QSC AG

Annual Report 2006

Key Data Highlights 2006

Plus – Growth Company QSC

+ growing

Key Data

All amounts in € million

	2006	2005	2004	2003	2002
Revenues	262.5	194.4	145.9	115.6	47.1
EBITDA	+21.2	+5.8	+3.2	-28.5	-60.3
EBIT	-7.2	-18.7	-22.7	-61.9	-101.1
Net loss	-5.3	-18.2	-21.6	-60.6	-102.6
Net loss per common share [1] (in €)	-0.04	-0.17	-0.21	-0.58	-1.01
Equity [2]	160.6	85.0	70.2	89.5	145.3
Balance sheet total [2]	299.9	151.3	116.0	132.7	194.6
Equity ratio (in percent)	53.6	56.2	60.5	67.4	74.7
Capital expenditures	40.1	20.1	15.9	8.5	11.8
Liquidity [2]	108.9	56.4	40.3	54.3	87.6
Share price [2] (in €)	5.00	3.86	3.66	3.03	0.38
Number of shares [2]	133,897,686	115,033,078	105,502,729	105,037,396	105,008,714
Market capitalization [2]	669.5	444.0	386.1	318.3	39.9
Employees [2]	675	450	367	373	433

Consolidated Financials Statements
2004 to 2006 under IFRS,
2002 and 2003 under U.S. GAAP

[1] basic and diluted
[2] as of December 31

2006 Highlights

+ + + Wholesale start by HanseNet + + +
In January 2006, QSC won a further strong wholesale partner in HanseNet and its Alice brand to market QSC's superfast ADSL2+ technology. Following the successful launch of this business, the two companies expanded their partnership in January 2007 to include some 100 additional cities.

+ + + TOYS"R"US new large account + + +
In May 2006, one of the world's largest toy retailers, TOYS"R"US, contracted with QSC for a virtual private network, an IP-VPN, to network all of its corporate locations in Germany, Austria, and Switzerland. QSC is operating this network, and additionally securing it with an intelligent backup solution.

+ + + Acquiring Broadnet majority + + +
With the acquisition in June 2006 of a majority interest in Broadnet AG, QSC strengthened its core business with enterprise customers. By year-end 2006, QSC had increased its holdings of this also publicly traded broadband provider to some 92 percent, and is now planning a merger.

+ + + Larger network with Plusnet + + +
Together with the German subsidiary of the Swedish-based TELE2 group, QSC formed network operating company Plusnet in July 2006. Plusnet will expand the existing DSL network from over 1,000 central offices today to nearly 2,000 by year-end 2007.

+ + + Wholesale partner freenet + + +
In August 2006, QSC was able to win a further strong wholesale partner. Since then, freenet has been very successfully marketing ADSL2+ connections with bandwidths of up to 16 megabits per second on the basis of QSC's nationwide infrastructure.

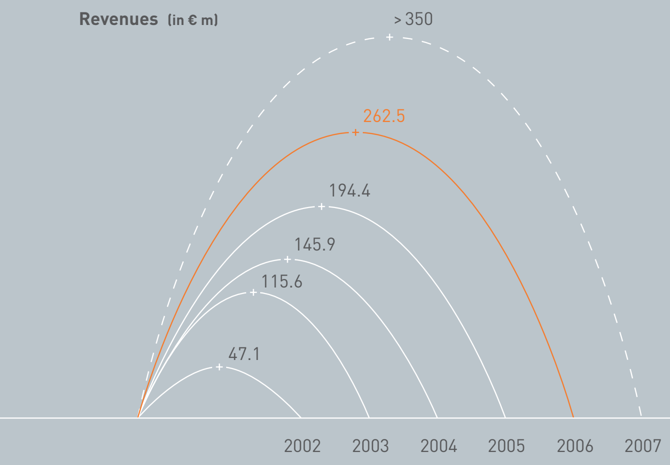
+ + + NGN running + + +
In the third quarter of 2006, QSC concluded the migration of its infrastructure to a Next Generation Network. The nationwide network is now based upon the IP standard throughout, thus enabling it to be operated considerably more easily and cost-effectively than classical networks.

+growing

+35%

Revenue growth in 2006

In 2006, QSC grew its revenues by 35 percent to € 262.5 million. Since going public, the Company has been generating rising revenues from quarter to quarter, and for years has been one of Germany's highest-growth technology companies. Over the course of the past five years, revenues have increased more than fivefold.



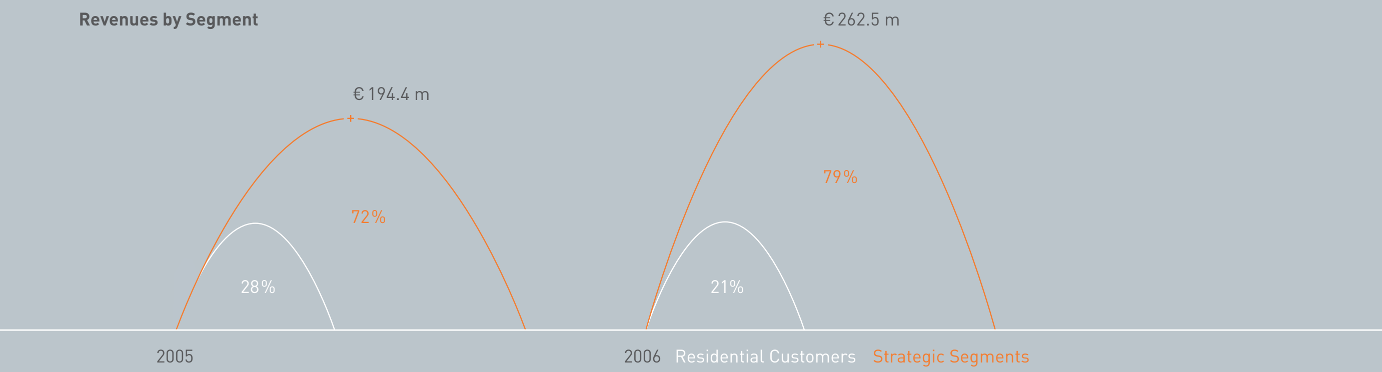
+improving

+ € 67 m

Growth in strategic segments

Early on, QSC focused on high-margin business with enterprises, and has been rapidly posting revenue growth in the three strategic segments Large Accounts, Business Customers, and Wholesale/Resellers – by 48 percent or € 67 million in 2006 alone. The percentage of total revenues accounted for by the Company's strategic segments rose to nearly 80 percent.

Revenues by Segment



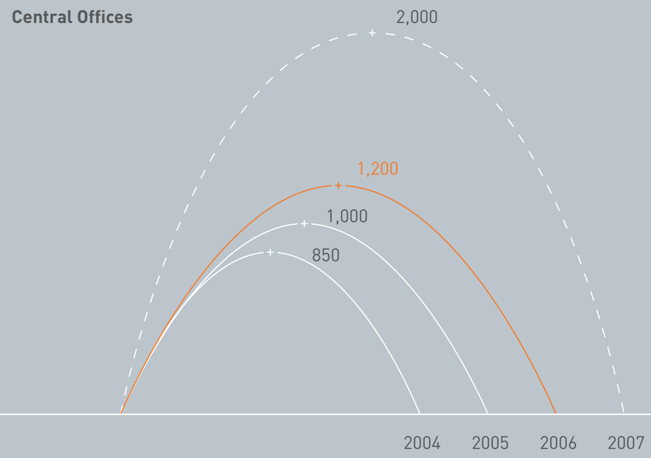
earning

Higher operating profitability in 2006

With an EBITDA of € 21.2 million, QSC has nearly increased its operating earnings before depreciation fourfold over the previous year. The Company's scalable business model will continue to afford high profitability growth in the future – for 2007, an EBITDA of between € 50 million and € 60 million is planned.

+266%

+expanding



New central offices by year-end 2007

In the summer of 2006, QSC formed network operating company Plusnet together with TELE2. Plusnet will be swiftly expanding the nationwide DSL network to nearly 2,000 central offices by end of 2007. QSC will then be able to directly reach some 50 percent of all German households and some 70 percent of enterprise networking sites.

+800

2006 +

QSC sustained its strong and profitable growth during 2006, earning its first **net profit** in the fourth quarter. The Company intends to sustain this dynamic development during 2007: QSC anticipates revenue growth to more than € 350 million, an increase in its EBITDA to between € 50 million and € 60 million, as well as a net profit for the year of between € 15 million and € 25 million.

This **profitable growth** stems from successes in the three strategic segments of Large Accounts, Business Customers, and Wholesale/Resellers. All three segments will benefit from the **swift expansion of the network** to nearly 2,000 central offices by the end of the current fiscal year. QSC will thus continue to develop into one of the leading providers of integrated telecommunication services and managed services for enterprise customers and wholesale/resellers in Germany.

Content

To Our Shareholders

QSC will sustain its strong and profitable growth also in the coming years. Swiftly expanding the network and focusing on high-margin strategic customer segments will serve as the foundation for continued growth of the value of the Company.

Letter to Our Shareholders

Dear Shareholders,

Quarterly net profit recorded for the first time in Q4 2006

QSC again accelerated its growth in 2006: Revenues rose by 35 percent to € 262.5 million; the year before, the growth rate had been 33 percent. And profitability has been rising at an even faster pace: EBITDA quadrupled in 2006 to nearly € 21.2 million, and over the course of the year the Company steadily moved toward crossing the net profit threshold. In the fourth quarter of 2006, QSC recorded its first net profit in the amount of € 2.8 million.

This strong and profitable growth stems from successes in the three strategic customer segments Large Accounts, Business Customers, and Wholesale/Resellers. We are operating in growth markets in all three of these areas, with QSC growing at an even faster pace than the respective market. We attribute this, on the one hand, to our years of experience and our success in high-margin business with enterprise customers. On the other hand, the migration of our entire network to a nationwide Next Generation Network (NGN) that was concluded last year now gives us a crucial competitive advantage.

Our infrastructure is now based virtually throughout on the Internet Protocol (IP), the transfer standard of the 21st century. This results in two major advantages: First of all, this enables us to be faster and more cost-effective in integrating intelligent IP-based services and functionalities, first and foremost Voice over IP, into data networks. Secondly, a consistent NGN can be operated and maintained considerably more efficiently than classical telephone networks. This has a positive impact on our cost structure, and thus on our ability to offer extremely competitive prices, without having to suffer any loss of margin.

Over and above the NGN, we also invested in our infrastructure in 2006. Thanks to the ADSL2+ technology upgrade of the network, QSC can today offer transfer speeds of up to 25 megabits per second nationwide, thus also enabling Triple Play offerings – Internet, Telephony, and Television over one and the same line.

The summer of 2006 marked a milestone in QSC's history with the establishment of Plusnet, the joint-venture network operating company held by QSC and TELE2. QSC contributed its DSL network with more than 1,000 central offices to its subsidiary, and TELE2, one of the leading alternative voice service providers for residential customers in Europe, made a € 50 million contribution to capital. This capital contribution will enable Plusnet to expand the DSL network to nearly 2,000 central offices by the end of this year. Moreover, TELE2 is also making a significant contribution to the network's fixed and variable operating costs, which will make a considerable improvement to further improving QSC's cost structure.

Swift expansion of the nationwide network by year-end 2007

By the end of the current fiscal year, QSC will then be able to directly reach some 50 percent of all households in Germany, along with some 70 percent of all networking locations under requests for proposals – QSC's clear strategic alignment to enterprise customers and TELE2's focus on residential customers complement one another ideally in this connection.

This greater network coverage and improved cost structure will serve as the basis for sustaining the Company's strong and profitable growth in 2007 and beyond. On the one hand, the expanded network will nearly double QSC's likelihood of winning requests for proposals from large accounts. On the other hand, QSC will thus be able to serve more business customers with its voice and data products over DSL lines. In this connection, QSC is additionally benefiting from its good reputation among small and medium enterprises. According to a survey conducted on behalf of QSC in 2006, half of all customers in this sector have already recommended us at least once. More locations will also make QSC an even more attractive partner in wholesale business, because telecommunication providers like HanseNet and freenet want to reach as many German residents as possible with their offerings. And even today, in no other line of business is QSC growing as quickly as in its wholesale business, which was only launched at the end of 2005.

With the expansion of its network, QSC is continuing to develop into one of the leading telecommunication providers for enterprise customers in Germany. Since March 2007, a new image has been underscoring our unique position as a premium provider. It shows that QSC offers its customers maximum quality and utility, thus increasing their productivity.

This kind of market positioning is only credible when it is backed up by the entire QSC team. And we would like to take this opportunity to thank all of our people for their accomplishments – it is only their personal commitment that makes QSC a premium provider. And these thanks naturally also go out to the nearly 190 employees of our new Broadnet subsidiary. We acquired some 92 percent of the shares in this company during the course of the year. The merger that is now planned will offer even better opportunities to integrate these people and their expertise in business with enterprise customers, thus opening up additional growth potential for QSC.

The acquisition of a majority stake in Broadnet, the establishment of Plusnet, as well as the profitable growth of our operating business, all contributed to the good performance of QSC shares during the course of the year. With their trading prices advancing by 30 percent, they rose faster than either the TecDAX or the DAX. The increasing interest on the part of European and U.S. investors is being heightened as a result of the growing number of analysts who publish research on QSC: Credit Suisse, Goldman Sachs, Merrill Lynch and others published their first research on our Company in 2006.

Profitability will also rise significantly in the current fiscal year

These kinds of analyses from prominent financial institutions are opening up new performance potential for our shares. However, the crucial factors will continue to stem from the growth of our operating business: In this connection, we are again planning revenue growth of significantly over 30 percent in 2007 to more than € 350 million, and EBITDA growth of at least 135 percent to between € 50 million and € 60 million. As long as our network is not being fully utilized – and at year-end 2006 the utilization factor stood at only around 30 percent on average – QSC's infrastructure-based business model will continue to afford this kind of disproportionate growth in profitability. And this is precisely what makes us so optimistic that QSC will sustain its profitable growth over the medium term, thus enabling it to create additional value for you, our dear shareholders.

Cologne, March 21, 2007

Dr. Bernd Schlobohm
Chief Executive Officer

Markus Metyas

Bernd Puschendorf

The Management Board

»The establishment of Plusnet as well as our successes in 2006 bring us that much closer to our goal of becoming one of the leading providers for enterprise customers and wholesale/resellers in Germany.«

»QSC reached the profitability zone in Q4 2006. Thanks to its scalable business model it will continue to see a strong rise in profitability during the years to come.«

Dr. Bernd Schlobohm (b. 1960) + Chief Executive Officer
A postgraduate engineer, he is responsible on the Management Board for Strategy, Technology, Corporate Communications, and Quality Management. In this position, during 2006 he drove the establishment of network operating company Plusnet as well as the Company's swift network expansion. Prior to cofounding QSC together with Gerd Eickers, Dr. Schlobohm had been in charge of business at Thyssen equity investment Spaceline Communication Services as well as technology operations at Thyssen Telecom.

»Our focus on business with enterprise customers early on has paid off: We are scoring points in the competitive arena with both our solutions competence and customer intimacy.«

Markus Metyas (b. 1963)
An investment banker, his responsibilities on the Management Board include Finance, Investor Relations, Procurement, Human Resources, and Legal Affairs, as well as Mergers & Acquisitions. In this connection, he was responsible for QSC's acquisition of a majority stake in Broadnet AG in 2006. Prior to joining QSC in February 2000, this postgraduate business administrator had supported European companies in both capital market transactions as well as corporate acquisitions and sales while at Morgan Stanley and Wasserstein Perella.

Bernd Puschendorf (b. 1950)
A businessman, he is in charge of Sales, Marketing, and Products as a member of the Management Board; in this connection, he played a key role in growing the Company's revenues in its strategic segments during fiscal 2006. Prior to his appointment to the QSC Management Board in March 2002, Bernd Puschendorf had held positions at IBM, Siemens, and other companies; from 1999 onwards he held the post of speaker of the management board in Germany of the Fujitsu Siemens joint venture.

The Supervisory Board

John C. Baker + Chairman
The founder and general partner of Baker Capital, a private equity fund based in the U.S., he represents QSC's largest shareholder. A Harvard graduate, he has been active in the private equity industry for more than 25 years and had invested in QSC prior to its initial public offering.

Gerd Eickers
After three years on the Management Board, the second QSC cofounder returned to the Supervisory Board in June 2004. Since February 2005, this postgraduate economist has additionally been serving as the president of VATM, the premier telecommunication industry association in Germany.

Norbert Quinkert
Having served for years as the chief executive officer of Motorola GmbH, he is now utilizing his global network as a partner in the Quinkert Herbold Fischer human resources consultancy. Prior to working for Motorola, he had been in charge of General Electric's business in Germany for years.

Herbert Brenke + Vice Chairman
An independent telecommunications consultant, he built mobile communications provider E-Plus in the 1990s, and was in charge of its business from 1993 to 1998. Prior to that, he had been in charge of Thyssen Rheinstahl Technik for many years. At the same time, he had been a member of the management team at Thyssen Handelsunion since 1983.

Ashley Leeds
This general manager of Baker Capital had already been focusing on the areas of telecommunication and media as an investment banker at Lehman Brothers. A Harvard graduate, she was one of the founding partners of Baker Capital.

David Ruberg
A postgraduate information technology professional, he today represents Baker Capital on the supervisory boards of various high-tech companies in the United States and Europe. Prior to that, he had personally managed the business of a U.S.-based broadband provider as its chief executive officer.

Report of the Supervisory Board

for fiscal year 2006 regarding the Company and the Group

In 2006, QSC AG sustained its strong and profitable growth, especially in the three strategic segments Large Accounts, Business Customers, and Wholesale/Resellers. As the Supervisory Board, we advised the Management Board, monitored its management of the Company, and performed the duties required by law and the Articles of Association. The Supervisory Board was directly involved in all decisions or measures of fundamental importance, in particular those relating to the Company's assets, finances, or earnings. The Supervisory Board approved all measures for which its consent is required by law, the Articles of Association, or the Rules of Procedure of the Management Board.

Management Board quickly and comprehensively informs Supervisory Board

Issues of the Supervisory Board + The Management Board regularly informed us on the development of business, including monthly and quarterly financial statements, as well as actual/target comparisons. Variances from plans and targets were explained in detail. Further inquiries and requests by the Supervisory Board for additional information were always quickly and comprehensively answered. The information from the Management Board covered the course of business, the Company's overall economic position, and, in particular, its revenue structure, new orders, receivables (including aging analysis), the methods and results of its risk identification and monitoring system, as well as all transactions of significance with respect to the Company's profitability and liquidity. It is the opinion of the Supervisory Board that the Company's internal risk monitoring and detection systems operate reliably. In joint meetings and telephone conferences, the Supervisory and Management Boards discussed key aspects of the Company's business policies and strategies, as well as its corporate development and planning. Moreover, the Chairmen of both bodies conducted regular conversations to discuss current issues. The main focuses of the Supervisory Board's activities in 2006 were:

1. Establishment of network operating company Plusnet GmbH & Co. KG
   The Management Board regularly reported to the Supervisory Board on the status of the months-long negotiations with Communication Services TELE2 GmbH that were involved in implementing this joint venture. The Management and Supervisory Boards deliberated on the general legal and economic details of the project, as well as on potential transaction options. On July 10, 2006, the Supervisory Board gave its consent to contributing QSC's nationwide DSL network to Plusnet GmbH & Co. KG.

2. Acquisition of a majority interest in Broadnet AG
The Management and Supervisory Boards discussed in detail the reasons for this acquisition and its objectives, as well as its implementation through the acquisition of a majority of Broadnet shares from its main shareholders and management, the subsequent takeover bid, and the ensuing acquisition of further shares from institutional investors – in each case, in exchange for new QSC shares from authorized capital – before the Supervisory Board granted its consent to each stage. In connection with this process, the Supervisory Board considered key financial indicators of the company and key operating data relating to the target company's network, as well as the situation on the capital market.

3. Sales activities
In 2006, the Supervisory Board continued to closely observe and monitor the development of sales activities, in particular the Company's partnerships with major wholesale partners like HanseNet/Alice and freenet.

4. Restructuring measures within the QSC group
Examples of this include, in particular, the merger of celox Telekommunikationsdienste GmbH into QSC AG as well as the transfer of the Company's residential customer business into wholly owned Q-DSL home GmbH. Prior to the Supervisory Board's consent to each respective step, the Management Board explained to the Supervisory Board the concept of the restructuring measure and its impact on the future strategic development of the QSC group.

Meeting of the Supervisory Board and its committees + Aside from the four regular meetings, the members of the Supervisory Board conducted four telephone conferences during the year under report. All members attended more than 75 percent of the Supervisory Board meetings in 2006, at least via telephone. Where necessary, resolutions on individual issues were additionally adopted in writing.

High attendance rate of the Supervisory Board members at meetings

The Compensation Committee met after each of the meetings of the Supervisory Board, thus four times during the year under report. This Committee, which was established in May 2001, consists of John C. Baker, Herbert Brenke, and David Ruberg. It deliberated the employment contracts with the members of the Management Board and the compensation paid to them, and regularly reported to the Supervisory Board on its activities. In particular, the Compensation Committee dealt with questions relating to variable compensation and targets for the members of the Management Board.

Corporate Governance + The Supervisory Board continuously monitored the evolution of the German Corporate Governance Code and its implementation at QSC AG. Following the requirements of the Code, the Supervisory Board also reviewed the efficiency of its own activities. At its meeting on November 29, 2006, the Supervisory Board reviewed and confirmed that QSC AG was in compliance with the recommendations of the Corporate Governance Code during the preceding year pursuant to the Statement of Compliance that had been adopted the year before. At the same time, the Management and Supervisory Boards jointly issued an updated Statement of Compliance pursuant to § 161 of the German Stock Corporation Act (AktG) and made this statement permanently available to the shareholders on the Company's website.
Three lawsuits for invalidation and nullification were initiated against the resolution of the Annual Shareholders Meeting on May 23, 2006, relating to extension of the term of convertible bonds from the "2001 QSC Stock Option Program"; the corresponding proceedings before the Regional Court of Cologne are still pending. The Company is represented in these actions by its Management and Supervisory Boards.

Explanation of statements provided pursuant to §§ 289, Sub-Para. 4, 315, Sub-Para. 4, German GAAP (HGB) + In its Management Report on the Company and the Consolidated Group, which was the subject of review by the Supervisory Board, the Management Board provided statements pursuant to §§ 289, Sub-Para. 4, 315, Sub-Para. 4, German GAAP (HGB). Pursuant to § 171, Sub-Para. 2, Sentence 2, German Stock Corporation Act (AktG), the Supervisory Board comments on these statements as follows: The statements relate to rules pertaining to the appointment and removal of members of the Management Board, to amendments to the Company's Articles of Association and Bylaws, to the authority of the Management Board to issue or buy back shares, as well as to the composition of the Company's subscribed capital. The Supervisory Board considers the statements pursuant to §§ 289, Sub-Para. 4, 315, Sub-Para. 4, German GAAP (HGB), to be accurate. In particular, the above-mentioned rules and authorities are those which are usual and customary at publicly traded corporations that are comparable to QSC AG and whose purpose is not aimed at impeding any potential takeover attempts.

Audit + Ernst & Young AG Wirtschaftsprüfungsgesellschaft, Eschborn/Frankfurt am Main, Germany, audited both the Annual Financial Statements of QSC AG for the year ended December 31, 2006, which were prepared by the Management Board in accordance with the accounting principles set forth in the German GAAP (HGB), as well as the Consolidated Financial Statements for the year ended December 31, 2006, which were prepared in accordance with International Financial Reporting Standards (IFRS), as well as the Management Reports of the Company and the consolidated group. The audit contract had been awarded by the Supervisory Board in accordance with the resolution adopted by the Annual Shareholders Meeting on May 23, 2006. The major focuses of the audit included initial consolidation of Broadnet AG, Plusnet GmbH & Co. KG, Q-DSL home GmbH and 010090 GmbH as well as the completeness and accuracy of the notes.
The independent auditor issued an unqualified opinion on the Company's Annual Financial Statements presented in accordance with HGB accounting principles as well as on the Consolidated Financial Statements presented in accordance with IFRS for the year 2006. In its meeting on March 28, 2007, the Supervisory Board discussed all of the above-indicated documents as well as the auditor's reports – including the practicality of utilizing accounting and valuation latitude as well as the potential risks resulting from future developments – with the Management Board and the independent auditor.
Having conducted its own examination, the Supervisory Board has no objections to the Annual Financial Statements of QSC AG for the 2006 fiscal year presented in accordance with HGB accounting principles, the Consolidated Financial Statements presented in accordance with IFRS, or the Management Report for QSC AG and the Management Report for the consolidated group, and concurs with the findings of the independent auditor. The Supervisory Board approves both the Consolidated Financial Statements presented in accordance with IFRS as well as the Annual Financial Statements presented in accordance with HGB accounting principles, with the latter thereby being formally adopted.

The Supervisory Board approves Consolidated Financial Statements

QSC's sustained strong growth and its success in reaching profitability net income in Q4 2006 was an achievement on the part of all of its people. We therefore wish to express our thanks both to the Management Board as well as to the entire QSC team for their tremendous commitment.

Cologne, March 28, 2007
On behalf of the Supervisory Board

John C. Baker
Chairman of the Supervisory Board

The QSC Share

The trading price of QSC shares rose by a strong 30 percent in fiscal 2006, thus clearly outpacing the TecDAX index. This good performance heightened attention on the part of national and international investors and analysts – 16 financial institutions are now regularly publishing research on QSC.

Share Price Up Sharply

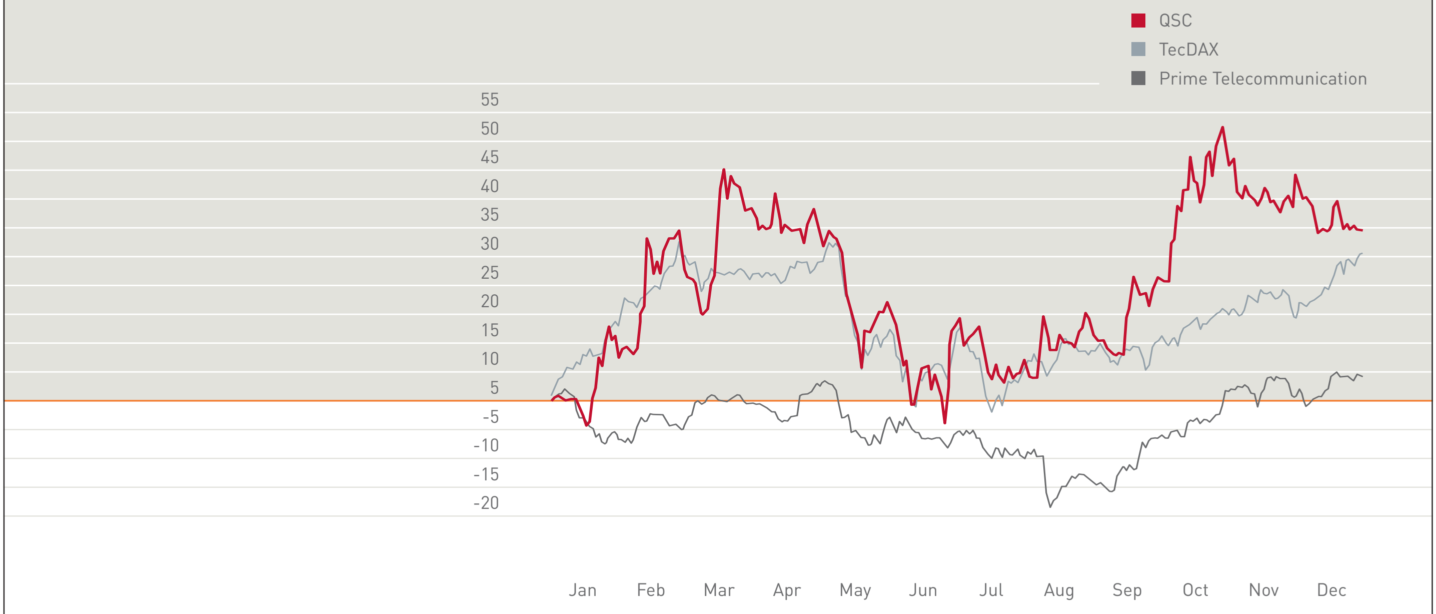
Positive stock market environment + The robust world economy, coupled with an unexpectedly strong recovery in Germany, produced a sharp rise in trading prices on German stock exchanges during the past year. The DAX rose by 22 percent for the year, with the TecDAX, the lead index for technology stocks, rising even stronger by 26 percent during the course of the year to close at 748.32 points. Many telecommunication stocks, on the other hand, suffered from the effects of the price war for residential customers as well as from the penetration of Voice over IP technology. Prime Telecommunication, the lead index for German telecommunication stocks, was only able to record a gain of 4.0 percent in 2006.

QSC shares rose impressively against industry trend

QSC shares impressively went against this industry trend, with their trading prices rising by 30 percent during the past fiscal year to close at € 5.00. The Company benefited in this connection from its focus on high-margin business with enterprise customers and its deployment of Voice over IP technology early on. In addition, investors also rewarded QSC's continued strong and profitable growth as well as the swift expansion and upgrade of its network.

During the course of the year, the performance of QSC shares paralleled the development of the capital market: In the first months of the year 2006, share prices rose across the board. Share price declines then predominated beginning in May and on through the summer, before a sharp recovery set in during the second half of the year. QSC shares reached their high for the year of € 5.76 on October 18, 2006.

QSC share price performance in 2006 (indexed)



Keen interest in QSC + 2006 saw a significant rise in the trading volumes of QSC shares on German stock exchanges, with average trading volumes rising by 43 percent over the year before, and amounting to some 300,000 QSC shares per day during the period covered by this report. On peak trading days, in fact, more than 1.5 million QSC shares changed hands. This again numbered QSC among the 30 most actively traded technology stocks in Germany in 2006, strengthening the Company's position in the TecDAX. The high liquidity of QSC shares also prompted several banks to issue their first certificates on QSC shares.

More and more analysts following QSC + The keen interest that is being displayed on capital markets is underscored by the rising number of studies on QSC that are being regularly published by European and U.S. financial institutions. In 2006, Credit Suisse, Goldman Sachs, and Merrill Lynch began to regularly follow the Company. This means that 16 banks, brokerage houses, and research institutions are now regularly publishing research on QSC shares, with the majority of the analysts issuing buy recommendations.

Most analysts issue buy recommendations on QSC shares

Demand on the part of institutional investors up sharply + The growing volume of analyst research has led to noticeable growth in international attention relating to QSC, in particular among institutional investors. At year-end 2006, more than two-thirds of the Company's freefloat were in the hands of institutional investors from Germany, the rest of Europe, and the United States.

Financial institutions that issue studies on QSC

Berenberg Bank
Commerzbank
Credit Suisse
Dresdner Kleinwort
DZ Bank
Goldman Sachs
HSBC Trinkaus & Burkhardt
HypoVereinsbank
Kepler Equities
Landesbank Baden-Württemberg
Merck Finck & Co
Merrill Lynch
Sal. Oppenheim
SES Research
UBS
WestLB

QSC's intensive and transparent investor relations work assures that these investors receive the information they need, while simultaneously sparking further interest. In 2006, the QSC Management Board presented the Company at 18 road shows conducted in all major financial centers in Europe and the United States. In addition, QSC also participated in capital market conferences conducted by leading financial institutions, including Commerzbank, Deutsche Bank, Dresdner Kleinwort, HypoVereinsbank, JPMorgan, Société Générale, and WestLB, and also presented itself at CeBIT as well as the German Equity Forum.

More information for private investors + QSC has traditionally attached key importance to the principle of fair disclosure and consequently informs all investors, both institutional and private, comprehensively and promptly about both current corporate events as well as the Company's quarterly and annual results. QSC utilizes its website at www.qsc.de/en/investor-relations.html as its central information platform. During the past fiscal year, the Company rigorously expanded its information offerings here.

2005 Annual Report convinces jury of manager magazin

The Company's Annual Report also serves as a key source of information. In its annual analysis ranking the content and design of the annual reports of publicly traded corporations, manager magazin ranked QSC's 2005 Annual Report entitled "Next Generation Connections" fourth among all TecDAX stocks. QSC views this high ranking as confirmation of its efforts aimed at comprehensively informing all shareholders with its reports.

Basic data about QSC shares

Trading symbol	QSC
ISIN	DE0005137004
Bloomberg symbol	QSC GR
Reuters symbol	QSCG.DE
Market segment	Prime Standard
Stock exchanges	Xetra and regional German stock exchanges
Index membership	TecDAX, F.A.Z.-Index, HDAX, CDAX,
	Midcap Market, Technology All Share,
	Prime All Share, Prime Telecommunication,
	Prime IG Fixed-Line Telecommunication
Designated sponsorship	HSBC Trinkaus & Burkhardt
	Landesbank Baden-Württemberg
	Sal. Oppenheim
	WestLB AG
Shares outstanding per December 31, 2006	133,897,686
Share class	No-par-value registered shares of common stock
Xetra price, closing at December 30, 2005	€ 3.86
Xetra price, maximum in 2006	€ 5.76
Xetra price, minimum in 2006	€ 3.64
Xetra price, closing at December 29, 2006	€ 5.00

Continuity in Shareholder Structure

Number of shares in circulation rises following Broadnet acquisition + The number of QSC shares rose by 18.9 million during the past fiscal year to a total of 133.9 million. This increase was mainly attributable to the acquisition of Broadnet AG, another publicly traded corporation. On June 7, 2006, QSC acquired a majority interest in this broadband provider from its former major shareholders and management in the form of a share swap, with the former shareholders receiving 1.0542 QSC share in exchange for each of their Broadnet shares. To effect the transaction, the Management and Supervisory Boards of QSC had resolved an € 11.23 million increase of capital from authorized capital through the issuance of 11.23 million new shares of stock against contributions in kind, under exclusion of the right of subscription. Following the transaction, these shares were easily placed with institutional investors – further documenting the keen interest in QSC that exists among institutional investors.

11.23 million new QSC shares easily placed

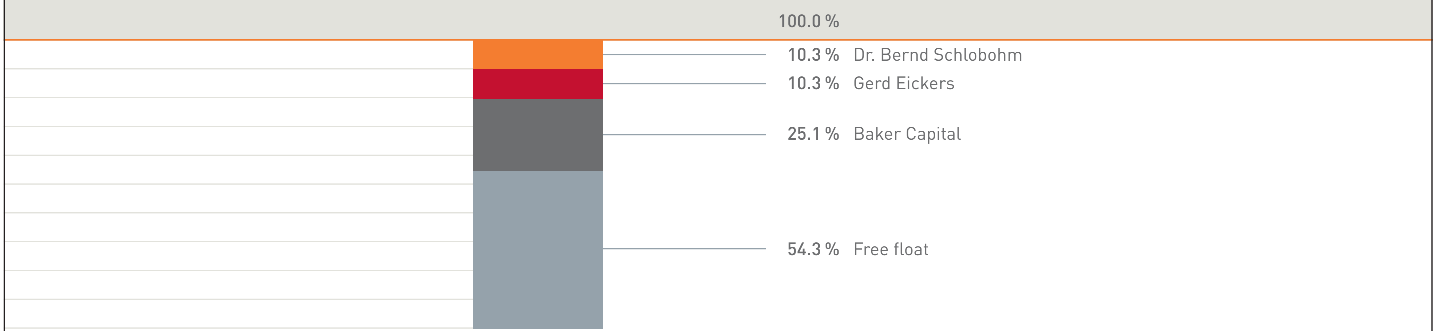
In July 2006, pursuant to the terms of the German Securities and Acquisitions Act (WpÜG), QSC made a public acquisition offer at the same terms and conditions, valid through the end of September. In this connection, Broadnet shareholders received almost 230,000 QSC shares in exchange for their Broadnet shares. In November 2006, QSC was then able to acquire a further 24.8 percent of the Broadnet shares on a share swap basis, issuing 4.92 million new shares for this purpose. Following this transaction, QSC holds some 92 percent of the shares of Broadnet.

In addition to the Broadnet acquisition, the conversion of 2.48 million convertible bonds by QSC employees into an equal number of shares also contributed to this increase. The higher number of conversions than in 2005 stemmed from the expiration of large parts of the 2001 Stock Option Program (SOP) during the past fiscal year. While the Annual Shareholders Meeting in May 2006 had resolved to extend the conversion term of this program by a further five years, lawsuits brought by individual shareholders have thus far prevented this resolution from going into force. Given the resulting insecurity, the majority of those entitled decided to make the conversion in 2006.

None of QSC's founders has ever sold a single share

Free float rises to over 50 percent + The issuance of 18.9 million new shares of stock increased the proportion of the Company's shares that are widely held to 54.3 percent in 2006. According to the Register of Shares, these shareholdings were distributed among approximately 30,000 QSC shareholders as of December 31, 2006. The Company's two founders, Dr. Bernd Schlobohm and Gerd Eickers, each hold 10.3 percent of the Company's shares, and U.S.-based Baker Capital investment company holds 25.1 percent. Neither QSC's two founders nor Baker Capital have ever sold a single share of QSC since the Company first went public. This continuity enhances the attractiveness of the Company's shares, especially in the eyes of institutional investors with a long-term view.

Shareholder structure as of December 31, 2006



Strategy

As it travels on the road towards becoming one of the leading providers of both integrated telecommunication and managed services for enterprise customers and wholesale/resellers in Germany, QSC is focusing on broadening its strategic lines of business on the basis of its expanded network.

The Broadband Provider for Enterprises

A clear vision + The Internet is developing into the central platform worldwide for work, information, communication, and entertainment, making broadband communication one of the key technologies of the 21st century. It takes powerful connections and intelligent services to enable the universal use of the Internet.
DSL technology is employed almost exclusively for broadband Internet access in Germany. QSC embraced precisely this technology at an early stage. Already in the late 1990s, the Company's founders recognized DSL's potential in the Internet Age and set about building a nationwide DSL network. Today, QSC is one of few infrastructure providers in Germany that is able to offer the entire spectrum of modern broadband communication on the basis of its own network.

A clear corporate objective + In the German broadband market, QSC is characterized by a high-quality network, by exceptionally good technology know-how and by outstanding service – all attributes that are highly valued, in particular by businesses . Early on, QSC focused on enterprises as its customers, and set itself a clear medium-term objective in this connection: QSC wants to be one of the leading solutions providers for enterprise customers and wholesale/resellers in terms of size and image.
In doing so, QSC has its sights set on both winning new customers as well as increasing the value added per customer through customer loyalty and the integration of network-related services. QSC has repeatedly been able to convince enterprises of every size through such factors as quality, flexibility, and service, thus strengthening its position as a premium provider. This alignment makes QSC unique in the German telecommunications market, and the Company views itself as being well positioned in the competitive arena, both now and in the future.

Plus – the Growth Strategy

Communication is changing the world.
Broadband is changing communication.
QSC is broadband.

Focusing on three
strategic lines of business:
Managed Services,
Direct Access and Wholesale

Focusing on High Growth Markets

Strategy with three focuses + As it travels the road toward becoming one of the leading providers of integrated telecommunication and managed services in Germany, QSC has its sights set on three focuses: Expanding its strategic lines of business, the resulting strong and profitable growth of its operative business, as well as expanding its network into one of the largest in Germany.

Expanding the strategic lines of business + QSC focuses on the three segments of Large Accounts, Business Customers, and Wholesale/Resellers, where the Company has identified three strategic lines of business with strong growth potential: Managed Services, Direct Access, and Wholesale. In all three fields, QSC is operating in growth markets and can fully bring to bear its expertise as a premium provider for enterprise customers.

Managed Services business includes building and operating IP-based virtual private networks (IP-VPN) for large accounts, as well as the add-on services that build upon them, such as hosting, security solutions, and workplace-related telecommunication solutions. This business is characterized by high per-customer revenues, attractive margins, and long contract terms. Once large and medium-size enterprises have transferred responsibility for building and operating their communication infrastructure to QSC, they have a significantly reduced willingness to change providers, which leads to relatively low contract termination rates – as long there is an acceptable relationship between quality and price. What's more, these kinds of close partnerships enable QSC to sell additional services within the framework of existing contracts.

The integration of additional services also numbers among the growth and profitability drivers in Direct Access business, i.e. direct connection of business customers' voice and data communication to the QSC network. In the case of small and medium-size businesses, QSC is having increasing success in the integration of voice and data services over one and the same broadband line. Direct connection of these kinds of businesses enables QSC to earn higher margins, while simultaneously leading to greater customer loyalty, which results in lower contract termination rates given appropriate quality and pricing.

Wholesale business is the third strategic line of business. Here, QSC is increasingly collaborating with wholesale partners who market DSL lines to residential customers under their own name and for their own account. This business is characterized by long-term collaboration with partners who possess mass-market experience. In this connection, QSC is benefiting from sustained high demand for DSL products on the part of residential customers, without the need to invest in building a brand and a corresponding sales and marketing organization. Moreover, strong demand on the part of wholesale partners is making a crucial contribution toward increasing the utilization factor of the QSC network.

Operating a nationwide
Next Generation Network
and expanding the DSL
network on the last mile

Focusing on three
strategic lines of business:
Managed Services,
Direct Access and Wholesale

Expanding the Nationwide Network

Strong and profitable growth + Over the course of the past five years, QSC has grown its revenues more than fivefold and steadily improved its profitability from year to year. In the years to come, the Company anticipates sustained high growth rates and disproportionately rising profitability.
There are two reasons why this kind of dynamic is crucial for QSC: First of all, this is the only way the Company can secure and broaden its leading position in the fast-growing German broadband market. Size is a key competitive factor here, since the market is characterized by such factors as efficiency gains, heavy investments, and consolidation.
Secondly, only with rapidly rising revenues can QSC make full use of the advantages offered by a network of its own, and thus the profitability opportunities inherent in its scalable business model – even with rapidly rising revenues, the fixed costs for the nationwide network remain largely constant.

Nearly 2,000 offices by year-end 2007 + QSC's successes with enterprise customers are based upon its own nationwide Next Generation Network and the broadband infrastructure over the last mile. In its strategic business with large accounts, business customers, and wholesale/resellers, QSC will therefore be able to benefit from the swift expansion of its network by year-end 2007. With nearly 2,000 central offices, the Company will then be able to directly reach some 50 percent of all German households and some 70 percent of those locations involved in requests for IP-VPN proposals. This will significantly increase QSC's chances of winning requests for proposals for IP-VPN solutions. At the same time, it will also increase the Company's attractiveness as a partner in wholesale business. In the case of business customers, QSC will be able to broaden its opportunities for directly connecting small and medium-size businesses to its network.

Unique positioning
as a premium provider
for enterprise customers

Operating a nationwide
Next Generation Network
and expanding the DSL
network on the last mile

Focusing on three
strategic lines of business:
Managed Services,
Direct Access and Wholesale

Clear Profile as a Premium Provider

QSC stands for quality + In support of its strategy, QSC is pursuing two objectives during the current fiscal year: On the one hand, the Company wants to bond its Broadnet subsidiary even more closely to itself; the planned merger will be a crucial step in this connection. On the other hand, the Company wants to use a new image to underscore its premium positioning in the German market. Although most customers have for years seen QSC as a premium provider, the Company now wants to further enhance this profile and thus actively utilize its unique positioning as a high-quality provider in the enterprise customer market as a competitive advantage.
In the future, customers should be able to measure QSC's performance on the basis of the following four attributes: Security, State of the Art, Simplicity, and Carefree Customers.

+ **Security.** QSC customers can expect reliable 24x7 Internet access, secure voice and data transmission within an IP-VPN, around-the-clock network monitoring, and continuously available service. They should simply have the feeling that they are "well taken care of" at QSC.

+ **State of the Art.** This means that QSC's offerings will always feature cutting-edge technology and its customers will be able to benefit from forward-looking solutions. QSC is one of the first providers to possess a nationwide Next Generation Network, which it can use as the basis for offering a wide range of IP-based services at fair prices.

+ **Simplicity.** QSC stands for a new virtue in the telecommunications market. Against the backdrop of complicated rate plans and offerings whose technology is difficult to understand, QSC views the key to success as being products and services that can be deployed rapidly and operated without any problems.

+ **Carefree Customers.** QSC no longer wants its customers to have to give any thought to their telecommunications, but to be confident in placing this issue in the hands of QSC's specialists, who will manage it to their complete satisfaction. And in such a way that the customer can strengthen and optimize its own core business.

QSC organization
in its entirety aligning
to a clear value system

Unique positioning
as a premium provider
for enterprise customers

Operating a nationwide
Next Generation Network
and expanding the DSL
network on the last mile

Focusing on three
strategic lines of business:
Managed Services,
Direct Access, and Wholesale

A Strong Team with Clear Values

Implementing the strategy from within + QSC's premium positioning necessitates that the entire organization be aligned to these kinds of quality and service expectations. The Company has formulated the way its sees itself in the form of four guiding principles.

+ **We are here to serve the customer.** The sole yardstick for QSC's performance is the way it values the customer. Carefree customers are the corporate objective.

+ **We are a strong team.** Success with the customer is the success of all of our people. QSC rigorously embraces fair, open, and trustful dealings with both internal and external counterparts, and fosters collaboration in a spirit of partnership at all levels.

+ **We live communication.** Good team performance is based upon clear, conscious, and specific communication that is typified by mutual respect. This is the kind of communication culture that characterizes a premium provider.

+ **We create values.** QSC gives each and every employee a high degree of responsibility. Their decisions are always guided by the objective of generating sustained profitability, thus assuring that the interests of the Company's customers and shareholders are in alignment.

QSC rigorously implements these guiding principles in its day-to-day business, because this is the only way that QSC can sustain its strong and profitable growth over the long term, and also smoothly integrate its acquisitions. These guiding principles serve as a kind of navigation system in integrating Broadnet AG, in which QSC acquired a majority interest in 2006, along with its nearly 190 people. And these guiding principles mandate a common value system for all employees in both companies.

Group Management Report for the 2006 Fiscal Year

In 2006, QSC rose its revenues by 35 percent, nearly grew its EBITDA fourfold and earned its first quarterly net income in Q4. For the current fiscal year, QSC plans on revenues of more than € 350 million as well as a net profit of between € 15 million and € 25 million.

QSC Reaches Profitability Zone

Quarterly net profit of € 2.8 million in the fourth quarter of 2006

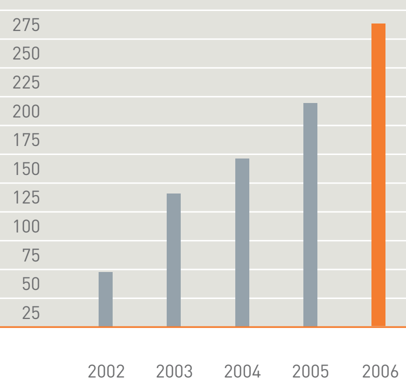
Improved revenue quality + During the past fiscal year, QSC grew its revenues by 35 percent to € 262.5 million, as opposed to € 194.4 million the year before. QSC recorded its strongest growth in business with wholesale/resellers, with revenues in this segment rising by 115 percent over the year before to € 65.4 million. This growth also stemmed from the successful launch of marketing for DSL lines through strong wholesale partners like HanseNet and freenet in 2006. Strong growth is also what characterized the Large Accounts and Business Customers segments, where 2006 revenues advanced by 27 percent to € 65.5 million for large accounts and by 31 percent to € 75.5 million for business customers. Within the course of the year, QSC thus increased the percentage of its total revenues in the strategic segments of Large Accounts, Business Customers and Wholesale/Resellers from 72 percent to 79 percent.

This significantly better revenue quality resulted in disproportionately high improvements in profitability. QSC grew its EBITDA to € 21.2 million in 2006, as opposed to € 5.8 million in 2005. The Company's net loss improved to € 5.3 million, as opposed to € -18.2 million in 2005. Sustaining its steady improvement in profitability, QSC earned its first quarterly net profit of € 2.8 million in the fourth quarter of 2006.

This strong growth stems from the Company's nationwide telecommunication infrastructure. At year-end 2006, the DSL network comprised more than 1,200 central offices. Network operating company Plusnet, which was formed in the summer of 2006, will be expanding this network to nearly 2,000 central offices by the end of this year. It will then be operating one of the largest DSL networks in Germany.

This network expansion will offer QSC further growth potential. The Company is planning revenue growth to more than € 350 million in 2007, along with an improvement in its EBITDA to between € 50 milllion and € 60 million and a net profit of between € 15 million and € 25 million.

Revenues (in € million)



Geared for Growth

BUSINESS OPERATIONS

Broadband communication for enterprises + QSC is a nationwide telecommunication provider with its own infrastructure and offers enterprise customers throughout Germany the entire spectrum of high-quality broadband communication – from complete site networking (IP-VPN) including managed services right through to the provision of voice and data services. The Company operates in three strategic segments in this connection:

+ **Large Accounts.** QSC offers corporates and medium enterprises direct, one-stop shopping for custom-tailored, high-quality telecommunication solutions. These managed services typically build upon IP-based virtual networks that are built and operated by QSC. In addition, the Company also offers a broad portfolio of add-on services. In this connection, QSC handles both network-based services, like the connection and hosting of customer servers, as well as operating and maintaining local infrastructures (LAN services), on the one hand. On the other, QSC also offers application-based services, such as ensuring high security standards, operating telephone systems, as well as hosting customer applications.

+ **Business Customers.** With products from QSC, both small and medium-size businesses as well as freelance professionals can operate all of their voice and data communication over one and the same broadband line. The spectrum of offerings ranges from broadband Internet connections and direct connections to the QSC voice network right through to standardized security modules. QSC works closely with regional marketing partners in providing sales support for business customers.

+ **Wholesale/Resellers.** A growing number of Internet service providers and telecommunication providers who do not possess infrastructures of their own are marketing DSL lines from QSC and the add-on services that build upon them under their own name and for their own account. Wholesale business, in which partners with mass-market experience handle marketing of DSL lines offering ADSL2+ speed to residential customers, is posting especially strong growth.

Moreover, QSC is also active in the Residential Customers segment with voice and data products. These offerings serve first and foremost to provide better network utilization outside customary business hours, with data services primarily addressing premium customers with their corresponding quality expectations.

The offerings in all segments are based upon QSC's nationwide infrastructure. The Company possesses a Next Generation Network, which enables nationwide utilization of Voice over IP technology throughout the entire network. Over the last mile, Plusnet, a network operating company that was formed in 2006 together with TELE2 as a minority shareholder, operates a nationwide DSL network that has been upgraded to ADSL2+ technology. The acquisition of a majority interest in Broadnet during 2006 affords the QSC Group access to a Wireless Local Loop in 42 regions.

Cutting-edge infrastructure at the core of QSC's scalable business model

This cutting-edge infrastructure serves as the core of QSC's scalable business model. As long as this infrastructure is not fully utilized, the Company can directly connect new customers without the need for any corresponding network expenses; at the moment, the network is operating at around 30 percent of line capacity on average. As a result, each additional euro in revenue generates above-average growth in profitability.

RESEARCH AND DEVELOPMENT

Broadband necessitates ongoing innovation + Broadband technology is one of the centerpieces of modern information and communication technology, thus making it a key technology of the 21st century. It is characterized by an ongoing innovation process, which the majority of users see in the form of higher bandwidths and new products.

For providers like QSC who specialize in enterprise customers, though, innovation primarily means innovations in quality and processes, as well as the development of additional network-related services. These innovations assure smooth migration of complex customer IT and telecommunication systems to the QSC world, and serve as a key prerequisite for sustained collaboration in a spirit of trust.

QSC repeatedly develops new products on the basis of these kinds of projects. At CeBIT 2006, for example, the Company presented VirtuOS, a virtual office application that opens up professional call management at attractive prices for business of every size. Last summer, the Company brought QSC-Mailsecurity to market, which offers easy-to-install, network-based protection against spam and viruses. Shortly afterwards, QSC enhanced its Voice over IP product portfolio to include the IPfonie 2006 client, which for the first time permits integration of video telephony.

The key role that is played by innovations and the way they are integrated into customer projects can also be seen from the organizational structure of research and development operations at QSC: New ideas are not developed by a separate, dedicated department, but instead are a central task for all employees. Especially in connection with process innovations, staff from sales and marketing and technology operations collaborate closely in order to ensure that customers receive premium service.

ORGANIZATIONAL STRUCTURE

Focus on core competencies + The dynamics of the markets and the resulting growth potential this offers necessitate a high degree of flexibility and integration power on the part of the QSC organization. In this connection, the Company has traditionally focused on its core competencies in technology and sales and marketing operations, while collaborating in a spirit of partnership with service providers in the upstream and downstream links in the value chain.

QSC AG is the parent corporation of the corporate group. It does business in the strategic segments of Large Accounts, Business Customers and Wholesale/Resellers. 430 people at both corporate headquarters in Cologne and in branch offices throughout Germany support businesses of every size, from initial contract and the development of custom-tailored IP-VPN solutions right through to billing of services. Part of the QSC team also consists of the employees of telephone provider Ventelo GmbH, which was acquired in late 2002, as well as of DSL provider celox Telekommunikationsdienste GmbH, which was acquired in 2005. In both cases, the QSC organization has proven how well and swiftly it is able to manage integration processes. QSC's corporate principles serve as the guidelines and as a kind of navigation system in connection with decision-making processes.

celox and Ventelo prove QSC's integration capabilities

One major equity investment consists of publicly traded Broadnet AG, in which QSC acquired a majority interest in June 2006. With its workforce of some 190 people, Broadnet also focuses on DSL business with enterprise customers. In January 2007, QSC announced that it intends to merge this subsidiary with the parent corporation in order to enable it to be legally and organizationally integrated.

A further major equity investment consists of network operating company Plusnet GmbH & Co. KG. The nearly 60 Plusnet employees operate a nationwide DSL network on behalf of shareholders QSC and TELE2, which they intend to expand to nearly 2,000 central offices by year-end 2007. Located at QSC headquarters in Cologne, this company provides basic DSL services exclusively to its two shareholders on a cost basis; the two shareholders then enhance these DSL preliminaries for their respective target groups and market them.

Q-DSL home GmbH is where QSC has consolidated its DSL residential customer business. Its spin-off into an autonomous organization in 2006 underscores QSC's own focus on strategic business with enterprise customers.

MANAGEMENT

Entrepreneurialism + QSC's business is managed by a three-member Management Board under the leadership of cofounder Dr. Bernd Schlobohm, who through his personal involvement represents the highly entrepreneurial spirit throughout the entire organization. The Compensation Report, which is an integral part of the Group Management Report, informs about the compensation of the Management Board. An approximately 20-person second management tier is responsible for operating business. A six-member Supervisory Board monitors the activities of the Management Board and advises it in an ongoing dialog.

QSC's operating business is divided into four segments. The Company employs the respective segment EBITDA, which is calculated as the respective net revenues less all costs directly attributable to that segment, as the key management parameter. EBITDA is also the central management parameter at the group level. QSC defines EBITDA as earnings before interest, taxes, amortization of deferred non-cash share-based payments, as well as depreciation and amortization on property, plant and equipment, and goodwill.

QSC reviews the profitability of new products and projects on the basis of multitier contribution margin calculations. These are structured analogously to the respective segment reporting, thus ensuring that decisions are made with a view to anticipated target margins.

GENERAL ECONOMIC CONDITIONS

Telco providers also benefit from increased willingness to invest

Growth spurt in Germany + Following years of low or even declining economic growth, the German economy developed on an unexpectedly positive note in 2006. Growing at 2.7 percent, gross domestic product rose faster than at any time since the year 2000. In addition to the country's traditionally strong exports, domestic capital spending increasingly proved to be the growth driver. The volume of capital investment rose by more than five percent, thus posting the highest growth rates since reunification. Telecommunication providers also benefited from this dynamic, as businesses of every size increasingly invested in modern broadband infrastructure.

Overall, revenues in the telecommunications industry in Germany rose by two percent to € 69 billion during the past fiscal year according to calculations from the German Association of Providers of Telecommunications and Value-Added Services (VATM). In this connection, alternative providers like QSC won further market share and for the first time generated more than one half of the industry's revenues.

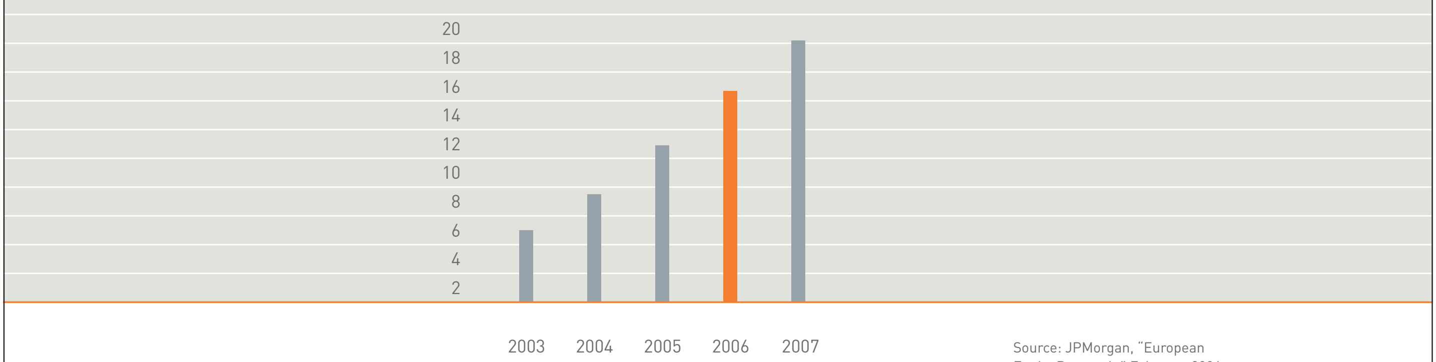
GENERAL INDUSTRY CONDITIONS

Germany a DSL country + Broadband business was again the key growth driver for the telecommunications industry last year. According to information from industry association BITKOM, one out of every three German households already had a DSL connection in the autumn of 2006, with this percentage expected to rise to 50 percent by year-end 2008. According to market research institute IDC, the corresponding expenditures are expected to rise from € 3.0 billion in 2006 to € 4.1 billion. QSC is benefiting from this rising demand primarily in its wholesale business with partners like HanseNet, freenet, and others who possess mass-market experience.

Demand for broadband is growing, especially as a result of the increasing selection of videos, television programming and games on the Internet; instead of lines with speeds of 1 or 2 megabits per second (Mbit/s), lines offering speeds of up to 16 Mbit/s are now increasingly being employed. These kinds of bandwidths can be offered by the ADSL2+ technology with which QSC has upgraded its network. ADSL2+ also enables one-stop shopping for Internet, telephony, and television over one and the same broadband line, i.e. Triple Play. Market observers are convinced that this convergence of telecommunications and media will meet with growing demand in the coming years. This Triple Play capability and the high bandwidths offered by ADSL2+ make QSC a preferred wholesale partner for providers who do not possess their own infrastructure in Germany.

In 2008, half of all German households will have DSL access

Broadband Connections in Germany (in millions)



Source: JPMorgan, "European Equity Research," February 2006

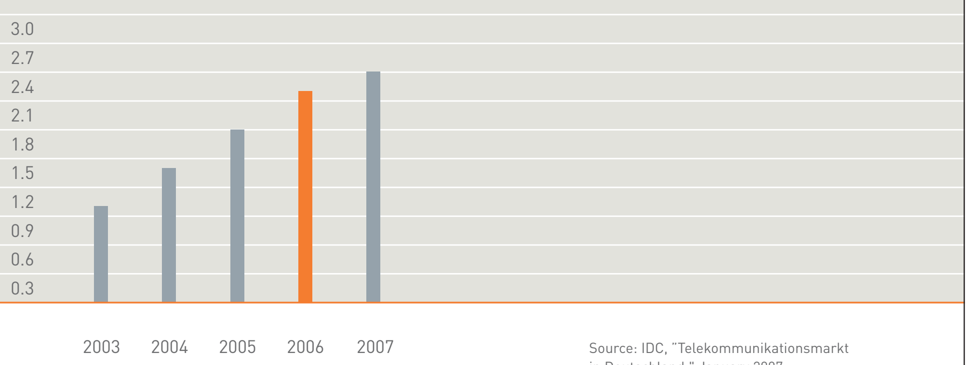
Little room for alternative technologies + The high availability of DSL leaves little room in Germany for alternative broadband technologies like cable television or wireless. In 2006, some 95 percent of all broadband accesses in Germany were DSL connections. And IDC predicts that this dominance will be sustained in the years to come.
In the opinion of QSC, wireless technologies like Wimax, WLAN or Wireless Local Loop (WLL), on the other hand, could represent a good supplement to DSL in regions not covered by this network. With the acquisition of its majority interest in Broadnet, QSC also acquired a WLL network in 42 German regions, and can thus now connect enterprise customers directly to its network within the corporate group, especially on the outskirts of metropolitan areas.

Enterprises opting for DSL + DSL technology is the dominant broadband technology at enterprises of every size in Germany: Within the space of one year, the number of DSL connections rose by 22 percent to 2.2 million, with the corresponding revenues totaling € 1.7 billion.
The strong growth of DSL technology at enterprises is essentially attributable to two factors: On the one hand, the number of Internet-based applications – from purchasing to logistics to sales and marketing – is on the rise, and thus the demand for bandwidth. On the other hand, a growing number of enterprises are using DSL in conjunction with Voice over IP technology in order to integrate their voice and data communication over one and the same line.

VoIP revenues to cross billion euro mark for the first time in 2007

The penetration of VoIP in the enterprise environment is documented by data from market researcher IDC. This shows that the number of VoIP-based connections at German enterprises of every size rose by 0.8 million to 2.4 million in 2006. IDC anticipates a further increase to 3.6 million during the course of 2007. According to this study, telecommunication providers will be able for the first time to record VoIP revenues totaling more than one billion euros.

Broadband Connections at Enterprises in Germany (in millions)



Source: IDC, "Telekommunikationsmarkt in Deutschland," January 2007

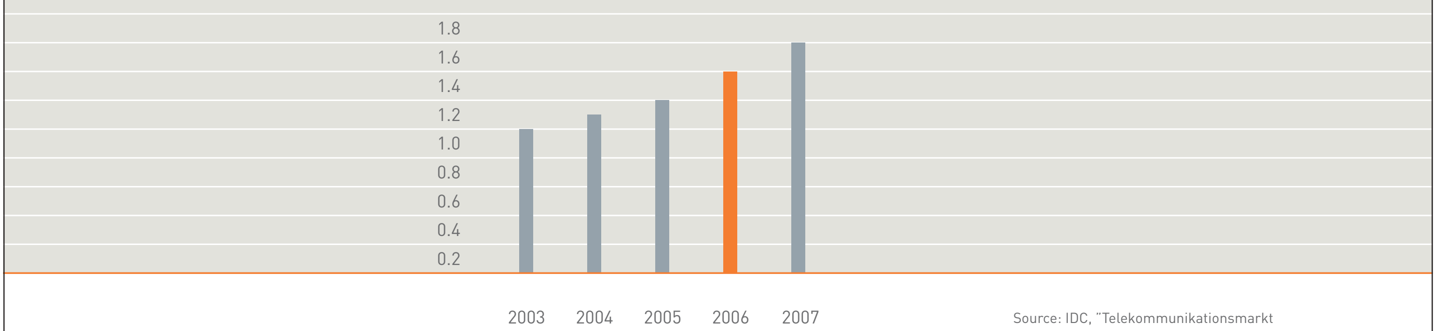
Managed services business rises sharply + The integration of VoIP is also proving to be one of the growth drivers in managed services business, i.e. the business in connection with virtual private networks (IP-VPN) as well as the corresponding add-on services. According to IDC, the IP-VPN market alone reached a total volume of € 1.4 billion in 2006, in addition to revenues in connection with network-related add-on services in the amount of nearly € 100 million – with revenues in this sector alone expected to quadruple by 2010.

This growing complexity of core business processes, and their transfer to telecommunication providers that this is bringing with it, is leading to a situation in which enterprise customers use multiple decision-making factors in opting for a provider: What also count, in addition to price, are quality, customer service, and solutions competence, as well as the size and security of the network. Competition on the basis of price alone, as can be observed in connection with residential customers, therefore does not occur to this extent in business with enterprise customers, nor would that be expected.

Due to the high expectations among customers, QSC additionally sees only a limited number of competitors in business with enterprise customers. This is because high quality and a competitive cost structure can ultimately only be achieved on the basis of a provider's own nationwide infrastructure; in addition, only complete control of the network enables custom-tailored solutions to be offered. QSC possesses one of the largest German DSL networks, and additionally enjoys a convincing competitive position with its clear focus on complex enterprise customer business. This enables QSC to make a particular contribution towards enhancing the productivity of both large and medium-sized businesses.

QSC contributes to enhanced productivity in businesses

Managed Services Market in Germany (in € billion)



Source: IDC, "Telekommunikationsmarkt in Deutschland," January 2007

Three attractive markets for the strategic segments + Strong growth is what characterizes all of the submarkets that are of relevance for QSC. In its solutions business with large accounts, the Company is benefiting from significantly rising demand for managed services on the basis of IP-VPN solutions. In its product business with business customers, there is growing demand for both DSL connections as well as for VoIP services. And in its wholesale business, QSC is participating in the unabatedly strong interest in DSL connections on the part of residential customers.

EVENTS OF MAJOR SIGNIFICANCE

Strong growth dynamic + QSC's operating business continued to be characterized by a strong growth dynamic in 2006. As planned, the strategic segments in particular contributed to this development. Nevertheless, the course of business was significantly impacted by two individual events during the past fiscal year: The acquisition of a majority interest in Broadnet AG and the formation of Plusnet GmbH & Co. KG.

Acquisition of majority stake in Broadnet through share swap increases equity

Acquisition of the majority interest in Broadnet AG + During the course of 2006, QSC acquired a total of 92 percent, or 14.9 million shares, of publicly traded Broadnet AG through a share swap. In June 2006, the former main shareholders and management of this company received 1.0542 share of QSC stock for each of their 10,654,555 Broadnet shares. Broadnet shareholders also utilized the same swap ratio for 217,847 of their shares in conjunction with the acquisition offer that ran from July 22 through September 29. In November 2006, QSC was able to acquire a further package of 4 million shares from institutional investors, with the swap ratio here ranging between 1.0542 and 1.23 share of QSC stock per Broadnet share, depending upon the occurrence of agreed conditions. To execute this transaction, QSC increased its capital stock by a total of € 16.4 million during the past fiscal year; the Company issued 16,381,831 shares from authorized capital against contributions in kind, with the right of subscription being excluded.
With its majority interest in Broadnet, QSC is strengthening its high-margin business with enterprise customers; in 2006, this Hamburg-based broadband provider generated more than 90 percent of its revenues with enterprise customers, earning an EBITDA of € 5.6 million, as opposed to € 4.6 million the year before.

Formation of network operating company Plusnet + In July 2006, QSC and the German subsidiary of the TELE2 group, Düsseldorf-based Communication Services TELE2 GmbH, formed Plusnet GmbH & Co. KG. Following approval by the German Cartel Office, Plusnet has been operating a nationwide DSL network of over 1,000 central offices since September 1, 2006. QSC contributed its DSL network to the new company for its Plusnet holdings of 67.5 percent, while TELE2 made a € 50 million cash contribution to finance further expansion of the network and holds 32.5 percent of the shares. The new network operating company will provide DSL preliminaries to its two share-holders at cost.

Plusnet will be expanding its DSL network to nearly 2,000 central offices by year-end 2007, at which time it will then be operating one of the largest broadband networks in Germany. This will afford QSC direct access to some 50 percent of all German households as well as to some 70 percent of those locations involved in requests for proposals for IP-VPN solutions. This expanded direct access will significantly strengthen QSC's competitive position in its strategic segments.

Expanded Network strengthens QSC's competitive position in its strategic segments

COMPARISON BETWEEN ACTUAL AND FORECAST COURSE OF BUSINESS

QSC meets forecasts + At the outset of the year, QSC had used three key performance indicators to illustrate its outlook for the 2006 fiscal year: Revenues were to rise to more than € 240 million, EBITDA was to reach between € 15 million and € 20 million, and capital expenditures were to total between € 20 million and € 25 million. Moreover, QSC planned to also reach the net profit threshold by year-end.

The improved revenue quality, thanks to growth in its strategic segments, along with the acquisition of a majority interest in Broadnet, necessitated that the forecast be updated twice during the course of the year. Most recently, the Company had anticipated revenues of nearly € 265 million as well as an EBITDA of between € 17 million and € 22 million, and it achieved this forecast. Earlier than had originally been expected, QSC reported a net profit in the fourth quarter of 2006.

The formation of Plusnet and the beginning of the expansion to nearly 2,000 central offices in particular, also led to an acceleration in the pace of capital expenditures in 2006, with QSC investing a total of € 40.1 million during the course of that year.

GENERAL REMARKS REGARDING THE COURSE OF BUSINESS

Strong and profitable growth in 2006 + QSC sustained its strong and profitable growth in the dynamically developing German broadband market for enterprise customers in 2006. With revenues of € 262.5 million, an EBITDA of € 21.2 million, as well as its first net profit in the fourth quarter of 2006, the Company succeeded in achieving its ambitious goals. The growth drivers proved to be the three strategic segments of Large Accounts, Business Customers, and Wholesale/Resellers. The acquisition of a majority interest in Broadnet AG, which also focuses on enterprise customers, serves as an ideal complement to the Company's operations and is opening up further growth potential for QSC for the current fiscal year. New potential will also stem from the accelerated expansion of the network by subsidiary Plusnet. Expansion of the DSL network to nearly 2,000 central offices by year-end 2007 will strengthen QSC's competitive position in all strategic segments.

Revenues and Profitability up Significantly

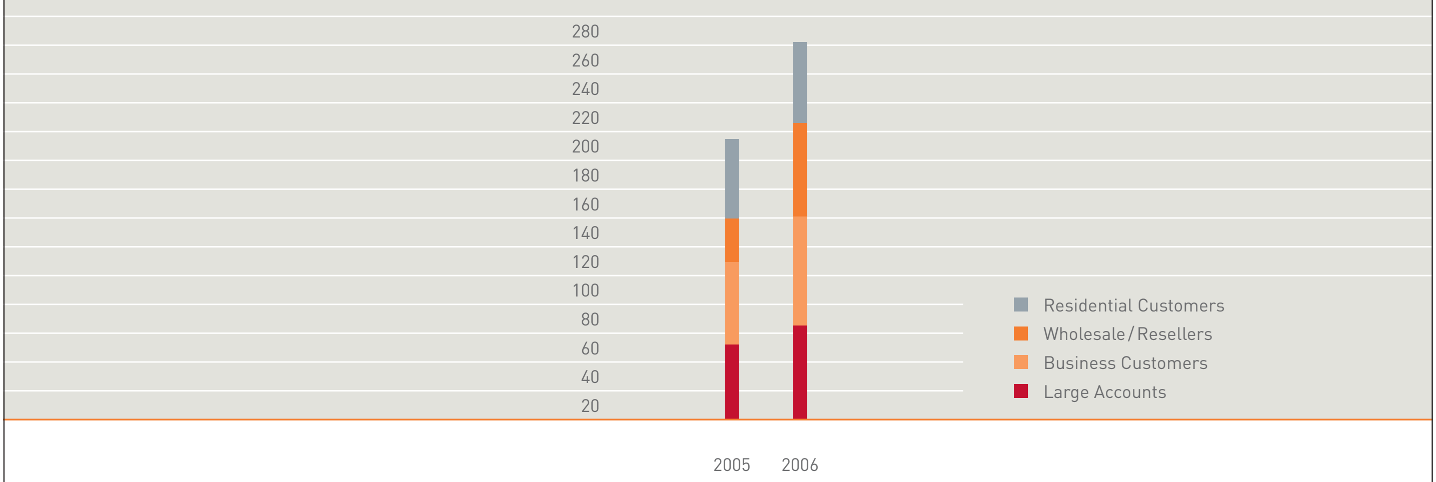
PROFITABILITY

Strong revenue growth + During the past fiscal year, QSC grew its revenues by 35 percent to € 262.5 million, as opposed to € 194.4 million the year before. The Company recorded its highest growth rates in business with wholesale/resellers, where revenues also rose by 115 percent to € 65.4 million as a result of the successful launch of marketing for DSL lines by wholesale partners with strong brands like HanseNet and freenet. Strong growth is what also characterized business with large accounts and business customers, while revenues in non-strategic business with residential customers remained virtually unchanged from the year before. This enabled QSC to further significantly increase the quality of its revenues during the past fiscal year. In 2006, the Company was already generating nearly 80 percent of its revenues in its three strategic segments.

Strong growth in all of the three strategic segments

Moderate rise in network expenses + Network expenses, which are recorded under cost of revenues, including depreciation and non-cash share-based compensation, rose by only 23 percent to € 203.6 million in 2006, as opposed to € 165.5 million the year before – during the same period, revenues rose by 35 percent.

Revenue Mix (in € million)



The disproportionately low rise in network expenses relative to revenues was essentially attributable to their composition. Approximately 40 percent of these expenses consist of fixed costs for building, operating and maintaining the Company's nationwide infrastructure, including the corresponding personnel expense and depreciation. These fixed costs remain largely constant as revenues rise, as long as this infrastructure is not being fully utilized – only around 30 percent of line capacities are currently being utilized.

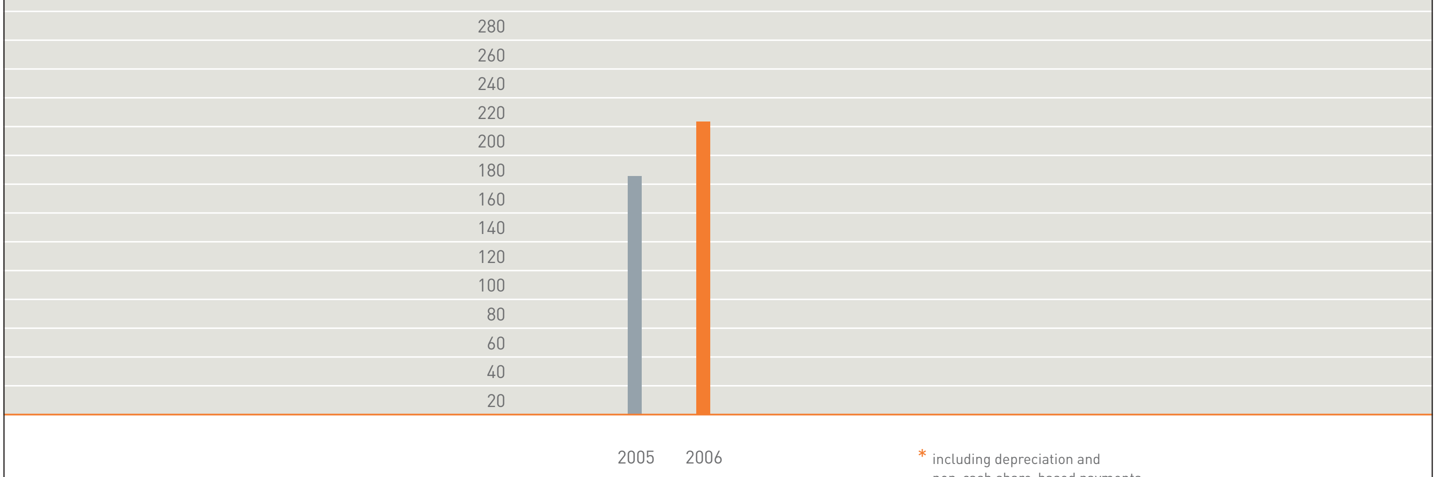
Consequently, the cost of building, operating and maintaining the network rose by only 8 percent to € 37.0 million during the past fiscal year. On the one hand, the initial consolidation of Broadnet; which at the time of its acquisition had been operating its own broadband network with nearly 600 central offices, led to a non-recurring rise in this line item. On the other hand, however, the migration of the entire infrastructure to a cost-effective Next Generation Network led to considerable savings during the course of 2006.

Considerable savings through migrating the network to an NGN

The personnel expense for building, operating and maintaining the network rose by 15 percent in 2006 to € 11.3 million.

In addition, one fixed element of network expenses consists of depreciation. In contrast to its quarterly reports, QSC includes depreciation in the respective expense line items in its Annual Report. In 2006, depreciation expense in connection with network expenses rose moderately by 6 percent to € 23.1 million as a result of the Broadnet consolidation.

Network Expenses* (in € million)



* including depreciation and non-cash share-based payments

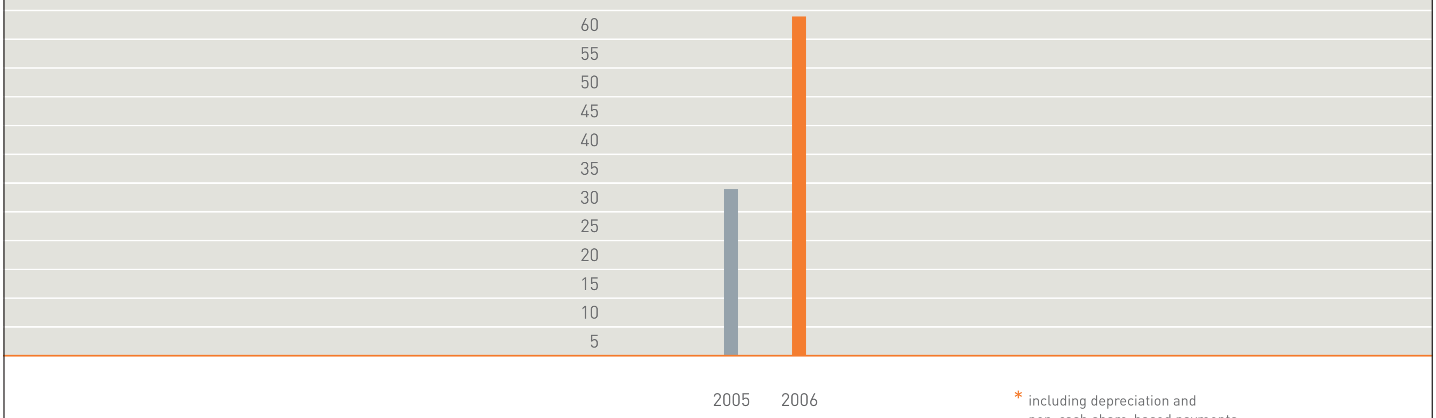
In contrast, around 60 percent of network expenses are attributable to the variable cost of materials; as a result of strongly rising revenues, these costs increased by 22 percent in 2006 to € 121.9 million. Cost of materials includes all customer-related costs. In particular, these include the ongoing fees that competitors have to pay to Deutsche Telekom for utilization of the unbundled last mile. Along with QSC's growing success in the marketplace, there was also a rise in expenses for customer-specific leased lines as well as interconnection fees.

Gross profit doubles + The moderate rise in network expenses by comparison with revenues due to the high percentage of fixed costs documents the scalability of QSC's infrastructure-based business model – rising revenues here do not correlate to corresponding increases in costs, thus enabling disproportionately high profitability growth. Gross profit, including depreciation and non-cash share-based payments, thus rose by 104 percent to € 58.9 million in 2006, as opposed to € 28.9 million the year before.

QSC's infrastructure-based business model is scalable

Highly efficient sales force + During the past fiscal year, selling and marketing expenses rose by 41 percent to € 43.1 million, as opposed to € 30.5 million the year before. During the course of 2006, QSC continued on schedule in expanding its sales and marketing organization in its strategic segments; as a result of this and the initial Broadnet consolidation, personnel expenses increased by 26 percent to € 16.6 million.

Gross Profit * (in € million)



* including depreciation and non-cash share-based payments

While QSC directly addresses and supports large accounts and wholesale/resellers exclusively itself, it predominantly collaborates with strong regional sales and marketing partners in connection with business customers. In 2006, the growing successes of these partners resulted in an increase in commission payments to € 12.5 million, as opposed to € 7.8 million the year before.

High efficiency through addressing customers directly

The high efficiency of addressing customers directly is underscored by the fact that advertising expenses continue to remain at a low level. During the past fiscal year, QSC spent € 2.7 million, predominantly on direct marketing activities – barely one percent of revenues.

Lean administration + In particular as a result of the Broadnet consolidation, general and administration costs rose by 51 percent to € 25.5 million in 2006, as opposed to € 16.9 million the year before. QSC is currently maintaining two administrations in its Hamburg and Cologne locations, with all of the functions required at publicly traded companies. In addition, administration expenses in 2006 also contained depreciation in the amount of € 3.0 million; included in this total were special depreciation allowances on previously capitalized telecommunication licenses. Due to the changeover in the way the German Federal Network Agency (Bundesnetzagentur) is financed from its former license model to a current contribution model, there is no further need for the corresponding licenses to be capitalized.

Broadband is process innovation + As in previous years, research and development expenses remained negligible at € 0.2 million in 2006, as opposed to € 0.4 million in 2005. These expenses essentially include the costs of developing new products, but not the development expenses incurred in connection with QSC's numerous process innovations. Research and development expenses therefore do not represent a suitable yardstick for adequately reflecting the Company's innovative strength in connection with ongoing processes and services.

New fee model for the Federal Network Agency triggers non-recurring effect + Other operating income rose to € 2.9 million in 2006, as opposed to € 0.6 million the year before. This rise stemmed, in particular, from the release of provisions for outstanding payments to the Federal Network Agency (Bundesnetzagentur) for telecommunication licenses. Since 2006, this agency has been financing itself from a telecommunication contribution, a levy on all market players, thus eliminating the reason for forming the provision.

Positive development of operating business + In its quarterly reports, QSC conforms to the customary international practice of presenting depreciation, amortization and non-cash share-based payments as a separate line item in its income statement. In these Consolidated Financial Statements, however, depreciation, amortization and non-cash share-based payments are included in the line items for network, general and administration, selling and marketing as well as research and development expenses. The following abbreviated income statement presents depreciation and amortization separately, thus affording a fast overview of the development of the Company's operating business:

	2006 in T €	2005 in T €
Net revenues	**262,522**	**194,387**
Cost of revenues *	(180,422)	(143,670)
Gross profit	**82,100**	**50,717**
Selling and marketing expenses *	(41,392)	(29,397)
General and administrative expenses *	(22,067)	(15,544)
Research and development expenses *	(207)	(324)
Other operating income	2.891	586
Other operating expenses	(158)	(261)
EBITDA	**21,165**	**5,777**
Depreciation	27,650	24,408
Non-cash share based payments	691	35
Operating loss (EBIT)	**(7,176)**	**(18,666)**

* excluding depreciation and non-cash share-based payments

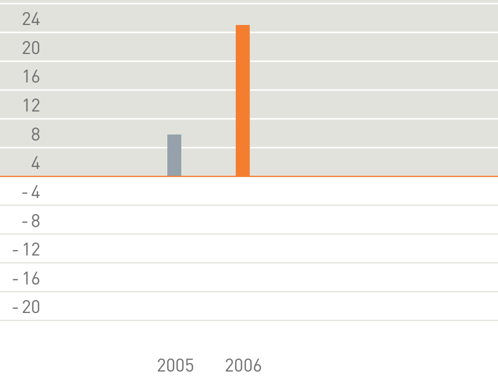
Strong growth in operating result + During the past fiscal year, QSC succeeded in nearly quadrupling its EBITDA, which rose from € 5.8 million in 2005 to € 21.2 million. Depreciation during the past fiscal year increased to € 27.7 million, as opposed to € 24.4 million the year before. Nevertheless, QSC was able to also significantly improve its operating result before taxes, its EBIT. At € -7.2 million, EBIT improved by € 11.5 million over its previous year's level of € -18.7 million.

First net profit in the fourth quarter of 2006 + Analogously to its EBIT, QSC was also able to significantly improve its net loss in 2006: At € -7.2 million before income taxes, it was almost a strong two-thirds lower than the previous year's level of € -18.2 million.
The initial capitalization of deferred taxes in 2006 amounted to € 1.9 million, leading to a net result of € -5.3 million after income taxes, as opposed to € -18.2 million in fiscal 2005. During the same period, earnings per share improved to € -0.04, as opposed to € -0.17 the year before.

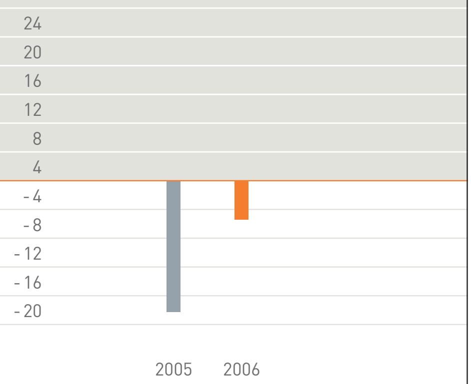
Leap in revenues and profitability in the fourth quarter of 2006

As a result of the steady improvement of its profitability during the course of the year, QSC was able to earn its first net profit in the amount of € 2.8 million in the fourth quarter of 2006 – during the corresponding period the year before, it had recorded a net loss of € -4.4 million. QSC earned an EBITDA of € 9.5 million on quarterly revenues of € 83.1 million.

EBITDA (in € million)



Net Loss (in € million)



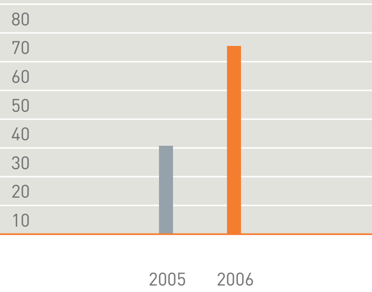
PROFITABILITY BY SEGMENT

Strong growth rates with wholesale/resellers + In 2006, QSC generated its strongest revenue growth in the Wholesale/Reseller segment, where revenues rose by 115 percent over the previous year to € 65.4 million. This extremely strong growth can be seen from a sequential quarter-to-quarter comparison over the course of the year: While revenues with wholesale/resellers had stood at € 7.6 million in the first quarter of 2006, they had already reached a level of € 28.9 million in the fourth quarter of 2006.
Wholesale business in particular, which had only been launched in late 2005, proved to be a growth driver over the course of the year. Providers with mass-market experience, like HanseNet, with its Alice brand, and freenet, marketed DSL lines from QSC offering speeds of up to 16 Megabits per second under their own names and for their own accounts.
Reseller business with telecommunication providers who do not possess their own nationwide infrastructure in Germany also developed on a positive note. Companies like BT Global Services, Colt and Equant often use QSC's lines in Germany in connection with global enterprise networking. Moreover, QSC's Next Generation network also afforded profitable expansion of business with resellers of voice services.
Following the exceptionally strong growth in the past fiscal year, the segment EBITDA rose by € 19.9 million to € 32.8 million in 2006, with the corresponding margin improving to 50 percent, as opposed to 42 percent the year before. In this connection, reseller business has traditionally offered even higher margins than wholesale business.

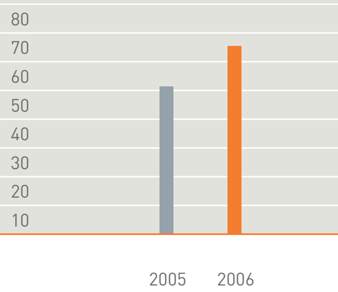
Significantly improved profitability and margin with wholesale/resellers

Successes with new and existing large accounts + The enormous growth potential that is offered by business with resellers and the establishment of wholesale business led to a concentration of in-house resources in this segment in 2006. In spite of that, though, QSC was also able to significantly increase its revenues in the Large Account segment by 27 percent; in 2006, these revenues totaled € 65.5 million, as opposed to € 51.4 million the year before.

Revenues Wholesale / Resellers (in € million)



Revenues Large Accounts (in € million)



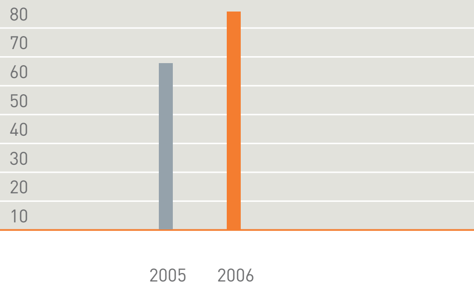
QSC achieved successes both in connection with new requests for proposals for site networking of large and medium-sized customers as well as in expanding the budgets of existing customers. In May 2006, for example, the Company received a contract from TOYS'R'US, one of the world's largest toy retailers, to build an IP-VPN in order to network its corporate locations in Germany, Austria and Switzerland. QSC is also operating this network and securing it by means of an intelligent backup solution. More and more customers expect this kind of combination of site networking and add-on services – thanks to the establishment of managed services business early on, QSC is very well positioned here.
Around 40 percent of revenue growth stemmed from add-on contracts from existing customers. In recent years, QSC has been more and more frequently serving as a second source in connection with large, nationwide site networking projects, i.e. as a second, additional supplier. As a result of QSC's security, service and flexibility, these customers are now contracting with QSC for additional sites and services.

In 2006, highest EBITDA margin in large account business again

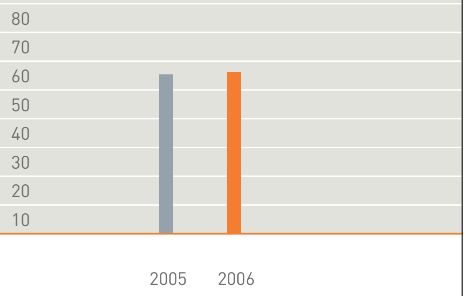
An EBITDA margin of 59 percent underscores the unbroken profitability of this segment. In absolute terms, the segment EBITDA rose to € 38.9 million during the past fiscal year, as opposed to € 33.0 million the year before.

Business customers the largest segment + Accounting for 29 percent of total revenues, product business with small and medium-size companies was again the segment with the highest revenues in 2006 – revenues with business customers rose to € 75.5 million, as opposed to € 57.5 million in 2005. This 31-percent growth was fueled, in particular, by the growing demand for integration of voice and data services over one and the same broadband line using Voice over IP technology; QSC's IPfonie products proved to be highly successful in the marketplace, especially in combination with the Company's Q-DSLmax data product.
Like QSC-Direct, the direct connection to the voice network, this broadband data product saw growing demand in the marketplace. In connection with expansion of the network, QSC will additionally be able to migrate preselection customers into direct customers in its telephone business, thus increasing both margin as well as customer loyalty.

Revenues Business Customers (in € million)



Revenues Residential Customers (in € million)



Overall, the EBITDA margin in the Business Customers segment stood at 52 percent in 2006 and therefore, as the other strategic segments Large Accounts and Wholesale/Resellers, at 50 percent or more. In absolute terms, the segment EBITDA rose to € 39.7 million in 2006, as opposed to € 23.5 million the year before.

High-margin revenues with residential customers + Revenues in the non-strategic Residential Customers segment remained virtually unchanged in 2006 at € 56.1 million, as opposed to € 55.1 million the year before. In this segment, too, QSC benefited from the growing demand for its IPfonie Voice over IP product. In addition, more and more customers are combining this product with the Q-DSL home premium data product, thus enabling them to eliminate the need for their conventional telephone connection. In classical voice business, the conclusion of the migration of the network to an NGN enabled call-by-call business to be expanded in the fourth quarter of 2006, without foregoing margin – the NGN enables high volumes of voice traffic to be handled cost-efficiently. These kinds of offerings have traditionally enabled QSC to provide better utilization of its network during the evening and nighttime hours, when enterprise customers are making hardly any use of the nationwide infrastructure.

More and more residential customers make calls via Voice over IP by QSC

This focus on high-margin revenues is what governs QSC's approach in the residential customer market with its fierce price competition. The Company takes care to assure that it will earn significant contribution and profit margins in connection with each and every offering and each and every product. This enabled the Company to maintain its EBITDA in this segment at a virtually constant level at € 16.7 million, as opposed to € 17.5 million in 2005; the corresponding margin was at 30 percent.

FINANCES

Sharp rise in cash flow from operating activities + The positive development of the Company's operating business during the past fiscal year is also reflected in its cash flow statements: QSC earned a cash flow from operating activities of € 11.7 million, as opposed to € 2.7 million the year before. On the other hand, the accelerated pace of capital spending resulted in a cash flow from investing activities of € -36.4 million, as opposed to € -17.8 million in 2005. In particular, the capital contribution to Plusnet from co-owner TELE2 led to a positive cash flow from financing activities of € 40.3 million.

Liquid assets nearly double + Totaling € 108.9 million as of December 31, 2006, QSC possessed nearly twice as much in liquid assets as the year before; on December 31, 2005, liquid assets had stood at € 56.4 million. QSC invests liquid assets in fixed-interest securities only. The Company records cash and cash equivalents as well as available-for-sale financial assets as liquid assets. The increase during the past fiscal year was essentially attributable to the capital contribution to Plusnet from TELE2, to the initial consolidation of Broadnet, as well as to the positive development of operating business.

QSC remains virtually debt-free + During the past fiscal year, too, QSC had no long-term debt to financial institutions. The Company utilizes only financial leasing, which is highly favorable by comparison with other forms of financing, to finance its investments in property, plant and equipment. As a result of significantly higher capital expenditures, long-term debt under financial leasing contracts totaled € 16.0 million for the past fiscal year, as opposed to € 10.7 million as of December 31, 2005; short-term debt under financial leasing contracts totaled € 13.4 million, as opposed to € 8.4 million the year before. QSC views the growing willingness on the part of lessors to offer financing at attractive terms as evidence of both its own financial strength as well as the soundness of its business model.

NET WORTH

Fast pace of capital expenditures + QSC's strong and profitable growth is based upon its nationwide Next Generation Network and broadband infrastructure over the last mile. During the past fiscal year, QSC broadened its competitive edge as an infrastructure provider and invested a total of € 40.1 million, as opposed to € 20.1 million the year before.

On the one hand, these capital expenditures served to conclude the migration of the entire nationwide network to a Next Generation Network. It is now based upon the IP standard throughout, thus enabling it to be maintained and operated significantly more cost-effectively and easily than classical networks. Moreover, the NGN affords greater flexibility and highly reduced costs in connection with the introduction of add-on services, thus also making it attractive for small and medium-size companies in the Business Customer segment. In addition, QSC upgraded its DSL network, the broadband infrastructure over the last mile, to ADSL2+ technology throughout.

Upgrade of the DSL network with ADSL2+ throughout

Moreover, subsidiary Plusnet started doing business in the fourth quarter of 2006, thus beginning earlier than had been planned with the expansion of the DSL network to nearly 2,000 central offices. This network expansion, which is scheduled to be concluded by year-end 2007, has already been fully financed through co-owner TELE2's capital contribution of € 50 million to Plusnet. From today's standpoint, QSC views network coverage of nearly 2,000 central offices as an optimum size for covering enterprise customer locations with respect to the cost-benefit ratio.

Over and above this significant expansion of coverage, the capital expenditures also included contract-related upfront expenses for new large accounts and wholesale/resellers. In order to equip customers with hardware, major capital spending is incurred here at the outset, which is amortized over the term of the contracts. During the past fiscal year, the strong revenue growth in these segments also resulted in an increase in contract-related upfront expenses.

Balance sheet characterized by growth and capital expenditures + QSC's balance sheet total doubled to € 299.9 million during the past fiscal year, as opposed to € 151.3 million the year before. In this connection, there were two reasons, in particular, for the rise in the value of long-term assets to € 133.6 million, as opposed to € 57.7 million in 2005. On the one hand, the acquisition of a majority interest in Broadnet increased goodwill to € 47.5 million, as opposed to € 9.3 million for the comparable period the year before. Secondly, the Broadnet consolidation as well as the Company's significantly higher capital expenditures resulted in an increase in property, plant and equipment to € 61.5 million, as opposed to € 33.4 million the year before.
Short-term assets, too, rose to € 166.4 million, as opposed to € 93.6 million the year before. On the one hand, this was attributable to the rise in liquid assets to € 108.9 million, as opposed to € 56.4 million the year before; on the other, it stemmed from an increase in trade receivables to € 52.8 million. In this connection, QSC continues to place particular emphasis on strict trade receivables management, consequently, allowances for bad debts on trade receivables rose only by € 1.0 million to € 3.9 million despite strongly rising revenues.

High equity ratio + During the past fiscal year, QSC's subscribed capital rose to € 133.9 million, as opposed to € 115.0 million the year before. On the one hand, this rise reflects the increases of capital from authorized capital against assets in kind to execute the acquisition of the Company's majority interest in Broadnet AG. Overall, this increased subscribed capital by € 16.4 million. On the other hand, the conversion of 2.5 million convertible bonds by QSC employees to an equal number of shares also contributed to this rise. In conjunction with the increases of capital, the capital surplus rose to € 558.0 million, as opposed to € 499.6 million in 2005. An equity ratio of 54 percent underscores QSC's continued sound financing structure.

Acquisition of a majority interest in Broadnet through share swap increases equity

Statements pursuant to § 315, Sub-Para. 4, German GAAP (HGB), and remarks + QSC's subscribed capital as of December 31, 2006, amounts to € 133,897,686, and is classified into 133,897,686 shares of no-par bearer stock. According to the share register as at December 31, 2006, the subscribed capital was divided among 30,539 shareholders. The Company's two founders, Dr. Bernd Schlobohm and Gerd Eickers, held 10.3 percent of the total of 133.897.686 shares, respectively, and U.S.-based Baker Capital held 25.1 percent. Since QSC went public, neither its founders nor the Baker Capital have ever sold a single QSC share. There are no pool contracts between the founders and the Baker Capital , and no privileges for the three legacy shareholders. In addition to the aforementioned shareholders, no other QSC shareholder possesses more than 10 percent of all shares.
Appointment and dismissal of members of the Management Board is governed by §§ 84, 85, German Stock Corporation Act, as well as by § 7 of the Articles of Association and Bylaws as amended January 16, 2007. Pursuant to § 7 of the Articles of Association and Bylaws, the Management Board can comprise one or more individuals. The Supervisory Board determines the number of members of the Management Board. Even if the capital stock of the Company amounts to more than three million euros, the Supervisory Board can stipulate that the Management Board consist of only one individual. Amendments to the Articles of Association and Bylaws are governed by §§ 179, 133, German Stock Corporation Act (AktG), as well as by § 15 and § 20, Sub-Para. 1, of the Articles of Association and Bylaws as amended January 16, 2007.

Under a resolution by the Annual Shareholders Meeting on May 23, 2006, the Management Board was authorized pursuant to § 71, Sub-Para. 1, No. 8, German Stock Corporation Act (AktG), to acquire QSC shares totaling up to 10 percent of the capital stock of the Company by October 31, 2007. These treasury shares can be acquired on the stock exchange or by means of a public acquisition offer, at the discretion of the Management Board. Moreover, in certain cases the Management Board was authorized to resell the treasury shares acquired under the authorization in a different manner than on the stock exchange or through an offer to all shareholders, or to call the shares. The Management Board has thus far not utilized this authorization.

The Management Board was authorized by resolution passed at the shareholder meeting on May 27, 2004 to increase capital stock until May 26, 2009, with approval of the Supervisory Board, on one or several occasions by up to € 50,000,000 by issuing new common registered shares in return for cash or non-cash contributions. By resolution passed at the shareholder meeting on May 23, 2006, this authorization was revoked with effect as of the date of entering the approved capital mentioned below in the commercial register, unless the Management Board had already decided on its use. By resolution of the Supervisory Board dated July 7, 2006, the resolution of the Management Board dated June 6, 2006 was confirmed and, upon partial exercise of the authorization, capital stock was increased by € 11,232,176 and € 229,655 in return for a non-cash contribution through the issue of registered no-par value shares. The Management Board was authorized by resolution passed at the shareholder meeting on May 23, 2006 to increase capital stock until May 22, 2011, with approval of the Supervisory Board, on one or several occasions by up to € 57,500,000 by issuing new no-par value registered shares in return for cash or non-cash contributions. By resolution of the Supervisory Board dated November 13, 2006, capital stock was increased upon partial exercise of this authorization by € 4,920,000 in return for the issue of new no-par value registered shares in return for non-cash contributions. Approved capital amounted to € 52,580,000 as of the balance sheet date.

The authorized capital is intended to enable QSC to respond swiftly and flexibly to opportunities that present themselves on the capital market and to obtain equity capital at favorable terms if needed. With the exception of Conditional Capital IV, the conditional capital is employed to secure the conversion rights of holders of convertible bonds that QSC has issued or can issue to members of the Management Board, to the managing directors of affiliated companies, to employees and to other individuals involved in the Company's success within the framework of existing stock option plans. The authorization to acquire and dispose of treasury stock is intended to enable the Company to swiftly and flexibly offer treasury shares to national and international investors, to expand the circle of shareholders and to stabilize the value of the shares. Moreover, the Company should have treasury shares available in order to be able to offer them as compensation in connection with the acquisition of enterprises or equity investments. Overall, these are rules that are usual and customary at publicly traded corporations and whose purpose is not to impede any potential takeover attempts.

The Conditional Capital as of the balance sheet date amounts to a total of € 30,878,284, and is classified into Conditional Capital III amounting to € 1.492 million, Conditional Capital IV amounting to € 25.0 million, Conditional Capital V amounting to € 1.387 million, Conditional Capital VI amounting to € 1.499 million, as well as Conditional Capital VII amounting to € 1.5 million.

Dedicated Team for Strong Growth

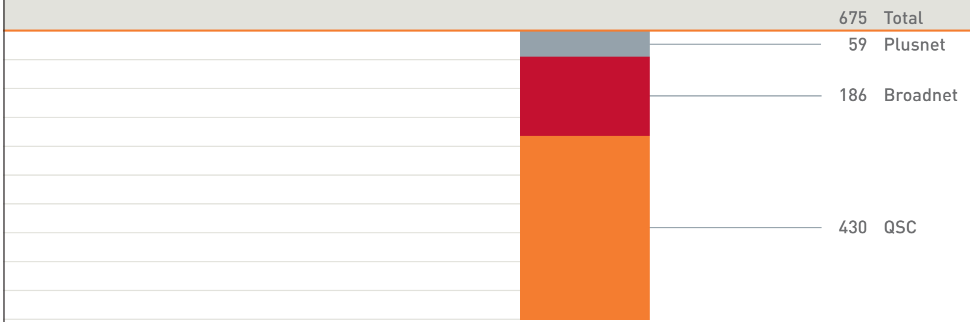
HUMAN RESOURCES

QSC workforce specifically expanded in 2006

Broadnet team strengthens QSC + The acquisition of a majority interest in Broadnet, as well as the specific expansion of the QSC workforce, led to an increase of 225 employees during 2006 to a total workforce of 675 people as of December 31, 2006. The corresponding personnel expense rose to € 41.0 million, as opposed to € 30.4 million the year before.
With their know-how and their customer relationships, the 186 people employed by Hamburg-based Broadnet will strengthen QSC's position in business with enterprise customers, especially in northern Germany. Moreover, Broadnet's focus on its core competencies of sales & marketing and engineering makes for a very good fit with the QSC organization. For this reason, too, the Company expects to see smooth, cross-locational collaboration between all of its people following the intended merger.
At Broadnet, former Thyssen Telecom management board speaker Dr. Hans-Peter Kohlhammer is responsible for the new subsidiary's business as its chief executive officer. Broadnet founder Frank Brügmann, who had resigned as CEO by mutual agreement in December 2006, will be available to him as a consultant.

Plusnet workforce driving network expansion + In addition to Broadnet, network operating company Plusnet is QSC's second major equity investment. As of December 31, 2006, this company, which was formed in the summer of 2006, employed a workforce of 59 people, the majority of whom had previously been employed in QSC's engineering operations. Plusnet is headquartered in the same building in Cologne as QSC and is headed up by Dr. Ralf Fischer, who had previously been in charge of managed services at QSC, and also, since December 2006, by Eivind Dugstad. The Plusnet team is responsible for both operating the nationwide DSL network and expanding it to nearly 2,000 central offices by year-end 2007.

Workforce as at December 31, 2006



Qualified staff for network expansion and strong growth + The strong dynamics of the Company's markets and the high quality expectations of our customers necessitate a corresponding level of training and education for the QSC workforce. The majority of the Company's people are skilled workers, while one third possess postgraduate degrees. Through both in-house and external continuing education opportunities, every employee is enabled to constantly update and broaden his or her knowledge.

Investing in the achievers of tomorrow + During the past fiscal year, QSC received more than 4,000 job applications, and was thus able to cover its additional need for qualified employees. In spite of this, the Company provides in-house training in the vocations of information technology specialists (focusing on systems integration and applications development), IT system technicians and administrative clerks. As of December 31, 2006, QSC employed 22 trainees for these vocations. The Company views training both as a major contribution toward securing future talent for itself as well as a way of offering school graduates vocational prospects in a forward-looking industry.

QSC provides training for future talent in various vocations

Entrepreneurial environment and compensation translates into loyal employees + Over and above vocational training, QSC views the ability to win and keep qualified people as being a major key to its future success. The Company utilizes employee stock option programs as an accompanying instrument in this connection, making key employees co-owners of QSC and strengthening their loyalty to the Company. The option of dedicating a portion of an employee's gross pay to a direct combined private old-age and survivor's pension insurance plan is also developing a long-term effect. Professionals and executives additionally benefit from a performance-based compensation system that includes a corresponding variable income element, which rewards the attainment of both personal and corporate goals.

Yet these kinds of monetary incentives, alone, are not enough to assure the loyalty of qualified employees over the long term. QSC therefore supports a work environment that affords every employee a high level of self-direction. Flat hierarchies, a corporate culture that embraces fairness, openness and respect, as well as the entrepreneurialism that is characterized by the Company's founder and Chief Executive Officer, assure the corresponding latitudes and fast decision-making processes. It is precisely these factors that make the Company a preferred employer in the telecommunications industry and create the foundation for collaboration in a spirit of partnership between all QSC employees and both their internal and external counterparts.

Expanding the Risk Management

THE RISK MANAGEMENT SYSTEM

Risk management a value-creating activity + The German Control and Transparency Act (KonTraG) of May 1, 1998, mandates that the management boards of stock corporations maintain an appropriate system for early identification and monitoring of existing risks. QSC also views efficient and forward-looking risk management as an important, value-creating activity that serves as a foundation for decision-making throughout all areas of the Company.

Systematically dealing with these potential risks and fostering a culture of thinking and acting with a view toward risks is therefore a key element in securing and shaping QSC's future in a highly dynamic environment. The strong growth in the broadband communication market for enterprise customers offers QSC and its shareholders enormous opportunities, but it also involves risks.

QSC's objectives include avoiding or minimizing existing and potential risks, while simultaneously taking advantage of opportunities that present themselves. There has to be a balanced relationship between opportunities and risks, because even the failure to identify opportunities can represent a risk for QSC. Its risk strategy is therefore aimed at using ongoing risk management to achieve an optimum balance between defending against risks and taking advantage of opportunities.

Aim of achieving an optimum balance between opportunities and risks

The high priority that QSC attaches to risk management is underscored by the expansion of the Company's risk management system (RMS) during the past fiscal year to include new risk management software. This software system utilizes database support to identify, analyze, and assess all risks, and associates them with risk avoidance and reduction measures. The software additionally includes reporting functions that present the status of these measures, thus providing the Management Board with an even better overview of the Company's overall risk management at all times.

METHODOLOGY OF THE RISK MANAGEMENT

Objective of securing long-term success + QSC has institutionalized a risk management system that includes intercoordinated rules, measures, and procedures for dealing with risks. Its purpose is to identify, analyze, assess, control, and monitor future risk-prone developments as early as possible in order to assure the Company's success over the long term. In this connection, the risk management system focuses on risk avoidance through prevention, by utilizing suitable measures to reduce existing risks, by compensating for and securing existing risks through the formation of accruals/provisions, and by taking out insurance coverage, as well as through the acceptance of residual risks in close coordination with corporate management.

Since risks can occur in all of the Company's operations, the RMS covers all operations and departments at QSC. The Company includes risk assessments in connection with all decisions at both the operational and corporate levels, and right from the very beginning is mindful of utilizing appropriate measures wherever possible to reduce those risks that do arise. Regular reporting supports the managers of the operations in identifying risks early on and taking them into consideration in connection with their decisions.

QSC's risk management system is divided into two major areas of responsibility. Corporate Risk Management is responsible for the annual risk inventory and the quarterly risk reports. The finance department is responsible for ongoing monitoring of corporate risks on the basis of key operational and financial performance indicators. Finance tracks the development of these risks in weekly reports as a kind of early warning system and reports to the Management Board.

Ongoing monitoring and assessment of risks that arise is handled decentrally by risk coordinators in the individual operations. They review their areas of responsibility with regard to whether previously unidentified risks have arisen and whether there has been a change in existing risks. Central Risk Management regularly monitors the introduction of appropriate measures and compliance with them. It also handles consolidation and documentation of the decentrally assessed risks, and produces a detailed quarterly risk report for the Management Board. At least once a year, the Management Board reports to the Supervisory Board with a detailed risk report, while using the RMS as the basis for also informing the Supervisory Board about all major risks and opportunities during the course of the year. Moreover, the RMS is also audited within the framework of the audit of the Company's Annual Financial Statements.

Management Board receives detailed quarterly risk report

To assure that all relevant risks are identified and taken into consideration within the RMS, Corporate Risk Management conducts an annual risk inventory during the first quarter of the year, in parallel with the risk report. With the involvement of the risk coordinators, all previously known risks are tabulated in this connection and classified according to the topicality they continue to pose. In addition, Corporate Risk Management performs a Company-wide review in order to determine whether any further, as-yet unknown, risks exist that would have to be monitored and taken into consideration within the regular reporting system in the future.

RISK OVERVIEW

Detailed on the following pages are those entrepreneurial, financial and information technology risks that QSC today views as being of major significance for its business operations.

The economy + Among the overall economic risks, QSC monitors the economic environment, in particular, because a weak economy impacts the willingness of enterprise customers to invest in modern telecommunication infrastructures.

During the recessions in the years 2002 and 2003, QSC was already able to demonstrate that it can grow strongly and profitably in a weak overall economic environment. Moreover, market researchers anticipate continued strong growth in the coming years in QSC's core market, broadband communication for enterprise customers.

Alternative technologies + Cable (TV) network operators are increasingly offering Internet access and voice telephony, in addition to television. QSC is attentively monitoring these Triple Play offerings on the part of cable network operators, which address the residential customer market exclusively, as they could pose potential competition to the Company's business with wholesale partners.

However, given the nationwide availability of DSL and the capital expenditures that would be required in the cable networks, QSC views Internet access via cable TV as being a niche product. According to calculations by market research institute IDC, DSL technology will continue to dominate the German broadband market in the coming years with a market share of some 90 percent. Given this backdrop, it is likely that wireless technologies like WLAN and Wimax will only be able to penetrate niche markets in the years to come. Although Wimax affords – under certain conditions – double-digit megabit transfer speeds like ADSL2+, it requires building an infrastructure of its own. An auction of the necessary licenses by the German Federal Network Agency (Bundesnetzagentur) in December 2006 had already finished at € 56 million – a clear indication that providers value the estimated revenue and profit potential with skepticism.

Competition + The German market for DSL products and services is seeing a concentration on only a few strong providers. QSC analyzes the changing competitive situation very closely, yet views itself as being well aligned as an infrastructure provider. Moreover, the strong dynamics of the DSL and IP-VPN markets additionally continue to make the possibility of a shakeout in the Large Accounts and Business Customers segments unlikely. In its wholesale/reseller business, the Company is benefiting from its focus on business with enterprise customers because, in contrast to its competitors, this prevents conflicts of interest from arising with respect to addressing residential consumers.

Regulatory environment + The decisions of the German Federal Network Agency can have either an indirect or direct influence on QSC's competitive position and market. This also applies with respect to the issue of bitstream access, and thus to the ability of potential competitors to offer DSL products with specific quality parameters under their own names and for their own accounts with significantly lower infrastructure investments. The utilization of bitstream access could increase competitive pressure on QSC. In complying with an order from the regulatory authority, Deutsche Telekom AG (DTAG) submitted a standard offering on January 13, 2007, which the German Federal Network Agency (Bundesnetzagentur) will review during the course of the year 2007.
Regardless of this current discussion, bitstream access also opens up opportunities to QSC, as the Company can use it to efficiently supplement its own network, thus enabling it to offer nationwide data networks to business customers under its own name.

Competitive behavior of Deutsche Telekom + As an infrastructure provider, QSC is significantly less dependent on former monopolist DTAG's reselling prices than the majority of the Company's competitors. Nevertheless, an aggressive pricing policy on the part of DTAG in connection with both the required preliminaries and the consumer market in particular, could have a negative impact on the margin situation in the German telecommunication market. In this connection, QSC continues to count on viable supervision by both the German Federal Network Agency (Bundesnetzagentur) as well as the European Commission. The Company is playing an active role in this connection within the framework of intensive talks and by commenting on various methods.

QSC counts on viable supervision by the German and EU authorities

In 2007, the German Federal Network Agency (Bundesnetzagentur) is scheduled to make a decision on DTAG's recurring and non-recurring preliminaries for unbundled access to subscriber lines. DTAG has made an application to increase the previously approved fees, which would also result in a higher burden for QSC. However, QSC assumes that in assessing these applications the regulatory authority will continue to follow the principle of cost-efficient provision of services, and continues to see considerable cost reduction latitude. Moreover, the German Federal Network Agency (Bundesnetzagentur) has in the past refused to follow DTAG's argumentation, and most recently ordered minor fee reductions in August 2005.

Another risk consists of DTAG's improved DSL network, the VDSL network. To offset its investments in increasing the speed of this network, DTAG is asking that regulatory requirements and the commitment to provide other market players with VDSL access be waived. In doing so, it is basing its argumentation upon the new § 9a of the German Telecommunication Modification Act that came into force in February 2007. This legislation calls for new markets to be excluded from regulation unless, for example, a long-term risk to competition that is documented on the basis of facts would require regulation. Should this endeavor succeed, DTAG would be given a virtual monopoly on broadband communication lines with speeds in excess of 25 MBit/s.

However, the question of whether improvement of DTAG's existing network, which was financed in the days of its monopoly position, with VDSL is covered by § 9a is controversial, as this network only involves equipping additional locations with a different development version of ADSL2+ technology (VDSL2 in this case). QSC anticipates that the European Commission will continue to refuse to tolerate monopolies within the single European market and will therefore insist on competitor access to DTAG's entire DSL network on all levels. The Commission has already signaled that it will initiate an EU breach of treaty action against the new German Telecommunication Modification Act. A determination that this legislation is in conflict with EU law could swiftly contain any harmful consequences of the German legislation.

ADSL2+ meets the requirements of the wholesale partners

Aside from the outcome of this decision, DTAG's VDSL offerings are primarily aimed at residential customers, and thus essentially only indirectly impact QSC's wholesale business operations. It is expected that the wholesale partners will continue to be able to meet the market's demand for services with their ADSL2+ offerings.

Expansion of wholesale business + Wholesale business poses the risk of dependency upon the success of the Company's marketing partners, as they are responsible for sales and marketing to end-customers. At the same time, it is necessary for QSC to incur significant preliminary expenses in connection with consolidating IT systems and building appropriate interfaces. Amortization of these preliminaries, in turn, depends upon the success of the Company's respective partners. In its wholesale business, QSC therefore collaborates exclusively with partners who possess mass-market experience. The rapid marketing successes of partners like freenet and HanseNet confirms this strategy, which focuses on strong market providers.

The success of these partners in the consumer market could result in an extremely high volume of new orders at QSC, necessitating both high-quality yet efficient handling of a large volume of customer data and tying up corresponding resources. Moreover, a high volume of orders necessitates the scalability of QSC's interfaces to DTAG, which has to provide the corresponding subscriber lines. However, QSC had aligned itself correspondingly prior to the launch of its wholesale business, and therefore views strongly rising demand among its wholesale/reseller partners as a tremendous opportunity and growth driver for the Company.

Penalties in project business + Within the framework of projects for large accounts and its wholesale/reseller partners, QSC enters into contracts that assure certain service levels, some of which involve potential penalties. This results in the risk of high recourse entitlements and expenses stemming from interruptions. This risk is minimized through intensive service level management, contractual agreements, and consistent monitoring of the entire network on a three-shift basis. QSC has thus far been able to assure the satisfaction of nearly all service level agreements.

The way QSC is financed + As of December 31, 2006, QSC possessed liquid assets totaling € 108.9 million. However, aggressive price competition or a sustained recession could result in the need for additional funding. The successful placement of QSC shares in connection with the acquisition of a majority interest in Broadnet AG documented the willingness on the part of the capital market in 2006 to embrace QSC's financing activities. The Company's strong and profitable growth, as well as its rising cash flow surpluses from operating activities, further reduce this risk.

QSC's own infrastructure + Through the establishment of Plusnet GmbH & Co. KG by QSC and TELE2 as a joint-venture network operating company, the vast majority of the risks in connection with the Company's network infrastructure are now being shouldered by Plusnet. Nevertheless, outages in the DSL network pose a risk to the entire QSC Group and its business operations. Within the framework of the group-wide risk management system, the risks faced by QSC's subsidiaries are therefore also taken into consideration. A potential network outage is a risk that is constantly monitored. In addition to a potential loss of image, the risk of indemnification claims or high penalties, in particular, following extended, widespread outages could result in corresponding expenses. Consequently, maintaining and constantly improving security and reliability throughout the network enjoys the utmost priority within the framework of QSC's business operations. The Company relies on redundancies within its network in this connection. Air conditioning equipment prevents potential heat-related hardware failures, while firmly defined access authorizations to all colocation rooms prevent misuse or sabotage. Through these and any number of further measures, the Company sees itself as being very well equipped for smooth DSL operations.

A lot of measures secure smooth network operations

Criminal intrusions into QSC systems + Unauthorized intrusions into QSC's IT network in the form of viruses, Trojan horses, or hackers could result in considerable damage, for example through data manipulation or file deletion. The same also applies with respect to insufficient data protection and uncontrolled access to QSC data centers. In the event of an outage of the operative IT systems, it would not be possible to handle new orders or resolve system interruptions; the resulting monetary damages and loss of reputation could be significant. To mitigate these kinds of risks, QSC has put in place special security coordinators in its IT operations. These coordinators bear the primary responsibility for a sophisticated security concept, which includes up-to-date firewalls and a multitier virus protection concept and results in virtually complete avoidance of the above-described risks. In addition, the Company-wide IT security policy provides all QSC employees with concrete guidance for avoiding IT security risks. As a result of all of these measures, IT security risks can be viewed as being under control according to reasonable standards.

Loss of data + Operating errors, hardware defects, or the destruction of the data center through an attack or natural disaster can result in a loss of business-critical data. The lack of data backups could increase this kind of risk. Growing volumes of data stemming from the Company's high pace of growth could additionally push the capacities of the Company's data storage and backup systems to their limits. In any event, a loss of operative data would make it impossible for the Company to operate.

High priority for data security at QSC

QSC combats these risks through extensive data backup measures. Complete backups are archived for years, and monthly backups are stored in separate physical locations. Central data inventories are automatically backed up daily to tape. A backup robot expands capacities. Thanks to these extensive measures as well as the Company's disaster recovery concept, the risk of data loss can be viewed as being under control.

OVERALL REMARKS ON RISK MANAGEMENT

Early information assured + Given the potential scope of damage and the likelihood that these and further potential risks could occur, it is currently reasonable to say that no risks are identifiable that could lead to a sustained material impairment of the financial or earnings positions of QSC AG. Organizationally, all equitable prerequisites have been put in place to enable the Company to be informed early on in the event of potential risk situations and take appropriate action. With the deployment of the new risk management software, the data inventory has been additionally expanded in order to afford consolidated monitoring and control of all risks at all times.

Nevertheless, as a result of these or other risks and incorrect assumptions, QSC's actual future results could vary materially from the expectations of the Company and its management. All statements contained in these Consolidated Financial Statements that are not historical facts are forward-looking statements. They are based upon current expectations and projections of future events, and are therefore subject to regular review within the context of the RMS.

Sustained Strong and Profitable Growth

GENERAL REMARKS

Above-average profitability growth in 2007 + QSC anticipates a continuation of its strong and profitable growth in the years to come. This will be driven by the dynamic development of the Company's strategic segments of Large Accounts, Business Customers, and Wholesale/Resellers. All three segments will benefit from the rising market demand that is expected, as well as from the swift expansion of the DSL network to nearly 2,000 central offices.

QSC anticipates revenue growth to more than € 350 million for the current 2007 fiscal year, along with an EBITDA increase to between € 50 million and € 60 million. Following the Company's first net income in the fourth quarter of 2006, QSC also anticipates net income of between € 15 million and € 25 million for the full 2007 fiscal year. The Company is planning capital expenditures of between € 60 million and € 70 million for the current year, of which Plusnet's network expansion scheduled for 2007 has already been fully funded through a € 50 million capital contribution by coshareholder TELE2.

QSC expects EBITDA to rise to between € 50 million and € 60 million

FUTURE GENERAL ECONOMIC SITUATION

Sustained high pace of capital expenditures + In spite of the increase in German value-added tax from 16 to 19 percent at the beginning of the year, economic researchers predict that the current fiscal year will see only a moderate weakening of the recovery in Germany. Most of them expect gross domestic product to grow by some two percent; in addition to exports, they also attribute this development to the continued willingness among enterprises to invest. And the telecommunications industry will benefit from this, as well. Industry association VATM estimates that total industry revenues will surpass the € 70-billion mark for the first time.

FUTURE INDUSTRY SITUATION

Continued strong growth of the DSL market + The strong demand for DSL connections will be sustained in 2007. In a study on the European broadband market, investment bank JPMorgan forecasts that the number of DSL connections in Germany will rise to 18.1 million in the current fiscal year, with this number increasing to 24.9 million by 2010. The majority of these new connections will be accounted for by residential households, as only some one-third of all households today have broadband Internet access. QSC will benefit from this anticipated dynamic growth through its wholesale/reseller partners with their mass-market experience.

Market research institute IDC expects the number of DSL enterprise connections in Germany to rise by nearly 250,000 during the current fiscal year to 2.4 million. Enterprises are increasingly opting to integrate voice and data services over one and the same DSL line through the utilization of Voice over IP (VoIP) technology. By 2010, the number of VoIP connections at German enterprises is expected to rise nearly fivefold.

Market volume for add-on services to quadruple by 2010

This growing demand for VoIP will also strengthen managed services business. By 2010, the market volume in Germany is likely to increase to more than € 2.0 billion. In this connection, IDC is forecasting a market volume of € 1.6 billion for IP-VPN solutions by the year 2010. Given the IDC data, QSC expects to see revenues for network-related add-on services quadruple to € 400 million by the year 2010.

ANTICIPATED PROFITABILITY

Strongest growth dynamic with wholesale/resellers + QSC continues to benefit from the strong growth of those submarkets that are of relevance for its strategic segments. In 2007, the Large Accounts and Wholesale/Resellers segments, in particular, will therefore be able to contribute a significantly above-average percentage to QSC's planned revenue rise to more than € 350 million.

The resulting improvement in the quality of the Company's revenues will make a major contribution to the strong profitability improvements that are anticipated in 2007. In addition, this improved profitability will also continue to stem from QSC's network-based and thus scalable business model, as network expenses will rise at only a disproportionately lower pace than revenues. QSC thus anticipates a significant rise in its EBITDA to between € 50 million and € 60 million for 2007.

Swift network expansion will result in a scheduled rise in depreciation and amortization during the current fiscal year. In spite of this, QSC is planning net income of between € 15 million and € 25 million for the full 2007 fiscal year.

ANTICIPATED FINANCIAL SITUATION

Network expansion fully funded + During the course of 2007, QSC subsidiary Plusnet will be expanding the nationwide DSL network to nearly 2,000 central offices. This will afford QSC direct access to approximately 50 percent of all German households as well as to approximately 70 percent of all enterprise locations that are of relevance for IP-VPN business. The capital expenditures required for this network expansion have already been fully funded since the autumn of the past fiscal year through a € 50 million cash contribution from Plusnet coshareholder TELE2.

Overall, QSC anticipates that capital expenditures will total between € 60 million and € 70 million during the current fiscal year. Over and above the network expansion, this total also includes contract-related upfront expenses for new enterprise customers in particular.

With liquid assets totaling € 108.9 million as of December 31, 2006, QSC has sufficient funding to accommodate its anticipated growth.

OPPORTUNITIES FOR QSC

Network expansion strengthens strategic segments + The expansion of the DSL network to nearly 2,000 central offices, which will be concluded by year-end 2007, will strengthen QSC's competitive position in the Large Accounts, Business Customers, and Wholesale/Resellers segments. In the case of large accounts, the strength of this expanded network will nearly double the likelihood of QSC being able to win requests for proposals for nationwide IP-VPNs to over 60 percent. Following this network expansion, QSC will be able to directly connect more locations to its network in connection with large accounts, thus enabling the Company to submit significantly more cost-effective proposals. The Business Customers segment, too, will be able to benefit from the greater number of directly connectable customer locations. Moreover, a larger network makes QSC an even more attractive partner in connection with wholesale/reseller business.

Positioned early on for Triple Play offerings + The DSL network operated by QSC subsidiary Plusnet has been fully equipped with ADSL2+ technology. This enables transfer speeds of up to 25 megabits per second, and thus Triple Play offerings, i.e. Internet, telephony, and television, from one and the same line and provider. Demand for such integrated offerings is expected to rise in the years to come. Thanks to its cutting-edge ADSL2+ network, QSC will number among the preferred technology partners in this connection.

ADSL2+ makes QSC the preferred technology partner

Next Generation Network simplifies VoIP integration + As early as 2005, QSC had already upgraded its entire network to an IP-based Next Generation Network. On the one hand, this NGN enables smooth integration of VoIP technology into existing networks, and thus also voice and data services to be offered over one and the same line. In addition, QSC is benefiting from the fact that an NGN is considerably easier and more cost-effective to maintain and operate than classical networks.

Next Generation Network strengthens residential customer business + The Residential Customers segment is also benefiting from the upgrade of the entire network to an NGN, as it enables high volumes of voice traffic to be cost-effectively handled. This means that QSC is able to offer competitive terms and conditions for both VoIP as well as classic voice telephony (call by call), without having to forego margins.

Strong growth in wholesale business + The successful launch of marketing for DSL connections in 2006 through HanseNet under the "Alice" brand and through freenet already demonstrated the potential that is offered by the wholesale business. QSC expects to see strongly growing revenues during the current fiscal year from its collaboration with these and further partners. As recently as January 2007, QSC broadened its partnership with Telecom Italia subsidiary HanseNet to include a further 100 German cities. And TELE2 is scheduled to begin nationwide marketing of fully unbundled DSL lines in the second half of the year. As a coshareholder in Plusnet, TELE2 will be obtaining these lines from the QSC subsidiary on a cost bases.

Increased chances of winning new large accounts

New revenue potential with large accounts + In 2007, QSC will have two focuses in its managed services with large and medium-sized enterprises: On the one hand, the Company intends to win further requests for proposals from large accounts, and expects to see the effect of the expanded network, in particular, come to bear in this connection during the course of the year. On the other hand, the Company aims to broaden its share of the telecommunication budgets of existing customers. QSC will be tapping into additional revenue potential here by integrating add-on services and Voice over IP.

Business customers opting for Voice over IP + In its product business with small and medium-sized organizations, QSC will be benefiting from the sustained high demand for DSL connections and from rising interest in integrated voice and data services; more and more business customers are now utilizing Voice over IP. In addition, QSC intends to continue to migrate preselection customers into direct access customers. Direct connections afford higher margins on the one hand, while enabling additional products and services to be integrated more easily on the other.

SUBSEQUENT EVENTS

QSC aims at merging Broadnet into QSC + QSC's Management Board and Supervisory Board resolved on January 30, 2007 to prepare for a merger of Broadnet into QSC, with a view to allow the legal and organizational integration of Broadnet into the QSC Group. In conjunction with the merger, QSC plans to grant QSC shares to Broadnet shareholders in exchange for Broadnet shares. QSC has initiated discussions with Broadnet to commence all necessary further measures jointly with Broadnet. In particular, an independent auditor will be engaged to determine the share exchange ratio.

Cologne, March 21, 2007

Dr. Bernd Schlobohm
Chief Executive Officer

Markus Metyas

Bernd Puschendorf

Financial Report

2006 was a successful year for QSC: Revenues grew faster than in the previous year and earnings continued to rise disproportionately. The Annual Financial Statements also document how well the Company is financed.

Consolidated Financial Statements

CONSOLIDATED STATEMENTS OF INCOME

Euro amounts in thousands (T €)

Notes	No.	2006	2005
Net revenues	7	**262,522**	**194,387**
Cost of revenues	8	(203,600)	(165,532)
Gross Profit		**58,922**	**28,855**
Selling and marketing expenses	9	(43,099)	(30,493)
General and administrative expenses	10	(25,518)	(16,916)
Research and development expenses	11	(214)	(437)
Other operating income	12	2,891	586
Other operating expenses	12	(158)	(261)
Operating loss		**(7,176)**	**(18,666)**
Financial income	13	2,205	1,015
Financial expenses	13	(2,234)	(815)
Share of profit of an associate	13	-	280
Net loss before income taxes		**(7,205)**	**(18,186)**
Tax income	43	1,859	-
Net loss		**(5.346)**	**(18,186)**
Attributable to:			
Equity holders of the parent		(5,416)	**(18,186)**
Minority interest	39	70	-
Net loss per share (basic and diluted) in €	14	**(0.04)**	**(0.17)**

CONSOLIDATED BALANCE SHEETS

Euro amounts in thousands (T €)

	Notes No.	Dec. 31, 2006	Dec. 31, 2005
ASSETS			
Long-term assets			
Property, plant and equipment	16	61,489	33,371
Goodwill	17	47,450	9,265
Intangible assets	19	18,051	8,804
Other long-term financial assets		160	293
Deferred tax assets	43	6,403	5,969
Long-term assets		**133,553**	**57,702**
Short-term assets			
Trade receivables	20	52,778	34,177
Prepayments	21	1,099	2,096
Other receivables and short-term financial assets	22	3,566	914
Available-for-sale financial assets	23	62,927	26,065
Cash and short-term deposits	23	45,986	30,313
Short-term assets		**166,356**	**93,565**
TOTAL ASSETS		299,909	151,267

SHAREHOLDERS' EQUITY AND LIABILITIES	Notes No.	Dec. 31, 2006	Dec. 31, 2005
Equity attributable to equity holders of the parent			
Capital stock	24	133,898	115,033
Capital surplus	25	557,961	499,643
Other capital reserves	27	(1,286)	(1,357)
Accumulated deficit		(533,697)	(528,281)
Equity attributable to equity holders of the parent		**156,876**	**85,038**
Minority interest	38	3,674	-
Total Shareholders' equity		**160,550**	**85,038**
Long-term liabilities			
Long-term liabilities of minority interest	31	49,860	-
Long-term portion of finance lease obligations	28	16,044	10,687
Convertible bonds	29	36	60
Accrued pensions	30	721	796
Deferred tax liability	43	5,084	3,847
Long-term liabilities		**71,745**	**15,390**
Short-term liabilities			
Trade payables	32	42,082	31,596
Short-term portion of finance lease obligations	28	13,443	8,437
Provisions	33	1,512	930
Deferred revenues	34	4,510	3,441
Other short-term liabilities	35	6,067	6,435
Short-term liabilities		**67,614**	**50,839**
Total liabilities		**139,359**	**66,229**
TOTAL SHAREHOLDERS' EQUITY AND LIABILITIES		**299,909**	**151,267**

CONSOLIDATED STATEMENTS OF CASH FLOWS

Euro amounts in thousands (T €)

	Notes No.	2006	2005
Cash flow from operating activities	36		
Net loss before income taxes		(7,205)	(18,186)
Depreciation and amortization		27,650	24,408
Non-cash share-based payments		1,014	152
Loss/(Gains) from disposal of long-term assets		69	(156)
Gains from disposal of long-term financial assets		-	(280)
Changes in provisions		(877)	(764)
Changes in trade receivables		(15,181)	(8,163)
Changes in trade payables		6,356	4,783
Changes in other financial assets and liabilities		(92)	906
Cash flow from operating activities		**11,734**	**2,700**
Cash flow from investing activities	37		
Purchase of available-for-sale financial assets		(59,192)	(19,970)
Disposal of available-for-sale financial assets		21,766	10,129
Payments related to acquisitions	39	20,197	1,539
Purchases of intangible assets		(6,076)	(5,812)
Purchases of property, plant and equipment		(13,148)	(4,153)
Proceeds from disposal of assets		47	176
Proceeds from disposal of financial assets		-	280
Cash flow from investing activities		**(36,406)**	**(17,811)**
Cash flow from financing activities	38		
Changes in convertible bonds		(24)	-
Assumption of minority interst liabilities		49,860	-
Proceeds from issuance of common stock		3,732	20,626
Payments related to financing acitivities		(2,751)	-
Proceeds from finance lease		-	6,752
Repayments of finance lease		(10,472)	(4,490)
Cash flow from financing activities		**40,345**	**22,888**
Change in cash and short-term deposits		**15,673**	**7,777**
Cash and short-term deposits at January 1		30,313	22,536
Cash and short-term deposits at December 31		**45,986**	**30,313**
Interest paid		1,474	765
Interest received		1,095	620

CONSOLIDATED STATEMENTS OF RECOGNIZED INCOME AND EXPENSES

Euro amounts in thousands (T €)

	2006	2005
Directly recognized in equity		
Changes in accrued pensions	165	-
Available-for-sale financial assets		
change in fair value	(185)	(1,253)
realized losses	(40)	(191)
Tax effect, total	131	71
Directly recognized in equity	**71**	**(1,373)**
Net loss	(5,346)	(18,186)
Net loss and recognized income and expenses	**(5,275)**	**(19,559)**
Attributable to:		
Equity holders of the parent	(5,344)	**(19,559)**
Minority interest	69	-

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY

Euro amounts in thousands (T €)

Notes	No.	Capital stock T €	Capital surplus T €	Other capital reserves T €	Accumulated deficit T €	Total T €
		Equity attributable to equity holders of the parent				
Balance at January 1, 2005		**105,503**	**474,750**	**16**	**(510,095)**	**70,174**
Net loss					(18,186)	(18,186)
Change in fair value of available-for-sale financial assets	27			(1,444)		(1,444)
Deferred taxes on available-for-sale financial assets	43			71		71
Issuance of common stock by assets in kind	24	3,584	10,178			13,762
Issuance of common stock authorized by shareholders' meeting		5,490	14,361			19,851
Conversion of convertible bonds	41	456	319			775
Non-cash share-based payments	41		35			35
Balance at December 31, 2005		**115,033**	**499,643**	**(1,357)**	**(528,281)**	**85,038**
Net loss					(5,416)	(5,416)
Change in fair value of available-for-sale financial assets	27			(225)		(225)
Deferred taxes on available-for-sale financial assets	43			90		90
Changes in accrued pensions	30			165		165
Deferred taxes on accrued pensions	43			41		41
Issuance of common stock by assets in kind	24	16,382	56,375			72,757
Conversion of convertible bonds	41	2,483	1,252			3,735
Non-cash share-based payments	41		691			691
Changes in minority interest	39					-
Balance at December 31, 2006		**133,898**	**557,961**	**(1,286)**	**(533,697)**	**156,876**

Minority interest T €	Total Share-holders' Equity T €	
-	**70,174**	**Balance at January 1, 2005**
	(18,186)	Net loss
	(1,444)	Change in fair value of available-for-sale financial assets
	71	Deferred taxes on available-for-sale financial assets
	13,762	Issuance of common stock by assets in kind
		Issuance of common stock authorized by
	19,851	shareholders' meeting
	775	Conversion of convertible bonds
	35	Non-cash share-based payments
-	**85,038**	**Balance at December 31, 2005**
70	(5,346)	Net loss
	(225)	Change in fair value of available-for-sale financial assets
	90	Deferred taxes on available-for-sale financial assets
	165	Changes in accrued pensions
	41	Deferred taxes on accrued pensions
	72,757	Issuance of common stock by assets in kind
	3,735	Conversion of convertible bonds
	691	Non-cash share-based payments
3,604	3,604	Changes in minority interest
3,674	**160,550**	**Balance at December 31, 2006**

Audit Opinion

We have audited the consolidated financial statements prepared by QSC AG, Cologne, Germany, comprising the balance sheet, the income statement, the statement of changes in equity, the statement of recognized income and expense, the cash flow statement and the notes to the consolidated financial statements, together with the group management report for the fiscal year from January 1 to December 31, 2006. The preparation of the consolidated financial statements and group management report in accordance with IFRSs as adopted by the EU, and the additional requirements of German commercial law pursuant to Sec. 315a (1) HGB are the responsibility of the parent company's management. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.
We conducted our audit of the consolidated financial statements in accordance with Sec. 317 HGB ["Handelsgesetzbuch": German Commercial Code] and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer [Institute of Public Auditors in Germany] (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of the entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.
In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to Sec. 315a (1) HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements, and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks relating to future development.

Eschborn/Frankfurt am Main, Germany, March 21, 2007
Ernst & Young AG
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft

Bösser	Janssen
Wirtschaftsprüfer	Wirtschaftsprüfer

Notes to the Consolidated Financial Statements for Fiscal Year 2006

CORPORATE INFORMATION

QSC AG (QSC, the Company or the Group) is a nationwide telecommunication provider with its own DSL network that offers comprehensive broadband communication to business customers and residential customers: From leased lines in a variety of bandwidths to voice and data services to networking of enterprise locations (IP-VPN).
QSC is a stock corporation registered in the Federal Republic of Germany whose legal domicile is Mathias-Brüggen-Strasse 55, 50829 Cologne, Germany. The Company is carried on the Register of Companies of the Local Court of Cologne under Number HRB 28281. QSC has been listed on the Deutsche Börse Stock Exchange since April 19, 2000, and on the Prime Standard since the beginning of 2003 following the reorganization of the equity market. On March 22, 2004, QSC was added to the TecDAX index, which includes the 30 largest and most liquid technology issues in the Prime Standard.

BASIS OF PREPARATION

1 General principles

The Company has prepared the consolidated financial statements as required in accordance with the rules of § 315a (1) of the German GAAP (HGB) in combination with article 4 of the regulation (EG) number 1606/2002 of the European Parliament and the council dated July 19, 2002 and is thus exempt from preparing consolidated financial statements in accordance with the German GAAP (HGB). The consolidated financial statements for the year ended December 31, 2006, have been prepared in accordance with the International Financial Reporting Standards (IFRS), and the supplementary rules of § 315a (1) HGB. The consolidated financial statements have been prepared in accordance with the IFRS and International Accounting Standards (IAS) issued by the International Accounting Standards Board (IASB) as well as their interpretation by the International Financial Reporting Interpretations Committee (IFRIC – originated from the former Standing Interpretations Committee, SIC) that are required to be applied in the EU and which are mandatory at the balance sheet date. The consolidated financial statements comprise the financial statements of QSC and its subsidiaries (the Group) as of December 31, each year. The consolidated financial statements are presented in euros and all amounts, except when otherwise indicated, are rounded to the nearest thousand (T €).

2 Basis of consolidation

The consolidated financial statements comprise the financial statements of QSC and its subsidiaries as at December 31 each year. The financial statements of the subsidiaries are prepared for the same reporting year as the parent company, using consistent accounting policies. All intragroup balances, transactions, income and expenses and profits and losses resulting from intragroup transactions that are recognized in assets, are eliminated in full. Subsidiaries are fully consolidated from the date of acquisition, being the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases. Minority interests represent the portion of profit or loss and net assets not held by the Group and are presented separately in the income statement and within equity in the consolidated balance sheet, separately from parent shareholders' equity. Acquisitions of minority interests are accounted for using the parent entity extension method, whereby, the difference between the consideration and the book value of the share of the net assets acquired is recognized as goodwill. The subsidiaries and associated companies that are included in the consolidated financial statements are listed in note 39.

3 Changes in accounting policies

The accounting policies adopted are consistent with those of the previous financial year except as follows:
QSC has for the first time adopted the following new and amended IFRS and IFRIC interpretations during the year. Adoption of these revised standards and interpretations did not have any material effect on the financial statements of the Group. They did however give rise to additional disclosures.

- Changes in IAS 19 - Employee Benefits
  The accrued pensions as of December 31, 2003, and 2004, were adjusted in conjunction with the changeover to IFRS. In connection with these adjustments, the Company adopted the amendments to IAS 19 published by the IASB in December 2004, from January 1, 2005, onwards. Amongst others, these amendments open up an option for the recognition of actuarial gains and losses. This option can only be used for all performance-oriented pension plans in a consistent manner. Therefore, QSC will recognize the actuarial gains and losses directly in equity not affecting net income.

- IAS 39 Amendment for financial guarantee contracts
  Amended the scope of IAS 39 to require financial guarantee contracts that are not considered to be insurance contracts to be recognised initially at fair value and to be remeasured at the higher of the amount determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets and the amount initially recognised less, when appropriate, cumulative amortisation recognised in accordance with IAS 18 Revenue. This amendment did not have an effect on the financial statements.

- Amendment for the fair value option
  Amended IAS 39 to restrict the use of the option to designate any financial asset or any financial liability to be measured at fair value through the income statement. The Group does not use this option, hence the amendment does not have an effect on the financial statements.

- IFRIC 4 - Determining Whether an Arrangement contains a Lease
  QSC adopted IFRIC Interpretation 4 as of January 1, 2006, which provides guidance in determining whether arrangements contain a lease to which lease accounting must be applied. This change in accounting policy has not had a significant impact on the Group as at December 31, 2006 or December 31, 2005.

4 Significant areas requiring the use of judgement and estimates

The application of accounting policies requires the use of judgement as well as of forward-looking assumptions and estimates. Actual results may differ from those assumptions and estimates, with the result that there is a substantial risk that a significant adjustment to the carrying amounts of assets and liabilities could become necessary within the coming fiscal year. The use of judgement, assumptions and estimates was necessary in particular importance for the accounting treatment of the following items:

The Group determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the 'value in use' of the cash-generating units to which the goodwill is allocated. Estimating a value in use amount requires management to make an estimate of the expected future cash flows from the cash-generating unit and also to choose a suitable discount rate in order to calculate the present value of those cash flows. The carrying amount of goodwill at December 31, 2006 was T € 47.450 (2005: T € 9.265). Further details are given in Note 18.

Deferred tax assets are recognised for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and level of future taxable profits together with future tax planning strategies. Further details are contained in Note 43.

The cost of defined benefit pension plans and other post employment medical benefits is determined using actuarial valuations. The actuarial valuation involves making assumptions about discount rates, expected rates of return on assets, future salary increases, mortality rates and future pension increases. Due to the long term nature of these plans, such estimates are subject to significant uncertainty. The net employee liability at December 31, 2006 is T € 721 (2005: T € 796). Further details are given in Note 30.

The expense recognized for share-based renumeration, in cases where equity instruments are used to remumerate work performed, is measured using an appropriate option price model. The computation uses assumptions relating to the risk-free interest rate relevant for the duration of the option, the expected dividend to be paid and expected market price volatility. Due to the the long-term nature of these remuneration arrangements, the estimates used are subject to significant uncertainties. The amounts, recognized in the future in profit or loss, totalled T € 1,124 (2005: T € 98) at December 31, 2006.

Trade account receivables are presented in the balance sheet net of allowances. Allowances for doubtful debts are measured on the basis of regular reviews and assessments which are performed in conjunction with credit monitoring. The assumptions applied to reflect future payment behavior and customer creditworthiness are subject to significant uncertainties. At December 31, 2006, allowances totalling T € 4,775 (2005: T € 1,822) were recognized on trade receivables.

Property, plant and equipment and intangible assets are measured on initial recognition at cost. Items of property, plant and equipment and intangible assets with a finite useful life are subsequently depreciated/amortized on a straight-line basis over the assumed useful lives of the assets. These assumed useful lives are determined on the basis of past experience and are subject to significant uncertainties, in particular with regard to unforeseen technological developments.

A provision is recognized when the Group has a legal or constructive obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to the settle the obligation and a reliable estimate can be made of the amount of the obligation. Such estimates are subject to significant uncertainties. At December 31, 2006, provisions totalling T € 1,512 (2005: T € 930) were recognized in the balance sheet.

5 Summary of significant accounting policies

Revenue recognition + Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Group and the revenue can be reliably measured. Revenue is measured at the fair value of the consideration received, excluding discounts, rebates, and other sales taxes or duty. The following specific recognition criteria must also be met before revenue is recognized:

- Revenue from the installation of leased lines is recognized by reference to the stage of completion. Stage of completion is measured by reference to labor hours incurred to date as a percentage of total estimated labor hours for each contract. Where the contract outcome cannot be measured reliably, revenue is recognized only to the extent of the expenses incurred that are recoverable.
- Revenue from the installation of customer lines is deferred and recognized on a time-apportioned basis over an average contractual term of 24 months.
- Revenue from the sale of goods is recognized when the significant risks and rewards of ownership of the goods have passed to the buyer, usually on dispatch of the goods.
- Revenue is recognized as interest accrues (using the effective interest method that is the rate that exactly discounts estimated future cash receipts through the expected life of the financial instrument to the net carrying amount of the financial asset).

Foreign currency translation + The consolidated financial statements are presented in Euro, which is the Company's functional and presentation currency. Transactions in currencies other than the Euro are originally recorded at the exchange rate at the day the transaction is made between the Euro and the respective foreign currency. The difference between the exchange rate at the day the transaction was made and the exchange rate at the balance sheet date or at the day the transaction is finally closed, if sooner, are included in the income statement.

Property, plant and equipment + Plant and equipment is stated at cost, excluding the cost of day-to-day servicing, less accumulated depreciation and accumulated impairment in value. The cost of day-to-day servicing includes the cost of replacing part of such plant and equipment when that cost is incurred if the recognition criteria are met. Depreciation is calculated using the straight-line method over the useful lives of the assets.

Plant and equipment that consists of different components which can be separated clearly and that have different useful lives, are split up for the purpose of depreciation. For the calculation of depreciation the different useful lives are used. The carrying values of plant and equipment are reviewed for impairment when events or changes in circumstances indicate that the carrying value may not be recoverable. An item of property, plant and equipment is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. Any gain or loss arising on derecognition of the asset (calculated as the difference between net disposal proceeds and the carrying amount of the asset) is included in the income statement in the year the asset is derecognized.
The asset's residual values, useful lives and methods are reviewed, and adjusted if appropriate, at each financial year end. When each major inspection is performed, its cost is recognized in the carrying amount of the plant and equipment as a replacement if the recognition criteria are satisfied.

The following estimated useful lives have been used in calculating depreciation:

	Useful life in years
Asset	
Network equipment and plant	5 to 8
Leasehold improvements	8 to 10
Electronic communication equipment	1 to 5
Office equipment and other assets	3 to 13

Borrowing costs + Borrowing costs are recognized as an expense when incurred.

Business combinations and goodwill + Business combinations are accounted for using the acquisition accounting method. This involves recognising identifiable assets and liabilities of the acquired business at fair value.
Goodwill acquired in a business combination is initially measured at cost being the excess of the cost of the business combination over the Group's interest in the net fair value of the acquiree's identifiable assets, liabilities and contingent liabilities. Following initial recognition, goodwill is measured at cost less any accumulated impairment losses. For the purpose of impairment testing, goodwill acquired in a business combination is, from the acquisition date, allocated to each of the Group's cash generating units that are expected to benefit from the synergies of the combination, irrespective of whether other assets or liabilities of the Group are assigned to those units.
The amount recognized as an impairment loss is determined by measuring the recoverable amount of the cash generating units to which goodwill has been allocated.
The cash generating units to which the goodwill is allocated by QSC correspond to the segments, which are determined by the group's primary reporting format. Impairment is determined by assessing the recoverable amount of the segments to which the goodwill relates. The recoverable amount of an asset is the higher of both amounts from fair value of an asset or a cash-generating unit, less selling cost and the useful life. Where the carrying amount of an asset exceeds its recoverable amount, the asset is recognized as impaired and is written down on its recoverable amount.

Other intangible assets + Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is the fair value as at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortisation and any accumulated impairment losses. Internally generated intangible assets, excluding capitalized development costs, are not capitalized and expenditure is reflected in the income statement in the year in which the expenditure is incurred.
The useful lives of intangible assets are assessed to be either finite or indefinite.
Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortisation period and the amortisation method for an intangible asset with a finite useful life is reviewed at least at each financial year end. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset is accounted for by changing the amortisation period or method, as appropriate, and treated as changes in accounting estimates. The amortisation expense on intangible assets with finite lives is recognized in the income statement in the expense category consistent with the function of the intangible asset.
Intangible assets with indefinite useful lives are tested for impairment annually either individually or at the cash generating unit level. Such intangibles are not amortized. The useful life of an intangible asset with an indefinite life is reviewed annually to determine whether indefinite life assessment continues to be supportable. If not, the change in the useful life assessment from indefinite to finite is made on a prospective basis.
QSC's intangible assets relate primarily to software, licenses and similar rights as well as one-time costs to switch on customer lines. The Company amortizes licenses over a period of 10 years and software over a period of 4 years. Non-recurring costs incurred to initial switch on customer lines are amortized over an average contractual period of 24 months.

Investments and other financial assets + Financial assets within the scope of IAS 39 are classified as either financial assets at fair value through profit or loss, loans and receivables, held to maturity investments, and available for sale financial assets, as appropriate. When financial assets are recognized initially, they are measured at fair value, plus, in the case of investments not at fair value through profit or loss, directly attributable transaction costs.QSC determines the classification of its financial assets after initial recognition and, where allowed and appropriate, re-evaluates this designation at each financial year end.
Financial assets at fair value through profit or loss includes financial assets held for trading and financial assets designated upon initial recognition as at fair value through profit and loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. Gains or losses on investments held for trading are recognized in the income statement.
Receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in active market. Such assets are carried at amortized cost using the effective interest method. Gains and losses are recognized in income when the receivables are derecognized or impaired, as well as through the amortization process.

Held-to-maturity investments are non-derivative financial assets which carry fixed or determinable payments and fixed maturities and which QSC has the positive intention and ability to hold to maturity. After initial measurement held to maturity investments are measured at amortized cost. This cost is computed as the amount initially recognized minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initially recognized amount and the maturity amount, less allowance for impairment. This calculation includes all fees and points paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums and discounts. Gains and losses are recognized in the income statement when the investments are derecognized or impaired, as well as through the amortisation process.
Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified in any of the three preceding categories. After initial measurement, available for sale financial assets are measured at fair value with unrealized gains or losses being recognized directly in equity in the net unrealized gains reserve. When the investment is disposed of, the cumulative gain or loss previously recorded in equity is recognized in the income statement. Interest earned or paid on the investments is reported as interest income or expense using the effective interest rate. Dividends earned on investments are recognized in the income statement as 'Dividends received' when the right of payment has been established.

Cash and short-term deposits + Cash and short-term deposits in the balance sheet comprise cash at banks and at hand and short term deposits with an original maturity of three months or less.

Provisions + Provisions are recognised when the Group has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation. Where the Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset but only when the reimbursement is virtually certain. The expense relating to any provision is presented in the income statement net of any reimbursement. If the effect of the time value of money is material, provisions are discounted using a current pre tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

Pensions + QSC operates two defined-benefit pension plans. The cost of providing benefits under the defined-benefit plans is determined separately for each plan using the projected unit credit actuarial valuation method. Actuarial gains and losses are recognized directly in equity in other reserves. The assumptions that were made by the Company to evaluate the actuarial obligations are specified in note 30.

Stock option programs + QSC's employees also receive share-based remuneration in the form of equity instruments in return for work performed. The expense of issuing these equity instruments (based on the stock option programs resolved or modified after November 7, 2002) are measured on the basis of the fair value of the equity instrument at the grant date using an appropriate option price -model. Further details are provided in Note 41. The expense recognized for granting equity instruments (as well as the corresponding increase in equity) is spread over the vesting period of the options. The amount recognized in the income statement reflects the change in the cumulative amount of deferred expense at the beginning and the end of the reporting period.
No expense is recognized for remuneration entitlements which cannot be exercised. If the terms and conditions of a share-based remuneration agreement are modified, QCS recognizes as a minimum the level of expense that would have arisen if the terms and conditions had not been modified. If a share-based renumeration agreement is cancelled, QSC accounts for the renumeration agreement as if it had been exercised on the cancellation date. Any previously deferred expense is recognized immediately as an expense in the income statement.
The dilutive effect of any outstanding stock options is taken into account as an additional dilution for the purposes of measuring earnings per share (see Note 14).

Leases + The determination of whether an arrangement is, or contains a lease is based on the substance of the arrangement at inception date of whether the fulfilment of the arrangement is dependent on the use of a specific asset or assets or the arrangement conveys a right to use the asset. A reassessment is made after inception of the lease only if one of the following applies:
a) There is a change in contractual terms, other than a renewal or extension of the arrangement;
b) A renewal option is exercised or extension granted, unless the term of the renewal or extension was initially included in the lease term;
c) There is a change in the determination of whether fulfilment is dependant on a specified asset; or
d) There is a substantial change to the asset.
Where a reassessment is made, lease accounting shall commence or cease from the date when the change in circumstances gave rise to the reassessment for scenarios a), c) or d) and at the date of renewal or extension period for scenario b).

Finance leases, which transfer to the Group substantially all the risks and benefits incidental to ownership of the leased item, are capitalized at the inception of the lease at the fair value of the leased property or, if lower, at the present value of the minimum lease payments. Lease payments are apportioned between the finance charges and reduction of the lease liability so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged reflected in the income statement.
Capitalized leased assets are depreciated over the shorter of the estimated useful life of the asset and the lease term, if there is no reasonable certainty that the Group will obtain ownership by the end of the lease term.
Lease arrangements which do not transfer substantially all the risks and rewards incidental to ownership from the Group to the lessee are classified as operating leases. Operating lease payments are recognized as an expense in the income statement on a straight line basis over the lease term.

Treasury shares + Own equity instruments which are reacquired (treasury shares) are deducted from equity. No gain or loss is recognized in the income statement on the purchase, sale, issue or cancellation of the Group's own equity instruments.

Taxes + Current income tax assets and liabilities for the current and prior periods are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted by the balance sheet date. Current income tax relating to items recognized directly in equity is recognized in equity and not in the income statement.

Deferred income tax is provided using the liability method on temporary differences at the balance sheet date between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax liabilities are recognized for all taxable temporary differences, except:
- where the deferred income tax liability arises from the initial recognition of goodwill or of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, where the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

Deferred income tax assets are recognized for all deductible temporary differences, carry forward of unused tax credits and unused tax losses, to the extent that it is probable that taxable profit will be available against which the deductible temporary differences, and the carry forward of unused tax credits and unused tax losses can be utilized except:
- where the deferred income tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss; and
- in respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred income tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized.

The carrying amount of deferred income tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred income tax asset to be utilized. Unrecognized deferred income tax assets are reassessed at each balance sheet date and are recognized to the extent that it has become probable that future taxable profit will allow the deferred tax asset to be recovered.

Deferred income tax assets and liabilities are measured at the tax rates that are expected to apply to the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the balance sheet date.

Deferred income tax relating to items recognized directly in equity is recognized in equity and not in the income statement. Deferred income tax assets and deferred income tax liabilities are offset, if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred income taxes relate to the same taxable entity and the same taxation authority.

Revenues, expenses and assets are recognized net of the amount of sales tax except:
- where the sales tax incurred on a purchase of assets or services is not recoverable from the taxation authority, in which case the sales tax is recognized as part of the cost of acquisition of the asset or as part of the expense item as applicable; and
- receivables and payables that are stated with the amount of sales tax included.

The net amount of sales tax recoverable from, or payable to, the taxation authority is included as part of receivables or payables in the balance sheet.

6 Future changes in accounting policies

Accounting Standards / Interpretations which are not yet mandatory + A number of new and amended Standards and Interpretations were issued by the IASB and the IFRIC over the course of 2006, which become mandatory for reporting entities either on 1 January 2007 or for financial years commencing after that date, and which have already been endorsed by the EU. This is the case for
- IFRS 7 – Financial Instruments: Disclosures
- IAS 1 – Presentation of Financial Statements – Capital Disclosures
- IFRIC 7 – Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies
- IFRIC 8 – Scope of IFRS 2
- IFRIC 9 – Reassessment of Embedded Derivatives

It is not expected that the new rules or amendments contained in the above-mentioned Standards or Interpretations will have a material effect on QSC's consolidated financial statements. The first-time application of IFRS 7 will, however, result in additional disclosures in the Notes and to a more detailed presentation. IFRS 7 replaces the existing IAS 30 (Disclosures in the Financial Statements of Banks and Similar Financial Institutions) as well as all disclosure requirements contained in IAS 32 (Financial Instruments: Disclosure and Presentation). The objective of the Standard is to make clear the significance of financial instruments for an entity's financial position and performance and to show the nature and extent of risks arising from financial instruments.

INCOME STATEMENT DISCLOSURES

7 Net revenues

Revenues are generated with wholesale partners and resellers and with direct customers. The resellers offer QSC's products and services to consumers under their own name and for their own account; in doing so, they serve as the interface to the consumer, thus also assuming the risk of bad debts. The structure of the Company's revenues by segment is shown in note 40.

8 Cost of revenues

	2006 in T €	2005 in T €
Cost of revenues		
Cost of materials	121,919	99,577
Building, operation and maintenance of the network	47,205	34,319
Depreciation and amortization	23,081	21,858
Personnel expenses	11,300	9,774
Non-cash share-based payments	95	4
Cost of revenues	**203,600**	**165,532**

The costs of revenues include the costs of materials, the costs of building, operating and maintaining the network, personnel expenses for employees whose jobs relate to technology, non-cash share-based payments under stock option programs, as well as depreciation and amortization on the hardware and software employed in connection with technology operations. Non-recurring costs of provisioning customer connections are capitalized and depreciated over the average contract term of 24 months.

9 Selling and marketing expenses

	2006 in T €	2005 in T €
Selling and marketing expenses		
Personnel expenses	16,642	13,181
Commissions	12,516	7,848
Other selling and marketing expenses	5,667	3,845
Allowance of bad debts and fair dealing payments	3,870	2,940
Advertising expenses and allowances	2,697	1,583
Depreciation and amortization	1,519	1,077
Non-cash share-based payments	188	19
Selling and marketing expenses	**43,099**	**30,493**

Selling and marketing expenses include, in particular, advertising expenses and advertising expense allowances, regular commission payments to dealers and distributors, allowances for bad debts, personnel expenses for sales and marketing employees, as well as depreciation and amortization on the hardware and software employed in connection with selling and marketing operations. Analogously to the provisioning costs, the non-recurring commission payments to dealers and dis tributors for each new customer line are capitalized and amortized over the average contract term of 24 months.

10 General and administrative expenses

	2006 in T €	2005 in T €
General and administrative expenses		
Other general and administrative expenses	9,905	8,441
Personnel expenses	12,162	7,103
Depreciation and amortization	3,043	1,360
Non-cash share-based payments	408	12
General and administrative expenses	**25,518**	**16,916**

In addition to the personnel expenses for the members of the Management Board and for staff position, as well as for employees from finance, central purchasing, human resources and legal operations who work in administration, the general and administrative expenses item also includes costs for the administration buildings, legal and consulting costs, corporate communication costs, including investor relations, as well as depreciation and amortization on the hardware and software employed in connection with administrative operations.

11 Research and development expenses

	2006 in T €	2005 in T €
Research and development expenses		
Personnel expenses	207	324
Depreciation and amortization	7	113
Research and development expenses	**214**	**437**

Research and development expenses essentially consist of the personnel expenses for the employees who work in these operations and expenses stemming from the depreciation and amortization of the hardware and software employed in connection with development operations.

12 Other operating expenses and income

	2006 in T €	2005 in T €
Other operating income		
Miscellaneous operating income	256	251
Reversals of unutilized provisions and write-off of liabilities	2,621	179
Gains from disposal of long-term assets	14	156
Other operating income	**2,891**	**586**

	2006 in T €	2005 in T €
Other operating expenses		
Miscellaneous operating expenses	75	240
Losses from disposal of long-term assets	83	21
Other operating expenses	**158**	**261**

Reversals of unutilized provisions and the write-off of liabilities relates primarily to amounts previously recognized as a result of licenses granted to QSC in conjunction with the (German) Telecommunication Act.

13 Financial result and income from associated companies

	2006 in T €	2005 in T €
Financial income		
Interest income	2,205	974
Gains from exchange rate differences	0	41
Financial income	**2,205**	**1,015**

	2006 in T €	2005 in T €
Financial expenses		
Interest expenses	2,223	797
Losses from exchange rate differences	11	18
Financial expenses	**2,234**	**815**

The Company's income from associated companies in the amount of T € 280 in 2005 represents payments from the liquidation assets of Netchemya S.p.A., of Italy (Netchemya), a QSC equity investment from fiscal 2000. The liquidation proceedings were concluded on October 31, 2005.

14 Earnings per share

	2006	2005
Earnings per share (basic and diluted) in €		
Net loss attributable to ordinary equity holders of the parent in T €	(5,416)	(18,186)
Weighted average number of common shares	123,992,746	108,967,370
Earnings per share (basic and diluted) in €	**(0.04)**	**(0.17)**

For the purposes of calculating undiluted earnings per share, the profit attributable to the holders of the Company's common stock are divided by the weighted average number of shares of common stock in circulation during the year.
For the purposes of calculating diluted earnings per share, the profit attributable to the holders of the Company's common stock is divided by the sum of the weighted average number of shares of common stock plus the weighted average number of shares of common stock that would arise if all potential shares of common stock with dilutive effect were converted into shares.

This dilutive effect was not taken into consideration for the 2006 and 2005 fiscal years, as QSC had incurred losses during these reporting periods and the adjustment would have resulted in a decrease in losses per share.
During the period between the balance date and the date on which the consolidated financial statements were authorized for issue, no transactions involving existing or potential shares of common stock have occurred which would have significantly changed the weighted average number of issued shares at December 31, 2006.

15 Personnel expenses and employees

	2006 in T €	2005 in T €
Personnel expenses		
Wages and salaries	35,560	25,747
Social security contribution	4,316	4,133
Net pension costs	435	502
Non-cash share-based payments	691	35
Personnel expenses	41,002	30,417

During 2006, the Group had on average 585 employees (2005: 419 employees).

BALANCE SHEET DISCLOSURES

16 Property, plant and equipment

	Network equipment and plant in T €	Operational and office equipment in T €	Total in T €
Cost			
Cost at January 1, 2005	104,746	20,251	124,997
Additions	16,616	4,232	20,848
Additions by consolidation	8,353	925	9,278
Disposals	(14,804)	(325)	(15,129)
Cost at December 31, 2005	**114,911**	**25,083**	**139,994**
Additions	25,743	6,304	32,047
Additions by consolidation	84,335	7,882	92,217
Disposals	(4,017)	(699)	(4,716)
Cost at December 31, 2006	**220,972**	**38,570**	**259,542**
Accumulated depreciation			
Accumulated depreciation at January 1, 2005	79,077	10,820	89,897
Additions	14,753	4,713	19,466
Additions by consolitdation	6,281	658	6,939
Disposals	(9,478)	(201)	(9,679)
Accumulated depreciation at December 31, 2005	**90,633**	**15,990**	**106,623**
Additions	14,390	6,562	20,952
Additions by consolidation	67,599	7,499	75,098
Disposals	(4,584)	(36)	(4,620)
Accumulated depreciation at December 31, 2006	**168,038**	**30,015**	**198,053**
Carrying amount at December 31, 2005	**24,278**	**9,093**	**33,371**
Carrying amount at December 31, 2006	**52,934**	**8,555**	**61,489**

The carrying amount of plant and equipment held under finance leases and hire purchase contracts totalled T € 27,636 (2005: T € 17,326) at December 31, 2006. Additions during the year amounted to T € 32,047 (2005: T € 20,848). At December 31, 2006, the line item "Network and equipment" includes assets under construction amounting to T € 1,588 (2005: T € 4,171).

17 Goodwill

	Goodwill in T €
Cost	
Cost at January 1, 2005	2,393
Additions	6,872
Disposals	-
Cost at December 31, 2005	9,265
Additions	38,185
Disposals	-
Cost at December 31, 2006	47,450
Accumulated amortization	-
Accumulated amortization at January 1, 2005	-
Additions	-
Disposals	-
Accumulated amortization at December 31, 2005	-
Additions	-
Disposals	-
Accumulated amortization at December 31, 2006	-
Carrying amount at December 31, 2005	9,265
Carrying amount at December 31, 2006	47,450

Additions in 2006 relate in particular to goodwill arising on the business combination with Broadnet. Further information is provided in Note 39.

18 Impairment of Goodwill

Goodwill acquired in conjunction with business combinations was allocated to the following cash-generating units, which correspond to QSC´s business segments, for the purpose of impairment testing:

	2006 in T €	2005 in T €
Carrying amount of goodwill		
Large accounts	5,386	-
Business customers	13,958	2,393
Wholesale/Reseller	27,264	6,872
Residential customers	842	-
Carrying amount of goodwill	47,450	9,265

The recoverable amount of the Group's cash-generating units is determined on the basis of their value in use, which, in turn, is measured using five-year cash flow forecasts. These future cash flows are discounted to their present value using a pre-tax discount factor of 10.5 percent (2005: 10.0 percent). Cash flows after five years are extrapolated on the assumption of a growth rate of 3 percent (2005: 3 percent). The assumed growth rate corresponds to the value commonly applied within the telecommunication sector.
The following assumptions, which are used to measure the value in use of cash-generating units, are subject to estimation uncertainties:

- gross profit margins
- discount factor
- price changes
- market share developments

Gross profit margins are determined on the basis of average values for past financial years. In this context, it should be noted that higher network capacity utilization as well as the growing size of the Group increase efficiency and have a positive impact on the development of gross profit margins. The discount factor reflects management's assessment of entity-specific risks and comprises a basis interest rate (risk-free and appropriate for an alternative investment with a similar maturity) and a risk-uplift factor (reflecting the risk structure of the Group and of the telecommunication sector in general). The rate of price changes applied in the forecasts is derived from actual price changes in the past (and which are used as an indicator for future price changes) and on the basis of forecasts conducted by independent market research institutions. The future development of market shares is one of the few assumptions where the cash-generating units differ significantly. QSC expects that the market share of all three strategic segments (Large Accounts, Business Customers, and Wholesale/Reseller) will rise, whereas the market share for the Residential Customers segment will drop.
QSC believes that, based on reasonable management judgement, no change to the underlying assumptions used to determine the value in use of the various cash-generating units would result in the carrying amounts of those cash-generating units significantly exceeding their recoverable amount.

19 Other intangible assets

	Licenses in T €	Software in T €	Other in T €	Total in T €
Cost				
Cost at January 1, 2005	1,516	5,957	5,791	13,264
Additions	-	1,632	4,404	6,036
Additions by consolidation	49	472	1,180	1,701
Disposals	-	-	-	-
Cost at December 31, 2005	**1,565**	**8,061**	**11,375**	**21,001**
Additions	36	2,765	5,211	8,012
Additions by consolidation	2,764	1,281	7,877	11,922
Disposals	(1,542)	(1,769)	(3)	(3,314)
Cost at December 31, 2006	**2,823**	**10,338**	**24,460**	37,621
Accumulated amortization				
Accumulated amortization at December 31, 2005	822	3,639	2,285	6,746
Additions	161	1,226	3,555	4,942
Additions by consolidation	38	424	47	509
Disposals	-	-	-	-
Accumulated amortization at December 31, 2005	**1,021**	**5,289**	**5,887**	**12,197**
Additions	233	1,568	4,897	6,698
Additions by consolidation	2,152	1,183	634	3,969
Disposals	(1,536)	(1,398)	(360)	(3,294)
Accumulated amortization at December, 2006	**1,870**	**6,642**	**11,058**	**19,570**
Carrying amount at December 31, 2005	**544**	**2,772**	**5,488**	**8,804**
Carrying amount at December 31, 2006	**953**	**3,696**	**13,402**	**18,051**

The line item Licenses includes the disposal during the financial year of Class 3 licenses for telecommunication services for the general public and Class 4 licences for voice telephone services based on telecommunication networks operated by the Group. These licenses were issued by the Federal Network Agency (Bundesnetzagentur). As a result of amendments to the (German) Telecommunication Act, the requirement to hold a license has been removed and replaced by an annual telecommunication levy, the exact amount of which is still be be fixed. QSC has accordingly recognized an impairment loss of T € 360 on the remaining carrying amount. It has also recognized a provision for the estimated amount of the outstanding levy. The column "Other" also includes intangible assets identified in conjunction with the purchase price allocation process, namely Broadnet's customer relationships (T € 6,050) and the Broadnet brand-name (T € 950).
At December 31, 2006, the line item "Other" contains capitalized costs incurred to initial switch on customer lines with a carrying amount of T € 6,217 (2005: T € 4,256). These costs are being amortized over an average contractual period of 24 months.

20 Trade receivables

	2006 in T €	2005 in T €
Trade receivables		
Trade receivables	52,776	34,168
Receivables from related parties	2	9
Trade receivables	**52,778**	**34,177**

Trade receivables do not bear interest and generally have an original maturity of between 30 and 90 days. At December 31, 2006, trade receivables amounting to T € 4,775 (2005: T € 1,822) were impaired. Allowances developed as follows:

	2006 in T €	2005 in T €
Trade receivables		
Trade receivables at January 1	1,822	3,649
Charge for the year	3,460	3,280
Amounts written off	(590)	(3,281)
Unused amounts reversed	(1,379)	(1,826)
Additions by consolidation	1,462	-
Trade receivables at December 31	**4,775**	**1,822**

The analysis of overdue trade receivables at December 31 on which no allowances were recorded was as follows:

	2006 in T €	2005 in T €
Non-impaired trade reseivables		
neither past due nor impaired	31,208	22,051
past due but not impaired		
< 90 days	20,001	10,998
91 - 120 days	1,021	493
> 120 days	548	635
Non-impaired trade reseivables	**52,778**	**34,177**

21 Prepayments

Prepayments total T € 1,099 (2005: T € 2,096) and essentially consist of prepaid expenses for leased lines and technology premises, as well as insurance.

22 Other receivables and short-term financial assets

Other short-term assets totalled T € 3,566 (2005: T € 914) and related primarily to tax receivables.

23 Cash and short-term deposits as well as available-for-sale financial assets

	2006 in T €	2005 in T €
Cash and short-term deposits and available-for-sale financial assets		
Cash and short-term deposits	45,986	30,313
Available-for-sale financial assets	62,927	26,065
Cash and short-term deposits and available-for-sale financial assets	108,913	**56,378**
Restricted cash	-	(4,300)
Available liquidity	108,913	**52,078**

Cash and short-term deposits as of December 31, 2005, include restricted cash in the amount of T € 4,300. This consists of the remaining portion of the second tranche of the acquisition price for the acquisition of Ventelo, which was paid in fincal year 2006. Available-for-sale assets comprise marketable commercial papers which are issued as bearer instruments by first-rate industrial or financial companies.

24 Capital stock

	2006	**2005**
Capital stock		
Capital stock in T €	133,898	115,033
No-par common stock in €	133,897,686	115,033,078

Each share of stock entitles the registered owner to cast one vote at the Annual Shareholders Meeting and enjoys full dividend entitlement. The voting right is not subject to any restrictions. The capital stock rose by T € 2,483 as a result of the issuance of shares of common stock in conjunction with stock option programs and by T € 16,382 as a result of a capital increase by assets in kind in conjunction with the acquisition of Broadnet.

25 Capital surplus

The capital surplus amounts to T € 557,961 as of December 31, 2006 (2005: T € 499,643). This amount includes deferred share-based remuneration of T € 1,124 (2005: T € 98) which relates to the Company's stock option program and which will be recognized in the future in profit or loss. Further details are explained in note 41.

26 Authorized and conditional capital

The Company's authorized capital was reduced T € 4,920 in 2006 following a non-cash increase in capital stock and amounts to T € 52,580 at December 31, 2006.
The Company's conditional capital amounts to T € 30,878 at December 31, 2006.

27 Other reserves

Other reserves include gains and losses on available-for-sale financial assets, as well as actuarial gains and losses on defined-benefit pension plans. The values for the 2006 and 2005 fiscal years are shown in the Consolidated Statement of Changes in Shareholders' Equity.

28 Finance lease obligations

	2006	2005
Finance lease obligations		
Long-term portion	16,044	10,687
Short-term portion	13,443	8,437
Finance lease obligations	**29,487**	**19,124**

A lease liability is classified as non-current if repayment to the lessor is due to take place within 12 months of the balance sheet date. The long-term portion of finance lease obligations does not contain any obligations with a maturity of more than 5 years. Total additions to property, plant and equipment in 2006 under finance leases (in particular relating to network components and equipment placed with customers) amounted to T € 18,899, of which T € 3,566 was depreciated in 2006. This expense is included in the depreciation expense on property, plant and equipment. The fair value of leased items at acquisition date corresponded largely to acquisition cost. The internal rate of return in the finance lease agreements averages 6 percent. Future obligations, including financing costs of T € 1,691 under these agreements amount to T € 15,636 for the year 2007, T € 11,622 for the year 2008 and T € 3,920 for the year 2009.

29 Convertible bonds

	2006	2005
Convertible bonds		
Amount of loan in T €	36	60
Number of convertible bonds	3,576,534	5,968,676

The convertible bonds issued in conjunction with stock option programs have a nominal value of € 0.01 each. The convertible bond item includes all convertible bonds subscribed by employees that have not yet been converted although they are still eligible for conversion.

30 Accrued pensions

Accrued pensions were restated at December 31, 2003 and 2004 in conjunction with the first-time adoption of IFRS. The amendments issued by the IASB to IAS 19 in December 2004 were applied for the first time with effect from January 1, 2005. Amongst other changes, these amendments allow an optional accounting treatment of actuarial gains and losses. This option is required to be applied for all of an entity's defined benefit plans and for all of its actuarial gains and losses. QSC has opted to recognize all actuarial gains and losses directly in equity.

	2006 in T €	2005 in T €
Pensions		
Present value of defined benefit obligation at January 1	857	636
Service costs	80	65
Interest costs	34	25
Losses from retroactive plan adjustments	-	145
Actuarial gains and losses	(171)	(5)
Benefits paid	(9)	(9)
Present value of defined benefit obligation at December 31	**791**	**857**
Fair value of plan assets at January 1	(61)	(51)
Expected return on plan assets	(2)	(2)
Actuarial gains and losses	6	5
Employer contributions for plan assets	(13)	(13)
Fair value of plan assets at December 31	**(70)**	**(61)**
Accrued pensions at December 31	**721**	**796**
Discount rate	4.70%	4.00%
Expected return on plan assets	3.50%	3.50%
Rate of compensation increase	3.00%	3.00%
Rate of pension indexation	3.00%	3.00%

The composition of the pension expense under defined-benefit plans is as follows:

	2006 in T €	2005 in T €
Net pension costs		
Service costs	80	65
Interest costs	34	25
Expected return on plan assets	(2)	(2)
Losses from retroactive plan adjustments	-	145
Net pension costs	**112**	**233**

One defined-benefit plan is secured through reinsurance that is classified as plan asset in accordance with IAS 19.

31 Long-term liabilities of other shareholders

The long-term liabilities of other shareholders correspond to the consolidated capital account of Communication Services TELE2 GmbH (TELE2) accounted for in the balance sheet of Plusnet GmbH & Co. KG (Plusnet). At the date of foundation of Plusnet, this item corresponded to TELE2's cash capital contribution to Plusnet (see Note 39).

32 Trade payables

	2006 in T €	2005 in T €
Trade payables		
to third parties	42,074	31,559
to related parties	8	37
Trade payables	**42,082**	**31,596**

All trade payables have a term of less than one year.

33 Provisions

	2006 in T €
Provisions	
Other provisions at January 1	881
Arising during the year	2,659
Utilized	(1,250)
Unused amounts reversed	(864)
Other provisions at December 31	**1,426**
Litigation risks at January 1	49
Arising during the year	53
Utilized	-
Unused amounts reversed	(16)
Litigation risks at December 31	86
Provisions	**1,512**

Other provisions comprise mainly obligations to the German Federal Network Agency arising in conjunction with the telecommunication levy payable under the German Telecommunication Act (T € 255), pending losses on onerous contracts relating to unused locations (T € 103), liabilities of uncertain amount and timing (T € 916) and credit notes to be issued (T € 50). These items are measured on the basis of past experience.

34 Deferred revenues

Revenues from non-recurring installation charges are capitalized and amortized over the estimated average customer subscription life of 24 months. Advance payments from customers are also deferred until such time as the corresponding performance has been provided.

35 Other short-term liabilities

All other short-term liabilities have a term of less than one year.

CASH FLOW STATEMENT DISCLOSURES

36 Cash flow from operating activities

Cash flow from operating activities amounted to T € 11,734 (2005: T € 2,700) in fiscal year. The reduction of the loss before tax, as adjusted for the higher level of depreciation and amortization, contributed T € 14,223 to the improvement in cash flow from operating activities. By contract, the increase in trade receivables to T € 15,181 (2005: T € 8,163) which was attributable to the higher level of sales revenue, had a negative impact on cash flow from operating activities.

37 Cash flow from investing activities

Cash flow for investing activities in 2006 totalled T € -36,406 (2005: T € -17,811). The net amount invested in available-for-sale financial assets in 2006 was T € 37,426 (2005: T € 9,841).
Cash outflow for property, plant and equipment and intangible assets amounted to T € 19,224 (2005: T € 9,965). The cash outflow for the acquisition of a subsidiary (net of acquired cash funds) related in 2006 to the acquisition of Broadnet AG (Broadnet). In 2005, it related to the acquisition of celox Telekommunikationsdienste GmbH (celox). Further details are contained in note 39.

38 Cash flow from financing activities

Cash flow from financing activities amounted to T € 40,345 in fiscal year 2006 (2005: T € 22,888). The increase resulted essentially from payments in connection with cash funds raised from other shareholders totalling T € 49,680 (2005: T € 0). This item reflects the injection of cash funds arising in conjunction with the contribution paid in by TELE2 to Plusnet.

OTHER DISCLOSURES

39 Subsidiaries and associated companies

QSC's consolidated financial statements include the following equity investments:

	Share as of Dec. 31, 2006 in %	Shareholders' equity 31.12.2006 in T €	Net(loss)/ profit 2006 in T €
Subsidiaries and associated companies			
Ventelo GmbH (Ventelo), Cologne	100	5,593	531 [1]
Broadnet AG (Broadnet), Hamburg	92.5	41,135	(364) [2]
Plusnet GmbH & Co. KG (Plusnet), Cologne	67.5	69,069	338 [3]
Q-DSL home GmbH (DSL home), Cologne	100	156	131 [1]
010090 GmbH (010090), Cologne	100	1,268	279 [1]
EPAG Domainservices GmbH (EPAG), Cologne	100	(343)	3 [1]

[1] German GAAP (HGB)
[2] IFRS consolidated
[3] IRFS

Broadnet + On June 6, 2006, QSC reached an agreement with the main shareholders and management of Broadnet for the acquisition of 67,2 percent of Broadnet's capital stock. On July 22, 2006, QSC issued a public take-over offer for Broadnet, offering Broadnet shareholders accepting the offer, 1.0542 QSC shares for each Broadnet share. The offer was duly accepted on behalf of 217,847 Broadnet shares. On November 13, 2006, QSC acquired an additional 25 percent of Broadnet's capital stock on the basis of a contract with institutional investors. Depending on a number of agreed conditions being met, the purchase price amounted to a minimum of 1.0542 and a maximum of 1.23 QSC shares for each Broadnet share.

Broadnet is a provider of broadband communication solutions in Germany based on WLL and DSL. Following the acquisition of the majority shareholding in Broadnet, QSC aims to strengthen its higher margin business with corporate customers. With its 92.5 percent shareholding, QSC will be able to implement further corporate organization measures within a short space of time with a view to integrating Broadnet fully into the QSC Group.

One important aspect of the acquisition method used to consolidate Broadnet for the first-time in accordance with IFRS 3 is the allocation of the purchase price to identifiable assets and liabilities and the recognition of the remaining amount (net of deferred tax) as goodwill. For the purposes of the purchase price allocation, all identifiable assets and liabilities were measured at their fair value. The purchase price for 92.5 percent of the shares amounted to T € 78,270 (including transaction costs of T € 2,423). In order to carry out the transactions involved, the Management Board and Supervisory Board resolved to increase the Company's capital stock by Euro 16,381,831 by the issue of 16,381,831 new shares out of authorized capital in return for assets in kind. QSC disbursed T € 160 in cash to acquire 13,565 Broadnet shares and to improve the public take-over offer.

Intangible assets were recognized for the Broadnet brand (T € 950) and for existing customer relationships (T € 6,050). Net of deferred tax liabilities of T € 2,793 relating to those items, the remaining balance of T € 36,320 was recognized as goodwill.
The fair values of Broadnet's identifiable assets and liabilities at the acquisition date were as follows:

	Recognized on acquisition in T €	Carrying amount in T €
Assets		
Long-term assets	18,072	18,072
Goodwill	1,857	1,857
Trademark	950	-
Customer base	6,050	-
Trade receivables	3,420	3,420
Other financial assets and prepayments	3,520	3,520
Cash and short-term deposits	22,781	22,781
Assets	**56,650**	**49,650**
Liabilities		
Deferred taxes	(2,793)	-
Trade payables	(4,128)	(4,128)
Provisions	(1,384)	(1,384)
Other short-term liabilities	(2,791)	(2,791)
Minority interests	(3,604)	-
Liabilities	**(14,700)**	**(8,303)**
Fair value of net assets	41,950	41,347
Goodwill arising on acquisition	36,320	
Total	**78,270**	
Total acquisition costs incl. direct acquisitions costs	(78,270)	
Issuance of common stock	75,686	
Cash and short-term deposits acquired	22,781	
Total consideration	**20,197**	

Broadnet's contribution to the consolidated net loss for the period from June 6 through December 31, 2006, amounted to T € 82. In consolidating Broadnet as of January 1, 2006, the pro-forma net loss contribution had amounted to T € -364, the pro-forma revenue contribution to T 51,105.

Plusnet + On July 10, 2006, QSC and TELE2, founded Plusnet. Following receipt of the approval of the Federal Germany Cartel Office on August 21, 2006, Plusnet commenced operations on September 1, 2006 in line with schedule. QSC and TELE2 hold 67.5 percent and 32.5 percent respectively of Plusnet's capital stock. The underlying agreement stipulates that major decisions are taken unanimously; however, decisions which only impact on QSC may be made without TELE2's approval. Plusnet's objective is operate a Germany-wide DSL network which is to be expanded from (at present) approximately 1,000 central offices to almost 2,000 central offices by the end of 2007. QSC will transfer its Germany wide DSL network to Plusnet, and TELE2 will make a cash contribution of Euro 50 million to finance further network expansion. Both shareholders are entitled to use the assets and services of Plusnet. The latter meets the criteria of a special purpose entity as defined by SIC-12 issued by the Standing Interpretations Committee Interpretation. Plusnet will take over responsibility for the provision of services relating to QSC's core activities which, if Plusnet did not exist, would have to be carried out by QSC itself. QSC has consolidated the special purpose entity with effect from September 1, 2006.

DSL home + On March 31, 2006, QSC acquired 100 percent of the shares of DSL home. The purchase price paid for the formerly non-operative Kristall 40. GmbH totalled T € 27. In accordance with § 123 (3) no. 1 of the German Company Transformation Law (UmwG), all retail customer contracts relating to DSL residential customer business were transferred to DSL home by way of spin-off. At the Annual General Meeting held on May 23, 2006, the shareholders gave their approval to the spin-off with retrospective effect from 1 January 2006. The Spin-Off and Transfer Agreement was signed on 9 August 2006.

010090 + On April 12, 2006, QSC 100 acquired 100 percent of the shares of 010090. The purchase price paid for the formerly non-operative Kristall 39. GmbH totalled T € 27. The company 010090 markets speech products for residential customers, in particular call-by-call products.

celox + On May 12, 2005, QSC acquired 100 percent of celox, a nationwide provider of professional solutions in the field of data communication for small and medium enterprises and major corporates. celox operated its own DSL network with over 170 colocation rooms in more than 30 German cities of medium size. Through this acquisition, QSC achieved both an especially swift and cost-effective further geographical expansion of the network, while simultaneously significantly broadening its customer base.

The purchase price for celox amounted to T € 13,954, including acquisition costs in the amount of T € 192. T € 13,762 of the purchase price was paid in the form of 3,583,776 new shares of stock, which were created from authorized capital against the contribution of all celox shares as well as a loan redemption entitlement against celox on the part of the legacy celox shareholders in the amount of T € 3,707. The fair values of identifiable assets and liabilities of celox at acquisition date were as follows:

	Recognized on acquisition in T €	Carrying amount in T €
Assets		
Long-term assets	2,442	2,442
Deferred taxes	2,564	-
Trademark celox	622	-
Customer base celox	558	-
Trade receivables	398	398
Other financial assets and prepayments	1,754	1,754
Cash and short-term deposits	1,731	1,731
Assets	**10,069**	**6,325**
Liabilities		
Deferred taxes	(471)	-
Trade payables	(295)	(295)
Provisions	(803)	(803)
Other short-term liabilities	(1,418)	(5,125)
Liabilities	**(2,987)**	**(6,223)**
Fair value of net assets	7,082	102
Goodwill arising on acquisition	6,872	
Total	**13,954**	
Total acquisition costs incl. direct acquisitions costs	(13,954)	
Issuance of common stock	13,762	
Cash and short-term deposits acquired	1,731	
Total consideration	**1,539**	

celox was merged into QSC with effect from January 1, 2006. In conjunction with this merger, QSC acquired a direct investment in EPAG, a former subsidiary of celox. In its function as domain registrar, EPAG specializes in the registration and administration of international domains. In the meantime, EPAG is a leading domain provider for resellers in Germany.

Ventelo + On December 13, 2002, QSC acquired 100 percent of Ventelo GmbH, Düsseldorf (Ventelo). Ventelo is a nationwide voice telephony carrier providing business customers with voice telephony services. Ventelo's market position in voice communications for business customers complements QSC's broadband data communications service to the same customer segment. Ventelo will further enhance QSC's ability to offer integrated telecommunication solutions for all business customer segments. Total acquisition costs for Ventelo were T € 11,454, including direct acquisition costs of T € 90.

Netchemya + For Netchemya S.p.A., Italy, one of QSC's investments made in 2000, the liquidation proceedings were concluded on October 31, 2005. QSC therefore wrote-off its remaining investment in Netchemya of T € 4,136 in 2002. In December 2004, QSC received a settlement payment of T € 375 and in 2005 of T € 280 that are included in income from associated companies.

40 Segment reporting

The source of QSC's reportable segments is the internal organization used by management for making operating decisions and assessing performance as. QSC is primarily operating in the customer segments Large Accounts, Business Customers, Wholesale/Resellers and Residential Customers.
The customer segment Large Accounts embraces customized solutions of voice and data communication for large and medium enterprises. In addition to the configuration and operation of IP-VPN networks, QSC also provides a broad range of network-related services.
In the Business Customer segment QSC summarizes its product business. QSC covers most of the needs of small and medium enterprises concerning modern voice and data communication by basically determined products and processes.
The Wholesale/Resellers segment includes the business with Internet service providers and telecommunication providers without proprietary infrastructure. They are marketing QSC's DSL lines as well as value-added services under their own name and for their own account.
In the Residential Customer segment the Company embraces the voice and data services for residential customers.

2006 in T €	Segment Large accounts	Segment Business customers	Segment Wholesale/ Resellers	Segment Residential customers	Recon- ciliation	Consoli- dated
Net revenues	**65,526**	**75,545**	**65,369**	**56,082**	**-**	**262,522**
Directly allocated costs	(26,636)	(35,892)	(32,536)	(39,371)	-	(134,435)
Contribution margin	**38,890**	**39,653**	**32,833**	**16,711**	**-**	**128,087**
Not allocated costs	-	-	-	-	(106,922)	(106,922)
EBITDA	**38,890**	**39,653**	**32,833**	**16,711**	**(106,922)**	**21,165**
Depreciation and amortization	(1,997)	(2,418)	(2,943)	(3,154)	(17,138)	(27,650)
Non-cash share-based payments	-	-	-	-	(691)	(691)
Financial result	-	-	-	-	(29)	(29)
Income tax profit	-	-	-	-	1,859	1,859
Net profit/(loss)	**36,893**	**37,235**	**29,890**	**13,557**	**(122,921)**	**(5,346)**
Long-term assets	7,155	17,179	10,769	15,054	249,752	299,909
Liabilities	3,475	4,059	2,662	2,928	126,235	139,359
Capital expenditures	3,423	3,982	2,716	2,958	26,980	40,059

2005 in T €	Segment Large accounts	Segment Business customers	Segment Wholesale/ Resellers	Segment Residential customers	Recon- ciliation	Consoli- dated
Net revenues	**51,393**	**57,530**	**30,388**	**55,076**	**-**	**194,387**
Directly allocated costs	(18,372)	(33,988)	(17,516)	(37,549)	-	(107,425)
Contribution margin	**33,021**	**23,542**	**12,872**	**17,527**	**-**	**86,962**
Not allocated costs	-	-	-	-	(81,185)	(81,185)
EBITDA	**33,021**	**23,542**	**12,872**	**17,527**	**(81,185)**	**5,777**
Depreciation and amortization	(1,995)	(2,296)	(1,619)	(2,913)	(15,585)	(24,408)
Non-cash share-based payments	-	-	-	-	(35)	(35)
Financial result	-	-	-	-	200	200
Income from associated companies	-	-	-	-	280	280
Net profit/(loss)	**31,026**	**21,246**	**11,253**	**14,614**	**(96,325)**	**(18,186)**
Long-term assets	7,969	13,381	10,881	15,897	103,139	151,267
Liabilities	3,917	4,510	3,179	5,722	48,901	66,229
Capital expenditures	2,372	2,730	1,924	3,464	9,641	20,131

Directly attributable costs consist of those segment expenses that can be directly allocated to the respective segment on the basis of revenues. Non-attributable costs are not apportioned among the segments, because they are structural costs for which it is not possible to make a causal allocation. In particular, the vast majority of these costs consists of the costs of building, operating and maintaining the network; these costs do not rise steadily on the basis of the number of customers and the volumes of traffic transported. In addition, these unallocated costs also include personnel expenses, administrative expenses, as well as segment-independent general advertising expenses. No further subclassification of the primary segments into secondary segments (geographical segments) was made, as QSC's telecommunication services are predominantly offered on a national scale.

41 Stock option programs

QSC has established a total of six stock option programs since 1999, which call for the issuance of convertible bonds having a nominal value of € 0.01 each to employees and, with the consent of the Supervisory Board, to members of the Management Board as well as to consultants and suppliers. The participants in these programs are granted the right to convert each convertible bond into one share of registered, no-par stock against payment of the exercise price. The exercise price of the convertible bonds represents the market price of the share on the valuation date. The convertible bonds have a term of five years and are subject to a vesting period of up to three years. On the basis of IFRS 3, no personnel expenses were recorded for the convertible bonds issued under the 2000, 2000A, 2001 and 2002 SOPs, as they were resolved by Annual Shareholders Meetings prior to November 7, 2002. The option values for the convertible bonds under the 2004 SOP were computed at the grant date with the aid of the Black-Scholes option-pricing model, with the following assumptions being employed:

SOP 2004	
Average expected life of options	5 years
Dividend yield	0.00%
Average risk-free interest rate	3.92%
Expected volatility (3 years)	40.96%
Average fair value of convertible bonds in €	1.87
Fair value of options granted for the year ended Dec. 31, 2006 in €	1,682,269

The convertible bonds outstanding as of December 31, 2006, and 2005, under all programs are shown below:

	Number of convertible bonds	Weighted average exercise price in €
Outstanding at December 31, 2004	6,032,443	1.92
Granted during the year	429,684	3.69
Forfeited during the year	(21,449)	2.23
Exercised during the year	(456,110)	1.70
Outstanding at December 31, 2005	**5,984,568**	**2.06**
Granted during the year	955,130	4.10
Forfeited during the year	(879,397)	3.74
Exercised during the year	(2,483,767)	1.96
Outstanding at December 31, 2006	**3,576,534**	**2.27**

42 Related party transactions

During 2006, QSC participated in transactions with companies affiliated with members of the management. According to IAS 24 related parties are individuals or companies with the possibility to influence or even control the other party. All contracts with these companies require the approval of the Supervisory Board and are made on the basis of arm's length principles.
IN-telegence GmbH & Co. KG provides value-added telecommunication services. Teleport Köln GmbH operates and maintains QSC's private broadcast exchange and in-house telephone systems. microShare AG provides consulting services to QSC on the conception, documentation and implementation of internal IT-based processes. QS Communication Verwaltungs Service GmbH provides consultancy on the integration of celox and Broadnet.

	Net revenues in T €	Expenses in T €	Cash received in T €	Cash paid in T €
For the year ended Dec. 31, 2006				
IN-telegence GmbH & Co. KG	29	(145)	29	(203)
Teleport Köln GmbH	-	57	-	103
microShare AG	-	-	-	-
QS Communication Verwaltungs Service GmbH	-	303	-	333
For the year ended Dec. 31, 2005				
IN-telegence GmbH & Co. KG	26	(67)	25	(73)
Teleport Köln GmbH	8	91	4	100
microShare AG	1	-	1	-
QS Communication Verwaltungs Service GmbH	-	192	-	220

	Trade accounts receivables in T €	Trade accounts payable in T €
At December 31, 2006		
IN-telegence GmbH & Co. KG	2	-
Teleport Köln GmbH	-	8
microShare AG	-	-
QS Communication Verwaltungs Service GmbH	-	-
At December 31, 2005		
IN-telegence GmbH & Co. KG	5	20
Teleport Köln GmbH	4	14
microShare AG	-	-
QS Communication Verwaltungs Service GmbH	-	3

43 Deferred taxes

For the calculation of deferred taxes compared to the previous year an unchanged income tax rate of 39.9 percent was used. This includes a trade tax rate of 18.37 percent, a statutory income tax rate of 25 percent plus a solidarity surcharge of 5.5 percent on the statutory income tax rate.

Deferred taxes for the fiscal years 2006 and 2005 are:

	At Dec. 31, 2006 in T €		At Dec. 31, 2005 in T €		2006 in T €	2005 in T €
	Assets	Liabilities	Assets	Liabilities	Income Statement	
Deferred taxes						
Intangible assets	-	4,864	-	2,948	878	(931)
Property, plant and equipment	-	171	-	513	342	(581)
Financial assets	90	32	839	-	(871)	849
Trade receivables	-	-	-	285	285	(285)
Trade receivables related parties	-	49	-	607	(49)	-
Prepayments	-	243	-	-	364	(389)
Deferred revenues	1,637	-	1,302	35	335	754
Accrued pensions and provisions	41	-	163	564	(128)	(70)
Other short-term liabilities	-	-	-		564	(768)
Total deferred taxes referred to temporary differences	**1,768**	**5,359**	**2,304**	**4,952**	**1,720**	**(1,421)**
Netting out	(275)	(275)	(1,106)	(1,106)		
Total deferred taxes referred to temporary differences after netting out	1,493	5,084	1,198	3,846		
Total deferred taxes referred to losses carryforward	4,910	-	4,771	-	139	1,421
Tax income/(expense)	-	-	-	-	1,859	-
Total deferred taxes	**6,403**	**5,084**	**5,969**	**3,846**		

The following table reconciles the expected income tax to the actual income tax expense. The expected tax income was calculated by multiplying net loss before taxes with the income tax rate of 39.9 percent:

	2006 in T €	2005 in T €
Reconciliation		
Net loss	**(7,205)**	**(18,186)**
Expected tax income	2,875	7,256
Tax effect of		
different tax rate	39	-
non-deductible expenses	-	(53)
neglected capitalization of deferred taxes		
referred to losses carryforward	(1,020)	(7,012)
Miscellaneous	(35)	(191)
Income taxes	**1,859**	**-**

At December 31, 2006, QSC has corporation tax and municipal trade tax losses available for carry-forward amounting in total to € 420 million. These tax losses can be carried forward without restriction for future offset against the taxable profits of entities in which the tax losses arose.

44 Litigations

QSC does not presently have any major litigations which could result in an expense for the Company.

45 Commitments and contingent liabilities

Commitments and contingent liabilities in the coming fiscal years for long-term contracts, in particular for fiber optic lines, technical premises, office premises and corporate vehicles, amount to T € 47,618.

	Dec. 31, 2006 in T €	Dec. 31, 2005 in T €
Commitments and contingent liabilities		
up to 1 year	29,630	35,078
1 to 5 years	17,938	36,829
more than 5 years	50	-
Commitments and contingent liabilities	**47,618**	**71,907**

As of December 31, 2006, QSC had guarantees in the amount of T € 8,466 (2005: T € 3,386) outstanding, primarily to suppliers for rental and other contractual obligations.

46 Compensation of the Management Board

The total compensation of the members of the Management Board is, to a very high degree, performance driven and comprises fixed and variable components. Total compensation for fiscal year 2006 amounted to Euro 2.18 million (2005: Euro 1.68 million).
Of the total amount, fixed and variable components accounted for 39 percent and 51 percent respectively. Variable remuneration is measured on the basis of the extent to which entity-specific and individual targets are achieved. The Supervisory Board's Compensation Committee determines these targets by at the beginning of each fiscal year and reviews them again at the end of the period. In addition to these key components, other benefits are granted in the form of company pensions, company cars or car allowance as well as the reimbursement of travel and other expenses. QSC considers that this description of the Management Board's compensation provides an important basis for assessing its appropriateness. The disclosure of compensation by individual, as recommended in Section 4.2.4, sentence 2 of the German Corporate Governance Code would not provide any additional understanding. QSC is exempted from the legal requirement to disclose compensation by individual (as introduced by the Management Board Compensation Disclosure Act dated August 3, 2005) as a result of the resolution taken at the Annual General Meeting on May 23, 2006. The exemption applies to the annual and consolidated financial statements for fiscal years 2006 to 2010. Further information is provided in the separate Corporate Governance and Compensation Report.

47 Declaration pursuant to § 161 AktG regarding compliance with the German Corporate Governance Code

The declaration pursuant to § 161 of the Stock Corporation Act (AktG) regarding compliance with the German Corporate Governance Code in the version dated June 2, 2005 and, after becoming valid, in the version dated June 12, 2006, has been issued by the Management Board and the Supervisory Board. Future amendments to the rules relevant for compliance with the Corporate Governance Code will be posted on the QSC website without delay. Further information is provided in the separate Corporate Governance and Compensation Report.

48 Auditors' fees

In 2006, the auditing firm appointed to audit QSC's annual financial statements received T € 210 for the consolidated financial statements audit, T € 145 for tax advisory services and T € 228 for other services. Other services are related to services in conjunction with capital increase.

49 Risks

The economy + A weak economy impacts the willingness of enterprise customers to invest in modern telecommunication infrastructures. This could have a negative impact on QSC's growth.

Alternative technologies + Cable (TV) network operators are increasingly offering Internet access and voice telephony, in addition to television. These Triple Play offerings, which address the residential customer market, could pose potential competition to the Company's business with wholesale partners.

Competition + The German market for DSL products and services is seeing a concentration on only a few strong providers. This could have a negative impact on QSC's positioning.

Regulatory environment + The decisions of the German Federal Network Agency can have either an indirect or direct influence on QSC's competitive position and market. The issue of Bitstream Access could increase competitive pressure on QSC.

Competitive behavior of Deutsche Telekom (DTAG) + As an infrastructure provider, QSC is significantly less dependent on former monopolist DTAG's reselling prices than the majority of the Company's competitors. Nevertheless, an aggressive pricing policy on the part of DTAG in connection with both the required preliminaries and the consumer market, in particular, could have a negative impact on the margin situation in the German telecommunication market. Another risk consists of DTAG's improved DSL network, the VDSL network. To offset its investments in increasing the speed of this network, DTAG is asking that regulatory requirements and the commitment to provide other market players with VDSL access be waived. Should this endeavor succeed, DTAG would be given a virtual monopoly on broadband lines with speeds in excess of 25 MBit/s.

Expansion of wholesale busines + Wholesale business poses the risk of dependency upon the success of the Company's marketing partners, as they are responsible for sales and marketing to end-customers. At the same time, it is necessary for QSC to incur significant upfront expenses in connection with consolidating IT systems and building appropriate interfaces. Amortization of these expenses, in turn, depends upon the success of the Company's respective partners.
The success of these partners in the consumer market could result in an extremely high volume of new orders at QSC, necessitating both high-quality yet efficient handling of a large volume of customer data and tying up corresponding resources. Moreover, a high volume of orders necessitates the scalability of QSC's interfaces to DTAG, which has to provide the corresponding subscriber lines.

Penalties in project business + Within the framework of projects for large accounts and its wholesale/reseller partners, QSC enters into contracts that assure certain service levels, some of which involve potential penalties. This results in the risk of high recourse entitlements and expenses stemming from interruptions.

Liquity and credit risk + As of December 31, 2006, QSC possessed liquid assets totaling € 108.9 million. However aggressive price competition or a sustained recession could result in the need for additional funding.

QSC's own infrastructure + Through the establishment of Plusnet GmbH & Co. KG by QSC and TELE2 as a joint-venture network operating company, the vast majority of the risks in connection with the Company's network infrastructure are now being shouldered by Plusnet.
Nevertheless, outages in the DSL network pose a risk to the entire QSC Group and its business operations. In addition to a potential loss of image, the risk of indemnification claims or high penalties, in particular, following extended, widespread outages could result in corresponding expenses.

Criminal intrusions into QSC systems + Unauthorized intrusions into QSC's IT network in the form of viruses, Trojan horses or hackers could result in considerable damage, for example through data manipulation or file deletion. The same also applies with respect to insufficient data protection and uncontrolled access to QSC data centers. In the event of an outage of the operative IT systems, it would not be possible to handle new orders or resolve system interruptions; the resulting monetary damages and loss of reputation could be significant.

Loss of data + Operating errors, hardware defects or the destruction of the data center through an attack or natural disaster can result in a loss of business-critical data. The lack of data backups could increase this kind of risk. Growing volumes of data stemming from the Company's high pace of growth could additionally push the capacities of the Company's data storage and backup systems to their limits. In any event, a loss of operative data would make it impossible for QSC to operate.

50 Subsequent events

QSC's Management Board and Supervisory Board resolved on January 30, 2007 to prepare for a merger of Broadnet into QSC, with a view to allow the legal and organizational integration of Broadnet into the QSC Group. In conjunction with the merger, QSC plans to grant QSC shares to Broadnet shareholders in exchange for Broadnet shares. QSC has initiated discussions with Broadnet to commence all necessary further measures jointly with Broadnet. In particular, an independent auditor will be engaged to determine the share exchange ratio.

Cologne, March 21, 2007

Dr. Bernd Schlobohm Chief Executive Officer	Markus Metyas	Bernd Puschendorf

Corporate Governance

The Company's sustained high growth dynamic necessitates good corporate governance. QSC has therefore traditionally attached great value to transparent, responsible and value-oriented management.

Responsible Corporate Management

Corporate Governance Report comprises Compensation Report + Good corporate governance means that a company is being responsibly managed and supervised – and this is precisely what QSC has been practicing for years. Management that is based upon sustained value creation, transparent communication as well as efficient collaboration between all corporate bodies in a spirit of trust have traditionally enjoyed high priority at QSC.

Since the German Corporate Governance Code (Code) went into force in 2002, QSC has therefore largely been in compliance with its recommendations. However the Company intentionally deviates from the Code in a few points. These are recommendations that are geared all too strongly toward managing and monitoring large corporations and do not sufficiently take into consideration the situation of lean companies with a strong entrepreneurial culture.

Speaking on both its own behalf and on behalf of the Supervisory Board, the Management Board of QSC reports below on corporate governance pursuant to Item 3.10 of the Code as most recently amended in June 2006, and also comments on these variances in this connection. The following report also integrates the Compensation Report called for by Item 4.2.5 of the Code.

QSC utilizes its website as its central information platform

Transparent information for shareholders + QSC utilizes its own website in order to promptly and comprehensively report throughout the entire year on all relevant developments within the Company. At www.qsc.de/en/investor-relations.html, shareholders can find Quarterly and Annual Reports, ad-hoc notices and press releases, a financial calendar and detailed documents relating to all major events. QSC additionally informs investors at regular gatherings in connection with analyst and investor conferences, in personal talks and in connection with telephone conference calls following the announcement of the Company's final quarterly and annual results.

The Annual Shareholders Meeting is the Company's central informational event for shareholders, with the Management Board submitting Annual and Consolidated Financial Statements to it. The Annual Shareholders Meeting decides on adoption of the financial statements, on ratification of the actions of the Management and Supervisory Boards, on election of members of the Supervisory Board and the independent auditor and on amendments to the Articles of Association, as well as on major and financial directions. Shareholders can comprehensively inform themselves about impending decisions sufficiently in advance of the Annual Shareholders Meeting on the basis of the Annual Report and the agenda of the Annual Shareholders Meeting. All documents and information are available on the QSC website.

QSC simplifies the ability of shareholders to exercise their rights at the Annual Shareholders Meeting. Shareholders who do not attend in person have traditionally been able to have their voting rights exercised either by a proxyholder of their choice or by a Company-appointed proxyholder bound by the shareholder's instructions.

Collaboration between corporate bodies in a spirit of trust + The Management and Supervisory Boards of QSC collaborate closely with one another to the benefit of the Company. Both of these corporate bodies view themselves as being committed to sustainably increasing the value of the Company. The Management Board promptly and comprehensively reports to the Supervisory Board on all relevant questions relating to planning, strategy and business development, as well as on risks and risk management. At regular meetings and in telephone conference calls, the Supervisory Board advises and monitors the activities of the Management Board, and discusses key issues frankly and in a spirit of trust. The Report of the Supervisory Board provides detailed information about the activities of this six-member corporate body.

The composition of the QSC Supervisory Board includes both shareholder representatives as well as a sufficient number of independent members. It is their conviction that the best approach is to jointly deliberate and monitor the work of the Management Board by bringing to bear their various qualifications and experiences. Consequently, with the exception of a three-member Compensation Committee, the Supervisory Board does not form any other committees; the same also applies with respect to the audit committee urged in Item 5.3.2 of the Code. The Supervisory Board in its entirety possesses a sound understanding of questions relating to accounting and risk management; the exclusion of individual Supervisory Board members would therefore mean having to forego valuable expertise.

Joint deliberation and monitoring is the best approach

Team-based Supervisory Board compensation + The joint effort on the part of the members of the Supervisory Board is also what governs their compensation. The Company therefore intentionally foregoes the option contained in Item 5.4.7 of the Code relating to success-based compensation and to special compensation for members on Supervisory Board committees.

The aggregate compensation paid to members of the Supervisory Board in fiscal 2006 totaled € 160,000. Supervisory Board Chairman John C. Baker and his Vice Chairman Herbert Brenke each received € 30,000 pursuant to § 10, Paragraph 5, of the Articles of Association, the other members € 25,000 each.

The table below presents individualized information relating to the compensation, number of shares and stock options held by members of the Supervisory Board. During the past fiscal year, Supervisory Board Chairman John C. Baker exercised 10,000 conversion rights from the 2002 Stock Option Program, with the new shares being transferred to his custody account.

	Compensation 2005 and 2006 in €	Dec. 31, 2006		Dec. 31, 2005	
		Shares	Convertible Bonds	Shares	Convertible Bonds
John C. Baker	30,000	10,000	-	-	10,000
Herbert Brenke	30,000	187,820	10,000	187,820	10,000
Gerd Eickers	25,000	13,853,484	-	13,853,484	-
Ashley Leeds	25,000	9,130	10,000	9,130	10,000
Norbert Quinkert	25,000	3,846	-	3,846	-
David Ruberg	25,000	4,563	10,000	4,563	10,000

Aside from this compensation, the members of the Supervisory Board did not receive any professional fees from QSC during the past fiscal year, in particular for consulting and go-between services.

Management Board responsible for corporate management + The Management Board manages the Company under its own responsibility, develops the Company's strategic alignment and assures compliance with statutory requirements as well as an appropriate system of risk management and controlling. The Management Board is made up of three members who complement one another very well in terms of their qualifications and experiences. The three members of the Management Board manage the Company as a team.

Management Board compensation rewards success + The aggregate compensation paid to members of the QSC Management Board is highly performance-oriented and comprises fixed and variable elements. Total compensation during the past fiscal year amounted to € 2.18 million as opposed to € 1.68 million the year before. 39 percent of this aggregate compensation consisted of fixed salary elements, 51 percent and 10 percent of other benefits variable salary elements. The variable salary elements are based upon the level of attainment of corporate and individual goals. They are determined by the Supervisory Board Compensation Committee at the beginning of each fiscal year and reviewed subsequent to the close of the fiscal year. In addition to these key components, other benefits are granted in the form of company pensions, company cars or car allowance as well as the reimbursement of travel and other expenses.

QSC views these remarks relating to the compensation paid to members of the Management Board as being crucial information for judging the appropriateness of this compensation. The individualization of this compensation called for in Item 4.2.4, Sentence 2, of the Code would not provide any additional insight. The legal obligation mandating the individualized disclosure of the compensation paid to members of management boards that was introduced under the Management Board Compensation Disclosure Act (Vorstandsvergütungs-Offenlegungsgesetz) of August 3, 2005, has been waived under a resolution adopted by the Annual Shareholders Meeting on May 23, 2006. This waiver applies to the Annual and Consolidated Financial Statements for fiscal years 2006 through 2010.

Stock options have a long-term incentive effect

In addition to monetary compensation, the members of the Management Board also receive a variable compensation element having a long-term incentive effect and risk character in the form of stock options, as called for under the Code. Like the QSC employees, the members of the Management Board participate in the Company's stock option programs (SOPs): QSC issues convertible bonds that entitle their holders to acquire one share of stock at the exercise price upon the expiration of a fixed term, sometimes consisting of multiple years; the value of the exercise price is based upon the trading price of the share at the time of exercise. The Notes to the Consolidated Financial Statements contain a detailed description of the individual programs.

The table below presents individualized information relating to the shares and stock options held by members of the Management Board. Due to the threat of the impending expiration of the 2001 SOP, Chief Financial Officer Markus Metyas converted all of his stock options from this program in July 2006, and simultaneously sold a corresponding number of shares, in order to cover the purchase price and tax burden. While the Annual Shareholders Meeting in May 2006 had resolved an extension of this stock option program through the year 2011, lawsuits brought by individual shareholders have thus far prevented this resolution from going into force.

	Dec. 31, 2006		Dec. 31, 2005	
	Shares	Convertible Bonds	Shares	Convertible Bonds
Dr. Bernd Schlobohm	13,818,372	350,000	13,818,372	50,000
Markus Metyas	179,807	675,000	2,307	1,525,000
Bernd Puschendorf	3,000	1,025,000	3,000	1,025,000

It is QSC's conviction that multi-year vesting periods and exercise prices that are marked to market fundamentally eliminate the need for cumbersome valuation of the stock options held by members of the Management Board (Item 4.2.5), the definition of potential restrictions with respect to unanticipated developments (Item 4.2.3, Paragraph 3, Sentence 4), as well as the need for defining demanding, relevant comparison parameters (Item 4.2.3, Paragraph 3, Sentence 2). Because the proven structure of the Company's stock option programs continues to be very suitable for a high-growth, founder-managed company like QSC.
The stock option program that was resolved by the Annual Shareholders Meeting in May 2006 contains, for the first time, restrictions to exercise rights. These are related to an absolute rise in QSC shares as well as their relative development in comparison to the TecDAX, respectively, thus leading to a further marked-to-market SOP.

Transparent communication + Openly and promptly informing all shareholders about relevant events within the Company is a key element of good corporate governance. QSC utilizes the Internet as a key information platform in this connection. In compliance with the Code, the Company permanently makes available on its website the current Statement of Compliance as well as previous Statements of Compliance going back five years.
The website additionally contains information relating to the acquisition or sale of QSC shares or derivatives based upon them by members of the Management and Supervisory Boards of QSC. Pursuant to § 15a of the German Securities Trading Act (WpHG), each member of either of these corporate bodies, as well as persons close to them, is obligated to disclose such transactions, along with the value of any transactions equaling or exceeding € 5,000 within a calendar year.

Trading Day / Stock Market	Names/Status	Financial Instrument	Type of Transaction	Par-Value in €/ Quantity	Volume in €	Remarks
March 06, 2006	Bernd Puschendorf	QSC shares	Sale	4.661	139,830.00	Within the 2001
Xetra	Management Board			30,000		SOP framework
March 08, 2006	Bernd Puschendorf	QSC shares	Sale	4.4053	176,212.00	Within the 2001
Xetra	Management Board			40,000		SOP framework
March 14, 2006	Bernd Puschendorf	QSC shares	Sale	4.665	139,950.00	Within the 2001
Xetra	Management Board			30,000		SOP framework
April 11, 2006	Markus Metyas	QSC shares	Sale	5.188	103,760.00	Within the 2001
Xetra	Management Board			20,000		SOP framework
April 20, 2006	Markus Metyas	QSC shares	Sale	5.000	100,000.00	Within the 2001
Xetra	Management Board			20,000		SOP framework
April 26, 2006	Markus Metyas	QSC shares	Sale	4.936	98,720.00	Within the 2001
Xetra	Management Board			20,000		SOP framework
April 28, 2006	Markus Metyas	QSC shares	Sale	5.092	203,680.00	Within the 2001
Xetra	Management Board			40,000		SOP framework
June 06, 2006	Gerd Eickers	QSC shares	Securities lending	4.360	see	Lending fee
Over the counter	Supervisory Board			11,232,176	remarks	0,5% p.a.
June 12, 2006	Gerd Eickers	QSC shares	Redemption of	3.940	see	Lending fee
Over the counter	Supervisory Board		Securities lending	11,232,176	remarks	0,5% p.a.
July 11, 2006	Markus Metyas	QSC shares	Sale	4.351	313,272.00	Within the 2001
Xetra	Management Board			72,000		SOP framework
July 12, 2006	Markus Metyas	QSC shares	Sale	4.367	157,212.00	Within the 2001
Xetra	Management Board			36,000		SOP framework
July 14, 2006	Markus Metyas	QSC shares	Sale	4.113	164,520.00	Within the 2001
Xetra	Management Board			40,000		SOP framework
17. Juli 2006	Markus Metyas	QSC shares	Sale	3.964	317,120.00	Within the 2001
Xetra	Management Board			80,000		SOP framework
July 18, 2006	Markus Metyas	QSC shares	Sale	3.919	391,900.00	Within the 2001
Xetra	Management Board			100,000		SOP framework
July 19, 2006	Markus Metyas	QSC shares	Sale	3.918	391,800.00	Within the 2001
Xetra	Management Board			100,000		SOP framework
July 20, 2006	Markus Metyas	QSC shares	Sale	3.963	396,300.00	Within the 2001
Xetra	Management Board			100,000		SOP framework

Trading Day / Stock Market	Names/Status	Financial Instrument	Type of Transaction	Par-Value in €/ Quantity	Volume in €	Remarks
July 21, 2006	Markus Metyas	QSC shares	Sale	3.909	156,360.00	Within the 2001
Xetra	Management Board			40,000		SOP framework
July 24, 2006	Markus Metyas	QSC shares	Exercise of	1.400	140,000.00	Within the 2001
Over the counter	Management Board		Convertible bonds	100,000		SOP framework
July 25, 2006	Markus Metyas	QSC shares	Exercise of	1.400	280,000.00	Within the 2001
Over the counter	Management Board		Convertible bonds	200,000		SOP framework
July 26, 2006	Markus Metyas	QSC shares	Sale	4.041	18,184.50	Within the 2001
Xetra	Management Board			4,500		SOP framework
July 27, 2006	Markus Metyas	QSC shares	Exercise of	1.400	38,500.00	Within the 2001
Over the counter	Management Board		Convertible bonds	27,500		SOP framework
Sep. 18, 2006	John C. Baker	QSC shares	Exercise of	1.000	10,000.00	Within the 2001
Over the counter	Supervisory Board		Convertible bonds	10,000		SOP framework
Nov. 15, 2006	Markus Metyas	QSC shares	Sale	5.295	794,250.00	
Xetra	Management Board			150,000		

High quality of accounting + QSC prepares its Consolidated Financial Statements under IFRS within 90 days following the close of the fiscal year. The Company additionally prepares Annual Financial Statements under HGB accounting rules for the purpose of satisfying the requirements under German corporate law.

QSC views its Consolidated Financial Statements and interim reports as a key information medium for its shareholders and third parties, and takes pains to assure that they are compiled with the utmost care. The Company therefore deviates from Item 7.1.2 of the Code and submits its interim reports within 60 days following the close of each reporting period. However QSC typically publishes a detailed notice containing preliminary key numbers within the first 45 days following the close of each reporting period, thus enabling shareholders to promptly inform themselves about the course of business.

Statement of Compliance

Declaration Pursuant to § 161 of the German Stock Corporation Act on Compliance with the German Corporate Governance Code in its version dated June 2, 2005, respectively as of its validity in its version dated June 12, 2006, at QSC AG

Since its formation, QSC AG has been committed to good corporate governance and has viewed transparency and value-driven management as essential. Consequently, the company implements nearly all recommendations set forth in the German Corporate Governance Code and adheres them in its daily work. Since submittal of its last Declaration of Compliance, the company has complied and continues to comply with the recommendations of the Government Commission "German Corporate Governance Code" in its version dated June 2, 2005, respectively as of its validity in its version dated June 12, 2006, with the following exceptions:

1. The recommendation that demanding, relevant comparison parameters be stipulated for stock options and comparable instruments for members of the Management Board
   (Item 4.2.3, Paragraph 2, Sentence 2, of the Code in its version dated June 2, 2005 resp. item 4.2.3, Paragraph 3, Sentence 2, of the Code in its version dated June 12, 2006)

2. The recommendation that a possibility of limitation (cap) for extraordinary, unforeseen developments be agreed for stock options and comparable instruments for members of the Management Board
   (Item 4.2.3, Paragraph 2, Sentence 4, of the Code in its version dated June 2, 2005 resp. item 4.2.3, Paragraph 3, Sentence 4, of the Code in its version dated June 12, 2006)

3. The recommendation that the company publish information relating to the value of stock options for members of the Management Board on the its website and in its Annual Report
   (Item 4.2.3, Paragraph 3, Sentence 2, of the Code in its version dated June 2, 2005) resp. the recommendation, to publish such information in a compensation report henceforward (Item 4.2.5 of the Code in its version dated June 12, 2006)

4. The recommendation that the compensation of the members of the Management Board be disclosed in individualized form in the notes to the consolidated financial statements
   (Item 4.2.4, Sentence 2, of the Code in its version dated June 2, 2005); the Company has been exempt from the statutory obligation to publish the compensation of the members of the Management Board in individualized form introduced by the Act on Disclosure of Executive Compensation of August 3, 2005 by resolution of the General Meeting of the Company of May 23, 2006 with regard to the individual and consolidated annual financial statements for the financial years 2006 to 2010, but no longer than up to May 22, 2011.

5. Formation of an audit committee
   (Item 5.3.2)

6. Taking into account the economic situation and performance of the company, as well as chair and membership positions on committees, in connection with compensation of the members of the Supervisory Board
   (Item 5.4.5 of the Code)

7. Publication of interim reports within 45 days
   (Item 7.1.2 of the Code)

QSC's corporate governance principles are regularly reviewed by the Management und Supervisory Boards. The company will promptly publish any future changes thereto with respect to conformity with the German Corporate Governance Code on its website.

Cologne, November 29, 2006

For the Management Board	For the Supervisory Board
Dr. Bernd Schlobohm	John C. Baker

Functions of the Supervisory Board

The members of the Supervisory Board represent functions in the following companies:

Member of Supervisory Board	Function	Company
John C, Baker	Member of Board of Directors	Digi TV Plus Oy, Helsinki, Finland, since June 2006
	Member of Board of Directors	Offermatica Corp., San Francisco, USA, since October 2006
	Member of Board of Directors	Verified Identity Pass Inc., New York, USA, since October 2006
Herbert Brenke	Chairman of Supervisory Board	ASKK Holding AG, Hamburg, Germany
	Chairman of Supervisory Board	Telegate AG, Martinsried, Germany
	Member of Supervisory Board	ASR Auto-Stern von Russland AG, Moscow, Russia, until December 2006
	Member of Supervisory Board	Broadnet AG, Hamburg, Germany, since September 2006
	Member of Supervisory Board	SHS Informationssysteme AG, Munich
	Member of Advisory Board	Küttner GmbH & Co. KG, Essen, Germany
Gerd Eickers	Chairman of Supervisory Board	Contentteam AG, Cologne, Germany, since September 2006
	Member of Supervisory Board	Amisco NV, Brüssel, Belgien, since January, 2007
	Member of Supervisory Board	Broadnet AG, Hamburg, Germany, since September 2006
	Member of Advisory Board	GTT GmbH, Duisburg, Germany
Ashley Leeds	Member of Board of Directors	Message Secure Corp., Lowell, USA
	Member of Board of Directors	Voltaire Ltd., Herzlia, Israel
Norbert Quinkert	Chairman of Supervisory Board	WISTA-Management GmbH, Berlin, Germany
	Member of Supervisory Board	ALD Vacuum Technologies AG, Hanau, Germany
	Member of Supervisory Board	IHP (Institut für Halbleiterphysik), Frankfurt/Oder, Germany
	Member of Supervisory Board	Pfalz Flugzeugwerke AG, Speyer, Germany
	Member of Supervisory Board	Motorola GmbH, Taunusstein, Germany
	Member of Advisory Board	Dresdner Bank AG, Frankfurt, Germany
	Executive Vice President	American Chamber of Commerce, Frankfurt, Germany
David Ruberg	Chairman of Supervisory Board	InterXion Inc., Amsterdam, The Netherlands
	Member of Board of Directors	Adaptix Inc., Seattle, USA
	Member of Board of Directors	Broadview Networks Inc., New York, USA

Glossary

ADSL + The Asymmetric Digital Subscriber Line. Transmission of digital data over a copper telephone line with "asymmetric" transfer rates of between 1.5 Mbit/s and 8 Mbit/s downstream and between 16 kbit/s and 800 kbit/s upstream.

ADSL2+ + An evolution of ADSL technology that primarily improves the transfer rates and ranges of an ADSL connection. Optimally, ADSL2+ affords transfer speeds of up to 25 Mbit/s downstream and 1 Mbit/s upstream.

Backbone + Supraregional network of several hubs, connected by fast transmission routes

Bitstream Access + A ramp-up product for broadband services that provides a network operator with broadband transfer capacity (e.g. on a DSL platform) between the end customer and a defined point of interconnection (POI) in the network of a further provider, thereby enabling him to acquire the bitstream and offer it on the basis of his own end-customer rate plans.

Broadband + A data transmission capacity of more than 128 kilobits per second.

Bundesnetzagentur (German Federal Network Agency) + The German regulatory authority for electricity, gas, telecommunications, postal and railway markets, the former Regulatory Authority for Telecommunications and Posts. Its mission is to monitor the market power of dominant providers and to assist competitors in achieving the required equality of opportunities.

Call-by-Call + Phone calls or Internet access via call-by-call enable a customer to dial the network prefix of his or her telephone provider of choice prior to each telephone call or Internet access.

Colocation Room (or central office) + The 'colocation room' at Deutsche Telekom is where the 'last mile' to an end-user begins. The central office houses the DSL infrastructure of alternative network operators such as QSC. This is where the twisted copper wire pair is handed over by Deutsche Telekom to the alternative network operator.

DSL + Digital Subscriber Line. A data transmission method that enables digital data to be transferred at high transmission rates over a normal copper-wire telephone line.

ICT + Information and Communication Technology. The ICT industry is made up of all vendors and providers of hard- and software, voice and data communication infrastructures and telecommunication end-user devices, as well as information technology services and telecommunication services.

IFRS + International Financial Reporting Standards, formerly called International Accounting Standards (IAS); international accounting rules to which corporations in Europe with a capital market focus have been subject since their 2005 fiscal year.

Intranet + An intranet is a network within an organization that is not publicly accessible, but that does fundamentally offer the same services as the Internet. It might be termed.

IP + Internet Protocol. The Internet is based upon the IP data transfer standard. The IP enables a data packet to be routed via multiple different computer platforms until it reaches its destination.

ISP + Internet Service Provider. An ISP enables customer data communication by providing Internet access and related services, e.g. the management of e-mail.

LAN + Local Area Network. A network confined to a particular geographical area or building (e.g. within a company).

Last Mile + Distance from the telephone outlet to the nearest local switching center (central office).

Line Sharing + A technique that affords joint utilization of a telephone line for both voice and broadband data transmission, whereby the services can also be made available by two different vendors in that the frequency bands used on the subscriber line are separated.

Leased Line + A permanent connection line that is always on.

Managed VPN + Network providers/carriers appropriately combine, plan and supply VPNs in a wide variety of network structures (corporate network, IPsec-VPN, MPLS-VPN) and their hybrid forms in accordance with customer requirements. They are operated by the carriers under defined, wall-to-wall service level agreements (SLAs).

Mbit/s / kbit/s + Megabits per second / kilobits per second. A measure unit for data transmission speed.

NGN + Next Generation Network. An NGN consolidates the wide range of transmission methods and network structures into a convergent network architecture. This integrates telecommunication networks, data networks and TV networks within an IP-based network, for example. QSC concluded the migration of its entire infrastructure to such an NGN during the past fiscal year.

Protocol + A protocol contains standards for controlled data transfer. Protocols, for example, stipulate the data structure, the structure of the data packets as well as their encoding. There are various protocols, such as http or IP, depending upon the application in question.

Router + A system that interconnects two networks and organizes messaging channels between the networks. Routers are primarily employed to link local area networks (LANs) with wide area networks (WANs)

SDSL + Symmetric Digital Subscriber Line. Symmetric transmission technology that allows data to be transferred in both directions at speeds of up to 2.3 megabits per second. SDSL requires merely a copper twisted-pair line, which is why it is also termed a Single Digital Subscriber Line. The SDSL line is always on, thus allowing it to serve as a substitute for conventional leased lines.

SLA + Service Level Agreement. Legal agreement that specifies the contractual agreements between a service provider and a user with respect to the quality of service (speed, bandwidth, availability.)

TAL + The German acronym for a subscriber line or local loop. The line between a central office and the subscriber's physical connection to the respective network.

TKG + The German acronym for the German Telecommunications Act. The TKG serves as the basis for liberalization of the telecommunication sector in Germany.

Triple Play + Triple Play is the term used for multimedia services that are provided by network operators, telecoms, cable TV network operators and Internet service providers. It offers telephony, Internet and entertainment offerings such as television or video on demand over one and the same line, usually broadband.

Unbundled access + The customer's connection is physically connected directly to the alternative carrier's network. In order to assure competition in the local service area, as well, the German regulatory authority wants new telecommunication providers to have a right to unbundled access to Deutsche Telekom's subscriber line.

VDSL + Very High Data Rate Digital Subscriber Line. An asymmetric data transmission technology that utilizes copper cables and affords downstream data rates of from 12.9 to 51.8 Mbit/s and upstream rates of between 1.6 and 2.3 Mbit/s.

Voice over IP + Voice over Internet Protocol. The technique of using the Internet Protocol (IP) to transfer voice communication over packet-switched data networks.

VPN + Virtual Private Network. In a VPN, several enterprise sites are connected through a public network to form a secure network that cannot be accessed by outsiders. Only authorized persons or sites are able to communicate with one another, access data or exchange data over this network infrastructure.

WAN + Wide Area Network. A network for voice and data transmission that comprises a very large geographical area. To some extent it may even cover countries or continents.

Wimax + Worldwide Interoperability for Microwave Access. Wimax is a new standard for wireless local area networks. Theoretically it is capable of offering ranges of up to 50 kilometers and data transfer rates of up to 70 Mbit/s.

WLAN + Wireless Local Area Network. A wireless network confined to a particular geographical area.

WLL + Wireless Local Loop. A technology that allows for wirelessly linking subscriber connections to the network.

Calendar

Annual Shareholders Meeting
June 5, 2007

Quarterly Reports
May 16, 2007
August 29, 2007
November 19, 2007

Contacts

QSC AG
Investor Relations
Mathias-Brüggen-Strasse 55
50829 Cologne, Germany
Phone +49-(0)221-6698-724
Fax +49-(0)221-6698-009
E-mail invest@qsc.de
Internet www.qsc.de

Investor Relations Partner
komm.passion
Schumacher's AG
Lucile-Grahn-Strasse 37
81675 Munich, Germany
Phone +49 89 48 92 72-0
Fax +49 89 48 92 72-12
E-mail qsc@komm-passion.de

Imprint

Overall responsibility
QSC AG, Cologne

Photography
Andreas Pohlmann, Munich

Art Direction
sitzgruppe, Düsseldorf

Print
Fries Printmedien GmbH & Co. KG, Cologne

Further information under www.qsc.de