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Corporate Governance

Introduction

The Company is aware of the importance of its Corporate Governance system in fulfilling its objective of creating value for all shareholders and making progress in sustainable development, and thus induces the Company to keep its own corporate governance system constantly in line with national and international best practices, as well as making sure that it is up to date with legislative changes.

During 2006, the Company – after having implemented changes according to the national legislation and regulations regarding market abuses – launched an overall survey and updating of its corporate governance instruments, in order to align them with provisions under the law no. 262/2005 and the legislative decree No. 303/2006 (henceforth, respectively, the “**Savings Law**” and the “**Corrective Decree**”), as well as recommendations in the new edition of the Self-Regulatory Code for listed companies published in March 2006 (henceforth the “**new Code of Conduct**”).

With reference to updates made according to the new Code of Conduct, we note that the Company – having formalized its adherence to this code at the Board of Directors meeting on March 12th, 2007 – avails itself of the faculty, conceded by the Borsa Italiana, to make reference in this Report to the Self-Regulatory Code published in July 2002 (henceforth the “**Code**”), indicating the completed or planned activities made in order to adhere to the recommendations indicated in the new Code of Conduct.

As a preview to the points elaborated in detail in this report, we note that the complete review of the governance framework – which was carried out by a specific working team coordinated by the Secretary to the Board of Directors and subject to constant attention (in three consecutive meetings during which the Board of Statutory Auditors participated as well) by the Committee for Internal Control and Corporate Governance, which formulated the proposals to the Board of Directors – brought about the defining of a series of changes that did not significantly modify the company governance, which proved to be largely in line, if not to the letter at least in substance, with the new relevant regulatory framework.

The governance system adopted by the Company, before and after the revision mentioned above, is and remains founded on the central position of the Board of Directors, on the presence of correct disclosure practices regarding the choices and the procedures for the decisions of the Company, on an effective system of internal controls, on an effective monitoring for potential clash of interests and on a rigorous code of conduct regarding the implementation of transactions with related parties.

These benchmarks are specified in the Code of Ethics, in the Company bylaws, in the Regulations regarding shareholders' meetings, and in a series of principles, rules and procedures that are available on the website of the Company at www.pirelli.com under the section dedicated to the Governance.

In compliance with the regulation of markets instructions organized and managed by Borsa Italiana and taking also into account information included in the “Guidelines for the drawing up of the annual report on corporate governance” published by Borsa Italiana and in the “Corporate governance reports handbook” published by Assonime, this report describes the main characteristics of the corporate governance system of the Company and the functioning of its various components during the 2006 financial year, as well as it accounts for its already existing activities and those planned for the future in order to ensure compliance with the new Code of Conduct, in accordance with Borsa Italiana indications made on November 16th, 2006.

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GOVERNANCE STRUCTURE

1. Company Organisation

The Board of Directors

In line with Italian regulations, the management of the Company is entrusted to a Board of Directors that plays an active role regarding its strategic directions, as well as its management control, while directing administration as a whole and having a direct hand in a series of decisions that are necessary or useful in the pursuit of the corporate aims.

In order to fulfil its tasks, the Board avails itself of the assistance of Committees established within it (i.e. the Remuneration Committee and the Committee for Internal Control and Corporate Governance), entirely composed of independent directors.

The Board of Statutory Auditors

According to the law and the Company bylaws, the Board of Statutory Auditors is entrusted with the following:

- the observance of the law and the bylaws;
- the respecting of proper administration principles;
- the adequacy of the organisational structure of the Company for the aspects within its competence, of the internal control and administration-accounting systems, as well as the latter's reliability in correctly representing management results;
- the methods of application of the corporate governance rules contained in the codes of conduct prepared by companies that manage regulated markets or associations of category, which the company declares to follow;
- the adequacy of the regulations imposed by the Company on its subsidiaries regarding the reporting of price sensitive information¹.

The Board of Statutory Auditors fulfils its tasks by exercising all of the powers conferred upon it by law and being able to count on a constant and analytical information flow from the Company, during and beyond the regular meetings of the Board of Directors and its Committees.

In fulfilling its functions, the Board of Statutory Auditors, besides participating in all the Board of Directors and Shareholders' Meetings, also takes part in the tasks of the Remuneration Committee and the Committee for Internal Control and Corporate Governance. Moreover, Paolo Francesco Lazzati, a Statutory Auditor, is a member of the Monitoring Board in accordance with the legislative decree No. 231/2001.

The Shareholders' Meeting

The Shareholders' meeting – that may be ordinary or extraordinary – has the competence, according to the law, for resolving upon a series of specified matters such as the approval of the financial statements, the election and the revocation of directors and statutory auditors, their fees and responsibilities, the purchase or sale of own shares, the modification of the Company bylaws, the issuance of convertible bonds, and, except for restricted cases, merger and division transactions.

The Shareholders' meeting, which may be held in Italy also out of the registered office of the Company, must be called within 120 days, or in special circumstances within 180 days, as from the end of the financial year; if the meeting is called within 180 days, the directors must indicate the reason for the delay in the Directors' Report included in the year-end financial statements.

In addition to the law and the bylaws, shareholders' meetings are governed by the Rules of Proceeding, which were approved by the shareholders' meeting held on May 11th, 2004 (available on the website of the Company www.pirelli.com in the section entitled "Governance"). In order to pay attention to the possible integration of the agenda on shareholders' request, as introduced by

¹ Now known as "sensitive information" (art. 114 of the Legislative Decree No. 58/1998).

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the Savings Law, the Board of Directors, in the meeting held on March 12th, 2007, resolved to propose to the shareholders – at the meeting called to examine the 2006 financial statements – some modifications to the Rules. For full details of these proposals, please see the report that was drafted by the Directors regarding this matter.

The Shareholders' Meeting is chaired, in the following order, by the Chairman of the Board of Directors, by a Deputy Chairman or a Managing Director; if there are two or more Deputy Chairmen or Managing Directors, they are chaired by the senior in age. In the absence of the aforementioned individuals, the Shareholders' Meeting is chaired by another person elected by the shareholders with the favourable vote of the majority of the capital represented at the meeting.

The Chairman of the shareholders' meeting – among other things – verifies that the meeting has been validly constituted, ascertains the identity of those present and their right to attend, including by way of proxies, ascertains the legal quorum and governs the proceedings, with the faculty to establish a different order for the discussion of the topics listed in the agenda indicated in the notice convening the meeting. The Chairman also takes appropriate action to ensure orderly discussion and voting, establishing the procedures and verifying the results. The decisions of the meeting are recorded in minutes signed by the Chairman of the meeting and the Secretary or by the Notary public.

The minutes of extraordinary Shareholders' Meetings must be prepared by a Notary public appointed by the Chairman of the meeting.

Audit of accounts

The audit of accounts activity is carried out by an auditing firm appointed during a Shareholders' Meeting and chosen among those listed in a specific register held by Consob.

The task – conferred in reference to the 2005-2007 financial years at the Shareholders' Meeting held on April 28th, 2005 – is currently entrusted to PricewaterhouseCoopers S.p.A., which was also appointed by other major Group companies to audit their accounts.

2. Composition of share capital

On March 12th, 2007 the share capital of Pirelli & C. S.p.A. was 2,791,311,344.64, divided into no. 5,367,906,432 shares with a par value of 0.52 each, of which no. 5,233,142,003 were ordinary shares and no. 134,764,429 were non-convertible savings shares.

The share capital may further increase up to a nominal maximum of 2,819,508,786.64 by means of the issue of a maximum of no. 54,225,850 ordinary shares 0.52 each, at a price of 1.15 each, of which 0.63 as a share premium, against the possible exercising of options granted to managers and cadres employed by the Company, by its subsidiaries and by the subsidiaries of the latter as part of the "Pirelli to People" and "Group Senior Executives" stock-option plans set up by Pirelli S.p.A. in 2001.

To the best of the Company's knowledge, no legal or natural person can exercise control according to the Article 93 of the Legislative Decree 58/1998 (henceforth the "Financial Services Act").

Participants in the Pirelli & C. S.p.A. Block Share Syndicate, the purpose of which is to ensure Pirelli & C. share structure stability, and an excerpt of the relevant agreement are listed at the bottom of this chapter and are available on the website of the Company at www.pirelli.com.

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Implementation of provisions in the self-regulatory code

1. Board of Directors

1.1 Role and functions

As mentioned, the Board of Directors plays a central role in the Company's corporate governance system; it has the power (and the duty) to direct Company business, pursuing and fulfilling its primary and ultimate objective of creating shareholder value.

Pursuant to Article 11 of the Company bylaws, the Board is responsible for the management of the Company and, to this end, it is vested with the broadest powers, except for those matters remitted by law or the bylaws to the authority of the shareholders' meeting.

In line with the provisions in the Self-Regulatory Code for listed companies (new edition published March 2006), the Board of Directors has the exclusive right to:

- examine and approve the strategic, business and financial plans of the Company and the Group;
- draw up and adopt the corporate governance regulations of the Company and define the governance guidelines of the Group;
- evaluate the adequacy of the general organisational, administrative and accounting structure of the Company as well as of those subsidiaries of strategic importance as set up by the Managing Directors, with special reference to internal auditing and the management of clashes of interests;
- grant powers to the Managing Directors and the Executive Committee (if established) and revoke them; fix the limits, the manner in which they have to be exercised and the frequency, at least on a quarterly basis, with which such bodies must report to the Board on the activity performed in the exercise of the powers granted;
- determine, after having examined the Remuneration Committee proposals and consulted the Board of Statutory Auditors, the remuneration of the Managing Directors and of those directors who are vested with special offices and, if the shareholder meeting has not already resolved upon it, allocate the total amount to which the members of the Board of Directors are entitled;
- evaluate the general performance of the Company, taking particularly into consideration the information received from the entrusted corporate bodies and compare periodically the results achieved with those planned;
- examine and approve all transactions involving the Company and its subsidiaries which have a significant impact on the strategy, the profitability, the assets or the financial position of the Company, paying particular attention to situations in which one or more directors act in their own interest or in the interest of third parties, and more generally to transactions with related parties. During the revision of the corporate governance instruments, it was expressly stated that the Board of Directors establish general criteria for the detection of these kinds of transactions;
- at least once a year, evaluate the size, composition and functioning of the Board itself and its Committees, expressing in case an opinion on the professional figures whose presence in the Board could be deemed advisable;
- establish the Self-Regulatory Body, pursuant to Legislative Decree 231 of June 8th, 2001;
- appoint and dismiss the position of the responsible for internal control, determine relevant duties and fees, taking into consideration the advices of the Committee for Internal Control, the Corporate Governance Committee and the Board of Statutory Auditors;
- assess and approve periodic reports prepared according to applicable legislation;
- exercise other powers and fulfil duties as required by the law and the Company bylaws.

1.2 Appointment of Directors

Since 2004, the Company bylaws have stated (in article 10) that the appointment of the Board of Directors shall take place through a slate vote and therefore they are already in line with the regu-

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lations introduced by the Savings Law in the Financial Services Act. This system ensures that – if more than one slate is presented – minority shareholders can elect one fifth of the Directors.

The slates presented by shareholders, undersigned by the parties submitting them, must be deposited at the registered office of the Company at least ten days prior to the date set for the shareholders' meeting to be held on first call and made available to anyone on request.

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

Only shareholders who, alone or together with other shareholders, hold at least 2 per cent of the share capital entitled to vote at the ordinary shareholders' meeting, may present slates, subject to their proving ownership of the necessary number of shares not later than two days prior to the date set for the shareholders' meeting to be held on first call.

Declarations in which the candidates individually accept their candidacy and attest, on their own responsibility, that there are no grounds for ineligibility or incompatibility, and that they meet the requirements prescribed by law and the bylaws, must be deposited together with the slates within the time limit specified above. The declarations must be accompanied by a *curriculum vitae* for each candidate regarding his personal and professional characteristics, with the possible indication that the candidate qualifies as independent.

As per international best practices, the renewal of the administrative body of the Company allows shareholders to vote individually on: (i) the number of people on the Board of Directors; (ii) the election of Directors through a vote on the presented slates; (iii) the duration of the mandate of the Board of Directors; and (iv) the pay packages of the Directors.

In reference to the election methods, it seems pertinent to note that the Board of Directors that convened on March 12th, 2007 – in order to align the above-mentioned elections system with the new provisions introduced by the Savings Law and the Corrective Decree, as well as recommendations in the new Code of Conduct – proposed some changes at the following Shareholders' Meeting aiming at (i) allowing for the percentage of share capital required to present slates to be less than 2% if so deemed by Consob (ii) increasing the time within which slates must be presented to 15 days, and (iii) together with the depositing of the curriculum vitae of each candidate, requiring a list of all the administrative and control positions that the candidate has held in other companies, and requiring that the candidate be suitable to be qualified as an independent Director according to legal and Company criteria.

During the same meeting, following a specific recommendation in the new Code of Conduct (criterion no. 1.C.3.), which requires the Board to express an opinion regarding the limit of the number of director's or auditor's positions held in other companies that can be considered compatible with administrative positions in Pirelli & C., the Board mandated the Committee for Internal Control and Corporate Governance to draw up a proposal regarding this point.

1.3 The composition of the Board of Directors

The Board of Directors of the Company, as established by the bylaws, consists of no less than seven and no more than twenty-three members.

The Board of Directors in office on April 28th, 2005 was renewed for three financial years (and will therefore be the Board that will convene for the approval of the financial statements at December 31st, 2007), and set the number of its members at twenty.

Through a vote, the minority list therefore nominated four Directors, i.e. one fifth of the total number. Two lists were presented, one by the participants in the Pirelli & C. S.p.A. Share Block Syndicate and the other by various savings management companies. Those proposing the slates made the candidates' profiles available so that the candidates' personal and professional characteristics, as well as some candidates' qualifications as independents, were made known prior to vot-

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ing. The *curricula vitae* presented when the slates were filed were promptly published on the Company web site at www.pirelli.com, where they remain available in an updated version.

During 2006, some changes were made in the system of directors. Specifically, following the resignation of the Director Carlo De Benedetti – which took place in May – the Board of Directors convened on September 12th, 2006 nominated Alberto Bombassei who, in accordance with legislation, will remain in office until the next Shareholder Meeting. Subsequently, on November 6th, 2006 Carlo Buora resigned from his post of Managing Director and Board Member (as well as General Manager) of the Company.

Not having added any more members, the Board of Directors is therefore currently comprised of the following 19 members:

Marco Tronchetti Provera	Chairman
Alberto Pirelli	Deputy Chairman
Carlo Alessandro Puri Negri	Deputy Chairman
Carlo Acutis	
Carlo Angelici	Member of the Committee for Internal Control and Corporate Governance
Gilberto Benetton	
Alberto Bombassei	
Franco Bruni	Member of the Committee for Internal Control and Corporate Governance
Gabriele Galateri di Genola	
Mario Garraffo	
Dino Piero Giarda	
Berardino Libonati	Chairman of the Remuneration Committee
Giulia Maria Ligresti	
Massimo Moratti	
Giovanni Perissinotto	
Giampiero Pesenti	Member of the Remuneration Committee
Aldo Roveri	Member of the Remuneration Committee
Carlo Secchi	Chairman of the Committee for Internal Control and Corporate Governance and Lead Independent Director
Paolo Vagnone	

Carlo Angelici, Franco Bruni, Mario Garraffo and Aldo Roveri were minority candidates.

Three of the members of the Board of Directors are *executive directors* as defined in Article 2.C.1 of the new Code of Conduct: The Chairman Marco Tronchetti Provera, and (due to the executive duties bestowed upon them regarding the companies Pirelli Tyre S.p.A. and Pirelli & C. Real Estate S.p.A.) Deputy Chairmen Alberto Pirelli and Carlo Alessandro Puri Negri.

The Board of Directors evaluated the role of *independent directors* based on the most rigorous requirements in the new Code of Conduct (criterion 3.C.1.) which states that an independent director may not be – by law – considered independent:

- a) if they, directly or indirectly or on behalf of subsidiaries, trust companies or through third parties, control the issuer or are able to exercise considerable influence, or are a participant in a shareholder agreement through which one or more individuals can exercise control or significant influence on the issuer;

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- b) if they have or have been in the past three financial years a member of prominence² of the issuer, or one of its strategic subsidiaries or a company under joint control with the issuer, or a company or a body that, alone or together with others in accordance with shareholders agreements, control the issuer or are able to exercise considerable influence;
- c) if directly or indirectly (e.g. through subsidiaries or bodies that have a significant position, such as a partner of a law firm or a consultancy company) they have, or had in the previous financial year, a close business, financial or professional relationship with the following:
 - the issuer, one of its subsidiaries, or any related prominent exponent thereof;
 - an individual who, alone or together with others within a shareholder agreement, controls the issuer, or – if a company or body – with related prominent exponents thereof;
 or if, in the previous three financial years, they were an employee of one of the above-mentioned individuals or bodies;
- d) if they receive, or in the past three financial years received, from the issuer or one of its subsidiaries or parent companies, a substantial bonus compared to their “fixed” salary as non-executive director of the issuer, including performance-based incentive plans, such as stock bonuses or other;
- e) if they have been a director for more than nine years of the past twelve;
- f) if they are an executive director in another company in which the executive director of the issuer holds the role of director;
- g) if they are a board member or director of a company or body belonging to the company mandated to audit the accounts of the issuer;
- h) if they are a close family member of a person that finds themselves in one of the situations described above.

Following a lengthy evaluation of the information supplied by the Directors and available to the Company, the Board of Directors – also based on declarations made by the same – judged 10 of the remaining 16 directors (Carlo Acutis, Carlo Angelici, Alberto Bombassei, Franco Bruni, Mario Garraffo, Dino Piero Giarda, Berardino Libonati, Giampiero Pesenti, Aldo Roveri and Carlo Secchi) may be qualified as independent directors, while the other six (Gilberto Benetton, Gabriele Galateri di Genola, Giulia Maria Ligresti, Massimo Moratti, Giovanni Perissinotto and Paolo Vagnone) may be qualified as non-executive directors.

Moreover, we note that the Board of Directors has checked that all directors qualified as independent may also be so deemed in accordance with the requirements for members of the board of statutory auditors in the Financial Services Act, as amended by the Savings Law.

A table at the end of this chapter shows the positions which the directors of the Company hold as director or member of the board of statutory auditors in other listed companies in Italy and abroad, in financial, banking and insurance companies, and in other large companies.

1.4 The role of Lead Independent Director

As of November 2005, in order to increase further the role of the ten Independent Directors, the Board of Directors decided to introduce a Lead Independent Director. The Lead Independent Director (Carlo Secchi, the Chairman of the Committee for Internal Control and Corporate Governance, was chosen) coordinates and acts as a point of reference for the requirements and contributions of the independent Directors.

The Lead Independent Director may also convene – on his own initiative or upon the request of other Directors – specific meetings solely for independent Directors (i.e. Independent Directors' executive sessions) in order to discuss subjects occasionally felt to be of interest to the functioning of the Board of Directors or management of the firm.

² The following are considered “members of prominence” of a company or body: the chairman of the body, the legal representative, the chairman of the board of directors, the executive directors and managers with strategic responsibilities within the company or body concerned.

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Please note that the Lead Independent Director may collaborate with the Chairman of the Board of Directors for the better functioning of the Board of Directors.

During 2006, two Independent Directors' executive sessions were held that involved the discussion of intrinsic subjects to the corporate governance of the Company, the role and function of the independent Directors and the accounting measurement of the shareholding held in Olimpia S.p.A..

During 2007, one Independent Directors' executive session has already been held.

1.5 Board performance evaluation

During 2006, for the first time, the Board of Directors made a self-evaluation of its performance (officially called a "Board performance evaluation"), thus adhering to international best practices and the provisions in the new Code of Conduct (criterion I.C.1., letter g); this evaluation studied the size, the composition and the functioning of the Board and its Committees, and was carried out with the assistance of a specialised external consultancy company that worked side by side with the Committee for Internal Control and Corporate Governance in order to set self-evaluation methods and analyse the results.

A generally positive evaluation of the Board and its work emerged from an analysis of the results, together with useful suggestions to improve its functioning further.

1.6 Board of Directors Meetings

During 2006, 10 Board of Directors meetings were held. The overall participation level of Directors was about 77%; the independent Directors ensured that their average overall attendance level was higher than 80%.

The bylaws do not provide for a minimum frequency of Board of Directors meetings. It is, however, the practice for the Board to convene on June 30th to examine the preliminary data, the budget project and the quarterly and biannual reports. As a rule, at the end of the last Board meeting of each financial period, the market is informed of the timing of the major company events (that is, Board and Shareholders' Meetings) planned for the following financial period. Any changes are promptly communicated to the market.

In November 2006, the Company distributed a schedule for five meetings in 2007. The schedule confirms the advance publication, also in 2007, of the budget documentation and the biannual report (making it possible, among other things, to take advantage of the exemption from the drawing up of the fourth 2006 quarterly report and of the second 2007 quarterly report).

The Board meetings may take place by means of telecommunication enabling participation of all parties concerned, with equal information, in the debate.

The Board of Directors meetings are convened by means of letter, telegram, fax or e-mail sent at least five days prior (or, in the event of emergencies, at least six hours prior) to the meetings. Each Director and Acting Auditor is called to the meetings.

Barring exceptional cases, the Directors and the Auditors have always received early enough the necessary documentation and data in order to express an informed opinion on the materials subject to their examination.

1.7 Directors' remuneration

In addition to reimbursement for expenses incurred in performing their duties, Directors receive annual fees determined by the shareholders' meeting (Article 14 of the bylaws).

The meeting of April 28th, 2005 decided "to establish a maximum of 1,200,000 as the total annual compensation to the Board of Directors pursuant to Art. 2389, paragraph 1, of the Civil Code, an amount to be distributed among its members in conformity with decisions taken in this regard by the Board."

At the same meeting, on April 28th, 2005, the Board of Directors established the distribution of the compensation as follows:

- € 50,000 annually for each of the 20 members of the Board of Directors;

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- € 25,000 annually for each of the members of the Committee for Internal Control and Corporate Governance;
- € 20,000 annually for each member of the Remuneration Committee, with the right being reserved to use the residual amount (65,000) in the future to give the Board a margin of organizational flexibility, including for the adoption of any new governance solutions.

A payment of 10,000 annually is also made to the Board member taking part in the Self-Regulatory Body as per legislative decree no. 231/2001 (Carlo Secchi).

The Board of Directors upon consultation with the Board of Statutory Auditors establishes remuneration for directors given particular tasks, as proposed by the Remuneration Committee. The current remuneration system provides for payments to comprise a fixed amount and an additional bonus linked to the performance of the Group, and to be related to the attainment of specific objectives set by the Board.

Information on the remuneration of the directors entrusted with special powers can be found in a chart in the notes to the financial statements for 2006.

Lastly, it should be noted that there are no stock-option plans for either the executive or the non-executive directors³.

1.8 Delegated powers

Taking into consideration and according to the new corporate regulations established in legislative decree no. 6/2003, the Chairman Marco Tronchetti Provera and the Managing Director Carlo Buora (the latter of which ended his mandate on November 6th, 2006) were identically recognized as legal proxies of the Company, each given legal powers to perform any pertinent act to corporate activity in its various manifestations.

Limits to the powers conferred have also been established and qualified as internal limits to the relationship between the delegating body of the Board and the parties with delegated powers: the Chairman Marco Tronchetti Provera has the power to guarantee Company and subsidiary bonds having individual values of more than 25 million, or for third parties regarding bonds with individual values of more than 10 million (in the latter cases another Director's signature must be included with the Chairman's signature); the General Manager Carlo Buora – as stated, as long as he fills this role – has quantitative limits to the powers to make transactions of greater significance (50 million regarding the undertaking or alienation of interests or shareholdings in companies or bodies, the subscription of capital increases and bonds, the signing of exchange and purchase/sale contracts involving real estate assets or financial instruments).

Furthermore, the Chairman, Marco Tronchetti Provera, was confirmed as having the following organizational functions:

- relations with shareholders and the information provided to them;
- coordination of the Managing Directors' activities;
- formulation, in agreement with the Managing Directors, of the general strategies and development policy for the Company and the Group, to be submitted to the Board of Directors together with extraordinary corporate actions;
- proposals, to be submitted to the Board of Directors in agreement with the Managing Directors, for the appointment of members of the General Managers' Departments and, after consulting the Remuneration Committee, for their compensation;
- chairmanship of the managing committees with strategic functions;
- all forms of communication to the market, with the right to delegate to the managing directors, in accordance with what is covered by the procedure for the management and communication to the market of privileged information, as approved by the Board on March 13th, 2006;

³ With the exception of Deputy Chairman Carlo Alessandro Puri Negri, in that, as Chief Executive Officer of Pirelli & C. Real Estate S.p.A., he holds stock options in that company.

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- the right to acquire from the Managing Directors and the management of the Group all the data and information considered necessary to carry out the above-mentioned functions.

Powers pertaining to their specific functions, subject to certain quantitative limits, have been granted to Claudio De Conto⁴, Chief Operating Officer, and to Luciano Gobbi⁵, Chief Finance and Strategic Planning Officer⁶.

Less broad powers have been granted to other managers of the Company to be used in their individual spheres of competence.

As in the past, in 2006 the Chairman, the Managing Director (during his mandate), the General Managers and the Managers used their delegated powers only for the ordinary management of the activities of the Company (in regard to which the directors were periodically informed) and submitted the transactions which were more important from an operational or financial perspective to the Board of Directors.

In fact, delegation does not mean the assignment of exclusive powers but is rather the solution adopted by the Company to ensure, in terms of the organization of the Board, the best degree of operational flexibility, both within the Company and in relation to third parties.

1.9 Provision of information to the Board of Directors

Pursuant to Article 11 of the bylaws (which incorporate the prescriptions of Article 150, paragraph 1 of the Financial Services Act), the Board of Directors and the Board of Statutory Auditors are kept informed, inter alia by the persons with delegated powers, about the performance of the Company, its general management, its prospects and the transactions of greatest significance for its profitability, financial position or assets and liabilities carried out by the Company or its subsidiaries; in particular, such persons report any transactions in which they have an interest, for their own account or on behalf of third parties, or that are influenced by the person, if any, who performs management and coordination activities. Such reports are made promptly and at least once every three months, on occasion of the Board of Directors meetings (and the Executive Committee, if established) or by means of a written communication.

In order to favour the orderly organization of the flow of information, in July 2002, the Company adopted a procedure with the rules to be followed to ensure compliance with the above-mentioned Article 150 with regard to the activities of the executive directors, both in exercising their delegated powers and in carrying out the transactions approved by the Board of Directors.

This procedure has also recently been subject to a review that involved Company governance frameworks. The Board of Directors meeting on March 12th, 2007 actually decided to adopt a general procedure on information flows to the Directors and Auditors, which incorporates more widely the procedure adopted to fulfil the obligations of art. 150 of the Financial Services Act. The new procedure aims at regulating and coordinating the various types of data flowing to Directors and Auditors, so that they all have the common aim of continuously making available to the members of these Boards the data needed to properly fulfil their directional, policy and control responsibilities.

The text of this new policy, shown at the end of this chapter, is also available on the website of the Company at www.pirelli.com, under the sectioned entitled "Governance".

1.10 Rules of conduct for transactions with related parties

The Company has also established since 2002 the rules of conduct for transactions with related parties, including intra-group business. The aim of the rules is to guarantee substantial and procedural

⁴ Up until November 7th, 2007, General Manager of Administration and Control.

⁵ Up until November 7th, 2007, General Manager of Finance.

⁶ Similar powers were given to General Manager of the Tires Sector, Francesco Gori, until June 30th, 2006, the date on which he began his role with the subsidiary Pirelli Tyre S.p.A., where he is Chief Executive Officer.

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fairness and transparency of transactions made by Pirelli & C. with parties related to Pirelli & C., either directly or through subsidiaries.

In fact, under the rules, the Board of Directors is required to give advance approval of transactions with related parties, including intra-group transactions, apart from those of a customary nature and those to be concluded at standard conditions. To this end, a provision is made for the Board to be adequately informed of all the relevant aspects: the nature of the relationship, the manner of carrying out the transaction, the economic and other conditions, the evaluation procedures used, the rationale for the transaction and the interest of the Company in its implementation and the associated risks. If the related party is a Director or a party related via a Director, the Director in question – unless the board decides otherwise – may only provide clarifications and must leave the meeting when the motion is examined and put to a vote. Depending on the nature, value and other aspects of related-party transactions, the Board of Directors may be assisted by one or more outside experts in order to prevent contracts from being concluded at inappropriate conditions. According to the circumstances, such experts express an opinion on the economic and/or legal and/or technical aspects of the transaction.

Finally, please note that in order to identify what constitutes a related party, the Company – as also indicated by Consob – defines the concept of “related party” according to the IAS/IFRS principles (specifically IAS 24).

The text of the main principles of conduct is shown at the bottom of this report, and is available on the website of the Company at www.pirelli.com under the section entitled “Governance”.

2. Committees

2.1 The Remuneration Committee

The Board has established, since 2000, the Remuneration Committee from among its members, charged with fact-finding and advisory functions.

In line with the provisions in the new Code of Conduct, this Committee:

- prepares proposals to the Board regarding the remuneration to the Board of Directors and those who hold certain roles, to ensure that they align with the objective of shareholder value creation in the medium-long term;
- periodically evaluates the remuneration criteria for the upper management of the Company and, upon request of the Board of Directors, prepares related proposals and recommendations, with specific reference to the adoption of possible stock option plans or stock bonuses;
- monitors the application of the decisions made by the relevant bodies and company policy regarding top management compensation.

The Committee – which may also request the assistance of external consultants in fulfilling its mandate – meets whenever its Chairman deems it appropriate or a meeting has been requested by another member of the committee or by a Managing Director. The Board of Statutory Auditors and, when considered appropriate, other Company representatives participate in the Committee meetings.

In full compliance with provisions in the new Code of Conduct, the Remuneration Committee consists exclusively of independent Directors: Bernardino Libonati (Chairman), Giampiero Pesenti and Aldo Roveri.

During 2006, the Remuneration Committee met four times during which it examined – and presented to the Board – pay packages to the Chairman, the Managing Director (also in reference to the end of the mandate regarding the roles covered by the same) and the General Managers, also disclosing the criteria underlying its decisions.

All members of the Remuneration Committee participated in the meetings, except for one absence during one meeting.

2.2 The Committee for Internal Control and Corporate Governance

The Board has established the Committee for Internal Control and Corporate Governance, which

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is charged with fact-finding and advisory functions, from amongst its members since 2000. In particular, this committee:

- a) assists the Board of Directors in establishing the guidelines for the internal control system and periodically verifying its adequacy and effective working, so as to ensure that the risks facing the Company are managed appropriately;
- b) evaluates the work plan prepared by the persons responsible for internal control, from whom it receives periodic reports;
- c) assesses, together with the financial officers and the independent auditors of the Company, the appropriateness of the accounting standards applied and their homogeneousness for the purpose of preparing the consolidated financial statements;
- d) evaluates the proposals made by independent auditors in order to be awarded the appointment, as well as the audit plan and the results set out in the auditors' report and in the letter of suggestions;
- e) reports to the Board of Directors at least once every half year, on the occasion of the approval of the draft of annual financial statements and the half-yearly report on the activity performed and the adequacy of the internal control system;
- f) performs the additional tasks that may be assigned to it by the Board of Directors, particularly with regards to relations with the independent auditors; and
- g) monitors compliance with the rules of corporate governance and their periodic updating and compliance with the rules of conduct adopted by the Company and its subsidiaries.

Similarly to the Remunerations Committee, the Board of Directors that convened on March 12th, 2007 provided for the adjustment of duties mentioned above to those required in the new Code of Conduct for committees and internal control (art. 8), as well as deciding that the Committee should continue to maintain the corporate governance prerogatives (see letter g above) that have characterised it since its establishment, as well as additionally providing for the following:

- that it expresses an opinion on those proposed for election, revocation or assigning of duties to the internal control provost and the manager proposed as the manager responsible for the preparation of company accounting reports;
- in case of the substitution of an independent Director, it shall propose a candidate to the Board of Directors for co-optation;
- that it defines the methods and effective times of the Board of Directors annual evaluation.

The Committee – which, as it has in the past, may also request the assistance of external consultants to fulfil its role – normally meets before the Board of Directors meetings are called for approval of the draft annual financial statements, the half-yearly report and the quarterly reports; it also meets whenever its chairman deems it appropriate or a meeting has been requested by another member of the committee or by a Managing Director.

The members of the Board of Statutory Auditors, the head of the Internal Control Committee and if deemed necessary other company representatives may participate in the meetings of the committee.

In line with best practices and in full compliance with the recommendations in the new Code of Conduct for listed companies, the Committee is exclusively composed of the following independent Directors: Carlo Secchi (Chairman), Carlo Angelici and Franco Bruni, two of which⁷, as ascertained by the Board of Directors convened on March 12th, 2007, possess adequate accounting and financial experience.

During 2006, the Committee for Internal Control and Corporate Governance met seven times and all members participated in these meetings.

The Committee actively contributed to the implementation process and the updating of Company corporate governance instruments. Specifically, following the addition of market abuse regulations in national law (EU Law 2004), the issuing of the Savings Law, the Corrective Decree and the new

⁷ Mr Bruni and Mr Secchi.

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Code of Conduct, the Committee for Internal Control and Corporate Governance in 2006 – availing itself of support from various Company departments – contributed to the defining of a procedure for the management and the market communication of sensitive information. Moreover, in 2007 it had already approved the interventions necessary regarding alignment with the new Code of Conduct (as cited throughout this Report), as well as drafting a procedure regarding information flows to Directors and Auditors, besides formulating proposals for modifications to the Company bylaws and shareholders' meeting regulations, which will be put forth at the Meeting called to examine the 2006 financial statements.

Also during 2006, the internal control provost of the Company (who is the head of the Internal Auditing Department) was able to refer his actions to the Committee for Internal Control and Corporate Governance through the submission of four reports. The Committee also monitored the activities carried out by the Internal Auditing Department of the Company, specifically examining the result of activities regarding the 2006 Audit Plan and approving the Audit Plan for the financial year 2007.

The Committee was also constantly informed on the auditing activities of the “231 organisational model” and the implementation of the “262 Project” (described below in paragraph 4) and, with the representatives of PricewaterhouseCoopers, verified the auditing activities plan.

Lastly, it was felt opportune to give an account of the development of the actions, legal and otherwise, that involved two ex-heads of Company Security that were subject to an investigation by the Committee for Internal Control and Corporate Governance, along with the Board of Statutory Auditors.

Specifically, during the meeting held on July 20th, 2006, the Committee analysed the affair that involved an ex-Manager of the Company, Giuliano Tavaroli – who up until a few years earlier had been the head of the Security Department – in a criminal proceedings case for conspiring to violate professional discretion. At this meeting, the Committee was informed of the verification activities carried out by the Company with the assistance of legal consultants, as well as the conduct taken in order to ensure a maximum level of collaboration and transparency of the Company regarding the court of jurisdiction, which – in June 2006 – had deposited a memorandum at the public prosecutor's office in Milan (an additional memorandum was thereafter deposited with the national prosecutor's office on December 6th, 2006).

During a meeting on September 8th, 2006, the Committee received notice of the outcome of the intrinsic verifications to the passive cycle of the security activities made during the April-May 2006 period by the Internal Auditing Department of the Company. This intervention allowed to the identification of some areas of improvement for which corrective actions were held necessary (i.e. the complete involvement of the Purchasing Division in security services procurement; the creation of a suppliers' registry listing only those who satisfy certain requirements regarding quality, financial reliability and trustworthiness; the establishment of adequate authorisation levels regarding security service purchase flows; the adoption of additional control measures that guarantee complete traceability for each phase of the purchasing process and the monitoring of the costs of the Security Department).

Subsequently, in October 2006, the Committee – with the assistance of legal consultants that aided the Company on this theme – investigated further developments that took place regarding the legal process following the injunction issued on September 20th, 2006 by the Preliminary Investigations at the Court of Milan (which became public domain following the full publication of this provision on the web site www.ilvelino.it) which remanded in custody Giuliano Tavaroli, as well as Pierguido Iezzi (along with others) who at that moment held the role of head of Pirelli & C.'s Security Division. The individuals mentioned above were charged with (i) conspiracy to commit crimes aimed at corrupting public officials, using data retrieved from unlawful use of their access to IT systems and embezzlement of Pirelli Group and Telecom Italian funds, (ii) several counts of embezzlement, (iii) corruption of a public official, and (iv) unlawful divulcation of sensitive and reserved information. The Committee specifically examined the position of Pierguido Iezzi since, up until the date of the injunction, no reasons existed that would lead one to believe or even presume that this individual

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could have been implicated in the affair and, following the application of precautionary measures, he was suspended from his position as head of Security.

Regarding the injunction, the legal consultants of the Company noted that (considering the significant level of transparency and collaboration shown by the Company, among other reasons) the order qualified Pirelli as an offended party and therefore subject to damages that occurred due to the felonies and – as of now – excludes the same from the application of the provisions in legislative decree no. 231/2001 on the administrative responsibility of companies, on the premises (i) that Company Top Management was unaware of the felonies, and (ii) according to the fact that the felonies were committed against, and not in favour, and not even in the interests of the Company.

Lastly, the Committee inquired as to the need for corrective actions regarding the internal control system, and acknowledged that the improvements made based on suggestions from an internal audit on Security functions (which, as mentioned, had already taken place during April and May 2006 based on an independent decision of the Company) constituted an adequate solution, despite having examined and promoted possible refinements to the system at subsequent meetings.

Lastly, during a meeting held on November 6th, the Committee – again discussing the matter – mandated the Internal Audit Department of the Company to launch the collection of data on the security service performance required by various company functions during the past few years through the initiation of a specific data requirements memo sent to all "front line" Company members. In tandem, the Internal Audit Department was also given the task of requiring employees in the Security division of companies in the Pirelli Group to declare if they had or had not kept copies of files or documents regarding duties assigned to this Department during the January 2000 – June 2006 period. From initial reports of the verifications made until now – which were still being made during the preparation of this report – no particular critical findings had come to light.

Finally, it should be noted that the Company has launched a civil lawsuit against the security service suppliers involved in the investigations, in order to be compensated for services that were not contractually fulfilled or were even illegal.

The Committee for Internal Control and Corporate Governance and the Board of Directors, taking into account the comments of the Board of Statutory Auditors, judged the internal control system of the Company and of its underlying Group to be adequate.

2.3 Elections Committee

The Board of Directors has decided not to establish an election committee charged with putting forward proposals for the position of Director, since at present the conditions envisaged by the Code for its establishment do not exist, because of the current ownership structure and, above all, the By-laws provision for the slate system, in view of the transparency this mechanism ensures in the selection of candidates.

The Board has made the same conclusions also in accordance of provisions in the new Code of Conduct.

In fact, since the Board considers the reasons mentioned above still valid, it has not felt that the constitution of a specific elections committee is necessary. Moreover, it has given the Committee for Internal Control and Corporate Governance the power to identify candidates to propose to the Board in the event that an independent Director is to be co-opted.

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3. Disclosure of sensitive information and insider dealing

3.1 Internal management and disclosure of documents and information

Market transparency, clarity, correctness and integrity of information are the values that are upheld by the conduct of the corporate bodies, the management and all the employees of the Pirelli Group. In March 2006, the Board of Directors of the Company adopted a specific procedure for the management and market communication of sensitive information that, keeping account of the regulations regarding market abuse, governs the management of sensitive information connected to Pirelli & C., its unlisted subsidiaries and the listed financial instruments of the Group, and as such all the members of corporate bodies such as the employees and collaborators of companies external to the Group that may have access to information that could evolve into sensitive information. This procedure also applies as instructions to all subsidiaries in order to obtain from them, without hesitation, the necessary information for the timely and proper fulfilment of financial reporting obligations.

This procedure also governs the registration (operative as of April 1st, 2006) of persons having access to privileged information.

The adoption of the new procedure is the most evident result of the work done by the working group set up by the Company to assess the consequences of the national regulation (EU Law 2004) implementing the Community Directive on Market Abuse

Both the Committee for Internal Control and Corporate Governance and the Board of Statutory Auditors were regularly updated on the activity of the working group and agreed with its results.

The text of the procedure may be consulted at www.pirelli.com, under the section entitled "Governance".

3.2 Insider dealing

Matters regarding the transparency of transactions on Company shares or financial instruments underlying or linked to shares made directly or by third parties for relevant persons or by persons closely related or linked to them (i.e. insider dealing) are currently fully governed by law and by regulations established by Consob (art. 114 of the Financial Services Act and art. 152-sexies and following amendments of the Issuer's Regulation), as of April 1st, 2006 over-riding the Code of Conduct of the Company regarding insider dealing, adopted as from December 2002.

Pursuant to the law, directors and statutory auditors of the Company, as well as "persons who carry out administrative [...] functions in a listed company and managers that have regular access to sensitive information [...] and have the power to make management decisions that could affect the performance and the future prospects of a listed company..." and others are obliged to disclose to the market any insider dealing transactions made on Company shares or financial instruments linked to these shares having a value of more than Euros 5,000 annually. The Company opted to identify these managers as its General Managers, and – as an example of self-regulation – as the Managing Director and General Manager of Pirelli Tyre S.p.A. (who, until June 30th, 2006, was the Managing Director of the Company). Similarly, disclosure obligations also involve Pirelli & C. Real Estate S.p.A., a company that is also listed on a regulated market.

Within the more general auditing process for the corporate governance instruments, despite being not obliged by law, the Board of Directors decided to institute a black out period for the persons mentioned above who must adhere to insider dealing regulations; they shall therefore abstain from making transactions on Company shares or on financial instruments linked to these shares. These periods may moreover be extended or suspended by the Board of Directors in exceptional cases.

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4. Internal Control

The internal control system of Pirelli & C. and the Group it heads is designed to ensure the provision of correct information and adequate cover of all the activities of the Group, with special reference to those areas that are considered to be potentially at risk

It has developed as a process intended to achieve substantial and procedural fairness, transparency and accountability by ensuring that transactions and, more generally, business related activities are efficient and can be known and verified, that financial information and accounting and operational data are accurate, that applicable laws and regulations are complied with, and that the assets of the business are safeguarded, not least with a view to prevent the perpetration of fraud against the Company and financial markets.

The cardinal rules of the internal control system of the Company are:

- i. separation of roles in the performance of the principal activities involved in each operating process;
- ii. traceability and constant visibility of decisions;
- iii. management of decision-making processes according to objective criteria.

Responsibility for the internal control system lies with the Board of Directors, which lays down the guidelines for the system and periodically verifies that it is adequate and working effectively. To this end, the Board refers to the Committee for Internal Control and Corporate Governance, as well as to a Provost, who is given an adequate level of independence and appropriate means in order to carry out this mandate, and who carries out typical audit functions to verify the adequacy and efficiency of this system; and, if anomalies are detected, who proposes the necessary corrective solutions.

A specifically nominated Director (currently the Chairman of the Board of Directors) has the mandate of identifying the main company risks that must periodically be examined by the Board and the execution of the policy lines defined by said Board, seeing to the planning, realisation and management of the internal control system, constantly verifying its overall adequacy, efficiency and adaptation to the changes in business conditions and legislation and regulation frameworks.

The internal control Provost – that the Board of Directors, with the approval of the Committee for Internal Control and Corporate Governance and in accordance with best practice, has identified as the head of the Internal Audit Department, also deciding his/her remuneration – is functionally responsible to the Committee for Internal Control and Corporate Governance and the Board of Statutory Auditors and hierarchically responsible to the Chairman of Pirelli & C. S.p.A..

The Internal Audit Department has a significantly important role in the internal control system and, also for activities performed regarding subsidiaries, it has the principal task of assessing the adequacy and functionality of control, risk management and corporate-governance processes throughout the entire Group by means of autonomous assurance and consultancy. The work of the Internal Audit Department is carried out in accordance with its mandate and is shared with the Committee for Internal Control and Corporate Governance, regarding the following aspects:

- mission;
- objectives and responsibilities (independence, complete access to information, activity framework, communication of results);
- improvement in the quality of internal audits;
- principles of professional ethics;
- professional reference standards.

The Company also has in place a planning and control system that focuses on individual sectors and operating units and produces a detailed monthly report for the General Managers, so that they have a useful tool with which to monitor specific activities.

In order to favour compliance with the strategies and guidelines adopted by the parent company, the relevant General Managers and senior executives sit on the Boards of Directors of the largest subsidiaries.

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Also regarding internal control, please note that – in order to comply with provisions in art. 154-bis of the Financial Services Act (as amended by the Savings Law, and more recently, by the Corrective Decree), which does not apply regarding financial statements for 2006 – the Company initiated a project (named “Project 262”), guided by a specific steering committee, with the objective of making a system of controls for administrative and accounting procedures available to the administrative boards and the managers involved in the preparation of corporate accounts for the preparation and the validation of periodic accounting reports, which allow these individuals to make the declarations regarding them as required by law. Please also note that the role of “manager responsible for the preparation of company accounting reports” will be introduced into the bylaws by the shareholders at the meeting called to approve the 2006 financial statements. Regarding the detailed report that will be published for this meeting, please note that the professional requirements of this new role will be set in the bylaws (i.e. administrative, financial and control experience); the person occupying this position will be nominated (and revoked) by the Board of Directors, subject to approval of the Board of Statutory Auditors, and the Board of Directors will also set the powers and duties for this role.

The internal control system described above has been further strengthened by the introduction of an organizational model that the Board of Directors approved on July 31st, 2003 and which was revised and modified according to updated regulations by a resolution of the Board of Directors on March 12th, 2007. Intended to ensure the creation of a system responding to the specific requirements deriving from the entry into force of Legislative Decree 231/2001, on the administrative liability of companies for criminal offences committed by their employees, the model consists of a set of principles and procedures arranged in a pyramid that, starting from the base, can be summarized as follows:

- **Group Code of Ethics**, which formulates the general principles (transparency, correctness and fairness) inspiring the conduct of business. It indicates the objectives and the values informing business activity in relation to the main stakeholders with which Pirelli & C. S.p.A. interacts on a daily basis: the shareholders, the financial market, customers, staff and the community.
- **General principles of internal control**, which qualify the Internal Control System and the field of application, and which extend uniformly across the various organizational levels;
- **Lines of conduct**, which set out specific rules aiming to avoid the creation of environmental situations that favour criminal activity in general, and in particular, crimes covered under legislative decree no. 231/2001, and translate the principles established by the Group Code of Ethics into operational terms.
- **Internal control checklists**, which set out the main phases of each high and medium risk process and of the instrumental processes, the specific checks to be performed with a view to reasonably anticipating the risks of any criminal offence, and specify the reports to be transmitted to the Self-Regulatory Body to draw the attention to situations of possible non-compliance with the procedures established in the organizational model.

A specific Self-Regulatory Body monitors the functioning of and the adherence to the organisational model. It is composed of Carlo Secchi, the Lead Independent Director and Chairman of the Committee for Internal Control and Corporate Governance, Paolo Francesco Lazzati, a member of the Board of Statutory Auditors, and Maurizio Bonzi, head of the Internal Audit Department and Provost of internal control. It is also ensured full independence from this Body, as well as having many expert professionals that contribute to corporate management control.

The Self-Regulatory Body is in charged of making recommendations to the Board of Directors for it to adapt the organizational model to changes in the legal framework, the nature of the business activities of the Company and the ways they are conducted. It reports to the Board of Directors, the Committee for Internal Control and Corporate Governance and the Board of Statutory Auditors on the checks performed and their results.

The shareholders' meeting of April 28th, 2005 fixed the annual gross fee payable to each member of the Self-Regulatory Body at Euros 10,000.

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With reference to unlisted Italian Group companies, the Self-Regulatory Body has been adapted by adopting the technical and operational solution that, while respecting the mandate and the powers reserved to the body by law, is appropriate to the size and organizational context of each company. A disciplinary system has been introduced to sanction non-compliance with the measures indicated in the organizational, operational and control systems.

Finally, it should be pointed out that the Internal Audit Department of Pirelli & C. provides, when requested by the self-regulatory bodies of Group companies, operative assistance in the management and analysis of information flows established pursuant to Art. 6, paragraph 2, letter d), of Legislative Decree 231/2001, as well as in implementation of specific audits on the basis of data received through the aforementioned information flows.

During the second half of the year, the Self-Regulatory Body became involved in the court case that implicated two ex-heads of the Security Department of the Company, as detailed more extensively in paragraph 2.2 above. The Self-Regulatory Body acknowledged that the injunction issued on September 20th, 2006 for the Preliminary Investigations of the Court of Milan (which, as stated, became public domain following the full publication of this provision on the web site www.ilvelino.it) which remanded in custody Giuliano Tavaroli, as well as Pierguido Iezzi who at that moment held the role of head of Pirelli's Security Division, qualified Pirelli as an offended party and therefore subject to damages that occurred due to the felonies committed and – in the current state – excludes it from the application of the provisions in legislative decree no. 231/2001 on the administrative responsibility of companies, on the premises (i) that Company Upper Management was unaware of the felonies, and (ii) according to the fact that the felonies were committed against, and not in favour, and not even in the interests of the Company.

As mentioned, the Board of Directors and the Committee for Internal Control and Corporate Governance believe that the internal control system of the Company and of the Group is adequate, following evaluations made based on indications received from the Board of Statutory Auditors and other information.

5. Relations with institutional investors and other shareholders

In line with its tradition of transparency and fairness, the Company actively promotes relations with shareholders, institutional and private investors and with financial analysts, with other market operators and with the financial community in general within the proper limits of their respective roles, and periodically organizes meetings with representatives from the Italian and international financial communities.

In March 1999, the Company established an Investor Relations Department to foster continuous dialogue with the financial market. The Investor Relations Department, which reports directly to Finance and Strategic Planning Managing Director Carlo Buora, is headed by Alberto Borgia and has its own section in the website of the Company at www.pirelli.com.

In this section of the website, investors can find every document of interest published by the Company, in English as well as in Italian, related to financial reporting (e.g., the annual financial statements and the half-yearly and quarterly reports) and the corporate governance system of the Company (e.g., the bylaws, the regulations for Shareholder meetings, the Rules of conduct for transactions with related parties, the procedure for information flows to Directors and Auditors, the procedure for the management and communication to the public of privileged information and the minutes of Shareholders' Meetings). The section also gives access to press releases distributed by the Company and the documentation that the Company makes available to the financial community in presentations and/or meetings and information on the share capital of the Company and shareholders (including the publication of shareholders' agreements).

Pirelli & C. was one of the first companies in Italy and Europe to publish specific inserts giving

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economic and financial data in the mass media, as well as one of the first to set up a kit on its website for small investors.

Investor queries may be sent to: e-mail: ir@pirelli.com; tel.: +39 02 64422949; fax: +39 02 64424686.

6. Shareholders' Meetings

It is the constant policy of the Company to use Shareholders' Meetings to communicate information on the Company and its prospects to the shareholders. Obviously, it does this in accordance with the rules governing confidential information and, where necessary, simultaneously communicates the same information to the market.

The Company carefully considers the choice of the place, date and time for convening Shareholders' Meetings, to facilitate the participation of the shareholders. All the Directors and all the members of the Board of Statutory Auditors make every possible effort to attend the meetings, especially those Directors whose positions permit them to make an important contribution to the discussion.

Moreover, in coherence with the bylaws that facilitates corporate involvement by minimising costs and charges, during 2005 article 7 (Shareholders' Meetings) in the Company Bylaws was modified to allow intervention in Shareholders' Meetings through the notice of intention, without the party concerned needing to produce any certification.

At the Meeting held on April 21st, 2006, in addition to approving the 2005 financial statements, shareholders deliberated to renew the mandate of the Board of Statutory Auditors (as detailed below) and authorised the purchase and alienation of ordinary and/or savings Company shares, within legal limits, for a period of 18 months.

7. Auditors

The Company bylaws provide that the Board of Statutory Auditors consists in three Standing Auditors and two Alternate Auditors. In order to allow minority shareholders to elect one Standing Auditor and one Alternate, Article 16 of the bylaws provides for use of the slate system, with one Standing Auditor and one Alternate elected from the slate that obtains the second largest number of votes (the minority slate). The other two Standing Auditors and the other Alternate are elected from the slate that obtains the largest number of votes (the majority slate). Shareholders who, alone or together with others, hold at least 2 per cent of the share capital entitled to vote at the ordinary shareholders' meeting, may present slates, subject to their proving ownership of the necessary number of shares not later than two days before the date set for the shareholders' meeting at the first call. Each shareholder may present or participate in the presentation of only one slate.

The slates, signed by the persons who present them, shall be deposited at the registered office of the Company at least ten days before the date set for the shareholders' meeting at the first call and made available to anyone who requests a copy. The slates must be accompanied by a professional curriculum vitae for each candidate and declarations in which the candidates individually accept their candidacy and attest, on their own responsibility, that there are no grounds for ineligibility or incompatibility, and that they meet the requirements prescribed by law and the bylaws.

Slates presented in violation of the above rule are considered null.

Subject to ineligibility, each candidate may only appear on one slate.

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

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

Additionally, according to the Company bylaws, the chairmanship of the Board of Statutory Auditors is to be given to the statutory auditor at the top of the slate which obtains the largest number of votes.

This clause – as detailed below – was not applied at the renewal of the mandate of the Board of Statutory Auditors resolved by the Shareholders' Meeting on April 21st, 2006, in that it went against the provision in art. 148 of the Financial Services Act as amended by the Savings Law, which stipulates the election of the Chairman from amongst the minority members.

In the event of death, resignation or disqualification of a Standing auditor, he (or she) is replaced by the alternate director elected on the same slate. If the Chairman of the Board of Statutory Auditors is replaced, the other Standing Auditor elected on the same slate takes the Chair (see the note at the end of this paragraph); if it is not possible to proceed in the manner described above, a shareholders' meeting is called to fill the vacancy or vacancies by means of a resolution approved by a relative majority of the votes cast.

When the shareholders' meeting has to appoint Standing Auditors and/or Alternates to bring the board up to full complement as provided for above or in conformity with the applicable law, it proceeds as follows: if statutory auditors elected from the majority slate are to be replaced, the appointment is made with the favourable votes of a relative majority without being tied to a slate; if, instead, statutory auditors elected from the minority slate are to be replaced, the shareholders' meeting replaces them with the favourable votes of a relative majority, choosing where possible from among the candidates on the slate from which the statutory auditor to be replaced was elected

In appointing statutory auditors who, for any reason, are not appointed following the procedure specified above, the shareholders' meeting votes according to the majorities required by law.

Statutory auditors whose term of office has expired may be re-elected.

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

The Board of Statutory Auditors instated until April 21st, 2006 was composed of Standing Auditors Luigi Guatri (Chairman), Roberto Bracchetti and Paolo Francesco Lazzati.

Franco Ghiringhelli and Sebastiano Guido were both Alternate Auditors

The Shareholders' Meeting held on April 21st, 2006 resolved to renew this Board for the 2006-2008 period, nominating Luigi Guatri, Enrico Laghi and Paolo Francesco Lazzati as Standing Auditors.

Luigi Guerra and Franco Ghiringhelli were appointed Alternate Auditors.

The election took place through a slate vote. The members of the Pirelli & C. block shares syndicate presented the sole slate. The level of authority and the reputation of the candidates proposed on this list are believed by the Company to be a possible reason why no other alternative slate was presented by the minority shareholders.

Lacking any Auditors on the Statutory Board chosen from the minority slate, the Shareholders resolved to confirm Luigi Guatri as Chairman of this Board.

The Shareholders also resolved that Euros 41,500 be the gross annual remuneration for each of the Standing Auditors, and Euros 62,000 be the gross annual remuneration for the Chairman of the Board of Statutory Auditors, also resolving that to the Auditor that is appointed to the Self-Regulatory Body as per legislative decree no. 231/2001 (Paolo Francesco Lazzati) is granted an additional gross annual remuneration of Euros 10,000.

During 2006, the Board of Statutory Auditors held 4 meetings prior to April 21st, 2006 and another 4 following that date. All members of this Board took part in these meetings except for one absence in two meetings; please also note that the members of this Board also attended the Shareholders' Meetings and the meetings of the Board of Directors of the Company and all seven of the meetings that were held during the year for the Committee for Internal Control and Corporate Governance, and all four of the Remuneration Committee meetings, as required by the corporate governance rules adopted by the Company, which offer the Board of Statutory Auditors

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the full possibility of directly following the activities of the Committees and performing the control functions of their role with greater efficiency.

In line with provisions in the new Code of Conduct (art. 10) and as expressly ascertained by the Board of Statutory Auditors, all Auditors may be defined as independent based on criteria contained in the new Code of Conduct regarding directors.

In order to conform the Company Bylaws' provisions relevant to the appointment of the Board of Statutory Auditors to the new regulations introduced in the Financial Services Act by the Savings Law and the Corrective Decree, as well as to the provisions of the new Code of Conduct, the Board of Directors held on March 12th, 2007 resolved to propose at the Shareholders' Meeting some amendments to the Bylaws, i.e.: (i) to eliminate the clause which limits the total number of offices a Board member may hold (ii) to amend the clause relevant to the election system of the Chairman of the Board of Statutory Auditors, (iii) to increase the period within which slates may be presented to 15 days, (iv) to align the percentage of corporate shareholdings required to present slates to the percentage required in the nomination of the Board of Directors, and (v) to require in any case that each candidate declare all offices held in management and supervisory bodies held in the past, filing such a list at the registered office together with their curriculum vitae.

The following tables summarise all the methods by which the main recommendations of the new Code of Conduct were adopted by the Company:

- Structure of the Board of Directors, the Remuneration Committee and the Committee for Internal Control and Corporate Governance
- Structure of the Board of Statutory Auditors
- Other provisions in the Code
- Offices held in management and supervisory bodies by members of the Board of Directors and the Board of Statutory Auditors in other listed companies, in financial companies, banks, insurance companies, or in other companies of significant size.

Table 1

STRUCTURE OF THE BOARD OF DIRECTORS AND THE BOARD COMMITTEES							Committee for Internal Control		Remuneration Committee	
Board of Directors ⁽¹⁾							***	****	***	****
Position	Name	executive	non-executive	independent ⁽²⁾	****	Number of other positions **				
Chairman	Marco Tronchetti Provera	X			100%	6				
Deputy Chairman	Alberto Pirelli	X			100%	6				
Deputy Chairman	Carlo Alessandro Puri Negri	X			90%	11				
Director	Carlo Acutis		X	X	60%	10				
Director	Carlo Angelici (*)		X	X	90%	1	X	100%		
Director	Gilberto Benetton		X		60%	11				
Director	Alberto Bombassei		X	X	-	3				
Director	Franco Bruni (*)		X	X	90%	3	X	100%		
Director	Gabriele Galateri di Genola		X		90%	11				
Director	Mario Garraffo (*)		X	X	90%	2				
Director	Dino Piero Giarda		X	X	50%	2				
Director	Berardino Libonati		X	X	100%	6			X	100%
Director	Giulia Maria Ligresti		X		80%	11				
Director	Massimo Moratti		X		30%	6				
Director	Giovanni Perissinotto		X		40%	13				
Director	Giampiero Pesenti		X	X	70%	12			X	75%
Director	Aldo Roveri (*)		X	X	100%	-			X	100%
Director	Carlo Secchi		X	X	100%	4	X	100%		
Director	Paolo Vagnone		X		60%	3				
Managing Director	Carlo Buora ⁽¹⁾	X			89%	-				
Director	Carlo De Benedetti ⁽¹⁾		X	X	67%	-				
Number of meetings held during the year		Board of Directors:			Committee for Internal Control:		Remuneration Committee:			
(the data refer to the entire financial period):		10			7		4			

LEGEND

* Indicates that the director was elected from a slate presented by a minority shareholders (quorum required: 2% of voting stock).

** The positions held on the Board of Directors or Statutory Auditors of other companies listed on Italian and foreign regulated markets, of financial banking and insurance companies, and of other large companies are shown in detail in the Report on Corporate Governance.

*** The "X" in one of these columns indicates membership in the relevant Board Committees.

**** Indicates the attendance of directors at the meetings of the Board of Directors and the Board Committees.

(1) Changes occurred during the 2006 fiscal year: (i) Mr. Carlo De Benedetti has held the position of director until May 5th, 2006, (ii) Mr. Alberto Bombassei has held the position of director as from September 12th, 2006, and (iii) Mr. Carlo Buora has held the position of director until November 6th, 2006.

(2) All the directors eligible for the independent requirement provided by the new Self-Regulatory Code have further declared to be eligible for the independence requirement requested by the article 147-ter, comma 4 of d. Lgs. 58/1998.

Table 2

BOARD OF STATUTORY AUDITORS			
Position	Name	Attendance at Board meetings	Number of other appointments**
Chairman	Luigi Guatri	87,50%	16
Auditor	Enrico Laghi	75%	19
Auditor	Paolo Francesco Lazzati	100%	23

Number of meetings held during the relevant fiscal year: 8 (of which 4 before April 21, 2006)

Quorum required for the presentation of slate by minority shareholders for the election of one or more auditors: 2%

LEGEND

* Indicates that the director was elected from a slate presented by minority shareholders (quorum required: 2% of voting stock).

** Indicates the number of the main appointments of statutory auditors or director of other companies, including those held in the Pirelli Group. In the Report on Corporate Governance, these appointments are shown in detailed.

(1) The information of the chart refer to the Board of Statutory Auditors appointed on April 21st, 2006. The prior Board of Statutory Auditors was composed as follows: Luigi Guatri (Chairman), Roberto Bracchetti and Paolo Francesco Lazzati (Acting Auditors), Franco Ghiringhelli and Sebastiano Guido (Alternate Auditors). Prior to April 21st, 2006, 4 meetings of the Board of Statutory Auditors were held with an aggregate attendance rate of approximately 92%. The information of the chart relating to the attendance of the Professor Luigi Guatri and Mr. Paolo Francesco Lazzati also take into account the meetings held prior to April 21st, 2006.

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Table 3

OTHER PROVISIONS OF THE SELF-REGULATORY CODE			
	YES	NO	Summary reasons for divergence from the recommendations of the Code
Delegated powers and transactions with related parties			
The Board of Directors has delegated powers and established:			
a) the limits to such powers?	X		
b) the manner of exercising them?	X		
c) the frequency of reports?	X		
Has the Board reserved the right to examine and approve transactions having a significant impact on the profitability, the assets and the liabilities or financial position of the Company (including transactions with related parties)?			
	X		
Has the Board established guidelines for identifying "significant" transactions?			
	X		
Are the above guidelines described in the report?			
	X		
Has the Board established special procedures for examining and approving transaction with related parties?			
	X		
Are the procedures for approving transaction with related parties described in the report?			
	X		
Procedures used for the most recent appointments of the Board of Directors and the Board of Auditors			
Were the nominations to the board of directors filed at least ten days in advance?			
	X		
Were the nominations to the board of directors accompanied by detailed information?			
	X		
Were the nominations to the board of directors accompanied by an indication as to whether they qualified as independent?			
	X		
Were the nominations to the board of statutory auditors filed at least ten days in advance?			
	X		
Were the nominations to the board of statutory auditors accompanied by detailed information?			
	X		
Shareholders' meetings			
Has the Company approved rules of proceeding for shareholders' meetings?			
	X		
Are these rules included in the report (or does the report indicate where they can be obtained/downloaded)?			
	X		
Internal control			
Has the Company appointed the persons responsible for internal control?			
	X		
Are such persons hierarchically independent from the heads of the operating units?			
	X		
Unit responsible for internal control (ex Art. 9.3 of the Code)			
	X		
Investor relations			
Has the Company appointed a person to be responsible for investor relations?			
	X		
Unit and contact details of the person responsible for investor relations.			
	X ¹		

¹ Investor Relations Department (directly under General Manager Finance and Strategic Planning), headed by Alberto Borgia; Contact details: e-mail ir@pirelli.com; tel.: +39.02.64422949; fax: +39.02.64424686.

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Posts of Director or Statutory Auditor held by members of the Board of Directors or members of the Board of Statutory Auditors in other listed companies, in financial companies, banks, insurance companies or companies of significant size

Marco Tronchetti Provera	Camfin S.p.A.	Chairman
	Gruppo Partecipazioni Industriali S.p.A.	Chairman
	Olimpia S.p.A.	Chairman
	Pirelli & C. Real Estate S.p.A.	Chairman
	Pirelli Tyre S.p.A.	Chairman
	Marco Tronchetti Provera & C. S.p.a.	Member of the Board of Managing Partners
Alberto Pirelli	FIN.AP di Alberto Pirelli & C. A.p.A.	Chairman
	Gruppo Partecipazioni Industriali S.p.A.	Deputy Chairman
	Camfin S.p.A.	Director
	GIM S.p.A.	Director
	KME S.p.A.	Director
	Pirelli Tyre S.p.A.	Director
Carlo Alessandro Puri Negri	Pirelli & C. Real Estate Franchising Holding S.r.l.	Chairman
	Pirelli & C. Real Estate Opportunities Società di	Chairman
	Gestione del Risparmio S.p.A.	
	Pirelli & C. Real Estate Società di Gestione del	Chairman
	Risparmio S.p.A.	
	Camfin S.p.A.	Deputy Chairman
	Pirelli & C. Real Estate S.p.A.	Deputy Chairman and Managing Director
	Gruppo Partecipazioni Industriali S.p.A.	Managing Director
	Aon Italia S.p.A.	Director
	Eurostazioni S.p.A.	Director
	Olimpia S.p.A.	Director
	Pirelli Tyre S.p.A.	Director
	Telecom Italia S.p.A.	Director
Carlo Acutis	BPC Investimenti SGR S.p.A.	Chairman
	Vittoria Capital N.V.	Chairman
	Banca Passadore & C. S.p.A.	Deputy Chairman
	Vittoria Assicurazioni S.p.A.	Deputy Chairman
	Camfin S.p.A.	Director
	Ergo Assicurazioni S.p.A.	Director
	Ergo Italia S.p.A.	Director
	Ergo Previdenza S.p.A.	Director
	IFT S.p.A.	Director
Yura International B.V.	Director	
Carlo Angelici	Stretto di Messina S.p.A.	Director
Gilberto Benetton	Autogrill S.p.A.	Chairman
	Edizione Holding S.p.A.	Chairman
	Ragione Sapa di G. Benetton e C.	Chairman
	Olimpia S.p.A.	Deputy Chairman
	Telecom Italia S.p.A.	Deputy Chairman
	Aldeasa S.A.	Director
	Autostrade S.p.A.	Director
	Benetton Group	Director
	Loyd Adriatico S.p.A.	Director
	Mediobanca S.p.A.	Director
Schemaventotto S.p.A.	Director	
Alberto Bombassei	Brembo S.p.A.	Chairman
	Autostrade S.p.A.	Director
	Italcementi S.p.A.	Director

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Franco Bruni	Pioneer Global Asset Management S.p.A.	Director
	Unicredito Banca Mobiliare S.p.A.	Director
	Unicredit Audit S.p.A.	Director
Gabriele Galateri di Genola	Mediobanca S.p.A.	Chairman
	Istituto Europeo di Oncologia S.r.l.	Chairman
	Assicurazioni Generali S.p.A.	Deputy Chairman
	RCS MediaGroup S.p.A.	Deputy Chairman
	Accor SA	Director
	Banca CRS S.p.A.	Director
	Banca Esperia S.p.A.	Director
	Fiera di Genova S.p.A.	Director
	Italmobiliare S.p.A.	Director
	San Faustin NV	Director
Commerzbank AG	Member of the Central Advisory Board	
Mario Garraffo	Recordati S.p.A.	Director
	Terna S.p.A.	Director
Dino Piero Giarda	Banca Popolare Italiana S.p.A.	Chairman
	ACEA S.p.A.	Director
Berardino Libonati	Alitalia S.p.A.	Chairman
	Banca di Roma S.p.A.	Chairman
	Unidroit	Chairman
	Mediobanca S.p.A.	Director
	Nomisma S.p.A.	Director
RCS Mediagroup S.p.A.	Director	
Giulia Maria Ligresti	Fonsai MB&A S.p.A.	Chairman
	Premafin Finanziaria Holding di Partecipazioni S.p.A.	Chairman and Managing Director
	Fondiarria Sai S.p.A.	Deputy Chairman
	Sai Holding Italia S.p.A.	Managing Director
	Saifin S.p.A.	Managing Director
	Finadin S.p.A.	Director
	Milano Assicurazioni S.p.A.	Director
	Sailux S.A.	Director
	Sainternational S.A.	Director
	Telecom Italia Media S.p.A.	Director
Helm Finance SGR S.p.A.	Director	
Massimo Moratti	F.C. Internazionale Milano S.p.A.	Chairman
	Sarint S.A.	Chairman
	Angelo Moratti di Gian Marco e Massimo Moratti & C. S.a.p.a.	Member of the Board of Managing Partners
	Interbanca S.p.A.	Director
	Saras S.p.A. Raffinerie Sarde	Managing Director
Telecom Italia S.p.A.	Director	
Giovanni Perissinotto	Banca Generali S.p.A.	Chairman
	Generali Finances S.A.	Chairman
	Generali Investments S.p.A. SGR	Chairman
	Generali Property S.p.A.	Chairman
	Banca della Svizzera Italiana S.A.	Deputy Chairman
	Alleanza Assicurazioni S.p.A.	Director
	Generale Espana Holding de Entidades de Seguros	Director
	Generali France Holding	Director
	Generali Property Investments Sgr S.p.A.	Director
	Ina Assitalia S.p.A.	Director
	Toro Assicurazioni S.p.A.	Director
	Partecipatie Maatschappij Graafschap Holland N.V.	Director
	Intesa San Paolo S.p.A.	Member of the Management Board

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Giampiero Pesenti	Italcementi S.A.	Chairman
	Franco Tosi S.r.l.	Chairman
	Italmobiliare S.p.A.	Chairman and Managing Director
	Ciments Francais	Deputy Chairman
	Fincomind AG	Deputy Chairman
	Ciments de Maroc	Director
	Compagnie Monegasque de Banque	Director
	Credit Mobilier de Monaco	Director
	Finter Bank Zurich	Director
	Soparfinter S.A. Luxembourg	Director
Mittel S.p.A.	Director	
R.A.S. S.p.A.	Director	
Aldo Roveri	-	-
Carlo Secchi	Lloyd Adriatico S.p.A.	Director
	Mediaset S.p.A.	Director
	Parmalat S.p.A.	Director
	R.A.S. S.p.A.	Director
Paolo Vagnone	R.A.S. S.p.A.	Managing Director and General Managing
	Mol Holding S.p.A.	Director
	UniCredito Italiano	Director
Luigi Guatri	Banche Popolari Unite S.c.p.A.	Chairman Board of Statutory Auditors
	Centrobanca S.p.A.	Chairman Board of Statutory Auditors
	Italmobiliare S.p.A.	Chairman Board of Statutory Auditors
	Movi Lemar S.p.A.	Chairman Board of Statutory Auditors
	Movi S.p.A.	Chairman Board of Statutory Auditors
	Permasteelisa S.p.A.	Chairman Board of Statutory Auditors
	Rhifim S.p.A.	Chairman Board of Statutory Auditors
	Wimed S.p.A.	Chairman Board of Statutory Auditors
	Granitifandre S.p.A.	Chairman Board of Statutory Auditors
	Finanziaria 2000 S.p.A.	Chairman Board of Director
	Vittoria Assicurazioni S.p.A.	Chairman Board of Director
	Maffei S.p.A.	Director
	Negri Bossi S.p.A.	Director
	Banco di Desio e della Brianza S.p.A.	Director
	Medinvest Int. ScA	Member of Supervisory Board
	Acbgroup S.p.A.	Chairman of the Supervisory Board
Enrico Laghi	Alitalia Servizi S.p.A.	Chairman Board of Statutory Auditors
	Raffineria di Gela S.p.A.	Chairman Board of Statutory Auditors
	Sarda Bitumi - Sarbit S.p.A.	Chairman Board of Statutory Auditors
	Alitalia - Linee Aeree Italiane S.p.A.	Statutory Auditors
	01 Distribution S.r.l.	Statutory Auditors
	Gruppo Editoriale Espresso S.p.A.	Statutory Auditors
	Iridium S.p.A. - in liquidazione	Statutory Auditors
	Loquendo S.p.A.	Statutory Auditors
	Servizi Aerei S.p.A.	Statutory Auditors
	Rainet S.p.A.	Statutory Auditors
	TM News S.p.A.	Statutory Auditors
	IT Telecom S.r.l.	Statutory Auditors
	Manzano Sviluppo S.r.l.	Statutory Auditors
	Beni Stabili Investimenti SGR S.p.A.	Chairman Board of Director
	FdP Consulting S.r.l.	Sole Director
	Europrom 2000 S.r.l.	Sole Director
	Banca Finnat Euroamerica S.p.A.	Director
	Beni Stabili S.p.A.	Director
Nomura SIM Italia S.p.A.	Director	

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Procedure for information flows to directors and auditors

1. Introduction

1.1 – The completeness of the available information to directors is essential for the proper fulfilment of their duties and responsibilities regarding the management, the direction and the monitoring of the business activities of Pirelli & C. S.p.A. (henceforth “Pirelli” or “the Company”) and of the Group.

1.2 – Similar appropriate information is due to the Board of Statutory Auditors.

1.3 – In compliance with the legal and the bylaws’ provisions, non-executive Directors and Auditors are therefore the receivers of a permanent information flows from the Executive Directors, who are coordinated by the Chairman of the Board of Directors who, if necessary, can refer to the Secretary to the Board of Directors of the Company.

1.4 – The purpose of the current procedure is to regulate the above-mentioned information flows in order to:

- guarantee the transparency of the management of the Company;
- ensure good conditions for efficacious and effective actions of direction and monitoring of the Company activities and management by the Board of Directors;
- supply the Board of Statutory Auditors with the requisite tools for an efficient fulfilment of its role.

2. Terms and procedures

2.1 – The information flows to Directors and Auditors is preferably provided with written documents, specifically:

- notes, memoranda, presentations and reports drawn up by Company offices or consultants, including those prepared for Board of Directors meetings;
- other documents, published and un-published, available to the Company;
- documents of accounting period of the Company that are intended for publication;
- quarterly financial reports including external information, drawn up according to specific guidelines.

2.2 – The above-mentioned documentation is timeless transmitted to non-executive Directors and Auditors and, in any case:

- with a sufficient frequency in order to ensure that legal and bylaws data provisions are respected,
- according to coherent deadlines with the scheduling of the single Board of Directors meeting.

2.3 – The information reproduced according to the procedures above are integrated (or, if necessary, omitted for reasons of privacy) with the comments made orally by the Chairman, the Executive Directors or by members of the management of the Group during Board of Directors meetings or specific informal meetings, open to Directors’ or Auditors’ participation, and organized in order to go into topics about the management of the Company.

2.4 – The transmission of documents and any other material to Directors and Auditors is coordinated by the Secretary to the Board of Directors of the Company, in agreement with the manager in charge of the preparation of the accounting documents of the Company, as per his competence.

2.5 – In any case, Directors and Auditors are the receivers of the information published by Pirelli as provided by legal provisions regarding Company reports (such as press releases and reports) and investment solicitation (reports that are denominated, anyhow).

3. Contents

3.1 – The information flow to Directors and Auditors – besides matters intended for the examination and/or the approval of the Board of Directors of the Company according to the law and the bylaws of the Company – includes:

- the general results of operations and their foreseeable development;

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- the completed activity, with specific reference to transactions involving significant economic, financial and equity income, to transactions with related parties and to atypical or unusual transactions;
- the instructions given during the execution of direction and coordination activities;
- any further activities, transactions or events that are deemed appropriate to bring to the attention of Directors and Auditors.

4. General results and development of operations

- 4.1 – The corporate activities of the Group are the focus of background information about management.
- 4.2 – Information are considered in a strategic perspective of planning and direction, as well as in terms of the attainment of results and in comparison with industrial and budget forecasts.
- 4.3 – General results and development of operations are regularly examined by the Board of Directors of the Company when they approve the accounting period reports. The attained results are compared:
- with historic figures (opportunistically reconstructed using pro forma figures in order to obtain homogeneous comparisons with previous periods);
 - with budget objectives, indicating the causes of possible variances, also in order to evaluate the effects of these variances on strategic or anticipatory objectives and/or on forecasts regarding following periods;
 - with the general trend of the sector and peers, in order to benchmark.

5. Business activity

- 5.1 – General information about the completed business activity concern executive businesses and developments of operations already decided by the Board of Directors, as well as activities performed by Executive Directors – also through units and subsidiaries of the Company – in the exercise of their duties.
- 5.2 – General information about the business activities are completed with a specific report of details regarding:
- transactions involving significant economic, financial and equity income;
 - operations with related parties;
 - atypical or unusual transactions.

6. Significant transactions

- 6.1 – The following – besides operations reserved to the Board of Directors according to the art. 2381 of the Italian Civil Code and the bylaws of the Company – are considered transactions involving significant economic, financial and equity income when Pirelli or subsidiaries carry out:
- the issues of financial tools for a total value higher than Euros 100 million;
 - the granting of personal and collateral securities in the interest of subsidiary companies (and in the interest of Pirelli regarding collateral securities) against bonds having a unit value higher than Euros 25 million;
 - the granting of loans or securities in favour or in the interest of third parties for amounts higher than Euros 10 million;
 - the granting of loans in favour of subsidiary companies and the investment or disinvestment transactions, also real estate transactions, transactions for the purchase and the assignment of share, of company and company branches, of assets and other activity, for amounts higher than Euros 100 million;
 - merger and division transactions, when at least one of the parties is a listed company or when subsidiary companies are involved if at least one of the parameters indicated below, in case of application, come out equal or higher than 15% of:

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- the total assets of the merged company or of the activities submitted to division/the total assets of the Company (figures taken from the consolidated balance sheet, if reported);
- the pre-tax results and the extraordinary parts of the merged company, or of the activities to be divided/the pre-tax results and extraordinary parts of the Company (figures taken from consolidated balance sheet, if reported);
- the total equity capital of the merged company, or of the company branch submitted to division/the total equity capital of the Company (figures taken from consolidated balance sheet, if reported).

6.2 – Informative report on transactions involving significant economic, financial and equity income shall highlight the strategic aims, the budget and the industrial plan coherence, the executive procedures (including economic terms and conditions for their fulfilment), the business developments as well as the possible changes and implications for the activities of the Pirelli Group.

6.3 – Informative reports shall also be made for transactions that, even if they are individually smaller than the above-mentioned threshold value, are associated within the same strategic plan or executive programme and therefore, considered altogether, exceed the threshold value.

7. Operations with related parties

7.1 – The following definitions must be made regarding the current procedure relating to “related parties”; these are defined according to international accounting standards concerning financial statements for transactions with related parties, adopted in accordance with art. 6 of EC Regulation n. 1606/2002.

7.2 – The Company adopted this apposite procedure in order to ensure that the principle of fairness was respected in substance and form for all transactions made, directly or through subsidiaries, with related parties with Pirelli

7.3 – Besides the transactions with related parties subject to the board approval according to the above-mentioned procedure (atypical, unusual or non-standard transactions), transactions with related infra-Group parties (i.e. companies owned by Pirelli or by the company that owns Pirelli) must be similarly reported to Directors and Auditors if they involve amounts higher than Euros 50 million, and those with associated non infra-Group parties if they involve amounts higher than Euros 500.000. For each of these transactions, the following points must be indicated:

- object and amount;
- the date of targeting of the contract(s) below or those linked anyway with the transactions;
- the identities of the counterparties (specifying the nature of their relationship with Pirelli).

7.4 – As to every quarter of statement, an overall figure of the transactions concluded with the individual parties related to Pirelli must be supplied, separating the transactions directly carried out with Pirelli and the transactions achieved by subsidiary companies.

8. Atypical or unusual transactions

8.1 – Transactions that form part of the ordinary business of the Company are considered typical, i.e. essential to the production and the dealing cycle of the Company. On the contrary, transactions are considered usual when intended for the fulfilment of ordinary requirements, i.e. requirements that normally belong to the business of the Company.

8.2 – In any case, transactions may be called neither typical nor usual when they actually present particular elements of criticality due to their specific characteristics and/or to their intrinsic risks, to the nature of the counterparty or to the time of their fulfilment.

8.3 – Information about atypical or unusual transactions highlight the interest below and illustrate the executive procedures (including the economic terms and conditions of their fulfilment), with specific reference to the estimative procedures followed.

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9. Direction and coordination activities

9.1 – Information about the execution of direction and coordination activities illustrate:

- the strategic aims, with specific reference to the entrepreneurial interest justifying them and the results that are followed;
- the executive procedures (including the economic terms and conditions of their fulfilment), with specific reference to the estimative procedures followed;
- the possible changes and implications on the execution of the company, also with reference to the budget and the industrial plan.

9.2 – Further updating on the affected transactions shall be supplied in order to estimate overall results of the direction and the coordination activities.

Data collection procedure

In order to allow an adequate information flow to non-executive Directors and to the Board of Statutory Auditors, information must be obtained by the Chairman and CEOs according to the procedure listed below.

1. Information about business activities, about transactions involving significant economic, financial and equity income, about infra-group transactions and atypical or unusual transactions.

Pirelli General Managers and the Heads of Business units/Central Functions/Business Operations that report directly to the Chairman and the CEOs (the so-called “Front Line”) through the General Manager and Chief Operating Officer transmit, on a quarterly basis, to the Chairman and the CEOs, with an apposite note, the activities that the competent structure carried out in the period, highlighting specifically the transactions involving significant economic, financial and equity income; the infra-Group transactions higher than Euros 50 million; non-standard, atypical or unusual transactions; the executive businesses and developments of operations already decided by the Board of Directors; as well as the main business activities carried out within the duties attributed to Managing Directors, including the most important launched projects and the most significant undertaken initiatives.

Informative reports shall also be made for transactions that, even if they are individually smaller than the above-mentioned threshold value, are associated within the same strategic plan or executive programme and therefore, considered altogether, exceed the threshold value.

2. Information about operations with related parties different than intra-group transactions

The purpose of the current procedure are the transactions with related parties carried out by Pirelli or by companies owned by Pirelli, with parties directly or indirectly related to Pirelli.

- a) the persons who, directly or indirectly, control Pirelli, also in virtue of shareholder agreement, individually or jointly with other persons included in these agreements;
- b) the persons who, directly or indirectly, exercise a significant influence over Pirelli. This influence is presumed in case of shareholdings equal to or higher than 10% of the authorized capital in the form of ordinary Pirelli shares;
- c) the members of the Board of Directors and Acting Auditors of Pirelli;
- d) the managers with strategic responsibilities in the Company, identified by the Board of Directors of Pirelli, or in its possible subsidiaries (i.e. “key managers”);
- e) the immediate family members of the persons indicated in letters c) and d), i.e. spouses and dependents, as indicated in civic records;

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- f) the companies upon which the persons indicated above in letters a) to e) exert control, directly or indirectly, also in virtue of shareholders agreement, individually or jointly with other persons included in these agreements;
- g) the companies on which the persons indicated above in letters a) to e) exert significant influence, if they are physical persons. This influence is presumed in case of shareholdings equal to or higher than 10% (in the case of listed companies) or 20% (in the case of unlisted companies) of the authorized capital in the form of voting shares at the general meetings;
- h) the companies in which the persons indicated above in letters a) to e) hold strategic management roles and the companies controlled by these companies;
- i) the joint ventures in which Pirelli participates;
- j) the pension funds for the employees of Pirelli or of related parties;
- k) the companies that share a majority of their Directors with Pirelli.

With the same regularity as mentioned under point 1 above, General Operations Management collects and transmits to the Chairman and to the CEOs declarations from the persons mentioned under letters a) to d) above pointing out the transactions involving amounts higher than Euros 500.000, or those with lower amounts but non-standard, achieved directly by or through one of the persons indicated in letters f) to k) above, also through third parties, with Pirelli or its subsidiaries, by themselves or, in the case of physical persons, by spouses or dependents, as indicated in civic records.

Amongst these information, must be pointed out transactions that, even if they are individually smaller than the above-mentioned threshold value, are associated within the same relation and therefore, considered altogether, exceed the threshold value.

General Operations Management also collects the declarations whereby the persons in letters a) to d) above: (i) list the companies for which they perform the cases in letters f) to j) above, as well as companies in which they hold the role of directors; (ii) update this list.

General Operations Management transmits the list to the parties related to Pirelli as specified above to the General Managers and to the Front Line.

The Front Line communicates on a quarterly basis to the Chairman and the CEOs the transactions completed with Pirelli – or companies controlled by Pirelli – also through third parties or indirectly related parties as specified in the list given by the General Operations Management, involving amounts higher than Euros 500,000 and, also if involving lower amounts, made under non-standard conditions.

Rules of conduct for effecting transactions with related parties

1. Transactions with related parties, including intra-group transactions, except for typical or usual transactions concluded at arm's length conditions, must be approved in advance by the Board of Directors.
2. Typical or usual transactions shall be taken to mean those which, by their object or nature, are not extraneous to the normal course of business of the Company and those which do not involve particular critical factors due to their characteristics or to the risks related to the nature of the counterpart or to the time at which they are concluded. Transactions concluded at arm's length conditions means transactions concluded at the same conditions as those applied by the Company to whatsoever party.

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3. The Board of Directors shall receive adequate information on the nature of the relationship, the manner of execution of the transaction, the economic and other terms and conditions governing it, the valuation procedure adopted, the underlying interest and motivations, and the possible risks for the Company. Where the relationship is with a Director or with a party related by means of a Director, the Director concerned shall limit himself to providing clarifications and shall leave the meeting of the Board when the decision is to be taken; the Board of Directors may also resolve in a different way.
4. Depending on the nature, value and other characteristics of the transaction, to guard against the transaction's being carried out at unsuitable conditions the Board of Directors shall be assisted by one or more experts, who shall express an opinion, according to the case, on the economic conditions and/or the legitimacy and/or the technical aspects of the transaction.
5. For transactions with related parties, including intra-group transactions, which are not submitted to the Board of Directors inasmuch as they are typical or usual concluded at arm's length, the Directors having delegated powers or the managers responsible for carrying out the transaction, without detriment to compliance with the specific procedure pursuant to Article 150.1 of the Consolidated Law on Financial Intermediation, shall collect and preserve, inter alia by type or group of transaction, adequate information on the nature of the relationship, the manner of execution of the transaction, the economic and other terms and conditions governing it, the valuation procedure adopted, the underlying interest and motivations, and the possible risks for the Company. For such transactions also, one or more experts may be appointed as provided above.
6. The experts are to be chosen from among persons of recognized professional experience and competence in the matters concerned. Their independence and absence of conflicts of interest will be carefully evaluated.

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Abridged form of Pirelli & C. Società per Azioni Shareholders Agreement

1. Type and objective of the agreement

The purpose of the Pirelli & C. shareholders agreement is to ensure a stable shareholder base and a uniform strategy in the management of the company.

2. Parties to the shareholders agreement and Pirelli & C. shares transferred to the agreement:

	Number of Shares granted	% of all shares granted	% of the total n. of ordinary shares issued
CAMFIN S.p.A.	1,027,455,727	42.48	19.63
MEDIOBANCA S.p.A.	233,001,859	9.63	4.45
EDIZIONE HOLDING S.p.A.	232,992,911	9.63	4.45
FONDIARIA - SAI S.p.A.	223,543,498	9.24	4.27
RAS S.p.A.	222,958,537	9.22	4.26
ASSICURAZIONI GENERALI S.p.A. (*)	222,958,531	9.22	4.26
CAPITALIA PARTECIPAZIONI S.p.A.	81,665,400	3.38	1.56
INTESA SANPAOLO S.p.A.	81,665,400	3.38	1.56
Massimo MORATTI (**)	60,300,084	2.49	1.15
SINPAR HOLDING S.A. - SINPAR S.p.A. (***)	32,048,563	1.33	0.61
Total	2,418,590,510	100.00	46.20

(*) n. 57,400,000 shares through La Fédération Continentale Compagnie d'Assurances Sur La Vie S.A., n. 82,779,265 shares through Ina Vita S.p.A. and n. 82,779,266 shares through Generali Vita S.p.A.

(**) Including 37,420,339 shares through CMC S.p.A. and n. 11,328,318 shares fiduciary owned by Istifid S.p.A.

(***) n. 19,797,563 shares of Sinpar Holding S.A. and n. 12,251,000 shares of Sinpar S.p.A.

3. The party, if any, which, through the agreement, can exercise control over the company

There is no party which, through the agreement, can exercise control over Pirelli & C..

4. Restrictions on the sale of the shares transferred and on the subscription and the purchase of new shares

The sale of the shares to third parties (and option rights in the event of a capital increase against payment) is prohibited. Shares can be sold freely and pre-emptively to subsidiaries, according to article 2359, paragraph 1, point 1 of the Italian Civil Code, and to the parent companies as well as other participants to the shareholders agreement.

Each participant may buy or sell additional shares for an amount not in excess of the higher of 20% of the shares already transferred by the participant itself and 2% of the ordinary share capital issued; purchases of greater amounts are permitted only with the intent of reaching a holding equal to 5% of the ordinary share capital issued, on condition that the amount in excess of the above limits came under the shareholders agreement.

CAMFIN S.p.A. is authorized to freely purchase additional Pirelli & C. shares; it can transfer shares to the shareholders agreement, but to the extent that, at any one time, the shares do not exceed 49.99% of total shares transferred by all the participants in the shareholders agreement. This has been decided so that a stable predominate position is not assumed in the shareholders agreement or a stable veto power is not exercised over common decisions.

Except where the Pirelli & C. ordinary shares in the shareholders agreement correspond to the majority of the voting rights in the ordinary shareholders' meetings, each participant (also through parent companies and/or subsidiaries) intending to purchase shares of that category shall inform the President in writing beforehand and the President shall inform the participant if, taking into account the laws in force concerning tender offers, the participant can proceed, in whole or in part, with the proposed purchase. Buy or sell the shares.

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5. Availability of the shares

The shares transferred shall remain at disposal of the participants in the shareholders agreement.

6. Bodies governing the agreement, composition, meetings and powers

The Body governing the agreement is the Shareholders Agreement Executive Committee.

The Shareholders Agreement Executive Committee shall consist of a president and vice-president, in the form of the president and the longest serving vice-president of Pirelli & C., and by a member representing each participant unless a participant has deposited more than 10% of ordinary share capital, in which case another member may be designated: for this purpose, in the event the shareholders agreement is composed of several companies related by a controlling relationship or belonging to the same parent company, their aggregate shall be considered for this purpose as one sole participant in the shareholders agreement.

The Shareholders Agreement Executive Committee shall be convened to evaluate the proposals to be submitted to the shareholders' meetings, for the possible earlier termination of the agreement and for the admission of new participants. The Shareholders Agreement Executive Committee shall also meet at least twice a year to examine the semiannual performance, the annual results, the general guidelines for the company's development, the investment policy and proposed significant divestitures and more in general, all the relevant matters of discussion by both the ordinary and extraordinary sessions of the shareholders' meetings.

7. Matters covered by the agreement

Those contemplated in points 4 and 6 above.

8. Majorities needed to reach decisions regarding the issues governed by the agreement

The Shareholders agreement Executive Committee approves its resolutions with the favourable vote of the majority of the shares transferred; the Shareholders agreement Executive Committee can designate a trusted person to represent the shares in the shareholders agreement at the shareholders' meetings in order to vote according to its instructions. Whenever the decisions of the Shareholders Agreement Executive Committee are not voted unanimously, the dissenting participant shall have the right to freely vote at the shareholders' meeting.

9. Term, renewal and cancellation of the agreement

The agreement shall be valid until April 15, 2010 and shall be tacitly renewed for a period of three years except for withdrawal, which can be exercised between December 15 and January 15 prior to the expiration date. In case of withdrawal, the shares transferred by the withdrawing party shall be automatically offered pro quota to the other participants. The agreement shall remain in force, whenever it is possible, at every expiration date, to renew the agreement for a percentage of Pirelli & C.'s subscribed ordinary share capital of not less than 33%.

10. Penalties for breach of the commitments contained in the agreement

They are not envisaged by the agreement.

11. Registration of the agreement at the Company Registry

The agreement is registered at the office of the Milan Companies Registry.

Milan, 19 January 2007