Quarterly Report . 2005 . January February March

Key data

	01/01/-31/03/ 2005	01/01/-31/03/ 2004
All amounts in € million		
Revenues	41.5	32.2
Gross profit	10.5	6.8
EBITDA	+0.5	+0.1
EBIT	-5.4	-6.1
Net loss	-5.1	-5.5
Net loss per common share[1] (in €)	-0.05	-0.05
Equity	65.1 [2]	70.5 [3]
Balance Sheet Total	108.5 [2]	114.8 [3]
Equity ratio (in percent)	60.0 [2]	61.4 [3]
Capital Expenditure	3.8	1.8
Liquidity	31.3 [2]	40.3 [3]
Share price as of 31/03/ (in €)	3.92	4.58
Number of shares as of 31/03/	105,641,123	105,256,694
Market capitalization as of 31/03/	414.1	482.1
Employees as of 31/03/	389	364

[1] basic and diluted
[2] as of March 31, 2005
[3] as of December 31, 2004

Communication is changing the world
Broadband reinvents communication
QSC is the broadband solution

QSC at a glance

Solutions business posting especially dynamic growth // In the first quarter of 2005, QSC grew its revenues by 29 percent to € 41.5 million, as opposed to € 32.2 million in the first three months of 2004. The Company posted its strongest growth rates in high-margin solutions business with large enterprise customers; in this segment, revenues rose by 75 percent to € 12.6 million.

Profitability continues to rise // With revenue growth of 29 percent, gross profit advanced by 54 percent to € 10.5 million in the first quarter of 2005, as opposed to € 6.8 million for the same quarter the year before. At the same time, QSC improved its EBITDA to € 0.5 million, as opposed to € 0.1 million in the first three months of 2004.

Demand-driven infrastructure expansion // QSC is expanding its network in three areas. Firstly, the Company is upgrading its network to a Voice over IP-capable Next Generation Network; secondly, it is adding further cities to its DSL network; and thirdly, it is equipping this DSL network with the new ADSL2+ standard on a step-by-step basis. In mid May, QSC additionally acquired Bonn-based celox Telekommunikationsdienste GmbH, which operates its own DSL network in over 30 cities, thus increasing QSC's network coverage to more than 100 cities.

Strong growth and acquisition prompt upscaled forecast // In connection with the celox acquisition, QSC has upscaled its revenue forecast for the current fiscal year, and is now predicting revenue growth of at least 25 percent to more than € 183 million. At the same time, the Company also anticipates a positive EBITDA of between € 4 to 8 million, as well as an operating cash flow of over € 10 million.

QSC share price growth outpacing the market // German technology issues were under pressure in the first quarter of 2005, with the TecDAX up by only 1 percent. With their trading prices advancing by 7 percent, QSC shares again outperformed the market. In May 2005, there was a successful private placement of some 2.9 million new shares of QSC stock with institutional investors in connection with the celox transaction.

Dear Shareholders,

At the beginning of the year, we announced that, during the current year, we intended to lay the foundation for QSC's strong and profitable growth in 2005 and beyond. With the acquisition of Bonn-based DSL network operator celox, the IP upgrade of our voice network to a Next Generation Network, the decision to equip our own DSL infrastructure with ADSL2+ technology, as well as the launch of our sales initiative targeting small and medium enterprises (SME), we have already started implementing this strategy during the first months of the year.
The results of the first quarter of 2005 illustrates how well QSC is positioned for further growth: We were able to grow our revenues by 29 percent to € 41.5 million and further accelerate the growth of both our gross profit and EBITDA. Our solutions business with large enterprise customers is growing particularly well, with revenues rising by 75 percent to € 12.6 million. For the first time, business with large enterprises was not only the segment with the highest margin but also the one with the highest share of overall revenues.

Large enterprise customers now the segment with the highest revenues and margins

The decisions outlined above will help enable us to further accelerate our growth, especially in the solutions business. Through the acquisition of Bonn-based celox Telekommunikationsdienste GmbH, for example, we were able to acquire an DSL network operator that is particularly successful with small and medium sized enterprise customers. There are three reasons why this acquisition will complement our business activities very well: Firstly, celox has its own infrastructure in small to medium-sized cities; cities in which QSC, itself, has thus far not been represented. In one step, QSC is able to expand its network coverage to over 100 cities, enabling us to implement a significantly higher percentage of nationwide VPN solutions over our own network and thus reduce production costs. Secondly, like QSC, celox is predominantly active in the fast-growing VPN business for enterprise customers. And thirdly, celox, too, is a founder-managed medium-sized company with a corporate culture that makes for a good fit with QSC.

celox' customer relationships and network coverage will also broaden QSC's opportunities in connection with the SME offensive that we launched at the beginning of the year. Small and medium enterprises are responding positively to our offers to link their locations for the first time via a secure and cost-effective VPN. The fact that QSC, itself, is a medium-sized company is proving to be a strong competitive advantage.

A further competitive advantage is proving to be the swift upgrade of our entire network towards a Next Generation Network that enables voice to be transmitted over DSL lines, and thus Voice over IP technology. With our new IPfonie products, QSC's customers are even able to retain their old telephone systems in utilizing the new technology. The resulting soft migration to Voice over IP is being very well received in the marketplace. In addition, the nationwide employment of IP technology also results in a clear cost advantage to QSC because a data network is easier to manage and to maintain than a conventional telephone network.

Over the course of the coming months, we will be equipping our network with the new ADSL2+ technology on a demand-driven basis. This technology allows transfer speeds of up to 16 Mbit/s, thus enabling high-quality reception of TV programs over DSL lines, for example. As we have already done in the past in expanding our own DSL infrastructure, we will be pursuing a "network follows customers" policy here, as well. In other words, we will only equip a location with ADSL2+ when we have enough local customers for this super-fast data transmission service.

With debitel, QSC wins a strong partner for residential customer business

In May, QSC was able to win debitel, one of Europe's largest network-independent telecommunication provider, as a partner for this demand-driven technology upgrade. This partnership will offer QSC the opportunity of expanding and upgrading its network on the basis of the latest standards and at the same time tapping into significant new revenue and profit potential, while simultaneously retaining its own focus on enterprise customers. In marketing the new products, QSC will be able to benefit from debitel's more than 6,500 marketing partners and its subscriber base of over eight million customers.
In the future, QSC, itself, will continue to focus on building and operating VPN solutions and on offering standardized telecommunication products for business customers. We view in these markets the greatest potential for sustaining our strong and profitable growth beyond 2005, and thus for further growing the value of QSC.

Cologne, May 2005

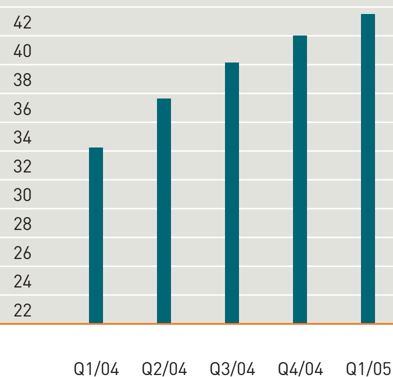
Markus Metyas	Dr. Bernd Schlobohm Chief Executive Officer	Bernd Puschendorf

QSC on growth course

QSC continued to grow its revenues, gross profit and EBITDA in the first quarter of 2005. At the same time, the Company expanded its DSL network, upgraded its voice network to a Next Generation Network, broadened its product portfolio and hired some 40 new employees, first and foremost in sales and marketing.

Sustained growth despite a weaker economy // With revenue growth of 29 percent, QSC went against the trend of the declining economy in Germany during the first quarter of 2005. The Company benefited from the sustained high demand on the part of business customers for innovative telecommunication solutions – from secure DSL connections right through to complex VPN solutions. The rapid penetration of Voice over IP technology is expected to offer additional growth potential. According to a study by corporate consultant Roland Berger, one in seven Germans will be utilizing this new technology during the next twelve months. At the same time business customers, as well, are increasingly considering the option of making phone calls over data lines – this will open up new opportunities, especially for DSL providers like QSC who own their infrastructure.

Revenues (in € million)



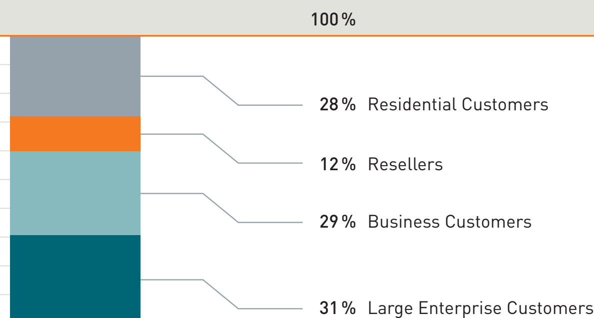
Revenues with large enterprise customers up by 75 percent

QSC growing in all segments // In the first quarter of 2005, QSC grew its revenues by 29 percent to € 41.5 million, as opposed to € 32.2 million in the first quarter of 2004. All four segments – large enterprise customers, business customers, value added resellers and residential customers – contributed to this revenue growth. Growth in the solutions business with large enterprise customers developed particularly strongly. In this segment, which offers the highest margins, QSC increased its revenues by 75 percent to € 12.6 million. New customers who will be communicating over VPNs from QSC in the future include French oil corporate Total as well as one of Germany's largest insurance companies. For the first time, large enterprise customers was the segment that generated the highest revenues, accounting for 31 percent of the Company's total revenues. QSC earned 29 percent of its total revenues with standardized solutions for small and medium enterprises in the business customer segment; this represents revenues of € 12.2 million. Right from the very beginning, the innovative Voice over IP solutions that QSC presented in advance of this year's CeBIT attracted keen interest.

The Company's business with value added resellers returned to double-digit growth rates, with revenues rising by 16 percent over the first three months of 2004 to € 5.1 million. In this segment, QSC is also benefiting from contracts with international carriers like AT&T, BT Global Services, Colt, Equant and MCI, who are collaborating with QSC as an infrastructure partner in building international VPNs in Germany.

With revenue growth of 25 percent to € 11.5 million, the residential customer segment continued to develop positively. In addition to the cities where QSC owns its network infrastructure, the Company has started in March of this year to offer a DSL resale product, Q-DSL tengo, which enables residential customers to use the Internet with QSC's high security standards and high service quality.

Revenue Mix (in percent)

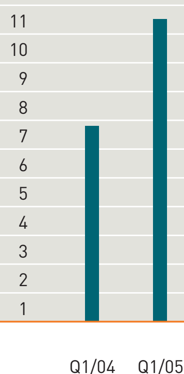


Disproportionate rise in gross profit // Network expenses, which are recorded under cost of revenues, totaled € 31.0 million in the first quarter of 2005, remaining virtually unchanged from the previous quarter. The 22-percent increase over the first three months of 2004 was essentially attributable to strong dynamics in the business with large enterprise customers. The growing number of new customers necessitates considerable upfront expenses for connecting them to the QSC network. In addition, the demand-driven expansion of QSC's own infrastructure also creates corresponding expenses for implementing and integrating those expansions into the existing network, over and above the capital investments.

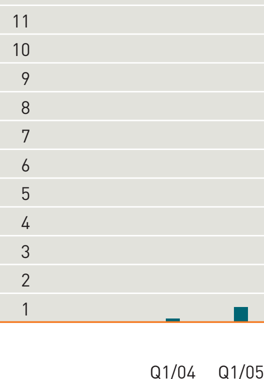
Nevertheless, QSC was able to grow its gross profit by 54 percent in the first quarter with revenue growth of 29 percent. Gross profit for the first three months of the current fiscal year totaled € 10.5 million, as opposed to € 6.8 million for the corresponding period the year before. This represents a gross margin of 25.3 percent, as opposed to 21.1 percent in the first three months the year before.

Gross profit tops € 10 million in first quarter of 2005

Gross Profit (in € million)



EBITDA (in € million)



QSC expands sales and marketing team

As planned, selling and administrative expenses rose in the first quarter of 2005. QSC has hired some 40 new employees since the beginning of the year in order to continue the utilization of existing growth opportunities with business customers, while at the same being able to increasingly address and support small and medium enterprise customers directly. As a result of these measures, sales and marketing expenses increased to € 6.1 million, as opposed to € 4.5 million in the first three months of 2004. During the same period, administration expenses rose by € 1.7 million to € 3.8 million. The € 0.9 million increase over the previous quarter was essentially attributable to the expiration of subleases at QSC's headquarters in Cologne, which provided the Company with the physical space required for expanding its sales and marketing organization.

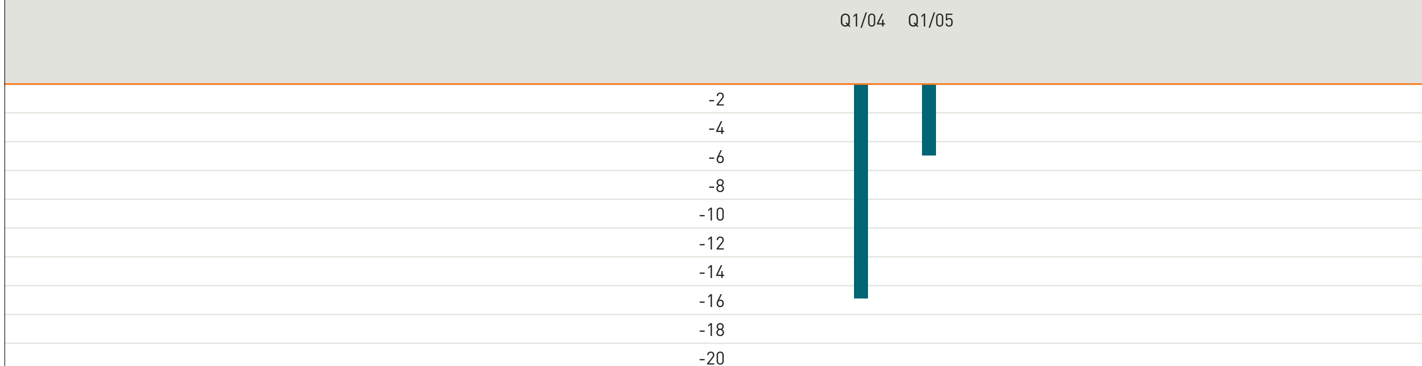
Positive EBITDA rises // QSC was able to grow its EBITDA in the first quarter of 2005. The Company's operating profit before depreciation totaled € 0.5 million, as opposed to € 0.1 million for the first three months of 2004. QSC defines EBITDA as earnings before interest, taxes, the pro-rated results of equity investments accounted for under the equity method, amortization of deferred non-cash compensation, as well as depreciation on plant and equipment and amortization of goodwill.

Depreciation and amortization expense declined to € 5.9 million in the first quarter of 2005; it had stood at € 6.2 million for the same period the year before. This reduction stemmed from the growing volume of fully depreciated assets, and improved the Company's EBIT and results for the period in the first three months of the current fiscal year. In the first quarter of 2005, EBIT amounted to € -5.4 million, as opposed to € -6.1 million for the corresponding quarter the year before, while the Company's net loss declined from € -5.5 million to € -5.1 million. Earnings per share for the first quarter of the current fiscal year amounted to € -0.05.

Demand-driven expansion of QSC's network // In expanding its network, QSC has been investing in three areas since the beginning of the year. Firstly, the Company is upgrading its voice network to a Next Generation Network with the support of Chinese-based technology supplier Huawei Technologies. This will enable seamless utilization of Voice over IP technology, even with conventional telecommunication systems. Secondly, QSC is broadening the coverage of its DSL network by connecting additional cities. And thirdly, QSC is beginning to upgrade its network with ADSL2+ technology, which allows data transfer speeds of up to 16 Mbit/s. QSC is partnering with debitel AG in connection with this expansion. This Stuttgart-based telecommunication provider, with more than 6,500 marketing partners and a customer base of over eight million subscribers in Germany, will be in charge of marketing the super-fast DSL connections; QSC is expanding its network according to existing demand. Overall, QSC's capital investments totaled € 3.8 million in the first quarter of 2005, as opposed to € 1.8 million during the same period the year before.
While this resulted in an increase in net cash used in investing operations, net cash used in operating activities declined from € -14.8 million in the first three months of 2004 to € -4.9 million as a result of progress in the Company's operating business. The cash burn for the first three months of the current fiscal year was significantly affected by annual pre-payments to Deutsche Telekom for the full fiscal year, which are due and payable during the first quarter. Net liquid assets, including fixed-interest securities, totaled € 31.3 million as of March 31, 2005.

Seamless Voice over IP throughout the entire QSC network

Operating Cash Flow (in € million)



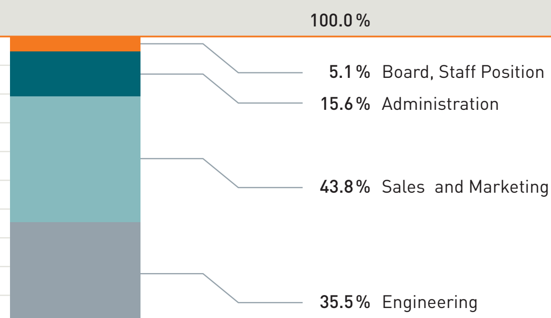
Aside from accounts payable under financial leasing agreements, QSC remained virtually debt-free. Accounts payable under financial leasing agreements rose to € 8.5 million as of March 31, 2005, to no small degree as a result of the Company's increased level of capital investment.
Due to the conversion of QSC convertible bonds to QSC shares under the Company's employee stock ownership plans, QSC's share capital rose moderately by € 138,394 to € 105.6 million during the past quarter. With an equity ratio of 60 percent, QSC views itself as well financed in view of the existing growth opportunities.

Strong revenue growth necessitates expansion of sales organization

Sales organization set for further growth // During the first quarter of 2005, QSC's workforce rose from 367 to 389 people. However, the Company has already hired a total of some 40 new employees since the beginning of the year, predominantly in sales and marketing. Accounting for 44 percent of the total workforce, these new hires increased the share of employees working in sales and marketing operations. 36 percent of the workforce are active in technical areas to assure smooth network operation, while simultaneously driving expansion and upgrading of this network. The percentage of administrative employees in the total workforce remained constant at 16 percent in the first quarter of 2005.

Regulatory authority moderately lowers TAL prices // Effective April 1, 2005, the regulatory authority (RegTP) lowered the price for a fully unbundled subscriber connection line (TAL) that competitors have to pay to Deutsche Telekom from € 11.80 to € 10.65. Although QSC views this reduction as a step in the right direction, it feels that further reductions are essential, especially in connection with the non-recurring fees incurred in connection with ordering or terminating a TAL. Although

Workforce Structure (in percent)



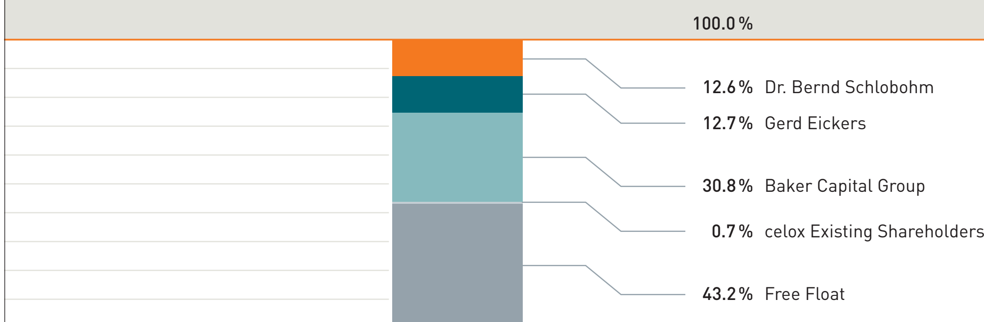
economically far more significant, these one-time fees are much less in the public focus. The one-time fees in connection with the installation of a TAL, for example, can be as high as € 104.08. Given this situation, QSC continues to count on a viable supervision by both the German RegTP as well as the EU Commission.
However, insufficient regulation, as well as other risks or incorrect assumptions, could mean that actual future results might vary materially from the Company's expectations. 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 could therefore change over the course of time.

celox acquisition strengthens QSC // Following the close of the first quarter on March 31, 2005, QSC announced the acquisition of Bonn-based celox Telekommunikationsdienste GmbH on May 12 of the current fiscal year. The purchase price amounted to € 13.8 million and was paid entirely as a contribution in kind in the form of shares issued under an increase of capital. 3,583,776 new shares of QSC stock were created for this purpose. Around 80 percent, representing 2,854,610 shares, were successfully placed with institutional investors on the day of the transaction; the former celox shareholders have agreed to a lock-up for the remaining 20 percent until at least December 31, 2005. As a result of the successful private placement, the percentage of widely held share capital of QSC AG rose to 43.2 percent.

Higher free float following celox transaction

Like QSC, DSL network operator celox is predominantly active in high-growth VPN business with small, medium and large enterprises. In 2004, its workforce of 61 people generated revenues of € 8.4 million and a moderate operating loss before interest, taxes, depreciation and amortization. With the acquisition of celox, QSC is expanding its network coverage to over 100 cities and more than 1,000 colocation rooms effective immediately. The larger network and expanded technology options will accelerate revenue and margin growth in the business with enterprise customers.

Shareholder Structure Following celox Transaction (in percent)



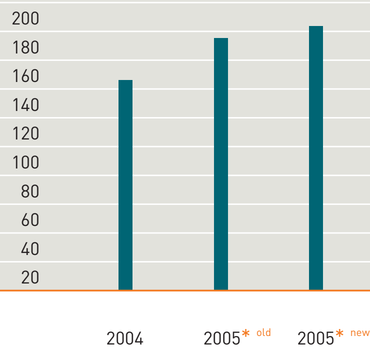
QSC raises revenue forecast // Given the positive trend of business development in the first quarter of 2005 and the celox acquisition, QSC upscaled its forecasts in mid May. The Company now anticipates revenues of at least € 183 million for 2005. This represents a revenue growth of more than 25 percent over the year before. QSC had previously been predicting that revenues would rise by at least 20 percent to more than € 175 million. The Company continues to anticipate a positive EBITDA of between € 4 to 8 million, as well as an operating cash flow of over € 10 million.

QSC now present in 100 cities with its own network

The celox acquisition and the expansion of its DSL network to more than 100 cities will strengthen QSC's core business in the large enterprise customer segment. QSC therefore anticipates a further acceleration of growth in this segment. Also contributing to these strong dynamics are a growing number of small and medium enterprises who are implementing their first nationwide VPN solutions with QSC.

QSC will also be tapping into new revenue potential by upgrading its DSL network with ADSL2+ technology in the coming quarters. QSC will leverage its partnership with debitel that was announced in mid May to market its products in the residential customer segment. Over and above this partnership in the residential market, QSC does not exclude the possibility of further partnerships with mobile operators or service providers in the market for business customers.

Revenue Forecast for 2005 (in € million)



* estimated

Statements of Operations

Consolidated Statements of Operations (unaudited)

(Euro amounts in thousands (T €), except for per share amounts)

	01/01/-31/03/ 2005	01/01/-31/03/ 2004
Net revenues	**41,502**	**32,180**
Cost of revenues	31,013	25,417
Gross profit	**10,489**	**6,763**
Selling and marketing expenses	6,086	4,533
General and administrative expenses	3,838	2,100
Research and development expenses	81	56
Depreciation and amortization	5,869	6,151
Operating loss	**(5,385)**	**(6,077)**
Other income (expenses)		
Interest income	401	598
Interest expenses	(105)	(31)
Other non-operating loss	(18)	(2)
Net loss before income taxes	**(5,107)**	**(5,512)**
Income taxes	-	-
Net loss	**(5,107)**	**(5,512)**
Net loss per common share (basic and diluted)	(0.05)	(0.05)
Weighted average shares outstanding (basic and diluted)	105,571,926	105,256,694

The accompanying notes to unaudited condensed consolidated financial statements are an integral part of these statements.

Balance Sheets

Consolidated Balance Sheets (unaudited)

(Euro amounts in thousands (T €))

	31/03/2005	31/12/2004
ASSETS		
Current assets		
Cash and cash equivalents	13,049	22,536
Marketable securities	18,297	17,785
Trade accounts receivable, net	29,932	25,616
Other receivables	798	3,207
Prepayments and other current assets	7,769	4,801
Total current assets	**69,845**	**73,945**
Non-current assets		
Other non-current assets	190	374
Plant and equipment, net		
Networking equipment and plant	22,182	25,669
Operational and office equipment	10,577	9,431
Total plant and equipment, net	**32,759**	**35,100**
Intangible assets, net		
Licenses	655	694
Software	2,645	2,318
Others	2	2
Total intangible assets, net	**3,302**	**3,014**
Goodwill	2,393	2,393
Total non-current assets	**38,644**	**40,881**
Total assets	**108,489**	**114,826**

	31/03/2005	31/12/2004
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Current liabilities		
Trade accounts payable	18,399	20,276
Trade accounts payable due to related parties	475	472
Accrued liabilities	8,920	6,871
Deferred revenues	1,298	1,370
Current portion of obligations under capital leases	3,263	2,647
Other current liabilities	5,430	8,239
Total current liabilities	**37,785**	**39,875**
Non-current liabilities		
Convertible bonds	59	60
Accrued pensions	314	316
Non-current portion of obligations under capital leases	5,210	4,105
Total non-current liabilities	**5,583**	**4,481**
Total liabilities	**43,368**	**44,356**
Shareholders' Equity		
Common stock	105,641	105,503
Additional paid-in capital	474,807	474,750
Other comprehensive income (loss)	(178)	259
Accumulated deficit	(515,149)	(510,042)
Total Shareholders' Equity	**65,121**	**70,470**
Total liabilities and Shareholders' Equity	**108,489**	**114,826**

The accompanying notes to unaudited condensed consolidated financial statements are an integral part of these statements.

Statements of Cash Flows

Consolidated Statements of Cash Flows (unaudited)

(Euro amounts in thousands (T €)

	01/01/-31/03/ 2005	01/01/-31/03/ 2004
Cash flow from operating activities		
Net loss	**(5,107)**	**(5,512)**
Adjustments to reconcile net loss to cash used in operating activities		
Non-cash compensation charge	-	30
Depreciation and amortization	5,869	6,121
Gain on sale of equipment	6	3
Bad debt expense	107	158
Change in operating activities		
Increase in trade accounts receivable	(4,423)	(6,377)
Increase in trade accounts receivable due to related parties	-	(1)
Increase in unbilled receivables	-	(609)
Decrease in other current receivables	2,409	2,359
Increase in prepayments and other current assets	(2,968)	(2,742)
Decrease/(Increase) in other non-current assets	184	(178)
Decrease in trade accounts payable	(1,874)	(5,703)
Increase in obligations under capital leases	1,721	463
Increase/(Decrease) in accrued liabilities	2,049	(1,689)
Decrease in deferred revenues	(72)	(23)
Decrease in other current liabilities	(2,809)	(1,068)
Decrease in accrued pensions	(2)	(19)
Net cash used in operating activities	**(4,910)**	**(14,787)**

	01/01/-31/03/ 2005	01/01/-31/03/ 2004
Cash flow from investing activities		
Change in marketable securities	(512)	(707)
Available-for-sale securities (unrealized gain)	(437)	67
Property acquired under capital leases	(2,601)	(496)
Purchases of intangible assets	(544)	(45)
Purchases of plant and equipment	(677)	(1,220)
Proceeds from sale of equipment	-	13
Net cash used in investing activities	**(4,771)**	**(2,388)**
Cash flow from financing activities		
Redemption of convertible bonds	(1)	(1)
Disposal of treasury stock	-	596
Proceeds from issuance of common stock	195	394
Net cash provided by financing activities	**194**	**989**
Net decrease in cash and cash equivalents	**(9,487)**	**(16,186)**
Cash and cash equivalents at beginning of the year	22,536	34,964
Cash and cash equivalents at end of period	**13,049**	**18,778**
Supplemental disclosures of cash flow information		
Cash paid during the period for		
Interest expenses	87	31

The accompanying notes to unaudited condensed consolidated financial statements are an integral part of these statements.

Statements of Equity

Consolidated Statements of Shareholders' Equity from January 1, 2004 to March 31, 2005 (unaudited)

(Euro amounts in thousands (T €), except for per share amounts)

	Ordinary Shares		Treasury Shares	
	Shares	T €	Shares	T €
Balance as of January 1, 2004	**105,037,396**	**105,037**	**358,747**	**(266)**
Net loss				
Other comprehensive income				
Comprehensive income				
Convertible bonds forfeited due to termination of employment (January 1, 2004)				
Issuance of common stock in connection with the conversion of convertible bonds (March 31, 2004)	219,298	219		
Issuance of common stock in connection with the conversion of convertible bonds (June 30, 2004)	51,969	52		
Issuance of common stock in connection with the conversion of convertible bonds (September 30, 2004)	85,600	86		
Issuance of common stock in connection with the conversion of convertible bonds (December 31, 2004)	108,466	109		
Disposal of treasury stock (March 31, 2004)			(122,865)	91
Disposal of treasury stock (June 30, 2004)			(235,882)	175
Amount amortized during the period				
Balance as of December 31, 2004	**105,502,729**	**105,503**	**-**	**-**
Net loss				
Other comprehensive loss				
Comprehensive income				
Issuance of common stock in connection with the conversion of convertible bonds (March 31, 2005)	138,394	138		
Balance as of March 31, 2005	**105,641,123**	**105,641**	**-**	**-**

	Additional Paid-In Capital T €	Deferred Compensation Account T €	Comprehensive Income T €	Accumulated Other Compre-hensive Income T €	Accumulated Deficit T €	Total Shareholders' Equity T €
	473,302	(75)		(46)	(488,483)	89,469
			(21,559)		(21,559)	(21,559)
			305	305		305
			(21,254)			
	(45)	45				-
	174					393
	12					64
	4					90
	41					150
	505					596
	757					932
		30				30
	474,750	-		259	(510,042)	70,470
			(5,107)		(5,107)	(5,107)
			(437)	(437)		(437)
			(5,544)			
	57					195
	474,807	-		(178)	(515,149)	65,121

The accompanying notes to unaudited condensed consolidated financial statements are an integral part of these statements.

Notes to the Interim Condensed Consolidated Financial Statements

1. Basis of presentation

General // The unaudited interim condensed consolidated financial statements ("interim financial statements") of QSC AG ("QSC" or "the Company") and subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States ("US GAAP"). All amounts, except per share amounts, are in thousands of Euro ("T €").
In the opinion of management, the interim financial statements reflect all normal recurring adjustments necessary for a fair presentation of the financial position, results of operations and cash flows of the Company. The interim financial statements should be read in conjunction with the December 31, 2004, audited consolidated financial statements. Operating results for the interim periods presented are not necessarily indicative of the results that may be expected for any future period.

Principles of consolidation // The interim financial statements include the accounts of QSC and its subsidiaries. All significant intercompany transactions have been eliminated in the consolidation. The equity method of accounting is used for companies and other investments in which QSC has significant influence. Generally, this represents ownership of at least 20 percent and not more than 50 percent.

Use of estimates // The preparation of the financial statements in conformity with US GAAP requires management to make estimates and assumptions related to the reported amounts of assets and liabilities and the disclosures of assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses for the period. Although these estimates are based on our knowledge of current events and actions we expect to undertake in the future, actual results may ultimately differ from estimates.

Foreign currencies // QSC's financial statements are presented in Euro, its functional 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 other non-operating income or other expense.

Cash and cash equivalents // Cash and cash equivalents consist of highly liquid instruments with original maturities of three months or less from the date of purchase.

Leasing // The accrual of leased equipment is not related to the legal owner, but the economic owner. The economic owner is realizing the risks and opportunities arising from the use of the leased equipment. In a capital lease the lessee is the economic owner, capitalizing the leased equipment and depreciating it over the useful life. A relevant liability is recorded that will be reduced by the lease payments.

Marketable securities // Trading securities, representing securities bought and held principally for the purpose of near term sales, are accounted for at fair value as of the balance sheet date, and unrealized gains and losses are included in earnings.
Held-to-maturity securities are accounted at amortized cost and unrealized gains and losses are included in earnings.
Available-for-sale securities are accounted for at fair value as of the balance sheet date and related unrealized gains and losses are included in other comprehensive income (loss), until realized.
A decline in value of any available-for-sale security below cost is deemed to be other than temporary resulting in a deduction in carrying amount to fair value. The impairment is charged to earnings and a new cost basis is established.

Earnings per share // Earnings per share is computed by dividing loss applicable to common stockholders by the weighted average number of shares of QSC's common stock outstanding. Diluted earnings per share are calculated in the same manner except that the number of shares is increased assuming exercise of dilutive stock options and convertible bonds where these are dilutive. For the three months ended March 31, 2005 and 2004, the dilutive effect of options was not considered because QSC recorded net losses and the impact of an assumed option exercise would be anti-dilutive.

Segment information // QSC applies the "management approach" in accordance with SFAS 131, "Disclosures about Segments of an Enterprise and Related Information", for identifying reportable segments. The management approach designates the internal organization used by management for making operating decisions and assessing performance as the source of QSC's reportable segments. QSC is primarily operating in the customer segments large enterprises, business customers, resellers and residential customers.
The customer segment large enterprises 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 reseller segment includes the business with Internet service providers and telecommunication providers without proprietary infrastructure. They are marketing 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 premium residential customers.
The positions that cannot directly be allocated to the segments are summarized in the reconciliation column. These costs are primarily personnel expenses, rental fees for leased lines, and expenses for repairs, maintenance and operation of our network and the rental fees for the colocation rooms.

01/01/-31/03/2005 in T €	Segment Large enterprises	Segment Business customers	Segment Resellers	Segment Residential customers	Recon-ciliation	Consoli-dated
Revenues	**12,642**	**12,218**	**5,134**	**11,508**	-	**41,502**
Directly allocated expenses	4,004	7,370	2,776	8,859	-	23,009
Gross profit	**8,638**	**4,848**	**2,358**	**2,649**	-	**18,493**
Not allocated expenses	-	-	-	-	18,009	18,009
EBITDA	**8,638**	**4,848**	**2,358**	**2,649**	**(18,009)**	**484**
Depreciation and deferred non-cash compensation expenses	381	242	274	644	4,328	5,869
Non-operating income	-	-	-	-	278	278
Net profit/(loss)	**8,257**	**4,606**	**2,084**	**2,005**	**(22,059)**	**(5,107)**
Assets as of March 31, 2005	2,264	1,438	1,628	3,827		

01/01/-31/03/2004 in T €	Segment Large enterprises	Segment Business customers	Segment Resellers	Segment Residential customers	Recon-ciliation	Consoli-dated
Revenues	**7,182**	**11,340**	**4,441**	**9,217**	-	**32,180**
Directly allocated expenses	3,396	6,535	1,670	5,885	-	17,486
Gross profit	**3,786**	**4,805**	**2,771**	**3,332**	-	**14,694**
Not allocated expenses	-	-	-	-	14,620	14,620
EBITDA	**3,786**	**4,805**	**2,771**	**3,332**	**(14,620)**	**74**
Depreciation and deferred non-cash compensation expenses	97	222	345	764	4,723	6,151
Non-operating income	-	-	-	-	565	565
Net profit/(loss)	**3,689**	**4,583**	**2,426**	**2,568**	**(18,778)**	**(5,512)**
Assets as of March 31, 2004	505	1,157	1,797	3,980		

Other comprehensive loss // Other comprehensive loss as of March 31, 2005, consists of the following:

	01/01/-31/03/2005 in T €
Unrealized loss on available-for-sale securities	(437)
Other comprehensive loss	**(437)**

New accounting standards // Effective January 1, 2002, the Company adopted the Standard of Financial Accounting Standards ("SFAS") 144, "Accounting for the Impairment or Disposal of Long-Lived Assets", which addresses financial accounting and reporting for the impairment and disposal of long-lived assets. These statements supersede SFAS 121, "Accounting for the Impairment of Long-Lived Assets to be Disposed Of". The Company reviews the carrying value of its long-lived assets, including fixed assets, investments, (this is tested for impairment in accordance with SFAS 142 as disclosed above), and intangible assets, for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be fully recoverable. Recoverability of long-lived assets, excluding goodwill (see discussion above), is assessed by a comparison of the carrying amount of the asset or the group of assets to the total estimated undiscounted cash flows expected to be generated by the asset or group. If the estimated future net undiscounted cash flows are less than the carrying amount of the asset or group, the asset or group is considered impaired, and an expense is recognized equal to the amount required to reduce the carrying amount of the asset to its then fair value. No adjustments were required to the carrying value of long-lived assets in the three months ended March 31, 2005 or 2004.
In June 2001, the Financial Accounting Standards Board ("FASB") issued SFAS 143, "Accounting for Asset Retirement Obligations". SFAS 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalized as part of the carrying amount of the long-lived asset. SFAS 143 is effective for fiscal years beginning after June 15, 2002. The adoption of SFAS 143 did not have a material impact on the results of operation or the financial position of QSC.

In June 2002, the FASB issued SFAS 146 "Accounting for Costs Associated with Disposal or Exit Activities". This Statement addresses financial accounting and reporting for costs associated with exit or disposal activities and nullifies Emerging Issues Task Force ("EITF") Issue No. 94-3 "Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring)". This Statement requires that a liability for a cost associated with an exit or disposal activity be recognized when the liability is incurred. Under Issue 94-3, a liability for an exit cost as defined in Issue 94-3 was recognized at the date of an entity's commitment to an exit plan. However, this standard does not apply to costs associated with exit activities involving entities acquired under business combinations or disposal activities covered under SFAS 144. The adoption of SFAS 146 did not have a material impact on the results of operations or the financial position of QSC.

In December 2003, the FASB issued FIN 46R (a revision of FIN 46 as issued in January 2003) "Consolidation of Variable Interest Entities", which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity. FIN 46R is effective for all interests in structures commonly referred to as special-purpose entities for periods ending after December 15, 2003, and for all other types of variable interests for periods ending after March 15, 2004. The Company does not have any variable interests in special-purpose entities, and therefore the adoption of FIN 46R did not have a significant impact on the financial position of the Company. In addition, the Company does not have any interests in any other variable interest entities, and therefore the Company does not anticipate that the adoption of FIN 46R will have a material impact on its results of operations or its financial position.

In December 2004, the FASB issued SFAS 123 (revised 2004), "Share-Based Payment" ("SFAS 123R"). SFAS 123R establishes accounting guidance for transactions in which an entity exchanges its equity instruments for goods or services. It also addresses transactions in which an entity incurs liabilities in exchange for goods or services that are based on the fair value of the entity's equity instruments or that may be settled by the issuance of those equity instruments. Equity-classified awards are measured at grant date fair value and are not subsequently remeasured. Liability-classified awards are remeasured to fair value at each balance sheet date until the award is settled. SFAS 123R applies to all awards granted after July 1, 2005, and to awards modified, repurchased or cancelled after that date using a modified version of prospective application. QSC does not anticipate that the adoption of SFAS 123R will have a material impact on its results of operations or its financial position.

2. Acquisitions and investments

Acquisitions // 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 enhances QSC's ability to offer integrated telecommunication solutions for all business customer segments. Total acquisition cost for Ventelo was T € 11,454, including direct acquisition costs of T € 90. As of March 31, 2005, a second and final tranche of T € 4,450 was outstanding that will presumably be paid in the second half of financial year 2005.
On April 1, 2002, Ventelo was outsourced from its former parent company Ventelo Deutschland GmbH due to §§ 159 et seqq. "Umwandlungsgesetz". Ventelo is responsible for potential liabilities of the former parent company for a period of five years. The estimated fair value of the identifiable net assets exceeds the purchase price, resulting in a negative goodwill of T € 193 and reducing the acquired assets, on a pro rata basis, by this amount.

Investments // Netchemya S.p.A., Italy, one of QSC's investments made in 2000, is currently in liquidation because follow-on funding and the implementation of the business plan were not secured. QSC therefore wrote-off its remaining investment in Netchemya of T € 4,136 in 2002.

3. Share capital

Nominal share capital // The nominal share capital of QSC as of March 31, 2005, consists of ordinary share capital of T € 105,641 (December 31, 2004: T € 105,503) and is divided into 105,641,123 (December 31, 2004: 105,502,729) ordinary shares having a notional value of one Euro each. Each share gives the registered holder one vote at the general meeting of shareholders and the right to fully share in dividends. There are no restrictions on voting rights. During the first three months ended March 31, 2005, nominal share capital increased by T € 138 due to the conversion of 138,394 convertible bonds. Employees used their right to convert their convertible bonds to registered ordinary shares of QSC.

4. Management Board and Supervisory Board

Management Board // Shares and conversion rights of members of the Management Board:

	March 31, 2005		March 31, 2004	
	Shares	Conversion rights	Shares	Conversion rights
Dr. Bernd Schlobohm	13,818,372	-	13,818,372	-
Markus Metyas	2,307	1,559,116	2,307	1,559,116
Bernd Puschendorf	-	1,000,000	-	1,000,000

Supervisory Board // Shares and conversion rights of members of the Supervisory Board:

	March 31, 2005		March 31, 2004	
	Shares	Conversion rights	Shares	Conversion rights
John C. Baker	-	19,130	-	19,130
Herbert Brenke	187,820	19,130	187,820	19,130
Gerd Eickers	13,853,484	9,130	13,853,484	9,130
Ashley Leeds	9,130	10,000	9,130	10,000
Norbert Quinkert	3,846	-	3,846	-
David Ruberg	4,563	19,130	4,563	19,130

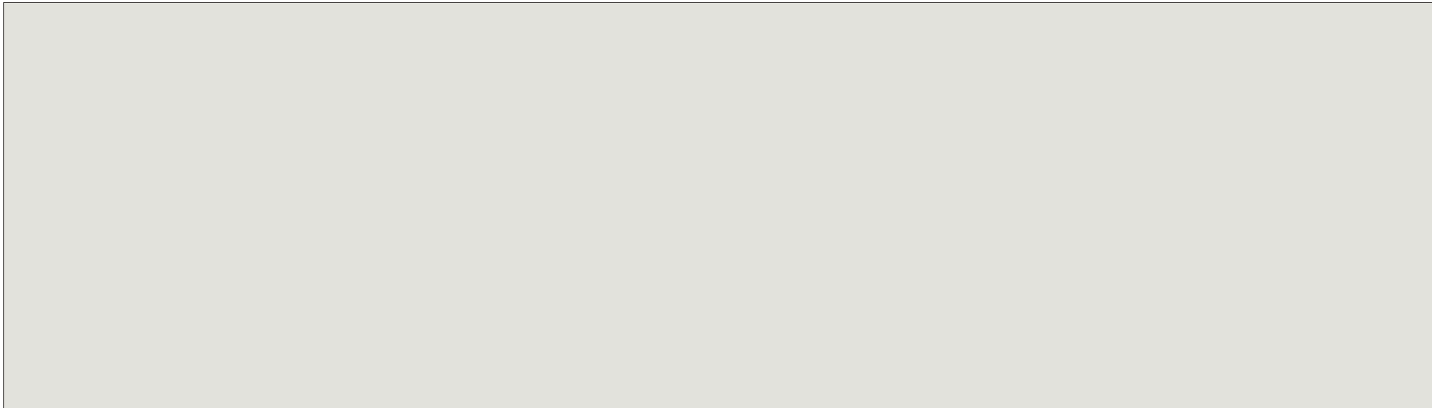
Events subsequent to the close of the reporting period // On May 12, 2005, QSC acquired 100 percent of the share capital of celox Telekommunikationsdienste GmbH of Bonn ("celox"). celox is a nationally operating telecom with its own infrastructure. Through this acquisition, QSC now possesses more than 1,000 fully-equipped colocation rooms in over 100 cities, as well as an expanded customer base in the large enterprise and business customer segments. The purchase price totaled T € 13,762, and was paid in the form of 3,583,776 new shares of stock. The new shares were created from approved capital against contributions of all celox shares as well as a loan redemption entitlement against celox GmbH held by the legacy celox shareholders. Following this partial utilization, the Company's approved capital now totals € 46,416,224. The authorization resolved by the Annual Shareholders Meeting on May 27, 2004, to acquire treasury shares up to an imputed share in the total amount of T € 10,000 through the stock exchange or on the basis of a public tender offer was revoked as per the adjournment of the Annual Shareholders Meeting on May 19, 2005, as it had been time-limited by law until October 31, 2005. It was replaced by a new, identical authorization to remain in effect until October 31, 2006.
Through resolutions of the Annual Shareholders Meeting on May 19, 2005, Conditional Capital I in the amount of € 9,126 was revoked and Conditional Capital III in the amount of € 4,652,014 was reduced by € 920,200 to € 3,731,814 with a view to the expiration of the conversion term and the term for issuing further convertible bonds. The resolution adopted by the Annual Shareholders meeting on May 17, 2002, to authorize the Management Board to issue convertible bonds, as well as the corresponding Conditional Capital IV, was revoked as per the adjournment of the Annual Shareholders Meeting on May 19, 2005, and replaced by a comparable authorization to issue option and/or convertible bonds at currently prevailing terms and conditions and a new Conditional Capital IV in the amount of € 25,000,000.

Cologne, May 2005

Dr. Bernd Schlobohm
Chief Executive Officer

Markus Metyas

Bernd Puschendorf



Calendar

Quarterly Reports
August 30, 2005
November 29, 2005

Conferences/ Events
June 28, 2005
Baden-Wuerttembergische Bank AG
Capital Market Conference 2005,
Frankfurt

November 21-23, 2005
German Equity Forum
Autumn 2005, Frankfurt

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Further information under www.qsc.de