QUARTERLY REPORT II / 2003

QSC AT A GLANCE

	01/04/-30/06/ 2003	01/04/-30/06/ 2002	01/01/-30/06/ 2003	01/01/-30/06/ 2002
All amounts in million EUR				
Revenues	28.3	12.0	55.8	21.5
Gross profit/loss	1.6	-2.3	2.1	-9.8
EBITDA	-7.2	-14.9	-17.2	-31.2
EBIT	-15.6	-24.0	-35.6	-48.4
Net loss	-15.2	-23.8	-34.0	-47.6
Net loss per common share [1] (in EUR)	-0.15	-0.24	-0.34	-0.47
Capital Expenditure	1.8	4.2	3.3	5.7
Equity			114.6 [2]	145.3 [3]
Balance Sheet Total			158.3 [2]	194.6 [3]
Equity ratio (in %)			72.4 [2]	74.7 [3]
Liquidity			68.1 [2]	87.6 [3]
Share price as of 30/06/ (in EUR)			1.69	0.67
Number of shares as of 30/06/			105,012,014	105,008,714
Market capitalization as of 30/06/			177.5	70.4
Employees as of 30/06/			392	306

[1] basic and diluted

[2] as of June 30, 2003

[3] as of December 31, 2002

COMMUNICATION IS CHANGING THE WORLD
BROADBAND REINVENTS COMMUNICATION
QSC IS THE BROADBAND SOLUTION

SUSTAINED IMPROVEMENT IN PROFITABILITY QSC reduced its EBITDA loss by more than 50 percent to EUR -7.2 million in the second quarter of 2003 (Q2 2002: EUR -14.9 million). This sharp improvement is attributable to sustained order growth from business and project customers. Growth in this segment also had a positive impact on revenues, which rose by 136 percent to EUR 28.3 million (Q2 2002: EUR 12.0 million).

CASH FLOW BREAKEVEN EARLIER THAN PLANNED For the ninth time in a row, QSC reduced its net cash outflow from quarter to quarter: from EUR -10.9 million in the first quarter of 2003 to EUR -8.6 million for the second quarter. Given this steady reduction, QSC now expects to reach the cash flow breakeven point during the first half of 2004.

INCREASED SHARE PRICE DEVELOPMENT In the second quarter of 2003, QSC shares again numbered among the top performers in the Prime Standard – the share price increased by 182 percent to EUR 1.69. In the first half of 2003, QSC's share price has even quadrupled. With a market capitalization of some EUR 230 million on July 31, 2003, QSC is now one of the 30 most highly capitalized technology stocks in the Prime Standard.

Dr. Bernd Schlobohm
Chief Executive Officer

Gerd Eickers
Chief Operating Officer

Markus Metyas
Chief Financial Officer

Bernd Puschendorf
Chief Sales Officer

Dear Shareholders,

In spite of the weak overall economy, QSC's business continued to develop well during the second quarter of 2003. So well, in fact, that in mid August we were able to raise the full year guidance we had published in February for the current fiscal year. We are now forecasting annual revenues of over EUR 115 million, as opposed to our previous guidance of EUR 105 to 115 million. Our anticipated EBITDA loss should be better than EUR -25 million; up until now, we had been anticipating a negative annual EBITDA of between EUR -25 and -30 million. We plan to reach the cash flow breakeven point during the first half of 2004, earlier than planned when we went public in April 2000.

This progress stems from our clear positioning as an integrated telecommunication provider for business customers. The 136-percent leap in revenues to EUR 28.3 million came mainly from sustained high order growth from business and project customers. Both, large corporates as well as small and medium-sized enterprises are recognizing that they can replace their expensive leased lines with high-quality DSL lines and build virtual private networks (VPNs) on the basis of QSC's broadband network.

Our own network gives us a competitive edge

What is crucial to QSC's acceptance is the fact that we are one of the few service providers with an own nationwide DSL network. This enables QSC to assure the high bandwidths and quality levels that organizations have come to depend upon in the Internet age. Since the beginning of July, QSC's major customers have been able to monitor the performance of their VPNs themselves. We offer maximum transparency with our QSC Scout Web-based monitoring tool, thus demonstrating the constant high quality of our network.

The integration of Ventelo is producing major synergies, especially in the networking area. As a result, QSC succeeded in increasing its gross profit from EUR 0.5 million in the first quarter of 2003 to EUR 1.6 million. Today, QSC owns a nationwide, consistent, high-performance network for voice and data communication. Above and beyond the network level, Ventelo and QSC are growing together to become a joint company faster than had been planned, which is already manifesting itself today in a sharp improvement in EBITDA.

A winning combination: rising revenues and significantly lower selling expenses

An additional reason why we are rapidly approaching the EBITDA breakeven point is QSC's focus on high-margin market segments, as well as the successes we are reaping through our strict cost management. At EUR 5.1 million, consolidated selling and marketing expenses were down 38 percent year-on-year for the second quarter of 2003. Our team of key account managers is typically addressing potential VPN customers directly today. In addition, we are using online media to address interesting customer groups efficiently. These activities are supplemented with intensive press relations efforts.

During the second quarter, there was a broad-based media response to our announcement to offer preselection rates for local telephone calls, as well as to the conclusion of our QSC-Voice rollout ahead of schedule. Today, our DSL-based digital voice product is already available in all QSC cities.

At the Annual Shareholders Meeting in Cologne in May 2003, we had already announced to you, our shareholders, that we would like to add a highly qualified member to our Supervisory Board. Mr. Norbert Quinkert, Chairman of Motorola GmbH in Germany, has been a member of the QSC Supervisory Board since late July. This seasoned executive possesses an in-depth understanding of the complex needs of major accounts in the IT sector, and with this expertise he is greatly adding to our competence in this field.

The capital market is increasingly rewarding our positioning as an integrated telecommunication provider for business customers. We are experiencing a noticeable rise in the number of inquiries from investors in Germany and other countries, and we dedicate a high level of importance to investor relations activities. Our medium-term goal remains our inclusion in the TecDax, the leading German index for technology stocks; our inclusion in the Nemax 50 since June 23, 2003, represents a major step in this direction.

The development of our share price in recent months is motivating the entire QSC team. However, we know that we have to work hard, one quarter after another, to earn the trust of the capital markets. Investors measure QSC against the benchmark of its operating results and its ability to meet its guidance. The next goal is to reach the EBITDA breakeven point – which we intend to achieve during the course of the fourth quarter of 2003.

Cologne, August 2003

Your QSC AG Management Board

C “Considerable synergies being seen in both selling and network expenses only six months after Ventelo acquisition.“

MANAGEMENT REPORT

Positive development of operating business enables guidance to be revised upward Continuing growth in high-margin services for business and project customers, as well as the rapid realization of synergies out of the Ventelo acquisition, produced a significant results improvement for the second quarter of 2003. Year-on-year, the EBITDA loss was reduced by more than 50 percent from the second quarter of 2002, and by 28 percent from the first quarter of 2003, to EUR -7.2 million.

Given this particularly positive development against the backdrop of an extremely weak economy in Germany, QSC revised its original guidance, dating from February 2003, for the current fiscal year. The EBITDA loss is now expected to be better than EUR -25 million, while revenues should total more than EUR 115 million. QSC now anticipates reaching the cash flow breakeven point during the first half of 2004, sooner than it had originally been planned.

Business customers already account for over 50 percent of total revenues

Revenues soar in the second quarter of 2003 QSC increased its second-quarter revenues by 136 percent year-on-year to EUR 28.3 million (Q2 2002: EUR 12.0 million). For the first half of 2003, revenues rose by 160 percent – from EUR 21.5 million for the first six months of 2002 to EUR 55.8 million. In addition to the Ventelo-consolidation effect, strong growth from business and project customers also contributed to this rise. Organizations of every size are increasingly opting for QSC's expertise in building and operating integrated telecommunication solutions. The share of total revenues accounted for by business customers reached 52 percent for the second quarter of 2003, as opposed to 32 percent in 2002 and 25 percent in 2001. This naturally led to a relative decline in the percentage of total revenues accounted for by pure access products from resellers. Yet the reseller business continues to remain an important element of the QSC business model.

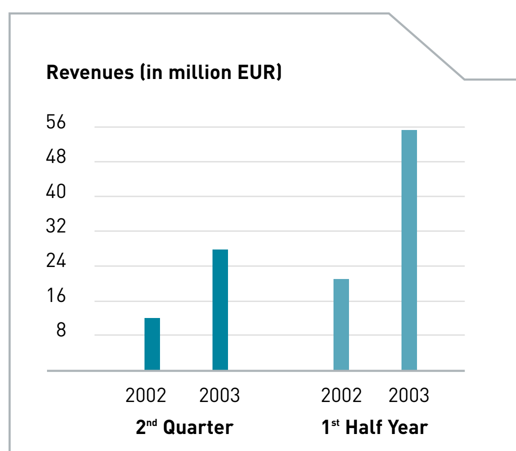
To no small degree, the company's successes with business customers are based upon the high quality of QSC's infrastructure. This performance was underscored by a six-month test conducted by trade journal Network Computing which dubbed the Q-DSLmax product as "synchronous DSL-Turbo" (issue of June 25, 2003). The residential customer product Q-DSL home continues to hold top rankings in tests, as well; as documented in this year's August issue of com!online.

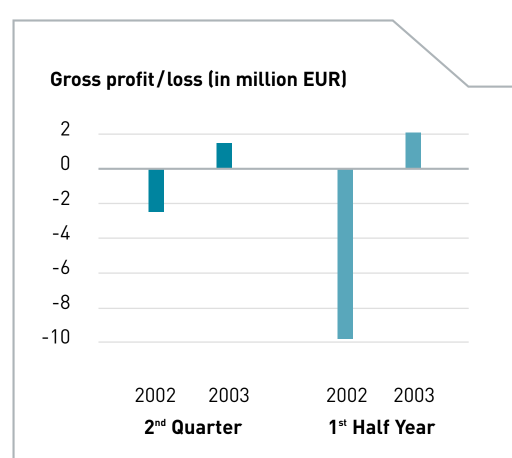
Synergy effects and strict cost management lead to sharp rise in profitability ⁄⁄ In spite of rising revenues, network expenses (shown under cost of revenues) were further reduced during the second quarter of 2003, a development that underscores the scalability of the QSC business model. Cost of revenues stood at EUR 26.7 million for the second quarter of 2003, as opposed to EUR 27.1 million for the preceding quarter. Due to the consolidation of Ventelo, network expenses increased by 87 percent compared to the second quarter 2002; a moderate increase with respect to the revenue growth of 136 percent.

Gross profit triples in the second quarter

As a result of this development, gross profit for the second quarter of 2003 tripled to EUR 1.6 million (Q1 2003: EUR 0.5 million). QSC earned a gross profit of EUR 2.1 million for the first six months of the current fiscal year (1st half of 2002: EUR -9.8 million).

At EUR 5.1 million, selling and marketing expenses were both significantly lower year-on-year (Q2 2002: EUR 8.2 million) as well as down from their level of EUR 6.0 million in the first quarter of 2003. Positioning QSC as a solutions provider for business customers is enabling the company to specifically and individually address distinct customer groups. The concept of jointly marketing voice and data solutions following the Ventelo acquisition is proving to be highly efficient. Only six months after the acquisition, considerable synergistic effects are materialising in both selling and network expenses.





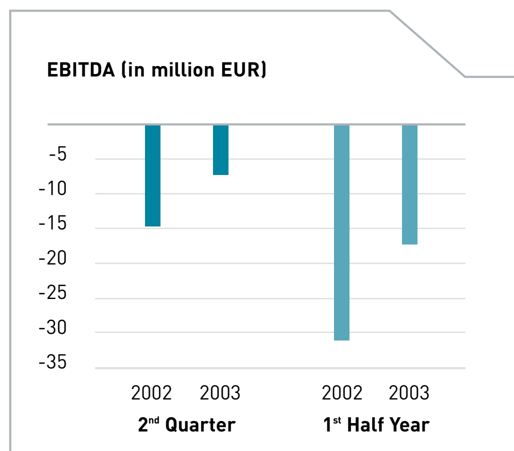
N “Negative EBITDA down more than 50 percent from second quarter of 2002 to EUR -7.2 million.“

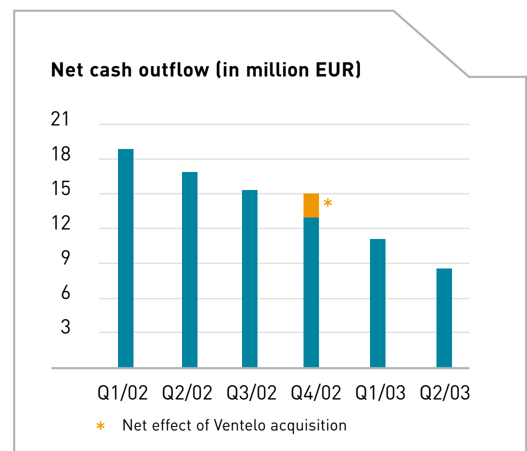
QSC Scout – an important selling point

The level of expenditures for research and development remained constant, totaling EUR 0.3 million. These expenditures were primarily used to complete QSC Scout, a Web-based monitoring tool, as well as to develop customer-specific solutions for project business. For the first time, QSC Scout enables customers to monitor the performance of their VPN solutions themselves and is thus becoming an important selling point.

EBITDA nearing the breakeven point // Rising revenues and lower operating expenses led to a strong improvement in EBITDA. At EUR -7.2 million, it was down by more than 50 percent from the second quarter of 2002 (Q2 2002: EUR -14.9 million). The EBITDA loss for the first half of 2003 was EUR -17.2 million (1st half of 2002: EUR -31.2 million). QSC defines EBITDA as earnings before interest, taxes, the pro-rated results of equity method investments, amortization of deferred non-cash compensation, as well as depreciation of non-current assets and amortization of goodwill.

Depreciation and non-cash compensation amounted to EUR 8.5 million for the second quarter of 2003 (Q2 2002: EUR 9.2 million). This reduction is attributable to two factors: first, declining prices for the hardware with which QSC equips each new customer, which are fully depreciated during the twelve-month period subsequent to their acquisition. Second, to the fact that more than three years after the capital investment phase began, the first plant and equipment assets have now been fully depreciated.





In the second quarter of 2003, the net loss reached EUR -15.2 million (Q2 2002: EUR -23.8 million), down 19 percent from the first quarter of 2003. The net loss improved by nearly 30 percent year-on-year for the first half of the current fiscal year, to EUR -34.0 million (1st half of 2002: EUR -47.6 million).

Cash burn down for the ninth time in a row // QSC reduced its net cash outflow for the second quarter of 2003 by more than 20 percent quarter to quarter, from EUR -10.9 million in the previous quarter to EUR -8.6 million. On June 30, 2003, the company's liquid assets totaled EUR 68.1 million. At EUR 1.8 million, capital investments remained at similarly low levels of the preceding quarters, funding primarily replacement and synergy investments for QSC's own network as well as selective network expansion on the fringes of metropolitan areas, such as in Offenbach and Esslingen.

The company's equity ratio of 72 percent as of June 30, 2003, documents QSC's balance sheet strength. The company continues to be virtually debt free, with non-current liabilities amounting to a mere EUR 0.4 million.

DSL continues to be a high-growth market // In the summer of 2003, economists upgraded their growth forecasts for Germany; the ifo Institute is predicting economic growth of 1.7 percent for the next year. An improved overall economic environment makes it easier for businesses to make investment decisions – including investments in new telecommunication solutions.

In spite of a persistently weak economy, however, the trend toward DSL was sustained during the second quarter of 2003. Demand for virtual private networks (VPNs) is proving to be a growth engine. A current Forrester study predicts that this segment will turn into an eight billion euro market in Europe within the next five years (May 2003: Europe's Managed IP VPN Market). Organizations with workforces of more than 250 people, in particular, are networking their locations and are increasingly using DSL as the platform technology in order to optimize cost, quality and usability. Forrester sees extremely strong growth potential for VPN solutions, whose complete operation is managed by service providers like QSC.

VPN solutions driving further growth of DSL market

“QSC expects to reach cash flow breakeven point ahead of schedule, during first half of 2004.“

QSC offers apprenticeships for the first time // QSC has created its first six information technology specialist training slots for the apprenticeship year that will begin on September 1, 2003. The company views in-house training as a cornerstone in assuring a long-term supply of new talent and at the same time as a way of living up to its social responsibility of offering a vocational training perspective to high school graduates.

QSC workforce declines moderately

The QSC workforce declined moderately during the second quarter of 2003. As of June 30, 2003, the company employed 392 people (March 31, 2003: 415 people). 46 percent of the total workforce are active in such customer-near fields as sales, marketing and service, while 37 percent are working in the technical departments.

Effective July 1, 2003, QSC outsourced maintenance of its network infrastructure as well as its technical service to Pan Dacom Networking AG, one of the leading providers of services and systems integration in the networking market. 12 QSC employees moved to Pan Dacom, which in the future will be assuring smooth operation of QSC's infrastructure with a total of up to 100 service specialists.

Risk management enjoys top priority // QSC continuously reviews internal and external factors that could be detrimental to the implementation of its own business model and monitors the way these factors are developing in an enterprise-wide risk management system. The latest forecasts for Germany's economic development are further reducing the risk that a sustained recession might prevent QSC from reaching the breakeven point with its existing war chest. One major additional risk is aggressive pricing on the part of former monopolist Deutsche Telekom. In July 2003, QSC was pleased to note the decision by the German regulator regarding the improper structuring of resale proposals by Deutsche Telekom.

As a result of these and other risks as well as incorrect assumptions, actual future results could vary materially from the company's expectations. All statements contained in these consolidated financial statements and management report 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.

Cash flow breakeven to be reached sooner than originally planned // The percentage of total revenues accounted for by high-margin services for business and project customers will continue to grow strongly in the quarters to come. During the current fiscal year, QSC has already succeeded in winning numerous new customers, especially in the project business. It will take several months to implement larger VPN solutions in distributed locations and incorporate customer-specific requirements. The successful implementation of these project-orders will begin to translate into additional revenues in the second half of 2003.

QSC is responding to the growing percentage of complex project business by expanding its software-supported and quality managements systems, allowing small teams to steer both internal and external processes such as leased line management. The company is thus able to manage growing order volumes with a constant number of employees.

Positive trend of business development enables forecasts to be revised upward

The successful business customer segment, in particular, prompted QSC in mid August to raise the full year guidance it had announced in February 2003. The company is now forecasting annual revenues of over EUR 115 million, as opposed to its previous guidance of EUR 105 to 115 million. Current planning now calls for an annual EBITDA loss of better than EUR -25 million; up until now, QSC had anticipated an EBITDA loss of between EUR -25 and -30 million for the full year 2003. Given the steady reduction in cash burn, QSC expects to reach the cash flow breakeven point ahead of schedule, during the first half of 2004; previous guidance had indicated that the company would reach this breakeven point sometime during the course of 2004. QSC continues to plan on reaching the EBITDA breakeven point during the course of the fourth quarter of 2003.

STATEMENTS OF OPERATIONS

Consolidated Statements of Operations (unaudited)
(EUR amounts in thousands (TEUR), except for per share amounts)

	for the three months ended June 30,		for the six months ended June 30,	
	2003	2002	2003	2002
	in TEUR	in TEUR	in TEUR	in TEUR
Net revenues	**28,262**	**11,968**	**55,828**	**21,523**
Cost of revenues	26,673	14,297	53,770	31,308
Gross profit (loss)	**1,589**	**(2,329)**	**2,058**	**(9,785)**
Selling and marketing expenses	5,105	8,171	11,132	14,183
General and administrative expenses	3,383	4,110	7,575	6,625
Research and development expenses	252	245	547	587
Depreciation and amortization (including TEUR 3,211 in non-cash compensation in the six months ended June 30, 2003; six months ended June 30, 2002: TEUR 3,577)	8,487	9,152	18,418	17,233
Operating loss	**(15,638)**	**(24,007)**	**(35,614)**	**(48,413)**
Other income (expenses)				
Interest income	444	728	1,439	1,944
Interest expenses	(3)	(10)	(5)	(100)
Share of post acquisition losses of equity method investees	-	(485)	-	(861)
Other non-operating income (loss)	13	-	193	(127)
Net loss before income taxes	**(15,184)**	**(23,774)**	**(33,987)**	**(47,557)**
Income taxes	-	-	-	-
Net loss	**(15,184)**	**(23,774)**	**(33,987)**	**(47,557)**
Net loss per common share (basic and diluted)	(0.15)	(0.24)	(0.34)	(0.47)
Weighted average shares outstanding (basic and diluted)	101,137,947	101,134,647	101,137,947	101,134,647

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

BALANCE SHEETS

Consolidated Balance Sheets (unaudited)
(EUR amounts in thousands (TEUR))

	as of June 30, 2003 in TEUR	as of Dec. 31, 2002 in TEUR
ASSETS		
Current assets		
Cash and cash equivalents	38,480	43,095
Marketable securities	29,617	44,526
Trade accounts receivable, net	19,231	16,948
Trade accounts receivable due from related parties	9	7
Unbilled receivables	137	239
Other receivables	3,497	9,476
Prepayments and other current assets	4,458	4,410
Total current assets	**95,429**	**118,701**
Non-current assets		
Investment in equity method investees	**301**	**301**
Other non-current assets	**422**	**460**
Plant and equipment, net		
Networking equipment and plant	49,830	61,463
Operational and office equipment	6,838	6,837
Total plant and equipment, net	**56,668**	**68,300**
Intangible assets, net		
Licenses	1,000	2,004
Software	2,045	2,420
Others	4	5
Total intangible assets, net	**3,049**	**4,429**
Goodwill	**2,393**	**2,393**
Total non-current assets	**62,833**	**75,883**
Total assets	**158,262**	**194,584**

	as of June 30, 2003 in TEUR	as of Dec. 31, 2002 in TEUR
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Short-term debt and current portion of long-term debt	188	-
Trade accounts payable	22,248	25,917
Trade accounts payable due to related parties	389	504
Accrued liabilities	11,979	17,871
Deferred revenues	1,426	2,028
Other current liabilities	7,054	2,549
Total current liabilities	**43,284**	**48,869**
Non-current liabilities		
Convertible bonds	60	50
Accrued pensions	334	321
Other non-current liabilities	-	90
Total non-current liabilities	**394**	**461**
Shareholders' Equity		
Common stock	105,012	105,009
Treasury stock	(266)	(266)
Additional paid-in capital	473,362	473,442
Deferred compensation	(1,767)	(5,058)
Accumulated other comprehensive income	103	-
Receivables due from shareholders	(1)	(1)
Accumulated deficit	(461,859)	(427,872)
Total Shareholders' Equity	**114,584**	**145,254**
Total liabilities and Shareholders' Equity	**158,262**	**194,584**

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

STATEMENTS OF CASH FLOWS

Consolidated Statements of Cash Flows (unaudited)
(EUR amounts in thousands (TEUR))

	for the six months ended June 30, 2003 in TEUR	2002 in TEUR
Cash flow from operating activities		
Net loss	**(33,987)**	**(47,557)**
Adjustments to reconcile net loss to cash used in operating activities		
Non-cash compensation charge	3,211	3,577
Depreciation and amortization	15,207	13,656
Loss/(Gain) on sale of equipment	1,074	(71)
Share of post acquisition losses of equity method investees	-	861
Non-cash interest expense	-	82
Change in operating activities		
Decrease/(Increase) in trade accounts receivable, net	(2,283)	2,220
Decrease/(Increase) in trade accounts receivable due to related parties	(2)	228
Decrease in unbilled receivables	102	7,052
Decrease in other receivables	5,979	3,577
Increase in prepayments and other current assets	(48)	(2,968)
Decrease in other non-current assets	38	13
Decrease in trade accounts payable	(3,784)	(11,957)
Decrease in accrued liabilities	(5,892)	(767)
Increase/(Decrease) in deferred revenues	(602)	1,783
Increase in other current liabilities	4,505	206
Increase in accrued pensions	13	16
Net cash used in operating activities	**(16,469)**	**(30,049)**

	for the six months ended June 30, 2003 in TEUR	2002 in TEUR
Cash flow from investing activities		
Change in marketable securities	14,909	(62,416)
Available-for-sale securities (unrealized gain)	103	-
Acquisition of business, net of cash acquired	-	(1,001)
Purchases of intangible assets	(168)	(222)
Purchases of plant and equipment	(3,898)	(4,698)
Proceeds from sale of equipment	797	229
Net cash used in investing activities	**11,743**	**(68,108)**
Cash flow from financing activities		
Raise/(Repayment) of short-term debt	98	(330)
Issuance of convertible bonds	10	12
Proceeds from issuance of common stock	3	-
Net cash (used in) provided by financing activities	**111**	**(318)**
Net decrease in cash and cash equivalents	**(4,615)**	**(98,475)**
Cash and cash equivalents at beginning of the year	43,095	153,776
Cash and cash equivalents at end of the period	**38,480**	**55,301**
Supplemental disclosures of cash flow information		
Cash paid during the period for		
Interest expenses	5	18

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

STATEMENTS OF EQUITY

Consolidated Statements of Shareholders' Equity from January 1, 2002 to June 30, 2003 (unaudited)
(EUR amounts in thousands (TEUR), except for per share amounts)

Balance at January 1, 2002
Reissue of treasury stock (January 1, 2002)
Convertible bonds forfeited due to termination of employment (January 1, 2002)
Reissue of treasury stock (April 1, 2002)
Convertible bonds forfeited due to termination of employment (April 1, 2002)
Convertible bonds forfeited due to termination of employment (October 1, 2002)
Amount amortized during the period
Net loss
Balance at December 31, 2002
Net loss
Unrealized holding gains on available-for-sale securities
Comprehensive income
Convertible bonds forfeited due to termination of employment (January 1, 2003)
Convertible bonds forfeited due to termination of employment (April 1, 2003)
Issuance of common stock in connection with the conversion of convertible bonds (June 30, 2003)
Amount amortized during the period
Balance at June 30, 2003

Ordinary Shares		Treasury Shares		Additional Paid-In Capital	Deferred Compen-sation Account	Compre-hensive Income	Accumul. Other Compre-hensive Income	Receivab. Due from Share-holders	Accumu-lated Deficit	Total Share-holders' Equity
Shares	Amount TEUR	Shares	Amount TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR
105,008,714	**105,009**	**1,125,473**	**(3,312)**	**473,480**	**(12,086)**		**-**	**(1)**	**(323,124)**	**239,966**
		(575,000)	2,869						(2,127)	742
				(45)	45					-
		(191,726)	177	76						253
				(46)	46					-
				(23)	23					-
					6,914					6,914
									(102,621)	(102,621)
105,008,714	**105,009**	**358,747**	**(266)**	**473,442**	**(5,058)**		**-**	**(1)**	**(427,872)**	**145,254**
						(33,987)			(33,987)	(33,987)
						103	103			103
						(33,884)				-
				(69)	69					-
				(11)	11					-
3,300	3									3
					3,211					3,211
105,012,014	**105,012**	**358,747**	**(266)**	**473,362**	**(1,767)**		**103**	**(1)**	**(461,859)**	**114,584**

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

QSC AG

Notes to condensed consolidated financial statements (unaudited)
(EUR amounts in thousands (TEUR), except for per share amounts)

1. Organization and basis of presentation

a) **Organization** // QSC offers its business and residential customers DSL-based (Digital Subscriber Line) broadband "always-on" connections to the Internet, with up and down-stream data transfer rates of up to 2.3 Mbit/s and voice telephony services. DSL-technology makes efficient use of the last mile on the basis of unbundled network access, thus multiplying data traffic speeds compared with standard subscriber connections. The QSC broadband network covers the 40 largest cities in Germany and reaches more than a quarter of the entire population. QSC serves the end-user market selling its products and services either direct or through retail and distribution partners. QSC also provides some of its services through sales partners acting as resellers.

b) **Basis of Presentation** // The interim consolidated financial statements of QSC are unaudited and have been prepared in accordance with generally accepted accounting principles in the United States ("US GAAP"). Certain information and footnote disclosures normally included in financial statements prepared in accordance with US GAAP have been condensed or omitted. In the opinion of management, the financial statements reflect all adjustments which are necessary to present fairly the financial position, results of operations and cash flows for the interim periods. The financial statements should be read in conjunction with the audited consolidated financial statements as of December 31, 2002 and 2001. The results for the six month period ended June 30, 2003, are not necessarily indicative of the results that may be expected for the year ending December 31, 2003.
All amounts except per share amounts are in thousands of EUR (TEUR).

c) **Principles of Consolidation** // The consolidated financial statements include the accounts of QSC and its subsidiaries. All significant inter-company 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% and not more than 50%.

2. Significant accounting policies

a) **Recently issued statements of financial accounting standards** ⁄⁄ Effective January 1, 2002, the Company adopted 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, and SFAS 142, with respect to the impairment. These statements supersede SFAS 121, "Accounting for the Impairment of Long-Lived Assets to be Disposed Of". The adoption of these standards did not have a material impact on its consolidated financial positions or results of operations.
The Company reviews the carrying value of its long-lived assets, including fixed assets, investments, goodwill, 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, is assessed by a comparison of the carrying amount of the asset (or the group of assets, including the asset in question, that represents the lowest level of separately-identifiable cash flows) 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. Fair value is determined by discounting the cash flows expected to be generated by the asset, when the quoted market prices are not available for the long-lived assets. No adjustments were required to the carrying value of long-lived assets for the period from January 1 until June 30, 2003.
On January 1, 2002, the Company adopted SFAS 142, which prohibits the amortization of goodwill and indefinite life intangible assets. Instead, goodwill and indefinite life intangible assets will be tested for impairment at least annually and on an interim basis when an event occurs or circumstances change between annual tests that would more-likely-than-not result in an impairment. Under SFAS 142, goodwill is assessed for impairment by using the fair value based method. The Company determines fair value by utilizing discounted cash flows. The fair value test required by SFAS 142 for goodwill and indefinite lived intangible assets includes a two-step approach. Under the first step, companies must compare the fair value of a "reporting unit" to its carrying value. A reporting unit is the level at which goodwill impairment is measured and it is defined as an operating segment or one level below it if certain conditions are met. If the fair

value of the reporting unit is less than its carrying value, goodwill is impaired and companies must proceed with step two. Under step two, the amount of goodwill impairment is measured by the amount that the reporting unit's goodwill carrying value exceeds the "implied" fair value of goodwill. The implied fair value of goodwill can only be determined by deducting the fair value of all tangible and intangible net assets (including unrecognised intangible assets) of the reporting unit from the fair value of the reporting unit (as determined in step 1). In this step, companies must allocate the fair value of the reporting unit to all of the reporting unit's assets and liabilities (a hypothetical purchase price allocation).

SFAS 142 requires companies to perform the impairment test at least annually and also upon adoption. Any impairment loss resulting from the adoption of SFAS 142 is treated as a change in accounting principle. QSC adopted SFAS 142 as of January 1, 2002, for goodwill and intangible assets arising from business combinations completed prior to July 1, 2001, and we have applied SFAS 142 for goodwill and indefinite-lived intangible assets arising from business combinations completed after June 30, 2001. Upon adoption of SFAS 142, for US GAAP purposes, we stopped amortizing goodwill. The Company did not have any impairment loss as a result of adopting SFAS 142 and as a result of performing the required annual impairment test which the Company has elected to perform on October 31, 2002. As SFAS 142 was adopted by the Company on January 1, 2002, there are no reconciling differences for the six months ended June 30, 2003 and 2002.

In December 2002, the Financial Accounting Standards Board ("FASB") issued SFAS 148 "Accounting for Stock-Based Compensation – Transition and Disclosure". This Statement provides additional disclosure requirements for stock-based compensation plans and alternative methods of transition for companies that elect to change from Accounting Principles Board ("APB") 25 "Accounting for Stocks Issued to Employees" to SFAS 123 "Accounting for Stock-Based Compensation" for stock-based compensation. Under SFAS 148 a company electing to adopt SFAS 123 prospectively for new stock-based compensation awards, while continuing to account for existing stock-based compensation awards under APB 25. SFAS 148 is effective for fiscal years ending after December 15, 2002. Beginning January 1, 2003, the Company has adopted a change in accounting principle for stock-based compensation. Accordingly, under the provisions of SFAS 148, QSC will report this change in accounting principle using the prospective method, whereby, stock-based compensation awards granted until December 31, 2002 are accounted for under the provisions of APB 25 and stock-based compensation awards granted after January 1, 2003, are accounted for under SFAS 123.

b) Use of estimates in the preparation of the financial statements // The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts and disclosure of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Although these estimates are based on our knowledge of current events and actions we may undertake in the future, actual results may ultimately differ from estimates.

c) Cash and cash equivalents // Cash and cash equivalents consist of highly liquid investments in bank balances and cash on hand.

d) Marketable securities // In accordance with SFAS 115, "Accounting for Certain Investments in Debt and Equity Securities", and based on the Company's intentions regarding these instruments, the Company has classified TEUR 26,525 marketable debt securities as held-to-maturity and has accounted for these investments at amortized cost. Marketable debt securitites of TEUR 3,092 has classified as available-for-sale and accounted at record date cost.

e) Loss per share // Under SFAS 128 "Earnings per Share", loss per share is computed by dividing loss applicable to common stockholders by the weighted average number of shares of QSC's common stock outstanding exclusive of shares subject to repurchase if specified conditions are not met. 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. The loss per share calculation does not include 3,877,367 shares issued to employees through the exercise of convertible bonds, which are subject to forfeiture, nor does it include the effect of the possible conversion of convertible bonds into 6,077,441 shares of QSC common stock.
For the six months ended June 30, 2003 and 2002, the dilutive effect of options was not considered because QSC recorded net losses and the impact of their assumed exercise would be anti-dilutive.

f) **Goodwill** // Goodwill consists of the excess purchase price over the fair value of the identifiable net assets acquired in acquisitions. With the adoption of SFAS 142 as of January 1, 2002, goodwill is no longer amortized, but tested at least annually for impairment.

g) **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 operating in one segment: fixed-wire integrated telecommunication services in Germany.

h) **Comprehensive income** // SFAS 130, "Reporting Comprehensive Income" requires companies to separately report components of comprehensive income. Comprehensive income includes net loss and other comprehensive income. Comprehensive income and other comprehensive income are shown in the statements of equity.

3. Acquisitions and Investments

a) **Acquisitions** // On December 13, 2002, QSC acquired 100% 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 ideally. Ventelo will further enhance QSC's ability to offer integrated telecommunication solutions for all business customer segments. Total acquisition cost for Ventelo was TEUR 11,515, including direct acquisition costs of TEUR 90, and is subject to certain purchase price adjustments which could result in reductions of purchase price up to TEUR 5,200. The amount of TEUR 5,200 is withheld as restricted cash on an escrow account. On April 1, 2002, Ventelo was outsourced from its former parent company Ventelo Deutschland GmbH due §§ 159 et seqq. "Umwandlungsgesetz". Due to § 133 "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 exceeded the purchase price resulting in a negative goodwill of TEUR 132 and reducing the acquired assets, on a pro rata basis, by this amount. The results of operations of Ventelo have been included in the consolidated financial statements since December 13, 2002.

b) Investments ⁄⁄ On April 26, 2001, the shareholders of ALCHEMIA S.p.A., Milan, Italy, one of QSC's strategic investments made in 2000, resolved to change the company's name to Netchemya S.p.A. ("Netchemya"). TISCALI S.p.A., a shareholder of Netchemya, made a strategic decision in the third quarter of 2002 to discontinue the resale of Netchemya's network based services and not to commit any further funding to Netchemya. This had a major adverse impact on Netchemya's future business activities and the shareholders took first measures to discontinue operations by way of voluntary liquidation. QSC has therefore written off its remaining investment in Netchemya of TEUR 4,136 in 2002.
On January 28, 2002, the Company acquired a 49% interest in Grell Beratungs GmbH, Cologne ("Grell"). Purchase price consideration consisted of 575,000 ordinary shares of QSC stock valued at EUR 1.29 per share which approximates the market price of the Company's stock when the acquisition was agreed to and announced. QSC uses the equity method for its investment in Grell. As a result of recent developments of this business, during the fourth quarter of 2002, QSC has recorded an impairment charge of TEUR 433 in 2002 relating to Grell to reflect its estimated fair market value of TEUR 301.

4. Employee equity incentive program

QSC accounts for its stock option plans under provisions of APB 25 for options granted to employees under stock option plans. Under APB 25, compensation expense is recognized, based on the amount by which the fair value of the underlying common stock exceeds the exercise price of the stock options at the measurement date. In the case of SOP2000A, the exercise price of 483,169 convertible bonds was reduced in November 2000. The 483,169 convertible bonds are therefore accounted for using variable plan accounting. QSC was not required to record any compensation expense in connection with the 483,169 convertible bonds subject to variable plan accounting as these bonds have a weighted average exercise price of EUR 4.23 and QSC's stock closed at EUR 1.69 on June 30, 2003, at Frankfurt Prime Standard stock exchange. All other convertible bonds and shares exercised under SOP2000A have a measurement date equal to the grant date. The same apply to the stock option plans SOP2001 and SOP2002. As of June 30, 2003, QSC had deferred compensation totalling TEUR 1,767. This amount is yet to be amortized as a charge to operations until the lock-up period will be ended. In the first six months 2003, QSC amortized TEUR 3,211 and TEUR 3,577 in the equivalent period of 2002.

5. Debt

Other non-current liabilities of TEUR 394 include convertible bonds of our employee equity incentive program and an accrual for existing pension obligations.

6. Shares and convertible bonds Management Board and Supervisory Board

Shares and conversion rights of Members of the Management Board:

	30/06/2003		30/06/2002	
	Shares	Conversion rights	Shares	Conversion rights
Dr. Bernd Schlobohm	13,818,372	-	13,818,372	-
Gerd Eickers	13,841,100	9,130	13,841,100	-
Markus Metyas	2,307	1,559,116	2,307	1,059,116
Bernd Puschendorf	-	1,000,000	-	1,000,000

Shares and conversion rights of Members of the Supervisory Board:

	30/06/2003		30/06/2002	
	Shares	Conversion rights	Shares	Conversion rights
John C. Baker	-	19,130	-	19,130
Herbert Brenke	187,820	9,130	187,820	9,130
Ashley Leeds	9,130	10,000	9,130	-
David Ruberg	4,563	19,130	4,563	9,130
Claus Wecker	83,025	-	83,025	-

CALENDAR

Quarterly Report III/2003
November 25, 2003

Conferences/Events
September 1, 2003
1st Investment Meeting, Frankfurt

September 11, 2003
International Engineering Consortium:
Broadband World Forum, London

October 21-22, 2003
Euroforum Conference:
TKG Amendment 2003, Cologne

November 26-27, 2003
German Equity Forum, Frankfurt

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