011**	**Changes**	
	(a)	**(b)**	**(a-b)**	**%**
	(millions of euros, except percentages and employees)			
Revenues	16,933	18,082	(1,149)	(6.4)
Consumer(1)	*8,835*	*9,168*	*(333)*	*(3.6)*
Business(2)	*2,777*	*3,064*	*(287)*	*(9.4)*
Top(2)	*3,102*	*3,529*	*(427)*	*(12.1)*
National Wholesale	*2,052*	*2,104*	*(52)*	*(2.5)*
Other	*167*	*217*	*(50)*	*(23.0)*
Operating profit (loss)	958	(2,136)	3,094	
% of Revenues	*5.7*	*(11.8)*		
Employees at year-end (units)	52,289	54,038	(1,749)	(3.2)

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(1) The company Matrix was sold on October 31, 2012. In 2012 Matrix was also classified under Other Operations, and thus excluded from the Consumer segment of Core Domestic. The periods under comparison have been reclassified accordingly.

(2) 2011 figures for the Business and Top segments have been reclassified for purposes of comparison with the 2012 figures, which take into account the new customer classification criteria introduced at the beginning of 2012.

· **Consumer:** revenues for the Consumer segment were 8,835 million euros, a decrease of 333 million euros compared to 2011 (-3.6%); although revenues declined, this reflects an improvement in the overall recovery from the reduction recorded in 2011 (-5.0%) despite the negative impact of lower termination rates (-211 million euros). This improvement was due in particular to a stabilization of the erosion in voice revenues (both Fixed and Mobile), strong growth in Browsing revenues and growth in sales of devices (+118 million euros, +35.4%), especially mobile internet enabled devices. The decrease, which is entirely attributable to revenues from services (-451 million euros, -5.1%), is due in addition to the aforementioned lower termination rates to traditional Voice and Messaging services, the effects of which are in part offset by growth in mobile internet (+70 million euros, +13%) and fixed broadband access (+34 million euros, +3.6%).

· **Business**: revenues in the Business segment were 2,777 million euros in 2012, a decrease of 9.4% or 287 million euros compared to 2011, due to erosion of the customer base (-6.6% Fixed and -4.8% Mobile, excluding data only lines, compared to 2011) and to a fall in usage and Average Revenue Per User (ARPU) especially on voice services.

· **Top**: revenues in the Top segment were 3,102 million euros in 2012, a decrease of 427 million euros (-12.1%) compared to 2011, mainly due to a slow down in demand due to the weak economy. Revenues from services decreased 260 million euros (-8.6%), primarily attributable to traditional voice and data services, only partly offset by growth in new services, in particular cloud and mobile internet. Revenues from sales decreased 167 million euros (-34% compared to 2011). This performance, in addition to the deteriorating economy already noted for services, also reflects more selective commercial policies aimed at improving profitability.

· **National Wholesale**: revenues in the Wholesale segment amounted to 2,052 million euros in 2012, a decline of 52 million euros (-2.5%) on 2011, mainly due to lower carrying and interconnection revenues, only partly offset by growth in access services to alternative operators.

· **International Wholesale**

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages and employees)			
Revenues	1,393	1,393		
Of which third parties	*985*	*960*	*25*	*2.6*
Operating profit	121	141	(20)	(14.2)
% of Revenues	*8.7*	*10.1*		
Employees at year-end (units)	935	1,009	(74)	(7.3)

International Wholesale segment revenues were 1,393 million euros in 2012, in line with the previous year.

During 2012 International Wholesale continued to pursue rationalization measures aimed at a more selective customer portfolio and traffic strategy.

Revenue performance in Voice (+1.4%) and IP/Data (+5.8%) businesses helped to contain the contraction reported in the other segments, especially multinational customers (-10%).

Operating profit (loss)

Operating profit (loss) was a profit of 1,078 million euros, compared to a loss of 1,996 million euros in 2011, up 3,074 million euros. This improvement in 2012 in reporting an operating profit is mainly due to the lower goodwill impairment loss of 4,016 million euros in 2012 attributable to the Core Domestic cash-generating unit compared to a goodwill write-off of 7,307 million euros in 2011.

The operating profit (loss) was impacted by the change in the following line items as reflected in the table below.

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages)			
Acquisition of goods and services	6,409	6,754	(345)	(5.1)
Employee benefits expenses	2,834	3,031	(197)	(6.5)
Other operating expenses	699	769	(70)	(9.1)

In detail:

- **acquisition of goods and services** decreased 345 million euros (-5.1%) compared to 2011. This decrease was mainly due to a decline in revenues due to other telecommunication operators, owing principally to the reduction in Mobile termination rates;

- **employee benefits expenses** decreased 197 million euros from 2011, attributable mostly to the reduction in the average salaried workforce by 710 compared to the previous year, offset by higher expenses as a result of the acquisition, as of January 1, 2012, of the Contact Center business and the related 249 staff from the company Advalso of the Olivetti Business Unit;

- **other operating expenses** decreased 70 million euros compared with 2011, as shown in the following table:

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages)			
Impairments and expenses in connection with credit management	370	389	(19)	(4.9)
Provision charges	92	50	42	84.0
TLC operating fees and charges	59	58	1	1.7
Indirect duties and taxes	103	108	(5)	(4.6)
Sundry expenses	75	164	(89)	(54)
Total	**699**	**769**	**(70)**	**(9.1)**

Employees

Employees are 52,289 as of December 31, 2012, a reduction of 1,749 units compared to December 31, 2011.

v **Brazil**

The following table sets forth certain financial and other data for the Brazil Business Unit for the years ended December 31, 2012 and 2011.

	Year ended December 31,					
	2012	2011	2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of euros, except percentages and employees)		(millions of Brazilian reais, except percentages and employees)			
Revenues	7,477	7,343	18,764	17,086	1,678	9.8
Operating profit	966	984	2,424	2,289	135	5.9
% of Revenues	*12.9*	*13.4*	*12.9*	*13.4*		
Employees at year-end (units)	11,622	10,539	11,622	10,539	1,083	10.3

Revenues

Revenues for 2012 were 18,764 million Brazilian reais, an increase of 1,678 million Brazilian reais on 2011 (+9.8%). Revenues from services were 16,420 million Brazilian reais, up from 15,353 million Brazilian reais in

2011 (+6.9%). Revenues from product sales increased from 1,733 million Brazilian reais in 2011 to 2,344 million Brazilian reais in 2012 (+35.3%), reflecting the company s strategy of market penetration with high-end handsets (smartphones/webphones and tablets) as an important lever for the expansion of revenues from data services.

Mobile Average Revenue Per User (ARPU) was 19.1 reais in 2012 compared with 21.4 reais for 2011 (-10.7%). The performance of ARPU and revenues from services not only reflects competitive pressures that have led to a decline in unit prices in the voice business, but also the lower mobile operator network interconnection rate, in force since February 2012.

The total number of lines at December 31, 2012 was 70.4 million, 9.8% higher than at December 31, 2011, representing a 26.9% market share measured by number of lines.

Operating profit

Operating profit was 2,424 million Brazilian reais, up 135 million Brazilian reais on 2011. Operating profit growth was sustained by the increase in revenues, mainly VAS, offset in part by higher termination costs due to increased traffic volumes and costs strictly linked to changes in the customer base.

It should be noted that operating profit includes the administrative penalties imposed by the Brazilian telecommunications authority (ANATEL) and other expenses of 53 million Brazilian reais. In particular, disputes with ANATEL concerning the years 2007/2009 and amounting to 26 million Brazilian reais, were recognized following confirmation by the Board of the Brazilian telecommunications authority of measures taken against TIM Brasil. An additional 11 million Brazilian reais relates to disputes with other operators regulated by ANATEL for the years 2008-2011.

With regard to changes in costs, the following table sets forth certain expenses for the years ended December 31, 2012 and 2011.

	Year ended December 31,					
	2012	2011	2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of euros)		(millions of Brazilian reais, except percentages)			
Acquisition of goods and services	4,508	4,399	11,313	10,234	1,079	10.5
Employee benefits expenses	344	321	865	747	118	15.8
Other operating expenses	719	747	1,804	1,738	66	3.8
Change in inventories	2	(19)	4	(45)	49	

· acquisition of goods and services were 11,313 million Brazilian reais (10,234 million Brazilian reais in 2011). The 10.5% increase compared to the previous year (+1,079 million Brazilian reais) was due to the following:

  · +418 million Brazilian reais in revenues due to other TLC operators;

  · +497 million Brazilian reais, mainly, for the purchases of products;

  · +191 million Brazilian reais for rent and lease costs;

  · -27 million Brazilian reais for external services costs;

· employee benefits expenses, were 865 million Brazilian reais, up 118 million Brazilian reais compared with 2011 (+15.8%). The average salaried workforce grew from 9,194 in 2011 to 10,051 in 2012. The percentage of employee benefits expenses to revenues was 4.6% in 2012, increasing 0.2 percentage points compared to 2011;

· other operating expenses were 1,804 million Brazilian reais, an increase of 3.8% (1,738 million Brazilian reais in 2011). Such expenses are set forth in the table below for the years ended December 31, 2012 and 2011.

	Year ended December 31, 2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of Brazilian reais, except percentages)			
Writedowns and expenses in connection with credit management	251	232	19	8.2
Accruals to provisions	228	140	88	62.9
TLC operating fees	1,223	1,290	(67)	(5.2)
Indirect duties and taxes	30	33	(3)	(9.1)
Sundry expenses	72	43	29	67.4
Total	**1,804**	**1,738**	**66**	**3.8**

Employees

Employees were 11,622 at December 31, 2012, an increase of 1,083 people compared to December 31, 2011 (10,539 units).

v **ARGENTINA**

The following table sets forth certain financial and other data for the Argentina Business Unit for the years ended December 31, 2012 and 2011.

	Year ended December 31, 2012	2011	2012 (a)	2011 (b)	Changes (a-b)	%
	(millions of euros, except percentages and employees)		(millions of Argentine pesos, except percentages and employees)			
Revenues	3,784	3,220	22,116	18,496	3,620	19.6
Operating profit	214	509	1,253	2,925	(1,672)	(57.2)
% of Revenues	*5.7*	*15.8*	*5.7*	*15.8*		
Employees at year-end (units)(*)	16,803	16,350	16,803	16,350	453	2.8

(*) Includes employees with temporary work contracts: 3 and 1 as of December 31, 2012 and 2011, respectively.

Revenues

Revenues in 2012 were 22,116 million Argentine pesos, an increase of 3,620 million Argentine pesos (+19.6%) compared with 2011 (18,496 million Argentine pesos) principally due to growth of the broadband and mobile customer base, as well as ARPU. The main source of revenues for the Argentina Business Unit is mobile telephony, which accounts for about 73% of the consolidated revenues of the Business Unit, increasing more than 22% compared to 2011.

Operating profit

Operating profit for 2012 was 1,253 million Argentine pesos compared to 2,925 million Argentine pesos for 2011. The decrease (1,672 million Argentine pesos) was mainly due to full impairment of the goodwill recognized at the time control was acquired by the Telecom Italia Group (979 million Argentine pesos), the partial impairment of its Customer relationships (501 million Argentine pesos) and an increase in amortization charges for Customer relationships resulting from the updating of their useful lives (383 million Argentine pesos).

Changes in costs are explained as follows:

- *acquisition of goods and services* were 9,927 million Argentine pesos (8,031 million Argentine pesos in 2011). The increase of 23.6% compared to the same period of the prior year (+1,896 million Argentine pesos) was mainly due to higher external service costs of 1,246 million Argentine pesos and higher purchases of raw materials, auxiliaries, consumables and merchandise of 424 million Argentine pesos;

· *employee benefits expenses* were 3,422 million Argentine pesos, an increase of 676 million Argentine pesos compared to 2011 (+24.6%). The increase was principally due to salary increases, resulting from the periodic revision of trade union agreements, mainly to reflect the effect of inflation, and staff restructuring costs of 90 million Argentine pesos only partially offset by a reduction in other employee benefits expenses totaling 65 million Argentine pesos. In addition, there was an increase in the average salaried workforce in the mobile area. The percentage of employee benefits expenses to total revenues is 15.5%, increasing 0.7 percentage points over 2011;

· *other operating expenses* were 2,387 million Argentine pesos, an increase of 25.4% (1,903 million Argentine pesos in 2011). Such expenses consist of the following.

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of Argentine pesos, except percentages)			
Impairments and expenses in connection with credit management	275	169	106	62.7
TLC operating fees and charges	424	348	76	21.8
Indirect duties and taxes	1,592	1,286	306	23.8
Sundry expenses	96	100	(4)	(4.0)
Total	**2,387**	**1,903**	**484**	**25.4**

Employees

Employees were 16,803 at December 31, 2012, an increase of 453 units compared to December 31, 2011 (16,350).

v MEDIA

On May 9, 2012, the Board of Directors of Telecom Italia Media approved of the decision of the Board of Directors of Telecom Italia S.p.A. to initiate the process of disposal of the Media segment. As a result, in May 2012 a company restructuring transaction was initiated that led to the creation of La7 S.r.l., a wholly owned subsidiary of Telecom Italia Media S.p.A., to which with effect from September 1, 2012 the television assets were transferred through the assignment of a business unit by Telecom Italia Media S.p.A.

The following table sets forth certain financial and other data for the Media Business Unit for the years ended December 31, 2012 and 2011.

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages and employees)			
Revenues	222	238	(16)	(6.7)
Operating profit (loss)	(263)	(88)	(175)	
% of Revenues	*(118.5)*	*(37.0)*		
Employees at year-end (units)	735	765	(30)	(3.9)

Revenues were 222 million euros in 2012, a decrease of 16 million euros compared to 238 million euros in 2011. Such revenues included:

- La7 (in 2011 and until June 2012 this Business area was called TI Media La7 and it included Corporate activities in addition to the TV business) revenues in 2012, before intragroup eliminations, were 123 million euros, down 16 million euros on the previous year. This result reflects the reduction in net advertising revenues which in 2012 declined by 3 million euros (-2.7% on 2011). This decline was exacerbated by the loss of revenues from the Competence Center, which ceased operations in September 2011, and had previously generated revenues of 13 million euros. In 2012, La7 had an average daily audience share of 3.5% and the La7d channel reported net advertising revenues of 8 million euros, up 2 million euros (+27.7%);

- MTV Group revenues were 55 million euros, before intragroup eliminations, a decrease of 19 million euros compared to 2011 (74 million euros). This decrease is mainly due to lower net advertising revenues (40 million euros in 2012 compared to 50 million euros in 2011) and the decrease in Playmaker activities to third parties by 7 million euros;

- revenues from Network Operator activities (TIMB), before intragroup eliminations were 75 million euros, compared to 55 million euros in the previous year, an increase of 20 million euros. The positive change is due both to the evolution of existing contracts and to new channels put under contract at the end of 2011 for digital terrestrial TV on Multiplexes, which led to the full use of the available digital band since February 2012.

Operating loss

Operating loss was 263 million euros, compared to a loss of 88 million euros for 2011, representing an increase of 175 million euros. Specifically, 2012 includes a total impairment of non-current assets and Goodwill of 157 million euros, established following the impairment test process and also taking account of the prospective sale of the investee LA7 Srl. The impairment loss relating to goodwill is 105 million euros (57 million euros of impairment loss in 2011).

In particular:

- the operating loss of LA7 was 160 million euros, an increase in the loss of 137 million euros compared to 2011 (23 million euros including the above mentioned compensation). This result largely reflects both the contraction in revenues mentioned above and higher operating costs mostly connected with programming costs of La7 and La7d channels (+30 million euros and +4 million euros, respectively);

- the operating loss of MTV group was 38 million euros, a decrease of 25 million euros compared to 2011 primarily due to the decrease in revenues described above, and as a result of the deep editorial transformation of the main channel which during the year went from being a purely musical channel to a more entertainment oriented channel targeted to a young/adult audience;

- the operating loss of the Network Operator was 54 million euros, an increase in the loss of 9 million euros over 2011; this result was influenced by the above mentioned increase in sales while operating costs were substantially in line with the previous year and by the goodwill writedown for 70 million euros in 2012 (43 million euros in 2011).

Employees

Employees were 735 at December 31, 2012, a decrease of 30 units compared to December 31, 2011 (765 units).

Sale of La7 S.r.l.

On March 4, 2013 the Board of Directors of Telecom Italia Media S.p.A., a subsidiary of Telecom Italia S.p.A., voted to grant a mandate to finalize the agreement for the sale of the entire investment in La7 S.r.l. to Cairo Communication S.p.A., excluding the 51% investment in MTV Italia S.r.l. On March 6, 2013, Telecom Italia Media and Cairo Communication signed an agreement for the sale of 100% of La7 S.r.l..

Under the agreements reached, Telecom Italia Media S.p.A. will receive a sale consideration of 1 million euros. La7 S.r.l. will be recapitalized for a sufficient amount to ensure a positive net financial position, at the transfer date, of no less than 88 million euros. This recapitalization will also contribute to reaching the agreed level of equity of 138 million euros at the transfer date.

As a result of the transaction, Telecom Italia S.p.A. has waived intragroup financial receivables, due from Telecom Italia Media S.p.A., for a total amount of 100 million euros.

According to the agreements, a long-term transmission capacity supply contract will also be entered into between La7 S.r.l. and Telecom Italia Media Broadcasting S.r.l.

This sale allows the Telecom Italia Group to terminate its financial support of La7 S.r.l. while keeping the network operator Telecom Italia Media Broadcasting S.r.l. within its scope of operations.

The completion of the sale is subject to the receipt of required regulatory approvals.

v OLIVETTI

On January 1, 2012, the activities and resources of the Advalso S.p.A. contact center were sold to Telecontact Center S.p.A. (a subsidiary of Telecom Italia Domestic Business Unit), as part of a project to bring all Telecom Italia Group call center operations under centralized management.

In addition, on June 13, 2012 the shareholders of the subsidiary Olivetti i-Jet S.p.A. voted to place the company in liquidation.

The following table sets forth, certain financial and other data for the Olivetti Business Unit for the years ended December 31, 2012 and 2011.

	Year ended December 31,			
	2012	2011	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages and employees)			
Revenues	280	343	(63)	(18.4)
Operating profit (loss)	(65)	(43)	(22)	(51.2)
% of Revenues	*(23.2)*	*(12.5)*		
Employees at year-end (units)	778	1,075	(297)	(27.6)

Revenues

Revenues for 2012 were 280 million euros, down 63 million euros compared to 2011. The decrease in revenues is largely related to: lower sales of 21 million euros in the indirect channel in Italy (SME and professional offices), the channel most exposed to the current weak economy; lower sales of 10 million euros in the International and Latin America areas, due to the cancellation of product supply contracts with unsatisfactory margins; and lower product supply contracts with Telecom Italia of 4 million euros. The remaining decline in revenues was due to lower sales of industrial applications resulting from the winding up Olivetti I-Jet S.p.A.

Operating loss

Operating loss was 65 million euros in 2012 compared with an operating loss of 43 million euros 2011.

The result is affected by provision charges for restructuring expenses and other winding up expenses totaling 31 million euros, as a result of the start of the liquidation of Olivetti I-Jet S.p.A, in accordance with the process of repositioning the Business Unit s activities, in line with the shift towards a paperless world and mobile applications.

In addition, the result was also affected, by impairment losses on assets of 3 million euros related to the winding-up Olivetti I-Jet S.p.A..

Employees

Employees at December 31, 2012 were 778, a reduction of 297 compared to December 31, 2011 (1,075 units).

5.2.8 YEAR ENDED DECEMBER 31, 2011 COMPARED WITH YEAR ENDED DECEMBER 31, 2010

Starting from the first half of 2012 the Telecom Italia Group early adopted and retrospectively applied the revised version of IAS 19 (*Employee Benefits*). Accordingly, the comparative figures of 2011 and 2010 have been restated on a consistent basis.

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v REVENUES

Revenues amounted to 29,957 million euros in 2011, an increase of 2,386 million euros, or 8.7%, compared to 27,571 million euros in 2010.

The table below sets forth for the periods indicated gross revenues by Business Unit and consolidated revenues.

	Year ended December 31,					
	2011		2010		Changes	
	Revenues(1) (a)	% of Consolidated revenues	Revenues(1) (b)	% of Consolidated revenues	(a-b)	%
	(millions of euros, except percentages)					
Domestic	18,991	63.4	20,025	72.6	(1,034)	(5.2)
Core Domestic	*18,082*	*60.4*	*19,022*	*69.0*	*(940)*	*(4.9)*
International Wholesale	*1,393*	*4.6*	*1,569*	*5.7*	(176)	*(11.2)*
Brazil	7,343	24.5	6,199	22.5	1,144	18.5
Argentina(2)	3,220	10.7	798	2.9	2,422	
Media, Olivetti and Other Operations(3)	700	2.3	854	3.1	(154)	(18.0)
Adjustments and eliminations	*(297)*	*(0.9)*	*(305)*	*(1.1)*	*8*	
Total Revenues	**29,957**	**100.0**	**27,571**	**100.0**	**2,386**	**8.7**

(1) Revenues are total revenues of the various business units of the Telecom Italia Group before elimination of intercompany sales (but after elimination of sales between companies within the same major business area).

(2) In the scope of consolidation since October 13, 2010.

(3) The Other Operations of the Telecom Italia Group consist of the financial companies and other minor companies not associated with the core business of the Telecom Italia Group.

Revenues in the **Domestic Business Unit** (divided into Core Domestic and International Wholesale) declined by 5.2% compared to 2010. The decrease in revenues, notwithstanding the weak domestic economy and continuing competitive pressures, was slowing and improving. This was due to higher mobile revenues (particularly revenues from services and internet mobile devices), protection of the value of the customer base and development of ICT services in the fixed area.

Revenues from services in 2011 indicated an improving trend over the prior year. Revenues from services in the mobile area were still being impacted, although to a lesser degree, by the competitive repositioning of TIM s plans particularly as regards voice traffic.

The fixed-line area, with a decline in revenues from services, displayed a considerable improvement in the fourth quarter of 2011. In particular, revenues from retail customers decreased at a lower pace than that recorded in 2010 and showed an improving trend during the course of 2011.

With respect to handset sales, revenues recovered entirely driven by the mobile area which benefited from a greater sales push on handsets offering mobile internet connectivity.

With respect to the **Brazil Business Unit**, revenues totaled 7,343 million euros in 2011, an increase of 1,144 million euros compared to 2010. Revenues from services increased, mainly due to the growth of the customer base (over 64 million mobile lines at December 31, 2011, up 25.6% over the prior year). Handset revenues also, increased significantly where, as in the domestic business, the strategy focused on smartphones and webphones as the lever for the growth of mobile data traffic revenues.

As for the **Argentina Business Unit** (included in the scope of consolidation since October 13, 2010), revenues totaled 3,220 million euros in 2011, an increase of 2,422 million euros compared to 2010 which only included the two and a half months in 2010. In particular, the increase was related to the mobile business revenues.

For a more detailed analysis of revenue performance by individual Business Units, reference should be made to Item 4. Information on The Telecom Italia Group 4.2 Business Units .

v **OTHER INCOME**

The following table sets forth other income for the years ended December 31, 2011 and 2010.

	Year ended December 31,			
	2011	2010	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages)			
Late payment fees charged for telephone services	71	72	(1)	(1.4)
Recovery of employee benefit expenses, purchases and services rendered	36	47	(11)	(23.4)
Capital and operating grants	24	38	(14)	(36.8)
Damage compensations, penalties and sundry recoveries	36	18	18	100.0
Sundry income	132	80	52	65.0
Total other income	**299**	**255**	**44**	**17.3**

v **OPERATING EXPENSES**

Our operating expenses amounted to 30,859 million euros in 2011, an increase of 8,851 million euros, or 40.2% compared to 22,008 million euros in 2010. The increase is attributable to the following:

· **Acquisition of goods and services** amounted to 12,859 million euros in 2011, an increase of 1,476 million euros, or 13.0%, compared to 2010 (11,383 million euros). The increase was largely due to the entry of the Argentina Business Unit in the scope of consolidation for the full-year 2011 (+1,052 million euros, including a negative exchange rate effect for 34 million euros) and the significant increase in the sales and technical costs of the Brazil Business Unit the main cause of the overall increase of 879 million euros needed to support the growth of the customer base and sales. Offsetting these increases in part were declines in the domestic business which benefitted from cost cutting actions which contributed to a reduction in purchases of 365 million euros compared to 2010 (-5.1%).

The following table sets forth acquisition of goods and services for the years ended December 31, 2011 and 2010.

	Year ended December 31,			
	2011	2010	Changes	
	(a)	(b)	(a-b)	%
	(millions of euros, except percentages)			
Purchase of goods	2,525	1,568	957	61.0
Portion of revenues to be paid to other operators and interconnection costs	4,232	4,275	(43)	(1.0)
Commercial and advertising costs	2,259	2,100	159	7.6
Power, maintenance and outsourced services	1,618	1,258	360	28.6
Rent and leases	647	594	53	8.9
Other service expenses	1,578	1,588	(10)	(0.6)
Total acquisition of goods and services	**12,859**	**11,383**	**1,476**	**13.0**

% on Revenues	*42.9*	*41.3*

· **Employee benefits expenses**

The following table sets forth employee benefit expenses for the years ended December 31, 2011 and 2010.

	Year ended December 31, 2011 (a)	2010 (b)	Changes (a-b)	%
	(millions of euros, except percentages)			
Employee benefits expenses Italian companies:				
Ordinary employee expenses and costs	3,144	3,273	(129)	(3.9)
Corporate restructuring expenses	12	258	(246)	(95.3)
Total employee benefits expenses Italy	**3,156**	**3,531**	**(375)**	**(10.6)**
Employee benefits expenses Outside Italy				
Ordinary employee expenses and costs	836	450	386	85.8
Corporate restructuring expenses				
Total employee benefits expenses Outside Italy	**836**	**450**	**386**	**85.8**
Total employee benefits expenses	**3,992**	**3,981**	**11**	**0.3**
% on Revenues	*13.3*	*14.4*		

The change was affected by:

- the increase connected with the consolidation of the Argentina Business Unit for the full year 2011 (+11,521 average salaried workforce compared to 2010);
- lower expenses owing to the contraction of the average salaried workforce (the above effect relating to the Argentina Business Unit is already excluded) by 3,301 compared to 2010;
- the provisions for expenses for mobility under Law 223/91, related to the 2010 agreements with the unions entered into by the Parent Telecom Italia S.p.A. and Telecom Italia Information Technology, had been adjusted by 12 million euros, of which 9 million euros for the Parent Telecom Italia and 3 million euros for Telecom Italia Information Technology.

The Group s average number of salaried workforce for the periods indicated was as follows:

	Year ended December 31, 2011 (a)	2010 (b)	Changes (a-b)	%

	(Full time equivalent units, except percentages)			
Average salaried workforce Italy	53,561	57,087	(3,526)	(6.2)
Average salaried workforce Foreign(1)	24,808	13,063	11,745	89.9
Total average salaried workforce(2)	**78,369**	**70,150**	**8,219**	**11.7**

(1) The increment in the average employees of the salaried workforce is primarily attributable to the consolidation of the Argentina Business Unit for the full year 2011 (15,232 average headcount in 2011).

(2) Includes the average employees with temp work contracts: 87 in 2011 (75 in Italy and 12 outside Italy). In 2010 the headcount was 84 (68 in Italy and 16 outside Italy).

Group s employees at December 31, 2011 and 2010 were as follows:

	As of December 31,			
	2011	**2010**	**Changes**	
	(a)	**(b)**	**(a-b)**	**%**
	(units, except percentages)			
Employees Italy	56,878	58,045	(1,167)	(2.0)
Employees Foreign	27,276	26,155	1,121	4.3