Pirelli & C. S.p.A.

SHAREHOLDERS' MEETING 10 MAY 2012

Reports of the Board of Directors
and proposals of resolution

Three-year (2012-2014) cash Incentive Plan

Three-year (2012-2014) cash Incentive Plan for the Group Management of Pirelli. Inherent and consequent resolutions.

Shareholders,

At its meeting on March 12, 2012, on motion by the Remuneration Committee and with the favourable opinion of the Board of Statutory Auditors, the Board of Directors approved the new Three-year (2012-2014) cash Incentive Plan for Pirelli Group Management (the "**LTI Plan**") – reflecting the new, challenging targets for the three-year period 2012-2014 set out in the Business Plan presented to the financial community on November 9, 2011. The LTI Plan is submitted for approval to the Shareholders' Meeting pursuant to Article 114-bis of Legislative Decree 58/1998 ("**TUF**") insofar as it envisages, inter alia, that a portion of the bonus be determined on the basis of a total shareholder return target calculated as performance of the Pirelli stock compared with the FTSE/MIB Index Total Return, periodically calculated by FTSE and present on the database of Borsa Italiana, and an index composed of selected peers in the tyre sector.

In this document, we present the principal information concerning the LTI Plan, while a more analytical description of that plan can be found in the Disclosure Document prepared pursuant to Article 84-bis (1) of Consob Resolution no. 11971 of May 14, 1999, as amended (the "**Issuers Regulation**"), which is also available to the public at the head office of Pirelli & C. S.p.A. (in Milan, Viale Piero e Alberto Pirelli 25), on its website www.pirelli.com and at Borsa Italiana S.p.A. (in Milan, Piazza degli Affari n. 6).

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Reasons for Adoption of the Plan[1]

In accordance with the best national and international practices, the 2012 Remuneration Policy adopted by Pirelli (the "**2012 Policy**") is designed to attract, motivate and retain resources possessing the professional qualifications necessary for profitably pursuing Pirelli Group objectives.

The 2012 Policy and the LTI Plan (which is an integral part of that policy) are defined in such a way as to align Management interests with those of shareholders, pursuing the primary objective of creating sustainable value in the medium-long term through the creation of an effective and verifiable link between compensation, on the one hand, and individual and Pirelli

[1] Information required pursuant to Article 114-bis (1)(a) TUF.

Group performance on the other.

The 2012 Policy has been prepared on the basis of Policy application experience last year. Therefore, its structure has been refined and its content expanded, by incorporating in it elements that had previously been contained in the application criteria, in view of facilitating full comprehension of the link existing between the structure of management remuneration and the creation of value over the medium-long term. The 2012 Policy also reflects the recent regulatory provisions adopted by Consob in Resolution no. 18049 of December 23, 2011.

<u>Recipients of the Plan</u>[2]

The LTI Plan is open to Pirelli Management (comprised of Executive Directors of Pirelli & C. and all Group Executives) and may also be extended to those who during the three-year period join Group Management or assume an Executive position. In these cases, inclusion in the Plan is conditioned on enrolment in the LTI Plan for at least one whole financial year, and the bonus percentages are pro-rated according to the number of months of participation in the Plan.

Participants in the LTI Plan include, inter alia, the Chairman and Chief Executive Officer of Pirelli & C., Marco Tronchetti Provera, the Deputy Chairman, Alberto Pirelli, the General Manager Francesco Gori, the Key Managers Francesco Chiappetta (General Counsel and Chief of Corporate and Institutional Affairs), Maurizio Sala (Chief Management Control) and Francesco Tanzi (Chief Financial Officer and Corporate Financial Reporting Manager).

<u>Performance Targets and calculation of Bonus</u>[3]

Insofar as the Management remuneration structure is broken down into three parts:

- fixed component;
- an annual variable component (MBO): a percentage of the fixed component is established, with percentages that rise according to the position held and considering the benchmarks for each position, with the target ranging from a minimum of 20% for Executives (managers at the Italian companies of Pirelli or employees of foreign companies controlled by the Group holding a position equivalent to that of an Italian manager) to a maximum of 100% for the Directors holding a special office who have been assigned specific functions. According to the beneficiary, it is designed to reward the annual performance of the Group, the Group company, and the company and/or the business unit to which he or she belongs. A limit is imposed on the maximum possible MBO bonus, which (i) for the Executives and Senior

[2] Information required pursuant to Article 114-bis (1)(b) and (b-bis) TUF.
[3] Information required pursuant to Article 114-bis (1)(c) TUF.

Managers (who report directly to the Chairman and Chief Executive Officer and the General Manager of Pirelli & C., and whose activity has a significant impact on business results), is double the possible target-based bonus, (ii) for the Key Managers, is equal to 150% of the gross annual fixed component of remuneration ("**GAS**"), (iii) for the General Managers, it is 200% of the GAS and (iv) for the Directors holding special offices and assigned specific functions, is equal to 250% of the fixed component for the principal operating office (in the case of Mr Tronchetti Provera, his position held at Pirelli Tyre S.p.A.). Payment of 50% of the MBO that might be accrued in 2012 and 2013 is deferred, and part of it (50%) is conditioned on attainment of the targets set in the LTI Plan:

- the medium-long term variable component (LTI Plan): this too is set as a percentage of the fixed component and is aimed at rewarding Group performance during the three-year period 2012-2014. Just like the MBO bonus, a limit is imposed on the maximum realisable amount for the LTI.

The LTI Plan is a cash incentive plan and does not envisage the grant of shares or stock options. It is composed of the:

(i) "**pure LTI Bonus**": conditioned on fulfilment of the three-year targets and determined as a percentage of the gross annual fixed component/GAS received by the beneficiary at the date on which participation in the Plan was decided. This bonus percentage rises according to the position held and considering the benchmarks applicable to each individual.

The maximum pure LTI Bonus cannot be more than 1.5 times the bonus that may be received if the targets are met.

If the targets are missed, the beneficiary is not vested, not even on a pro-rated basis, for distribution of the pure LTI Bonus;

(ii) "**co-investment LTI Bonus**": which includes a mechanism for "co-investment" of part of the MBO. The participant in the LTI Plan "co-invests" 50% of his 2012 and 2013 MBO (hereinafter, the "**co-invested MBO**").

Given the operating rules of the LTI Plan, half of the "co-invested MBO" is not subject to additional performance targets, and may thus be qualified as "**deferred MBO**."

Payment of the other half is conditioned instead on fulfilment of the three-year targets and is thus a variable medium-long term component. If the targets are met, in addition to return of the co-invested MBO, the Plan participant is entitled to it being increased by between 50% and 125%. The co-invested MBO supplement is granted in the amount of 50% of what is "co-invested" on fulfilment of the three-year targets. The variation in the supplement (up to 125% of the co-invested MBO) is based instead on additional medium-long term targets.

The deferred MBO will be returned to participants in the LTI Plan whose employment relationship is terminated (during the three-year period 2012-2014 before closure of the LTI Plan) for no fault of their own (and thus including natural events).

For the Directors holding special offices and assigned specific functions at the Company (which is the case of the Chairman and Chief Executive Officer, Mr Tronchetti Provera) who leave office upon expiry of their term or for no fault of their own (and thus including natural events) before closure of the LTI Plan, the co-invested MBO shall be returned with the 150% supplement while the pure LTI Bonus will not be paid, not even on a pro-rated basis.

The 2012-2014 LTI Plan includes a financial access condition comprised by the net cash flow of the Group accumulated over the three-year period. Another condition for access to the pure LTI Bonus consists of attainment of the value creation target, which in addition to recognition of 100% of the pure LTI Bonus also qualifies the recipient for the 50% supplement of the co-invested MBO.

The following two types of targets and related weights are established for the pure LTI Bonus:

- "Target-based value creation objective" that measures the capacity of the company to create value over the medium-long term considering the profitability of ordinary operations compared with the amount of invested capital and its cost. In particular, this target is equal to the difference between NOPAT (Net Operating Profit After Tax) and the weighted average cost of capital plus working capital.

  Fulfilment of the target-based value creation objective (determined by considering a cumulated EBIT for the three-year period corresponding to the amount set in the Three-year Business Plan) qualifies the beneficiary to receive 100% of the pure LTI Bonus.

  Two thirds of the difference between the target-based pure LTI Bonus and the maximum LTI Bonus will be determined by achievement of the value creation result.

  The remaining one third of the difference between the pure LTI bonus and the maximum LTI bonus is determined by achievement of the total shareholder return ("TSR") target calculated as performance of the Pirelli stock compared with (i) the FTSE/MIB Index Total Return, periodically calculated by FTSE and present on the database of Borsa Italiana and (ii) an index composed of selected peers in the tyre sector.

For the LTI co-investment bonus component**:**

- fulfilment of the value creation target level qualifies the employee for return of the co-invested MBO plus a supplement of 50%;
- the supplement of the co-invested MBO may reach a maximum of 125% on condition of

satisfaction of two other objectives, unrelated to each other:

1) two thirds of the incremental difference between the supplement of 50% of the co-invested MBO and the supplement of 125% of the co-invested MBO are calculated in relation to improvement in the average return on sales target result for the three-year period 2012-2014 (“**ROS 2012-2014**”), which is the weighted average of the ratio between operating income net of restructuring expenses and consolidated net sales accumulated during the three-year period net of non-recurring transactions;
2) the remaining one third of the difference between the supplement of 50% of the co-invested MBO and the supplement of 125% of the co-invested MBO is calculated on the basis of a Sustainability indicator in relation to the position of Pirelli in the following indices: (i) Dow Jones Sustainability Index, Autoparts and Tyre segment, and (ii) FTSE4Good Tyre.

If the access condition and/or target-based value creation objective are not met, the LTI Plan participant is entitled to return of half of the co-invested MBO (return of the co-invested MBO not subject to performance conditions).

Bonus payment period

If the targets are met, the payment date of the medium-long term bonus (pure LTI Bonus and co-investment LTI Bonus; the “**Payment Date**”) in favour of the LTI Plan participants is scheduled to take place no later than April 2015, on condition that their term and/or employment relationship has not terminated for any reason at December 31, 2014.

Please refer to the Disclosure Document for a description of the effects of termination of the employment relationship or expiry of one’s term in office.

Duration of Plan and Amendments

The 2012-2014 Plan terminates on the Payment Date. Please refer to the Disclosure Document in regard to existing procedures for carrying out any revision of the LTI Plan.

Special incentive fund for worker participation in businesses[4]

The Plan does not receive any support from the Special Incentive Fund for worker participation in businesses, pursuant to Article 4(112) of Law 350 of December 24, 2003.

[4] Information required pursuant to Article 114-bis (1)(d) TUF.

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The LTI Plan must be considered "particularly material" insofar as it applies, inter alia, to the Chairman and Chief Executive Officer of Pirelli & C. and the Key Managers by virtue of their regular access to insider information and authority to take decisions that can impact the evolution and future prospects of the Group.

Considering that the LTI Plan is a cash incentive plan, insofar as it does not involve the grant of shares or stock options, but only a cash incentive that is partially based on the performance of Pirelli & C. common stock in reference to benchmark companies, the Disclosure Document prepared pursuant to applicable laws and regulations does not contain the information required for mechanisms that consider the granting of shares or stock options.

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Shareholders,

on the basis of the foregoing presentation, we ask that you:

1. approve – pursuant to Article 114-bis of Legislative Decree 58 of February 24, 1998, as amended – adoption of a three-year incentive plan for 2012/2014 (the LTI Plan) for Pirelli Group Management, partially based on financial instruments, in the terms illustrated in this Report and as better illustrated in the Disclosure Document (prepared pursuant to Article 84-bis (1) of the Issuers Regulation). The LTI Plan envisages that, inter alia, the remaining one third of the difference between the target-based pure LTI Bonus and the maximum LTI Bonus be determined on the basis of a total shareholder return target calculated as performance of Pirelli stock compared with the FTSE/MIB Index Total Return, periodically calculated by FTSE and present on the database of Borsa Italiana and an index composed of selected peers in the tyre sector;

2. grant the Board of Directors – and for it, the Chairman – all power as necessary for full, complete implementation of the LTI Plan.