ANNUAL REPORT 2000

QSC

the power behind

QSC AT A GLANCE

All amounts in million EUR, except per share amounts	01/01/ to 31/12/1999	01/01/ to 31/12/2000
Revenues	1.6	5.0
Pre-tax loss	-7.5	-89.2
Loss per Share	-4.2	-1.2
Capital Expenditure	7.2	85.8
Liquidity	137.2	294.8
Equity	130.1	339.1
Cities	1	44
Metropolitan Service Centers	1	44
Central Offices	17	862
DSL-Lines	–	9,090
Employees	45	194

THE INTERNET IS CHANGING THE WORLD

BROADBAND WILL CHANGE THE INTERNET

QSC IS THE BROADBAND SOLUTION

CONTENT

LETTER TO THE SHAREHOLDERS

Dear shareholders,

QSC looks back on a successful year 2000. Within less than a year, we managed to establish our DSL network infrastructure in the 40 largest cities in Germany. We are thus in a position to serve up to 20 million potential users. Going public in April 2000 was without doubt a major event of the year, because without our IPO, we would not have been able to expand at this pace. I would like to use this first Annual Report as an opportunity to describe to you the goals your company is pursuing.

Guided by the company's mission – "The Internet is changing the world – Broadband is changing the Internet – QSC is broadband" – we have made QSC a strong and efficient provider of broadband networking. QSC stands for quality, service and communications, and is based upon a young, dynamic and customer-centered corporate culture.

Unlike some competitors, our management team has many years of experience in the telecommunications industry and in successfully competing against Deutsche Telekom. All our employees have extensive know-how from various fields of telecommunications and information technology. They are therefore the safeguards not only for innovative business ideas, but also for the quality, efficiency and performance of our products and services.

Every single employee was involved in an outstanding team effort that resulted in reaching the target for 2000 – building our network infrastructure. Providing virtually 100-percent coverage in all the major cities of Germany, we now have acquired a decisive competitive lead that we will continue to build on in the future.

WE STRIVE TO CONVINCE THE FINANCIAL COMMUNITY OF QSC'S MERITS BY DELIVERING NEW PRODUCTS, IMPROVING FINANCIAL PERFORMANCE AND A HIGH QUALITY INVESTOR RELATIONS EFFORT.

During the current business year, our efforts will be concentrated on acquiring new customers. Products and services for private customers will be added to those already offered to corporate customers. In addition to fast Internet access, we will also provide a full range of Internet services as a service bundle, as well as other broadband applications. This new service represents an important step forward in the current year. The creation and expansion of our internet services will allow us to access the end-user market to provide customers directly with services such as domain reservation and the provision of e-mail accounts. By integrating voice-based services (telephony) into our wide-ranging package of broadband services, we are moving ourselves one level higher in the value chain. Through close collaboration with our partners, we will not only be marketing our own products but also adding innovations in the broadband field to the QSC network.

Our objective is that every QSC customer receives high-speed access to the entire fascinating world of the Internet from the office or home. Slow connections over the so called 'last mile' must no longer be a factor preventing video-conferencing, downloading films from the Internet or simultaneous project work by people at different locations. As one of the first companies operating in this field in Germany, QSC offers convenient, high-speed access at a high quality standard. Our aim is to increase our competitive lead during the years ahead.

Last year, unfortunately, we did not succeed in convincing the capital markets of our vision. The generally bearish sentiment that has afflicted the telecommunications sector in particular, was certainly a factor that made our investor relations work more difficult. You may rest assured that we will do everything in our power in 2001 to convince the financial markets of QSC's merits, in the form of new products, improving financial performance and intensified communication efforts.

Finally, I would like to thank you, the shareholders, for the trust and confidence you have shown in the company. I would also like to express my praise and recognition to the entire QSC team for their untiring efforts.

Yours sincerely,

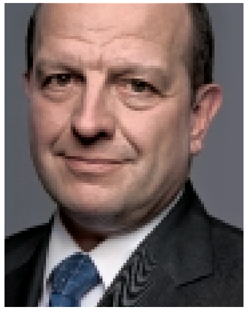
Bernd Schlobohm

MANAGEMENT BOARD

Bernd Schlobohm

Co-founder and Chief Executive Officer since 1999. The holder of a doctorate in engineering is responsible for strategy and marketing.

Gerd Eickers



Co-founder and Chief Operating Officer since November 2000. The experienced telecommunication specialist manages technology and sales.

Markus Metyas

Chief Financial Officer since April 2000. The former investment banker is in charge of finance, personnel and legal.

SUPERVISORY BOARD

John C. Baker

Chairman of the Supervisory Board

The General Partner of the US Fund Baker Capital Communications represents the largest shareholder of QSC.

Herbert Brenke

Deputy Chairman of the Supervisory Board

The independent consultant in the telecommunications industry built up the mobile telecommunication provider E-Plus and is chairman of the Supervisory Board of telegate AG.

Manjit Dale

Managing Partner of Deutsche Bank Capital Partners, London. This institution invested in QSC at an early stage.

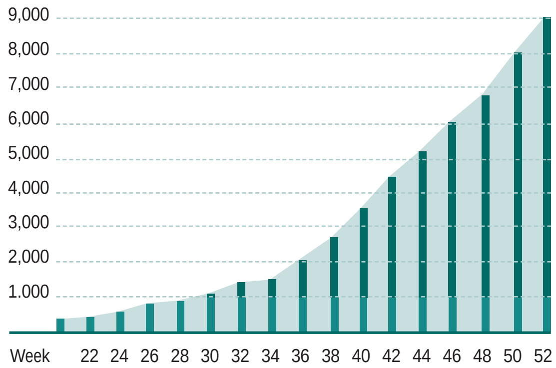
Ashley Leeds

The experienced investment banker has held a senior management position at Baker Communications for many years.

David Ruberg

The trained mathematician and computer scientist is Chief Executive Officer of the US company Intermedia Communications.

Line Sales as at December 31, 2000



The network – from construction to high utilisation

After the successful roll out of its broadband infrastructure in the 40 largest cities in Germany, QSC has attained its first objective – namely to establish a network with nationwide coverage. The company has installed its technology in more than 800 co-location rooms so far, thereby reaching 20 million potential users. More than 9000 lines were sold by December 31, 2000 compared to 3200 lines by September 30, 2000 – this increase exemplifies the dynamic growth currently achieved by the company. A total of 89 sales partnerships played a major role in attaining this position.

With EUR 85.8 million invested in tangible assets during the year 2000, the most investment intensive phase of the network roll-out has been finalised. Revenues during the past business year reached almost EUR 5.0 million. Pre-tax losses amounted to EUR 89.2 million, an improvement on the planned figure. At the end of the reporting period, QSC had cash and cash equivalents totaling EUR 294.8 million and no debt.

Strong cash flow position thanks to IPO

On April 19, 2000 QSC was quoted for the first time ever on the Neuer Markt and Nasdaq – a milestone in the company's history. The IPO generated the cash resources that were needed by the company to build its nationwide network infrastructure. The offering proceeds of EUR 283.2 million allow to invest – in accordance with the business plan – without any further increases in share capital.

On the whole, 2000 was a poor year in the equity markets and the share price performance was rather dissatisfying as a result. Nevertheless, going public was the right step to take in order to ensure the financing of the necessary investments.

Core activities: creating the network

Broadband technology enables data to be transmitted much more rapidly than is possible with conventional ISDN technology. With QSC's SDSL-technology, users can download and upload data to and from the Internet at speeds of up to 2.3 megabits per second – and with the same transmission capacity in both directions.

ADVANTAGE OF QSC'S TECHNOLOGY: HIGH DATA TRANSFER SPEEDS, LOW COSTS, SIMPLE IMPLEMENTATION.

To implement this process, QSC rents space in the central offices (co-location rooms) of Deutsche Telekom where the DSL equipment is then installed. Unused twin core copper cables that are already in place are upgraded with the required technology by QSC.

EVEN AFTER COMPLETING THE MOST INTENSIVE PHASE OF NETWORK ROLLOUT, QSC REPORTS CASH AND CASH EQUIVALENTS OF EUR 294.8 MILLION.

The final step is to install a new telephone socket in the end user's premises.

High-speed fibre optic cables lead from the co-location rooms to QSC's own network nodes, the Metropolitan Service Centers. Lines are bundled here and connected at low cost to the various Internet and telecommunications service providers.

QSC is far ahead of competitors

By building its network infrastructure so quickly, QSC acquired a crucial competitive advantage. The company is present in the 40 largest cities in Germany, compared to alternative DSL providers such as HighwayOne or Riodata which – according to our estimates – have fewer than 20 points of presence in commercial operation. The only competitor that currently has a larger DSL network is Deutsche Telekom.

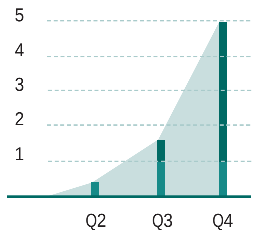
In cities connected to its network, QSC is able to provide high-speed access to the Internet in virtually every district and in less time than even the main competitor, Deutsche Telekom. 95% of QSC's customers are connected within 20 working days.

Compared to Deutsche Telekom, QSC has yet another, decisive advantage: Deutsche Telekom's T-DSL product relies on ADSL-technology, which means that users are able to download data from the Internet at up to 768 kilobits per second, but upload at only 128 kilobits per second. This product caters to the typical private customer, and differs substantially in quality and performance from the QSC products, which are primarily geared to business customers. Criteria such as guaranteed bandwidth, high reliability, multi-user environments and permanent network monitoring play a much more important role for this latter group of customers. Corporate customers receive a static IP-address, which is the prerequisite for so-called Virtual Private Networks or other e-commerce applications such as online shops.

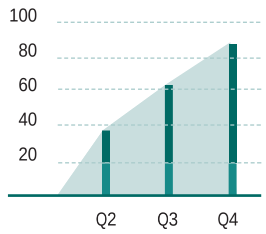
Positives: consistent cost management and strong cash flow

By going public, QSC acquired the capital resources necessary to invest in the network. As at December 31, 2000, cash and cash equivalents amounted to EUR 294.8 million. Active cost management contributes to our ability to execute our business plan without planning additional capital increases. This is an outstanding situation to be in at a time when the first bankruptcies are being registered by Neuer Markt companies and other companies, including competitors, are seeking follow-up financing.

Revenues (in Mio. EUR accumulated)



Capital Expenditure (in Mio. EUR accumulated)



QSC is a step ahead of its competitors internationally as well. American DSL providers have cash-flow problems that originate from their core business operations, mainly because of the percentage of customers who do not honor their payment obligations. QSC has taken appropriate receivables management steps to minimise its bad debt risk. Before concluding new partnership deals, QSC checks the creditworthiness of its prospective partners.

89 DISTRIBUTION PARTNERS EMPLOYING 1000 SALES PEOPLE ENSURE THE SALE OF QSC'S SERVICES IN THE 40 LARGEST GERMAN CITIES.

Tight monitoring of outstanding receivables creates transparency in this regard. If applicable, the company uses bank guarantees and bad debt insurance policies to protect it against defaulted payments.

During the 2000 business year, the company also began to implement the risk management system now required by law. This system includes extensive reporting as well as documentation of actions taken, and is complemented by a detailed controlling system.

Strong sales partners

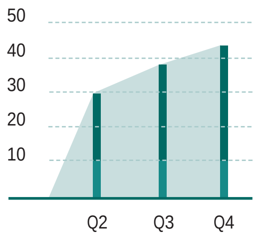
During the past business year, QSC succeeded in signing up no less than 89 co-operation and sales partners who handle the consumer marketing side of operations. Internet and telecommunications service providers dispose of enormous customer potential to the benefit of QSC. Partners include, among other big players, Cable & Wireless, Level 3, Mediaways, Talkline, UUNET and Worldcom.

The year 2000 was dominated by essential technical preparations for connecting these partner networks to the QSC infrastructure. Only when this work has been completed sales partners are able to start marketing and distributing the DSL-based products. This work also explains why QSC revenues did not begin to show any substantial rise until the end of the year, even though many co-operation agreements had already been signed earlier in the year.

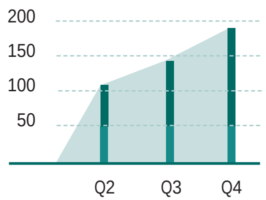
Basis for success – a good team

Fast corporate growth and consistent implementation of business strategy require a strong management team and a skilled workforce. The number of employees rose during the year from 45 to 194. No fewer than 72 employees are deployed in the technical division to set up and manage the network itself.

Cities



Employees



In February 2000, Markus Metyas was appointed Chief Financial Officer. He has many years of experience in investment banking, and in the financing of telecommunication companies make him the ideal finance expert for the company. In November 2000, Gerd Eickers was appointed to the Board of Management as Chief Operating Officer. As a co-founder of QSC, Gerd Eickers had previously been the Vice-Chairman of the Supervisory Board. Torsten C. Scheuermann left the Board of Management and the company in November 2000.

Outlook

During the last business year, efforts were concentrated on rapidly creating our network infrastructure at attractive locations in Germany. In 2001, there are not many attractive sites left for expansion. Based on individual location analyses, co-location rooms for DSL upgrading will only be applied in those areas characterised by a high user potential. This means that investment in network expansion will be much lower in the future than has been the case up to now. From April 2001 onward, QSC will be operating in the market as an Internet service provider, thus positioning itself one level higher in the value chain. QSC will now be a direct provider of services such as domain reservation, provision of e-mail accounts and web space, as well as security standards using firewalls.

QSC will be linking its Metropolitan Service Centers (MSCs) with its own backbone in 2001. Once this has been accomplished, sales partners will no longer have to connect to each MSC in order to provide their services. This will significantly reduce the amount of time needed for technical preparations prior to activation of a distribution partnership. Applications such as Video-on-Demand will then be stored at specific sites, while still being available for use throughout the country. During the current business year, QSC will be launching an ADSL product for private customers.

All these activities are aimed at continuing our exponential sales growth in 2001 and to secure long-term earnings potential. As envisaged in the business plan, income will remain negative in 2001. This is due to further investment in the network and network optimization, to the establishment of the new service offering referred to above, and to investment in terminal equipment for customers. Generation of the first profits is expected by the company to occur during the 2003 business year.

IN 2001, QSC MOVES ONE STEP AHEAD IN THE VALUE CHAIN AND BECOMES INTERNET SERVICE PROVIDER ITSELF.

REPORT OF THE SUPERVISORY BOARD

THE SUPERVISORY BOARD HAS BEEN INFORMED ABOUT THE COURSE OF BUSINESS ON A REGULAR BASIS. IT APPROVED THE ANNUAL FINANCIAL STATEMENTS WITHOUT QUALIFICATIONS AND WOULD LIKE TO THANK THE MANAGEMENT BOARD AND ALL THE EMPLOYEES FOR THEIR WORK.

In accordance with legal requirements and the articles of incorporation, the Supervisory Board monitored and advised the Management Board in the financial year 2000.

The term of office of all Supervisory Board members came to an end at the close of the annual shareholders' meeting on March 11, 2000. Mr. Claus Wecker and Mr. James G. Cosgrove withdrew from the Supervisory Board on that date, and we would like to take this opportunity to express our gratitude for the work they performed. The other members of the Supervisory Board were re-elected; Mr. Manjit Dale and Mr. David Ruberg were appointed as new members of the Supervisory Board at the shareholders' meeting on March 11, 2000. Gerd Eickers resigned from his office as member of the Supervisory Board with effect from expiration of December 31, 2000 in order to take office on the Management Board.

Particularly at four meetings held on March 10, May 17, July 12 and November 16, 2000, as well as in three telephone conferences on January 30/31, April 16/17 and December 20, 2000, the Supervisory Board was informed in detail, in the form of reports by the Management Board, about the course of business, the company's economic situation and about all transactions of significance for the profitability and cash flow situation of the company.

By resolution of April 16/17, 2000, the Supervisory Board established an “Audit Committee” in conformity with NASDAQ-rules. After the company was exempted from the respective formal requirement, said Committee was dissolved by resolution of November 16, 2000, because the Supervisory Board is convinced that it can best discharge its monitoring responsibilities by acting as a whole.

The Supervisory Board discussed key aspects of the company's business policies and operations with the Management Board. Its approval was obtained for all measures for which such approval is required by law, the Articles of Incorporation or the rules of procedure of the Management Board.

In addition to current business development, planning and strategy as well as initial experience with measures of early identification and monitoring of risks, the focal points at the various meetings held during the past financial year were preparation of the initial public offering of the company's shares, the creation of the employees share ownership plan 2000A, the participations in the Netherlands and Italy, and the further development of reporting systems.

The annual financial statements of QS Communications AG pursuant to HGB (German Commercial Code) as at December 31, 2000 and the management report as well as the annual financial statements of QS Communications AG pursuant to US-GAAP, which were prepared according to the Rules and Regulations Neuer Markt, as at December 31, 2000 were presented to the Supervisory Board, examined and discussed with the auditors mandated by the Supervisory Board, namely Arthur Andersen Wirtschaftsprüfungsgesellschaft, Steuerberatungsgesellschaft mbH (a firm of chartered accountants and tax consultants), Eschborn/Frankfurt am Main, at the meeting on March 15, 2001. The HGB-annual financial statements of the company for the year 2000 were granted an unqualified auditor's certificate. The US-GAAP annual financial statements were also reviewed by Arthur Andersen and received an unqualified auditor's certificate, too.

Having conducted its own examination, the Supervisory Board has no objections against the annual financial statements of QS Communications AG for the 2000 financial year pursuant to HGB and to US-GAAP and the management report and concurs with the findings of the auditors.

At its meeting on March 15, 2001, the Supervisory Board approved the annual financial statements pursuant to US-GAAP and approved the annual financial statements pursuant to HGB, which have therefore been formally established.

The Supervisory Board would like to thank the Management Board and all employees of the company for their commitment and dedication, without which the company's successful development in the past financial year would not have been possible.

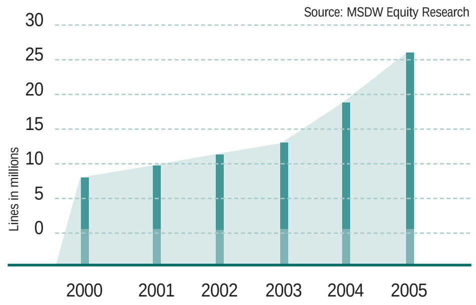
On behalf of the Supervisory Board

John C. Baker
Chairman of the Supervisory Board

KELLOGG (DEUTSCHLAND) GMBH

As the subsidiary of a globally operating food group, KELLOGG (DEUTSCHLAND) GMBH relies on the fastest technology for data transfer. In order to keep employees updated at any time and any place, the management decided to implement DSL by QSC. This enables the group to use the unbeatable logistic and economic advantages made available nowadays by the professionally used high-speed Internet. QSC provides a fast and reliable dispatch of data via the Internet and links the worldwide network in an optimized way with the company's network. As a result, data always leave the company when they are still brand-new and fresh similar to the products of the breakfast nutrition specialist.

Broadband Access Lines



The future of the Internet has begun

Collaborating on projects from different locations, downloading full-length films from the World Wide Web, or holding virtual shareholders' meetings – actually implementing these future ways of exploiting the Internet depends on one crucial factor – bandwidth. The applications just mentioned will remain a fantasy if, but only if, the prevailing transmission speeds for Internet access remain at 56 kilobits per second (conventional modem) or a maximum of 128 kilobits per second (with ISDN channel bundling).

QSC is one of the first companies to provide transmission speeds of up to 2,300 kilobits (equivalent to 2.3 megabits) per second to a broad clientele, making it possible for users to enjoy movies on their PCs or TV screens via data transmission lines. By providing this service, QSC is positioning itself at an early stage in one of the most promising telecommunications markets of the future: DSL (for "Digital Subscriber Line").

Rapid market growth

Frost & Sullivan, the market researchers, are not alone in thinking that the future of the Internet lies in broadband access. They estimate that the European market for DSL technology will grow at a fast clip until 2006 – at average rates in excess of 50% a year.

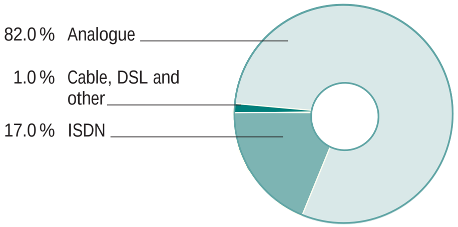
Two competing technologies dictate current market trends: SDSL which is used by QSC and ADSL which is distributed by Deutsche Telekom under the brand name T-DSL. QSC provides symmetric DSL (SDSL) with the various products it markets under the speedw@y-DSL brand. This technology enables equally high transmission speeds of up to 2.3 megabits per second for both uploading and downloading of data. With ADSL based T-DSL – the asymmetric version of DSL – data can be downloaded from the Internet at up to 768 kilobits per second, and uploaded at a speed of 128 kilobits per second. These products meet the requirements of residential customers. In the future, QSC expects to provide the residential market with a competitive product based on ADSL-technology.

How DSL excels

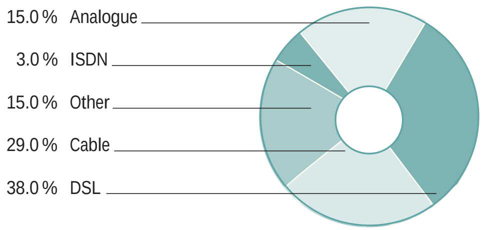
Many telecommunications companies have already constructed high-performance fibre optic networks spanning the world to link the most important cities with each other and the Internet. However, before final consumers can use these fast networks, they first have to establish a connection to them by bridging the so-called last mile. The most widespread technology used for accessing the Internet is ISDN. Every Internet user has discovered what it means when large volumes of data are downloaded by this means – waiting. DSL bridges the last mile at a much greater speed than ISDN and enables business and residential customers to surf the Internet without having to wait.

DURING THE NEXT YEAR WE EXPECT DSL TO ESTABLISH ITSELF AS THE LEADING INTERNET ACCESS TECHNOLOGY.

Access Lines by Technology 2000 (%)



Access Lines by Technology 2008 (%)



Little chances in Europe for alternative access technologies

Besides DSL, broadband access is also available on the European market via fibre optic, TV-cable and Wireless Local Loop. However, the barriers to market entry are considerable for all three alternatives.

Laying fibre optic cables is expensive. Even providers of this technology admit that the physical laying of new cables and the installation of the requisite technology consumes large sums of money. Smaller companies or residential customers cannot afford the user fee and are therefore not target users. Fibre optic access is an interesting proposition only for large companies that require extremely high transmission capacities.

TV-cable qualifies itself for data transfer only to a limited extent. The cable TV network is based on an infrastructure, where all end users share a limited transfer capacity. Guaranteed bandwidth becomes a quite difficult feature. Due to this fact, TV-cable is the most preferred broadband access technology for business customers – even in the US.

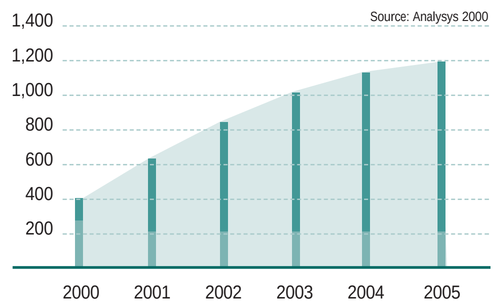
In addition, the former TV-cable net of Deutsche Telekom is not upgraded yet for interactivity and connects only a small part of end users. The coverage of the level four net – the equivalent to the last mile – is quite weak. The above mentioned unfavourable technical condition will hinder a widespread upgrade of the German TV-cable network. Competition in the market for residential customers is not expected before 2003.

Wireless Local Loop (WLL) bypasses the last mile using wireless technology. Before it can be used, it is necessary to install antennae at the user and base stations either on masts or high buildings from which the data are then forwarded. Depending on the number of users per base stations, transmission rates ranging from 2 to 10 megabits per second can be achieved. After receiving the licences in 1999 under the condition of providing broadband coverage on a widespread basis within 12 months, very few companies have met this condition. The proliferation of WLL has hardly been noticeable so far. In our opinion, WLL could be successful in areas where cable and DSL are not available.

DSL, by contrast, uses an infrastructure that is already in place – the telephone network. QSC's technology can be installed without difficulty and – given the relatively low user fees – is an attractive option for small companies and residential customers.

HAVING DSL IS WHAT MATTERS MOST: ONLY THIS TECHNOLOGY ENABLES COMPANIES TO IMPLEMENT AMBITIOUS WEB PROJECTS LIKE ASP SERVICES OR INTERACTIVE WEBSITES.

European SME's with interactive websites (in 000's)



QSC operates in a fascinating market segment

In delivering its fast Internet access, QSC has focused on the market segment comprising small and medium-sized enterprises (SMEs). Analysys, a market research company, predicts that the SME segment will demonstrate the strongest growth potential in the data communications field.

They base their prediction on the simple fact that large corporations have already invested huge amounts in e-business. Market participants with less financial clout are now compelled to catch up. Many companies are integrated into the supply chains of major corporations that already handle many of their business processes over the Internet.

Growing demand for broadband applications

Widespread availability of fast and inexpensive Internet access options stimulates the demand for and development of services and applications for which broadband technology is a must. One particular example is complex web hosting – outsourcing large volumes of data to third-party specialists – and additional services such as Video-on-Demand or Virtual Private Networks (VPN).

A classical application of web hosting is e-commerce. Customers order products online with ever-greater frequency and expect immediate order processing and delivery. This can only be done if all stock management activities are web-based. The same applies to billing and monitoring payments. With few exceptions, small companies are unable to install their own technology to handle these complex processes, and tend increasingly to outsource such applications to specialised web hosting providers.

Web hosting can involve much more than this, however. Application Service Providers (ASPs) supply the requisite information technology as a complete package – in many cases with greater cost efficiency because they can operate the computers around the clock. The only condition for users is that they have an always-on connection that is both fast and inexpensive.

Virtual Private Networks are now almost commonplace. VPNs enable all the employees of a company, including external offices, to be linked together within one and the same network. Such a network can only operate efficiently when users have high-speed access.

Thanks to the scalability of QSC products, end users can adapt the transmission capacities that best suit their needs. QSC's Network Operation Center ensures that orders are processed quickly. Fast construction of its DSL network means that QSC is now able to provide even the latest applications soon after release and in many parts of Germany.

A NETWORK FOR EVERYBODY

IN THE YEAR 2000 ALONE, QSC INVESTED EUR 85.8 MILLION TO UPGRADE EXISTING COPPER LINES FOR DSL SERVICES.

High-speed in the 40 largest cities

From Munich to Hamburg, from Aachen to Berlin – QSC's DSL technology is now available throughout the 40 largest cities in Germany. A total of EUR 85.8 million was invested by the company in the year 2000 to transform the last mile into a fast broadband connection.

The QSC network connects end users to the central offices of Deutsche Telekom. The network architecture has the same structure in every city: the core elements of the network are co-location rooms – the central offices of Deutsche Telekom – and Metropolitan Service Centers, QSC's proprietary sites where additional technology can be installed.

The central offices of Deutsche Telekom originally served no other purpose than to connect subscribers to the telephone network. Ever since the Internet assumed a key role in business and private communication, the need for transmission capacities has continuously increased, not only for voice but also for data communication. ISDN may recently have qualified as "state of the art", but the enormous speed at which the Internet has been growing has necessitated faster and more efficient connecting lines: the broadband technology. It is precisely high-speed connections of this kind that QSC supplies to its customers.

In order to offer an alternative over the last mile, QSC installs its technology in the central offices of Deutsche Telekom. The company applies to the national incumbent for the so-called co-location area, which is usually provided within 16 weeks of the official application. Installation of the technical equipment then begins. QSC upgrades existing copper lines belonging to Deutsche Telekom in order to carry DSL traffic. If the end user wants fast access to the Internet, all it needs to do is to install a new telephone socket.

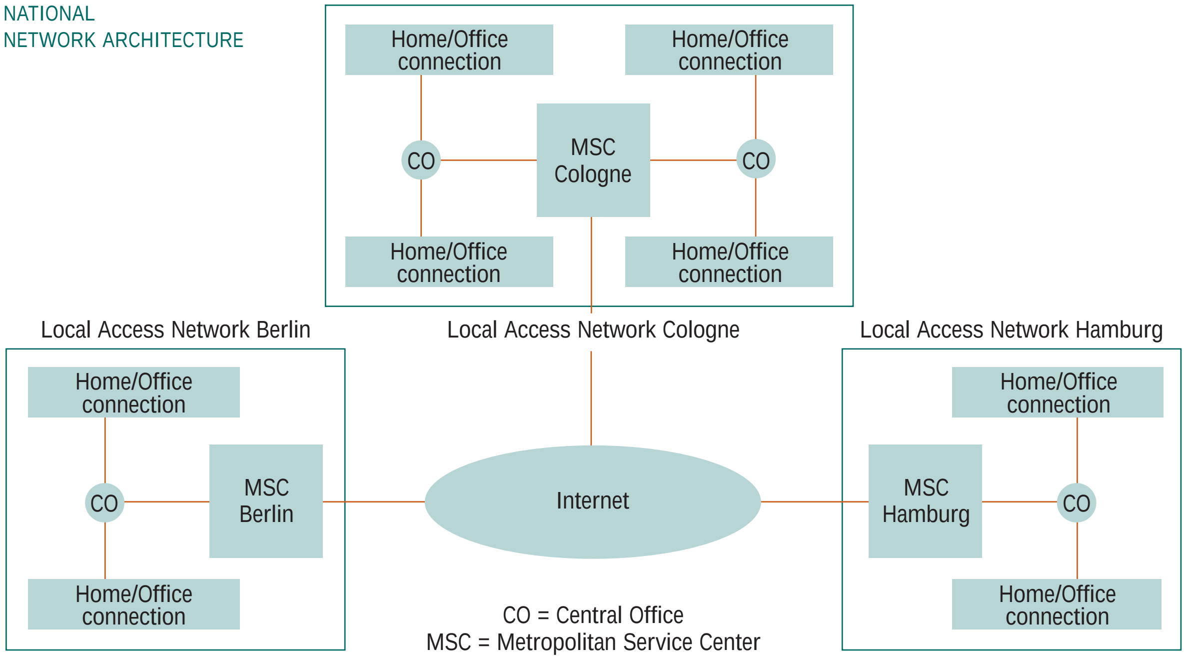
QSC ACCELERATES THE DATA TRANSFER SPEED BETWEEN THE CO-LOCATION OFFICE OF DEUTSCHE TELEKOM AND BUSINESS AND RESIDENTIAL TELEPHONE SUBSCRIBERS.

The heart of the network:
Metropolitan Service Centers

A high-performance fibre optic cable connects the co-location rooms at Deutsche Telekom to the Metropolitan Service Centers. The latter are set up and operated by QSC. From these centers, value-added services such as Video-on-Demand or web hosting are provided using a large number of servers. The technical equipment in each Metropolitan Service Center also enables separate customer lines to be bundled, so that they can then be routed to the various Internet service providers quickly and inexpensively, and in order to ensure fast connections to the Internet.

SOPHISTICATED NETWORK: QSC CONNECTS ITS CUSTOMERS VIA CENTRAL OFFICES OF DEUTSCHE TELEKOM TO ITS OWN NETWORK.

NATIONAL
NETWORK ARCHITECTURE



CO = Central Office
MSC = Metropolitan Service Center

Considerable investments in the network

The main part of the company's capital expenditure went into equipment. EUR 79 million – less than budgeted – were spent to construct the network as well as IT systems and to purchase the required hardware for connecting end users. Actual operating expenses in 2000 were 8 percent below what was expected by the capital markets. These savings were made possible by falling prices for leased fibre optic connections and by flexible contracts with suppliers. In the reporting period, QSC completed the most investment intensive part of its network construction successfully.

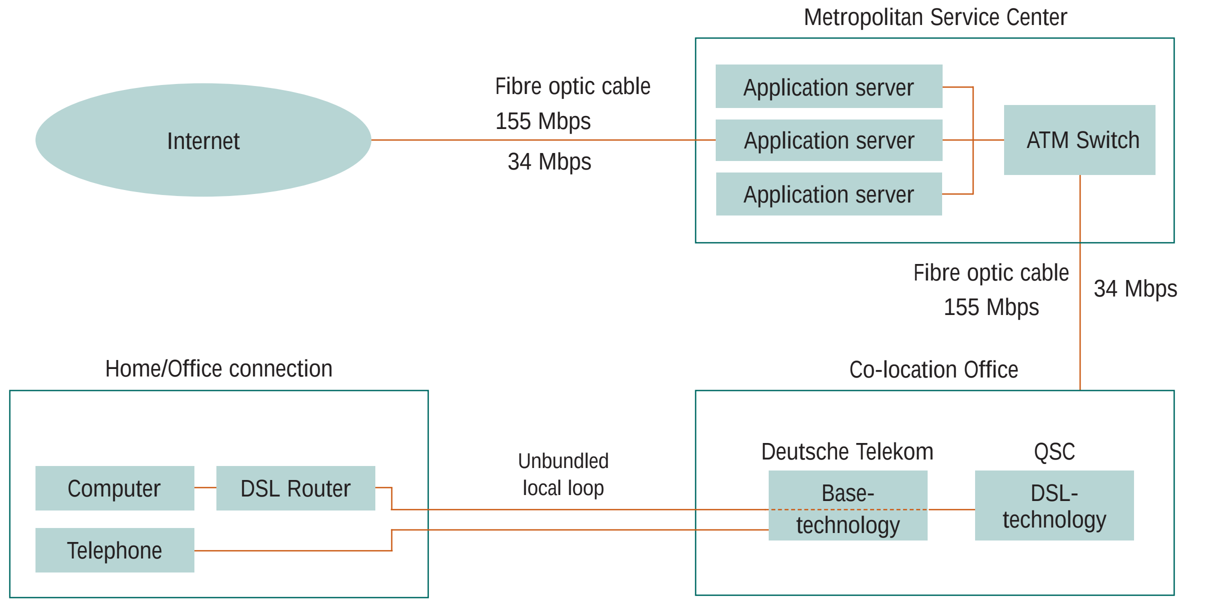
IN THE MSC, QSC CONNECTS EXTERNAL INTERNET SERVICE PROVIDER VIA FIBRE OPTIC LEASED LINES.

The network is based on co-location

Network roll-out and coverage proceeded in line with the original business plan. This was possible despite the fact that co-location rooms applied for by QSC were granted with considerable delays. Deutsche Telekom complied with the 16-week transfer deadline in only a few cases. Delays also resulted in providing leased fibre optic connections.

Nevertheless, QSC achieved its targets. This demonstrates the continuous and lasting input of all employees, on one hand. On the other hand, it proves the rapidly increasing demand for broadband enabling QSC to market its lines at a faster rate than originally planned. In the business year 2001, the company is largely independent from external interferences in regard to network infrastructure and can emphasize on marketing its local access broadband network.

LOCAL NETWORK ARCHITECTURE



STRONG PARTNERS

QSC HAS ESTABLISHED A WIDESPREAD NETWORK OF DISTRIBUTION PARTNERS. 89 SALES PARTNERS ALREADY SIGNED DISTRIBUTION AGREEMENTS.

Major advances in the first year

By creating its own networks in the 40 largest German cities last year, QSC established the basis for the successful marketing of broadband telecommunications lines. In line with its strategy, the company attracted many distribution partners with whom co-operation agreements were subsequently signed.

SUCCESSFUL PARTNERS OF QSC: AMONG OTHERS THE TELECOMMUNICATION SPECIALISTS MEDIAWAYS, TALKLINE, UUNET AND WORLDCOM.

A total of 89 companies, mainly telecommunications service and Internet service providers, are now physically connected with the QSC network. As a specialist for DSL, QSC profited extensively from the customer relationships already established by its partners.

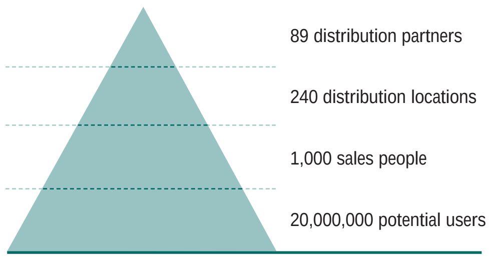
Success based on sales through co-operation

Towards the end of the year, QSC signed a distribution agreement with WorldCom, truly a global player in the telecommunications field. Since 1998, this global carrier has been providing voice-based services on its own city-based networks. All points of presence are connected to the global WorldCom data network. WorldCom markets its products primarily to business customers and is thus a perfect partner for QSC.

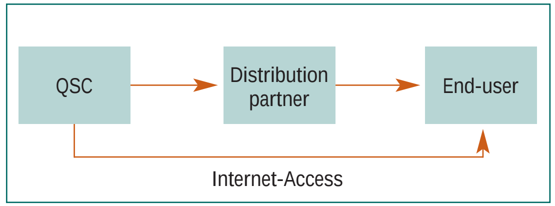
The co-operation with Talkline marks a similar milestone among the partnerships concluded. Talkline is a leading mobile telephony provider, fixed network provider and Internet service provider with its own fibre optic backbone network. More than a million business and residential customers use Talkline’s innovative solutions on the last mile. These are matched by QSC in the form of fast, scaleable Internet access services.

mediaWays, a subsidiary of Spain’s Telefonica, has been a partner of QSC since August 2000. This company operates one of the largest IP networks in Europe. In Germany, the company ranks number two after Deutsche Telekom with its Internet and network services. Its customers include DaimlerChrysler, Deutsche Bank, Bertelsmann, AOL, Hewlett Packard, Lycos and RTL. Value-added services of the future, such as unified messaging – using all forms of communication from a common interface –, voice/data integration and video/ audio streaming, are already included in its range. QSC and mediaWays are working jointly to develop additional products that exploit the potential of new technologies.

Distribution power with partners



Distribution strategy 2000



In October, QSC signed a partnership agreement with one of the most important Internet service providers (ISPs), UUNET. The latter is the biggest Internet services communication company for business clients, part of the WorldCom telecommunications group and owner of a 120,000-kilometer fibre optic backbone network. QSC provides fast, easy access to this high-performance network.

Business links with Cybernet were forged by QSC in March last year. Cybernet, the leading European Internet service provider with its own high-speed backbone, offers e-business solutions for companies of all sizes, and concentrates its efforts on DSL technology. QSC provides the high-performance connection to the Internet in the form of its scaleable SDSL products.

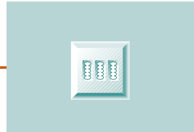
Joint success

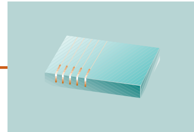
These numerous partnerships give QSC a wealth of sales and growth opportunities. QSC and its partners are currently engaged in creating the technical foundations for jointly providing their products and services. In view of these multiple partnerships, QSC expects revenues to grow exponentially during the current business year.

From April 1, 2001 onwards, QSC itself will be entering the end-user market by directly marketing a range of services such as domain installation, administration of e-mail accounts or the provision of web hosting space. This new focus of activities enlarges the potential revenue scope for the company, which at the same time gains direct contact to the end-users.

The installation process

1. Customer signs a contract
2. Installation of a telephone socket at the customer's home or office
3. QSC connects DSL-Router
4. The Customer starts right away





New products for the new millennium

The future may belong to the Internet, but fast, inexpensive access is essential to the success and development of the latter. QSC offers the perfect solution through speedw@y-DSL. This product ensures fast data transfer over a broadband Internet connection, reducing not only waiting and working time online, but also the associated costs.

Other benefits include the fixed IP-addresses that enable customers to operate their own web or mail servers. In addition, speedw@y-DSL establishes the basis for connecting complete local networks using broadband technology.

Installation: quick and easy

Speed is key at QSC. 95% of the new customers are connected to the broadband network within an average of only 20 working days. Deutsche Telekom installs a new telephone socket to connect the end-user on behalf of QSC, which is then responsible for installing the DSL router.

The advantage of scalability is that, even when the customer decides to subscribe to a particular service, it always has the option of switching to a different bandwidth. The sales partners provide additional assistance in selecting the appropriate solution. www.qsc.de lists the partners who provide QSC services.

The products

speedw@y-DSL	Small Office Solution
speedw@y-DSL 1	144 kbit/s
speedw@y-DSL 2	256 kbit/s
speedw@y-DSL 5	512 kbit/s
speedw@y-DSL	**Business Professional**
speedw@y-DSL 10	1.024 kbit/s
speedw@y-DSL 20	2.300 kbit/s

The solution for small businesses

The Small Office Solution was designed for large volumes of data and a small number of computers. The product caters to professional groups such as doctors or architects who transfer enormous amounts of data, for example when sending X-ray pictures or blueprints electronically.

speedw@y-DSL 1, which features a transmission speed of 144 kilobits per second, is conceived as an alternative to ISDN for Internet access and is particularly suitable for teleworkers, freelancers and self-employed users. speedw@y-DSL 2 provides a transmission rate of up to 256 kilobits per second and is aimed at smaller companies for e-mail and Internet applications.

More power thanks to higher speed

speedw@y-DSL 10, with a transmission speed of 1,024 kilobits per second, enables e-commerce applications, extended even to complex online shops and access to large-scale local networks. Anyone requiring higher speeds will choose the fastest type of line, speedw@y-DSL 20, which transports data at 2.3 megabits per second, thus representing the best alternative to the conventional leased line. These product variants are also ideally suited to companies with several branches.

New applications for broadband Internet

Ever-higher transmission speeds result in new applications. Video conferencing and business TV, for example, become genuine options for business customers. Private customers also benefit, for example, from Video-on-Demand.

Last year, QSC started a project to supply Video-on-Demand. In collaboration with media[netCom] AG, a Marburg based company, the virtual video shop is currently being tested in 50 households in the Cologne area.

In the current business year, QSC expects to launch an ADSL product tailor-made to residential customers.

Kleinofen GmbH

IT – these two letters comprise one of the largest fastest-growing sectors of the economy. Kleinofen GmbH integrates IT directly with the requirements of the media sector: This is where success or failure depend on an unrestricted, fast information flow. Tightly interlinked work processes providing a fast data exchange require fast Internet access during hectic everyday operations. The Dusseldorf based company's own high-speed QSC Internet access offers decisive advantages: As an example, highly complex in-house developed IT systems may be distributed and adapted to the particular needs of advertising agencies, publishers and printers. At the same time, Kleinofen created complex multimedia presentations that – thanks to DSL by QSC – do not fail to impress even over the Internet.

DIFFICULT TIMES WERE PREVALENT IN THE STOCK MARKETS IN 2000. COMPREHENSIVE IR-ACITIVTIES ARE THE BASE TO BUILD LONG-TERM CONFIDENCE IN QSC.

Going public

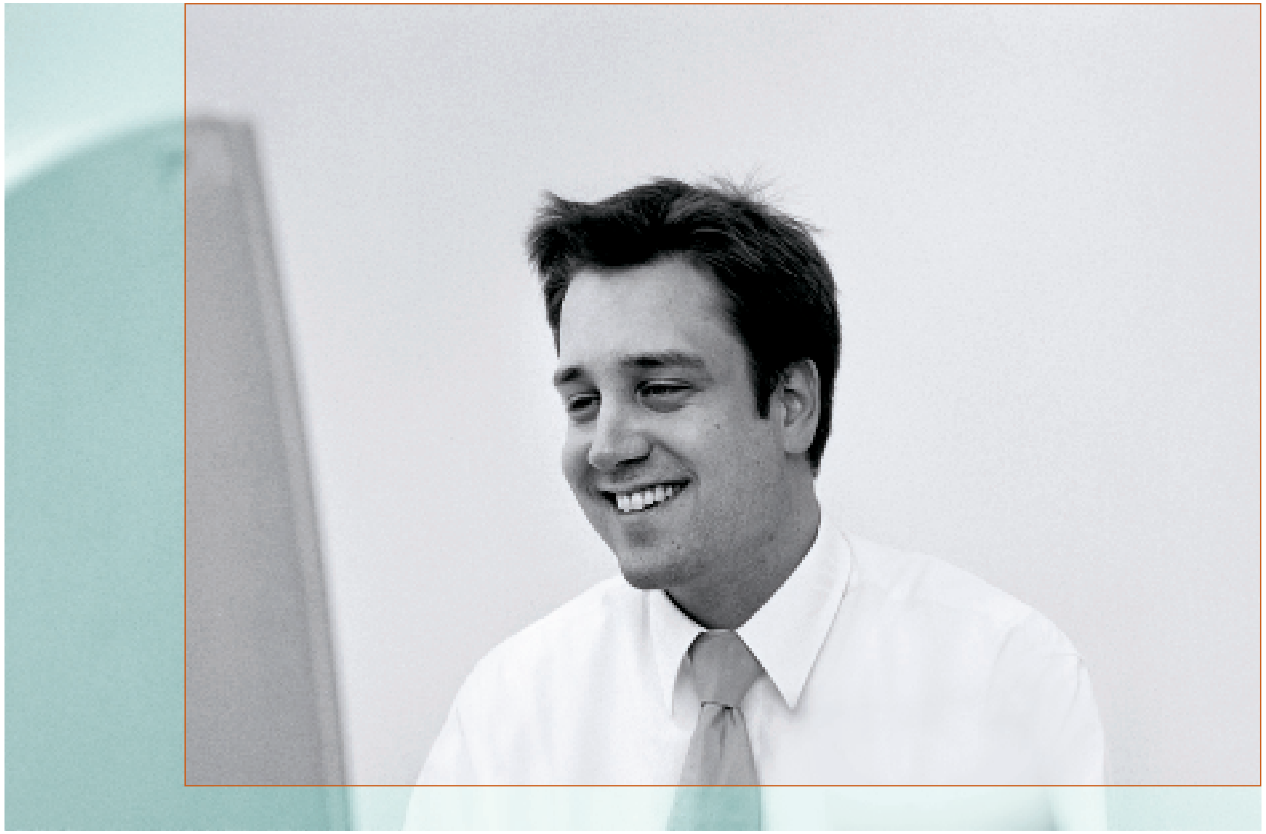
QSC was first listed as a public company on April 19, 2000. The IPO price was EUR 13, and the first quoted price was EUR 19. A total of 20.2 million shares were issued that day. Three weeks later, the underwriting banks – Morgan Stanley, Deutsche Bank, Salomon Smith Barney and Commerzbank – exercised their Greenshoe option for 3.03 million shares. The IPO netted a total of EUR 283.2 million in proceeds for QSC.

From the very first day, QSC has been listed on two exchanges – the Neuer Markt in Frankfurt and the Nasdaq market in New York. The Nasdaq listing gave QSC its first opportunity to address US-investors who were already familiar with DSL due to the history of broadband access in the USA. The so-called ADSs (American Deposit Shares) are traded in USD and represent two QSC shares.

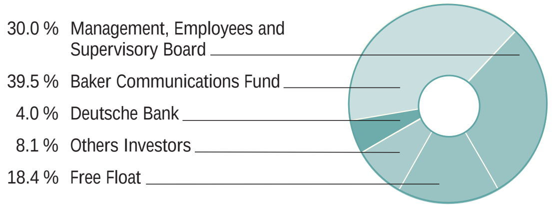
Bearish sentiment detrimental to QSC share price

2000 was a turbulent year for investors. Exaggerated rises in stock prices until March were followed by dramatic downward corrections throughout the rest of the year. Telecommunications stocks were among the worst hit. QSC shares were no exception, declining substantially until the end of the year.

One major factor for this dissatisfying trend was the disappointing business growth and stock prices of American DSL providers such as Covad, Northpoint and Rhythms. The QSC share price dropped in concert with these companies, even though the American market differs considerably from the German. For example, the last mile in Germany is only 1 – 1.5 km long, a distance so short that good transmission quality is easily obtained. In the USA, by contrast, average distances to the nearest central office are almost twice as long. Moreover, the German telephone networks have been fully modernised in recent years, thus enabling broadband data transmission facilities to be used without having to install new lines. Almost 100% of lines in Germany are now DSL-capable, compared to about 70% in the USA.



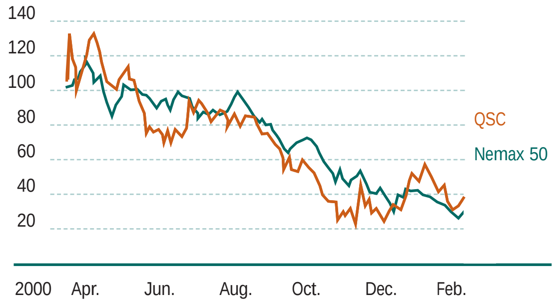
Ownership structure



As at December 31, 2000, ten German and International brokers, banks and research analysts had current research coverage on QSC. QSC will continue to intensify its communication efforts to ensure that additional brokers, banks and research analysts are aware of QSC's expanding efforts to provide broadband networking to the Internet.

IN LINE WITH NEUER MARKT, QSC'S SHARE PRICE EXPERIENCED A SHARP DECLINE IN 2000.

Relative Performance of QSC against Nemax 50



Key shareholders remain loyal to QSC

Baker Communications Fund, a US private equity fund, holds 39.5% of QSC's share capital, making it the company's biggest investor. 30.0% of the shares are held by members of the Supervisory Board, the Board of Management and employees, while a further 12.1% are in the hands of institutional investors who took a stake in the company before it went public. 18.4% of the shares are publicly held. Although the lock-up period for pre-IPO shareholders ended in October 2000, the largest part of those investors have kept their positions in QSC unchanged to this day. Last October, they extended the lock-up period by a further six months. This means that more than 87% of the shares outside the free float may not be sold until then. This was an important move to strengthen confidence among the free float shareholders, particularly at a time of sharp declines in the share price.

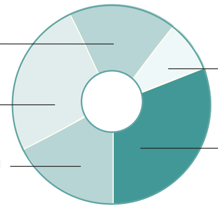
Investor Relations

Regular contact between the company and its investors is frequent when times are good, but is all the more important when the going is tougher. Company managers have presented at many events, including New York, Washington, London, Frankfurt, Madrid and Geneva, in order to inform investors and analysts about QSC. As well as direct contact with banks and investment brokers, investor relations work by management has also included participation at numerous investor conferences on the telecommunications industry. The management will continue and expand on these activities in the current year.

RAPID WORKFORCE EXPANSION

MORE THAN 35% OF THE EMPLOYEES ARE INVOLVED IN NETWORK DEVELOPMENT AND CONSTRUCTION.

A well qualified team



Focus on technology and distribution

The company's rapid growth is reflected in the number of employees, which grew by 45 to 194 in the course of the year in line with the fast network expansion and the signing of many distribution deals.

Almost four out of ten employees are directly involved with the core operations of the company, namely DSL technology. These telecommunications specialists safeguard smooth, fault-free network operation, and are responsible for network architecture and new product development.

QSC's customer focus is evidenced by the second main area, in which 35% of employees are engaged – Customer Care and Sales. Customer Care is the first contact for enquiries of all kinds, and carries out all work on the user's premises.

Extensive know-how is necessary when working with sophisticated DSL technology. QSC attaches great importance to the references that new recruits are able to provide. Every employee has completed some kind of vocational training, while one in five is a university or polytechnic graduate.

During the past business year, telecommunications specialists were among the most sought after professional groups on the labour market. For this reason, QSC uses a number of recruiting instruments in order to cover its personnel requirements. These range from classical job advertisements in print media, through advertisements on the Web, to the use of online employment exchanges. In addition, the company uses various recruiting events at universities and technical training centres in order to find suitable personnel. Through these means, we have succeeded in putting together a skilled and motivated team.

A broad range of further training ensures that the know-how of all employees is kept up to date. Courses range from simple computer software courses to highly specialized seminars for telecommunications experts.

Attractive stock option plan

As an incentive for new recruits, QSC offers its employees stock options. These take the form of five-year convertible bonds for which QSC pays interest at 3.5% p.a.; the bonds can later be converted to QSC stock. To ensure long-term involvement in the company, the lock-up period for shares out of the convertible bond is fixed at 3 years. A year after conversion, at the earliest, employees are allowed to sell up to 20% of the total of available shares.

The use of the stock option program demonstrates the willingness of the QSC workforce to commit itself to the company on a long-term basis. As at December 31, 2000 3,9 million shares have been converted out of the bond.

DAKOSY AG

With its headquarters in Hamburg and a staff of more than 70 specialists, DAKOSY Datenkommunikationssystem AG provides electronic processing for high volumes of data, especially for companies whose business success depends crucially on the speed of data transmission i.e. mostly globally operating transportation enterprises and logistics service providers. These enterprises send complex data bases over the DAKOSY computing center to the logistic links all over the world in order to manage their intermodal transportation requirements. QSC AG with its first-class infrastructure is the ideal partner for data professionals because the professional QSC SDSL technology guarantees not only speed, but also top reliability, a precondition set forth also by our ca. 600 DAKOSY clients – 24 hours a day, 7 days a week.

CONTENT

INDEPENDENT AUDITORS' REPORT

To the board of directors,
the shareholders and the supervisory board of
QS Communications AG, Köln

We have audited the consolidated balance sheets of QS Communications AG, Köln, and its subsidiaries (the "Group") as of December 31, 2000 and 1999 and the consolidated statements of income, changes in shareholders' equity and cash flows for the years then ended. The preparation of the consolidated financial statements was done in accordance with accounting principles generally accepted in the United States (U.S. GAAP) and is the responsibility of the management board of QS Communications AG. It is our responsibility to render an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the German generally accepted principles for the audit of financial statements. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall presentation of the consolidated net worth, financial position and results of operations in the consolidated financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements of QS Communications AG, Köln, as of December 31, 2000 and 1999 with due regard to the principle of materiality and in compliance with U.S. generally accepted accounting principles (U.S. GAAP), present in all material respects a true and fair view of the net worth, financial position and results of operations of the Group.

Eschborn/Frankfurt am Main, Germany, March 20, 2001

Arthur Andersen
Wirtschaftsprüfungsgesellschaft
Steuerberatungsgesellschaft mbH

Fluck	Zschockelt
Wirtschaftsprüfer	Wirtschaftsprüfer

STATEMENTS OF OPERATIONS

CONSOLIDATED STATEMENTS OF OPERATIONS FOR THE YEARS ENDED DECEMBER 31, 2000 AND 1999 (EUR amounts in thousands (TEUR), except for per share amounts)

	2000 in TEUR	1999 in TEUR
Net revenues	**4,971**	**1,595**
Operating expenses		
Network expenses (inclusive of TEUR 2,197 in non-cash compensation expenses in 2000; 1999: TEUR 514)	62,783	2,937
Selling and marketing expenses (inclusive of TEUR 757 in non-cash compensation expenses in 2000; 1999: TEUR 243)	17,281	2,297
General and administrative expenses (inclusive of TEUR 5,534 in non-cash compensation expenses in 2000; 1999: TEUR 956)	20,771	4,232
Research and development expenses (inclusive of TEUR 644 in non-cash compensation expenses in 2000; 1999: TEUR 157)	2,097	381
Other operating income, net	0	(83)
Total operating expenses	**102,932**	**9,764**
Operating loss	**(97,961)**	**(8,169)**
Other income (deductions)		
Non-operating loss	(8)	(7)
Share of post acquisition losses	(1,398)	0
Interest income	10,213	649
Interest expense	(20)	0
Net loss before taxes	**(89,174)**	**(7,527)**
Tax (provision) benefit on income	24	2
Net loss	**(89,150)**	**(7,525)**
Distribution to preferred shareholders	n/a	(120,873)
Loss attributable to common shareholders	(89,150)	(128,398)
Loss per common share (in EUR)	(1.15)	(4.22)
Weighted average number of common shares used in computing loss per share	77,769,576	30,420,000

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

CONSOLIDATED BALANCE SHEETS AS OF DECEMBER 31, 2000 AND 1999
(EUR amounts in thousands (TEUR))

	2000 in TEUR	1999 in TEUR
ASSETS		
Current assets		
Cash and cash equivalents	294,780	137,197
Trade accounts receivable, net	16,476	6,844
Unbilled receivables	11,747	8,424
Other receivables	11,225	1,048
Prepayments and other current assets	2,648	32
Deferred tax asset	0	0
Total current assets	**336,876**	**153,545**
Non-current assets		
Property, plant and equipment, net		
Networking equipment and plant	67,212	4,761
Operational and office equipment	6,075	696
Total property, plant and equipment, net	**73,287**	**5,457**
Intangible assets, net		
Licenses	2,491	1,969
Software	1,271	114
Others	11	5
Total intangible assets, net	**3,773**	**2,088**
Investment in equity method investees	5,427	0
Other non-current assets	317	0
Total non-current assets	**82,804**	**7,545**
Total assets	**419,680**	**161,090**

	2000 in TEUR	1999 in TEUR
LIABILITIES AND SHAREHOLDERS' EQUITY		
Liabilities		
Current liabilities		
Trade accounts payable	35,644	27,684
Deferred revenues	239	4
Other accounts payable	874	588
Other reserves and accrued liabilities	43,638	2,591
Deferred income tax	0	24
Total current liabilities	**80,395**	**30,891**
Non-current liabilities		
Convertible bonds	15	1
Accrued pensions	130	103
Total non-current liabilities	**145**	**104**
Total liabilities	**80,540**	**30,995**
Shareholders' equity		
Convertible preferred stock, 46,684,053 shares authorized at December 31, 1999; 46,684,053 shares issued and outstanding at December 31, 1999	0	79
Common stock, 124,316,037 and 33,492,420 shares authorized at December 31, 2000 and 1999, respectively; 105,008,714 and 33,300,774 shares issued and outstanding at December 31, 2000 and 1999, respectively	105,009	56
Treasury stock, 934,954 shares as at December 31, 2000	(4,125)	0
Additional paid-in capital	477,304	286,465
Deferred compensation	(21,515)	(28,060)
Receivables due from shareholders	(1)	(63)
Accumulated deficit	(217,532)	(128,382)
Total shareholders' equity	**339,140**	**130,095**
Total liabilities and shareholders' equity	**419,680**	**161,090**

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

CONSOLIDATED STATEMENTS OF CASH FLOWS FOR THE YEARS ENDED DECEMBER 31, 2000 AND 1999 (EUR amounts in thousands (TEUR))

	2000 in TEUR	1999 in TEUR
Cash flow from operating activities		
Net loss	**(89,150)**	**(7,525)**
Adjustments to reconcile net loss to cash (used by) provided by operating activities		
Non-cash compensation charge	9,132	1,870
Depreciation and amortization	9,442	488
Loss (Gain) on sale of equipment	8	(4)
Share of post acquisition losses	1,398	0
Increase in trade accounts receivable, net	(9,632)	(3,241)
Increase in unbilled receivables	(3,323)	(8,424)
Increase in other receivables	(10,177)	(992)
Decrease in inventories	0	14
Increase in prepayments and other current assets	(2,616)	(8)
Increase in deferred tax assets	0	0
Increase in other non-current assets	(317)	0
Increase in trade accounts payable	7,960	25,234
Increase/(Decrease) in advance payments received	0	(16)
Increase in deferred revenues	235	4
Increase in other accounts payable	286	190
Increase in accrued pensions	27	38
Decrease in accrued taxes	0	(689)
Decrease in deferred income taxes	(24)	(2)
Increase in other reserves and accrued liabilities	41,047	2,433
Net cash (used by) provided by operating activities	**(45,704)**	**9,370**

	2000 in TEUR	1999 in TEUR
Cash flow from investing activities		
Investment in equity method investees	(6,825)	0
Purchases of intangible assets	(2,174)	(2,092)
Purchases of plant and equipment	(76,846)	(5,154)
Proceeds from sale of equipment	53	51
Net cash used in investing activities	**(85,792)**	**(7,195)**
Cash flow from financing activities		
Proceeds from capital subscribed, net of issuance costs	293,190	135,681
Proceeds from convertible bonds issued	14	1
Purchases of treasury stock	(4,125)	0
Distributions to partners	0	(714)
Net cash provided by financing activities	**289,079**	**134,968**
Net increase in cash and cash equivalents	**157,583**	**137,143**
Cash and cash equivalents at beginning of period	137,197	54
Cash and cash equivalents at end of period	**294,780**	**137,197**
Supplemental disclosures of cash flow information		
Cash paid during the year for		
Interest	20	0
Income taxes	0	418

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

CONSOLIDATED STATEMENTS OF SHAREHOLDERS' EQUITY FOR THE YEARS ENDED DECEMBER 31, 2000 AND 1999 (EUR amounts in thousands (TEUR))

	Convertible Preferred Shares		Ordinary Shares		Treasury Shares		Additional Paid-In Capital	Deferred Compen-sation Account	Capital of Limited Liability Company	Retained Earnings/ (Accumulated Deficit)	Receivables due from Shareholders	Total Shareholders' Equity
	Shares	Amount TEUR	Shares	Amount TEUR	Shares	Amount TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR
Balance at January 1, 1999									**51**	**730**		**781**
Issuance of common stock (August 5, 1999) in connection with conversion from limited liability company to a corporation			30,420,000	51					(51)			0
Issuance of preferred stock A (August 5, 1999)	10,373,220	17					7,652					7,669
Issuance of preferred stock A (October 14, 1999)	14,510,340	24					10,713					10,737
Issuance of common stock in connection with the conversion of convertible bonds (October 14, 1999)			2,880,774	5			2,126					2,131
Initial deferred compensation recorded							29,931	(29,931)				0
Amount amortized during the period								1,871				1,871
Issuance of preferred stock B (December 22, 1999)	21,800,493	0					0					0
Beneficial conversion feature on Series B preferred stock							120,873					120,873
Dividend on Series B preferred stock		37					120,837			(120,873)		1
Less expenses of private placement offering							(5,667)					(5,667)
Receivables due from shareholders											(63)	(63)
Net loss										(7,525)		(7,525)
Distribution to partners										(714)		(714)
Balance at December 31, 1999	**46,684,053**	**78**	**33,300,774**	**56**			**286,465**	**(28,060)**	**0**	**(128,382)**	**(63)**	**130,094**
Issuance of common stock in connection with the conversion of convertible bonds (March 22, 2000)			15,210	15			(4)					11
Purchase of treasury stock (March 13, 2000)					6,084	(4)	(61)	61				(4)
Convertible bonds forfeited due to termination of employment (March 14, 2000)							(92)	92				0
Purchase of treasury stock (March 28, 2000)					54,756	(40)	(551)	551				(40)

	Convertible Preferred Shares		Ordinary Shares		Treasury Shares		Additional Paid-In Capital	Deferred Compen-sation Account	Capital of Limited Liability Company	Retained Earnings/ (Accumulated Deficit)	Receivables due from Shareholders	Total Shareholders' Equity
	Shares	Amount TEUR	Shares	Amount TEUR	Shares	Amount TEUR	TEUR	TEUR	TEUR	TEUR	TEUR	TEUR
Stock split (April 3, 2000)				79,851			(79,851)					0
Issuance of preferred stock B (April 3, 2000)	800,594	801					3,635					4,436
Issuance of common stock in connection with the conversion of convertible bonds (April 11, 2000)			978,083	978			4,440					5,418
Initial deferred compensation recorded							8,629	(8,629)				0
Issuance of common stock in connection with the initial public offering at the Frankfurt Stock Exchange (April 14, 2000)			18,152,000	18,152			217,824					235,976
Issuance of common stock in connection with the initial public offering at the New York Stock Exchange (April 14, 2000)			2,048,000	2,048			24,576					26,624
Conversion of preferred stock to common stock (May 5, 2000)	(47,484,647)	(879)	47,484,647	879								0
Issuance of common stock in connection with the exercise of Greenshoe (May 15, 2000)			3,030,000	3,030			36,360					39,390
Less issuance costs							(18,728)					(18,728)
Purchase of treasury stock (August 11, 2000)					18,252	(13)	(184)	184				(13)
Purchase of treasury stock (August 18, 2000)					48,008	(36)	(483)	483				(36)
Convertible bonds forfeited due to termination of employment (September 1, 2000)							(23)	23				0
Convertible bonds forfeited due to termination of employment (October 1, 2000)							(23)	23				0
Convertible bonds forfeited due to termination of employment (October 14, 2000)							(68)	68				0
Purchase of treasury stock (November 20, 2000)					807,854	(4,032)	(4,557)	4,557				(4,032)
Amount amortized during the period								9,132				9,132
Receivables due from shareholders											62	62
Net loss										(89,150)		(89,150)
Balance at December 31, 2000	**0**	**0**	**105,008,714**	**105,009**	**934,954**	**(4,125)**	**477,304**	**(21,515)**	**0**	**(217,532)**	**(1)**	**339,140**

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

QS COMMUNICATIONS AG, COLOGNE

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
(EUR amounts in thousands (TEUR), except for per share amounts)

1. Organization and basis of presentation

(a) Organization

QS Communications AG (in the following referred to as "QSC") was organized in January 1997 as a limited liability company under the name QS Communication Service GmbH. In the second half of 1999, it was registered as a stock company in Cologne, North Rhine Westphalia, Germany under the name QS Communications AG. QSC provides high-speed Internet and corporate network access over standard copper telephone lines. QSC uses digital subscriber line technology, known as DSL technology, to deliver always-on connections with data transfer rates ranging from 144 kilobits per second to 2.3 megabits per second both to and from the user. The use of dedicated copper telephone lines ensures secure data transmission. QSC provides its services through sales partners, mainly national and local Internet service providers and local and long distance telephone companies, serving small- to medium-sized enterprises and small office/home office customers.

(b) Basis of Presentation

The financial statements include the accounts of QSC. QSC holds a 50 % stake in QS Communications (Benelux) B.V. Amersfoort/Netherlands (in the following referred to as "QSC Benelux"), and a 30 % stake in ALCHEMIA S.p.A., Milano/Italia (in the following referred to as "Alchemia"). In fiscal year 2000 the investments were accounted for using the equity method of accounting. No goodwill arose from these investments. QSC's share of losses from these investments is shown in the consolidated statement of operations as a single amount under the heading "Other income (deductions)". In the balance sheet these investments are recorded at cost less QSC's share of post acquisition losses (see Note 7).
QSC maintains its financial records in accordance with the German Commercial Code, which represents generally accepted accounting principles in Germany (''German GAAP''). Generally accepted accounting principles in Germany vary in certain respects from United States generally accepted accounting principles ("US GAAP"). Accordingly, QSC has recorded certain adjustments in order that the accompanying financial statements are in accordance with US GAAP.
All amounts except per share amounts are in thousands of EUR (TEUR).
Based on a resolution of the general meeting on March 11, 2000 QSC carried out a 1,521 for 1 stock split. All statements regarding number of share amounts give effect to this stock split.

2. Significant accounting policies

(a) 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. Actual results could differ from those estimates.

(b) Reclassifications

Certain prior year balances have been reclassified to conform to the current year presentation.

(c) Concentrations of credit risk

QSC sells its DSL services through sales partners. For the year ended December 31, 2000 three customers accounted for 63% of QSC's revenues. The same three customers accounted for 16.3% of accounts receivable as at December 31, 2000. The following table shows customers representing more than 10% of QSC's revenues:

	Dec. 2000		Dec. 1999	
	% of Revenues	% of Accounts Receivable	% of Revenues	% of Accounts Receivable
Customer A	41%	14%	23%	95%
Customer B	11%	2%	23%	0.5%
Customer C	11%	0.3%	19%	0%
Customer D	–	–	14%	3%
Customer E	–	–	10%	0%

QSC has taken several precautionary measures to manage its credit risk. Prior to signing contracts with potential sales partners, QSC obtains credit reports from a leading German credit information agency. QSC performs ongoing credit evaluations and secures bank guarantees from certain sales partners. Trade accounts receivable are stated at their nominal value net of allowances for doubtful accounts. Specific allowances are calculated on an item by item basis.

(d) Cash and cash equivalents

The cash and cash equivalents consist of bank balances, cash on hand and marketable securities with an original term of three months maximum. Due to the very short terms of investments, the carrying amounts of the cash and cash equivalents are almost equal to their market value.

(e) Loss 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 conversion of convertible preferred stock where these are dilutive.
QSC was transformed from a limited liability company into a non-publicly listed stock company in 1999. The transformation became effective with the registration in the commercial register on August 5, 1999. Basic and diluted earnings per share amounts for the period ended December 31, 1999 were calculated using the weighted average number of common shares outstanding from August 5 to December 31, 1999.
For the period ended December 31, 2000 the dilutive effect of options and preferred stock has not been considered because QSC has a net loss and the impact of their assumed exercise would be anti-dilu-

tive. The loss per share calculation does not include 3,874,067 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 1,516,423 shares of QSC common stock. The loss per share calculation does not include 47,484,647 preferred shares for the period January 1, 2000 to May 5, 2000. The 47,484,647 preferred shares were converted into 47,484,647 ordinary shares of QSC on May 5, 2000, as of which date they were included in the loss per share computation.

(f) Unbilled receivables

Unbilled receivables represent amounts recognized as revenues related to services performed during the reporting period but for which invoices have not been generated at period end. Invoices are generally issued within 30 days of the services being performed. At such time, amounts classified as unbilled receivables are reclassified to accounts receivable.

(g) Intangible assets

Intangible assets consist mainly of licenses based on the German Telecommunications Law and capitalized standard software. Amortization of software is calculated using the straight-line method over the useful life of 4 years. Licenses are amortized on a straight-line basis over an estimated useful life of 10 years.

(h) Property, plant and equipment

Property, plant and equipment is recorded at historic cost. Maintenance and repairs which do not improve or extend the useful lives of the respective assets are expensed when incurred. Disposals are removed from both cost and accumulated depreciation accounts, with the resulting gain or loss reflected in the statements of operations as non-operating income (loss). QSC capitalizes costs associated with the deployment and expansion of its network as and when the risk of loss related to equipment and facilities are transferred to QSC.
Depreciation on assets is calculated using the straight-line method over the useful lives of the assets. Low value items (with acquisition costs under TEUR 0.4) are expensed in the year of acquisition.

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

	Useful life in years
Networking equipment and plant	8
Leasehold improvements	8
Electronic communication equipment	1 to 5
Company cars	3 to 5
Office equipment and other assets	4 to 10

(i) Impairment of long-lived assets

QSC periodically reviews the carrying value of its long-lived assets for possible impairments in accordance with Statement of Financial Accounting Standard (SFAS 121), "Accounting for the Impairment of

Long-Lived Assets and for Long-Lived Assets to be Disposed Of". An impairment loss is recognized whenever it is demonstrated that the carrying value of a long-lived asset is not recoverable based on expected future undiscounted cash flows related to that asset. The amount of the impairment loss to be recorded is based on the difference between the estimated fair value of the asset, based on discounted future expected cash flows, versus its carrying value. No impairment losses have been recognized to date.

(j) Pensions

Provisions for pensions are determined using the projected unit credit method in accordance with Statement of Financial Accounting Standards No. 87 (SFAS 87), „Employers' Accounting for Pensions".

(k) Other reserves and accrued liabilities

The accompanying financial statements include provisions for accrued expenses and contingent liabilities to the extent that such amounts are probable of incurrence and reasonably estimable.

(l) Recognition of revenues and income

QSC derives its revenues from (i) the provision of DSL-based telecommunications services and (ii) the provision of services based on the service agreement with IN-telegence GmbH & Co. KG ("IN-telegence").

(i) Revenues from DSL-based telecommunication services

QSC has agreements with sales partners authorizing them to enter into access agreements between QSC and their customers. Under the agreement, each sales partner is responsible for the acquisition of end users, the conclusion of access agreements and for after-sales customer service. Invoicing for QSC products and services is effected by the sales partner. The sales partner is also responsible for collecting any amounts due from its customers for QSC's DSL services.
The sales partner must pay QSC within two weeks after the end of the previous month all amounts billed for the previous month net of a certain percentage the sales partner deducts for its services under the agreement with QSC. The sales partner must pay QSC irrespective of whether it has collected the amounts due from its customers. The credit risk from the access agreement between QSC and the end user rests with the sales partner. The sales partner is the principal customer interface and assumes the credit risk associated with the transaction. QSC reports its revenues net of the sales partner's commission.
Revenues from DSL services are recognized when the services are provided. Revenues related to installation services are deferred and recognized over the average subscriber life of twelve months. Payments received in advance of providing services are recorded as deferred revenues until the period such services are provided.

(ii) Revenues from services based on the service agreement with IN-telegence

These are revenues arising from the service agreement with IN-telegence (see Note 3a). Revenues arising from the service agreement are recognized on a straight-line basis over the term of the service agreement with IN-telegence.

(m) Network expenses

These costs consist primarily of monthly rental costs for lines between the end user and central office, between central office and Metropolitan Service Center and between Metropolitan Service Center and the sales partner. These costs also include line installation costs, rental costs for the central offices and Metropolitan Service Centers and expenses associated with the design and deployment of the network.

(n) Advertising expenses

Advertising costs are expensed as incurred. Advertising expense was TEUR 13,834 in 2000 and TEUR 382 in 1999.

(o) Stock-based compensation

QSC accounts for stock-based employee compensation arrangements in accordance with the provisions of Accounting Principles Board Opinion No. 25 (APB 25), "Accounting for Stock Issued to Employees", for options granted to employees under stock option plans. QSC has adopted the disclosure provisions of Financial Accounting Standard No. 123 (SFAS 123), "Accounting for Stock-Based Compensation", but opted to remain under the expense recognition provisions of APB 25 in accounting for options granted under its convertible bond plans. QSC amortizes stock-based compensation recorded in connection with its convertible bond plans over the vesting period of the convertible bonds.

(p) Income Taxes

QSC utilizes the liability method of accounting for income taxes in accordance with Statement of Financial Accounting Standards No. 109 (SFAS 109), "Accounting for Income Taxes". Under the liability method, deferred taxes are determined based on differences between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. Valuation allowances are recorded to reduce deferred tax assets when it is more likely than not that a tax benefit will not be realizable.

In Germany, until the tax law was changed in October 2000, income was taxed at two different rates. A higher "undistributed" tax rate is applied to income generated but not distributed to shareholders. Upon distribution, such income is taxed at a lower "distributed" tax rate. QSC records deferred taxes at the undistributed tax rate. A tax credit is then recorded for differences between the undistributed and distributed tax rates in the period in which income is distributed to shareholders, and the related deduction is claimed on QSC's tax return.

As described above, effective October 2000, all income will be taxed at one rate. Accordingly, QSC has applied this enacted rate when measuring deferred tax assets and liabilities as of December 31, 2000.

(q) Segment information

QSC applies the "management" approach in accordance with Statement of Financial Accounting Standards No. 131 (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. In fiscal year 2000 QSC operated in one segment: Internet and corporate network access in Germany.

3. Related party transactions

During 2000, QSC participated in transactions with companies affiliated with Bernd Schlobohm, Chief Executive Officer of QSC, Gerd Eickers, a member of the supervisory board of QSC until December 31, 2000 and three other officers of QSC. The business relationships and transactions with related parties during 2000 were as follows:

(a) IN-telegence

QSC owns a telephone switching system. The switching facility allows QSC to offer dial-up narrow band access to its sales partners. The dial-up access through the switching facility assists QSC in its sales efforts, providing a migration path to broadband access.

IN-telegence provides value added telecommunication services. Its customers are content providers who, via service numbers such as those with prefixes 0800, 0180 and 0190, provide entertainment services, weather forecasts, stock quotes and other services to the public. The user of this service pays a premium on the price of the telephone call to these numbers to compensate the content provider for its service. Even though IN-telegence enters into direct contracts with the content providers, the public can only access the content providers' service numbers via the QSC switching facility and Deutsche Telekom's network. The cash flows between the parties involved in this business are as follows:

- Deutsche Telekom collects all telecommunication fees from value added service calls from end users.
- Pursuant to the interconnection agreement between QSC and Deutsche Telekom, Deutsche Telekom deducts a collection fee and a network usage fee and transfers the remaining funds to QSC.
- When QSC receives payment from Deutsche Telekom, it transfers the payment without deduction to IN-telegence. QSC acts as an intermediary between IN-telegence and Deutsche Telekom in relation to these payments. Consequently, QSC reports sales from these transactions on a net basis.
- IN-telegence deducts a margin and transfers the remaining monies to the content providers.

QSC receives a monthly flat fee from IN-telegence for letting it route its traffic through the QSC switching facility. In addition, QSC receives a second monthly flat fee representing a fixed percentage on the capital QSC invested in building the switching facility as well as an amount for the depreciation of these assets. At the same time, QSC pays IN-telegence a flat fee for building the necessary infrastructure and for operating the switching facility. QSC commits no resources other than the switching facility to this business.

The business relationship between QSC and IN-telegence is governed by a service agreement. Under its terms, QSC only has an obligation to pay IN-telegence after receipt of funds from Deutsche Telekom. The credit risk rests with IN-telegence.

Annual payments under the service agreement from QSC to IN-telegence amount to TEUR 74. IN-telegence's payments to QSC are TEUR 267 per annum. QSC has entered into a lease agreement with IN-telegence for QSC's Metropolitan Service Center in Cologne. Annual lease payments are TEUR 49. During 2000, QSC sold computing equipment to IN-telegence at net book value (TEUR 5).
As at December 31, 2000, TEUR 22,892 (1999: TEUR 6,340) were recognized as accounts payable to IN-telegence. This balance results from QSC acting as an intermediary between IN-telegence and Deutsche Telekom, i.e. an equivalent amount is recognized as a receivable from Deutsche Telekom AG (see Note 4). The payables to IN-telegence only become due after QSC has received the equivalent amounts from Deutsche Telekom.
As at December 31, 2000, IN-telegence owed QSC an amount of TEUR 1,237 (1999: 37), representing receivables arising from the service agreement between the parties and from QSC acting as an intermediary between IN-telegence and Deutsche Telekom.

(b) QS Communication Verwaltungs Service GmbH ("Verwaltung")

Gerd Eickers was the Managing Director of Verwaltung and a supervisory board member of QSC until December 31, 2000. During 2000, Verwaltung provided QSC and its customers with consulting services relating to technical, economic and regulatory issues in the German telecommunications market, the development and expansion of the business as well as the recruitment of qualified management personnel. QSC paid Verwaltung a total of TEUR 131 (1999: TEUR 157). As at December 31, 2000 QSC owed Verwaltung TEUR 5 (1999: TEUR 4).

(c) MVC Teleconferencing GmbH ("MVC")

MVC Teleconferencing provided a call center for QSC, handled the recruitment and management of agents and housed QSC's call center in MVC's office premises during the first half of 2000. In addition, QSC used MVC's services to conduct national and international audio conferences. QSC paid MVC a total of TEUR 21 (1999: TEUR 5) during 2000. There were no accounts payable as at December 31, 2000 (1999: TEUR 5).

(d) Teleport Köln GmbH ("Teleport")

Teleport installs and maintains QSC's PBX (private broadcast exchange). QSC paid TEUR 32 for these services in 2000 (1999: TEUR 2). As at December 31, 2000 payables to Teleport amounted to TEUR 8 (1999: TEUR 0).

(e) DaSNet Systemhaus GmbH ("Dasnet")

QSC purchased computing and telecommunication equipment from Dasnet paying TEUR 65 during 2000 (1999: TEUR 40). As at December 31, 2000 accounts payable to Dasnet showed a balance of TEUR 2 (1999: TEUR 0).

(f) Baker Capital Corp. ("Baker")

Baker, which has entered into a management agreement with one of QSC's principal shareholders, provided consulting services on international regulatory framework issues. QSC paid Baker TEUR 145 (1999: TEUR 283). There were no accounts payable to Baker as at December 31, 2000 (1999: TEUR 0). The following table sets forth the development of related party transactions from 1999 to 2000:

	Revenues in TEUR	Ex-penditure in TEUR	Cash Received in TEUR	Cash Paid in TEUR
Fiscal Year 1999				
IN-telegence	379	143	3,032	42,473
Verwaltung	8	162	8	157
MVC	6	5	6	0
Teleport	22	2	22	2
Dasnet	0	40	0	40
Baker	0	283	0	283
Fiscal Year 2000				
IN-telegence	272	127	1,364	90,258
Verwaltung	0	114	0	131
MVC	0	14	0	21
Teleport	0	35	0	32
Dasnet	0	58	0	65
Baker	0	145	0	145

4. Accounts receivable

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Trade accounts receivable	16,476	6,844
Less: Allowance for doubtful accounts	0	0
Trade accounts receivable, net	**16,476**	**6,844**
Unbilled receivables	**11,747**	**8,424**
Other receivables		
Tax claims	11,155	676
Others	70	372
Other receivables, net	**11,225**	**1,048**

As at the end of 2000, TEUR 11,205 of trade accounts receivable are receivables from Deutsche Telekom (see Note 3a). TEUR 11,689 of unbilled receivables also relate to Deutsche Telekom (see Note 3a).

The following reflects QSC's activity in its allowance for doubtful accounts for the years ended December 31, 1999 and 2000:

	Beginning Balance in TEUR	Charged to Cost and Expenses in TEUR	Charged against Existing Reserves in TEUR	Ending Balance in TEUR
Year ended Dec. 31, 1999	4	(4)	0	0
Year ended Dec. 31, 2000	0	0	0	0

5. Property, plant and equipment

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Cost		
Networking equipment and plant	75,199	4,974
Operational and office equipment	7,310	747
Cars	38	72
	82,547	**5,793**
Less: Accumulated depreciation	(9,260)	(336)
Property, plant & equipment, net	**73,287**	**5,457**

The increase in capital expenditure for facilities and equipment is due to QSC's rapid network expansion during 2000. Principal expenditures include the set-up of Metropolitan Service Centers, the procurement and establishment of co-location rooms in Deutsche Telekom's central offices as well as purchase and installation of equipment.

6. Intangible assets

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Cost		
Licenses	2,867	2,078
Software	1,497	119
Others	13	5
	4,377	**2,202**
Less: Accumulated depreciation	(604)	(114)
Intangible assets, net	**3,773**	**2,088**

QSC requires licenses of class 3 to be able to operate transmission lines in Germany as well as licenses of class 4 for the provision of voice telephony services. These licenses are awarded by the German regulatory authority and are subject to an initial, one-time fee. QSC, together with other German license holders, is involved in litigation against the German regulatory authority appealing the authority's license fee directive. As QSC believes that it is probable that the courts may uphold the German regulatory authority's license fee directive, QSC has recorded its licenses at the value imposed by the regulatory authority.

7. Investment in equity method investees

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Investment in equity method investees	**6,825**	**0**
Less: Share of post acquisition losses	(1,398)	0
Investment in equity method investees, net	**5,427**	**0**

On June 17, 2000 QSC entered into a shareholders' agreement with Stirlink B.V. to found QSC Benelux. QSC acquired a 50% share in QSC Benelux for TEUR 3,000. QSC plans to offer broadband access services for Internet and other data communication services based on DSL-technology in the Benelux market through QSC Benelux. On December 15, 2000 QSC entered into a shareholders' agreement with Kiwi II Ventura – Serviços de Consultoria S.A. and Pino Partecipazioni S.p.A. to found Alchemia. The purpose of Alchemia is to offer broadband access services based on DSL-technology in Italy. QSC invested TEUR 3,825 in Alchemia representing 30% of Alchemia's total share capital. Both investments in QSC Benelux and Alchemia were paid for in cash by QSC.

8. Other liabilities

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Other accounts payable		
Social security	868	79
Others	6	509
	874	**588**
Other reserves and accrued liabilites		
Outstanding invoices	36,230	390
Contingencies	3,454	1,970
Vacation outstanding	540	173
Employee bonus and remuneration	2,350	0
Workmen's compensation	26	7
Tax consulting/legal fees	1,038	51
	43,638	**2,591**
	44,512	**3,179**

86% of outstanding invoices relate to network expenses and network roll-out costs yet to be invoiced by Deutsche Telekom AG and Lucent Technologies Network Systems GmbH ("Lucent").

9. Employee benefit plan

As at December 31, 2000 there was one employee benefit plan for one of QSC's executive managers. The commitment is reinsured. Pension benefits are fixed at a monthly amount after old-age retirement.

Total pension expenses were:

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Components of net periodic benefit costs:		
Service cost	22	34
Interest cost	4	4
Net periodic benefit cost	**26**	**38**

The following table sets forth the funded status of QSC's pension plan, amounts recognized in QSC's balance sheets, and the principal weighted average assumptions inherent in their computation:

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Change in benefit obligation		
Benefit obligation at beginning of year	63	64
Service cost	22	34
Interest cost	4	4
Actuarial loss (gain)	12	(40)
Benefit obligation at end of year	**101**	**62**

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Change in plan assets		
Fair value of plan assets at end of year	–	–
Funded status	(100)	(62)
Unrecognized net actuarial loss (gain)	(30)	(40)
Unrecognized prior service cost	–	–
Prepaid (accrued) benefit cost	**(130)**	**(102)**
Weighted-average assumptions as of December 31,		
Discount rate	6%	6%
Expected return on plan assets	3%	3%
Rate of compensation increase	3%	3%

The pension accruals are calculated based on the mortality tables of Prof. Dr. Heubeck as of 1998.

10. Share capital

On April 19, 2000 QSC concluded the initial public offering of 20,200,000 of its shares at an offering price of EUR 13 per share. On May 9, 2000 the underwriters exercised their option to acquire 3,030,000 additional shares to cover over-allotments. QSC realized net proceeds of TEUR 283,262 after deducting underwriting commissions and other expenses resulting from the offering. Subsequent to the offering QSC's shares commenced trading on the Neuer Markt, a market segment of the Frankfurt Stock Exchange, under the symbol QSC. QSC's American Depositary Shares ("ADS") commenced trading on the NASDAQ National Market under the symbol QSCG. Each ADS represents two shares in QSC's common stock.

As a result of the initial public offering 47,484,647 shares of common stock were issued upon the conversion of preferred stock on May 5, 2000.

Nominal share capital

The nominal share capital of QSC consists of ordinary share capital of TEUR 105,009 and is divided into 105,008,714 ordinary shares having a notional value of EUR 1 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. In 1999, QSC had a nominal share capital of TEUR 134 being divided into 79,984,827 ordinary shares with a notional value of EUR 0.0017 each. The nominal share capital as at the end of 1999 was divided into 33,300,774 shares of common stock and 46,684,053 shares of preferred stock.

Conditional capital

As at December 31, 2000 QSC had conditional capital of TEUR 2,537 which relates to stock option plans for QSC's employees as well as Advisory and Supervisory Board members. In 1999, QSC had increased its nominal share capital conditionally by TEUR 5.2.

Treasury shares

Since the initial grants of convertible bonds certain employees have terminated their employment with QSC. As a result, 59,319 convertible bonds were forfeited and 127,100 shares were transferred back to QSC. On November 20, 2000, QSC exercised its call option to acquire 807,854 treasury shares at a purchase price of EUR 4.99 per share. As at December 31, 2000, QSC had acquired 934,954 (1999: 0) treasury shares through either forfeiture or purchase having a total notional value of TEUR 935 and representing 0.89% of total common stock. QSC intends to offer its treasury stock for sale to employees.

11. Employee equity incentive program

In order to attract and retain staff, QSC implemented a stock option plan in 1999 ("SOP2000") for all employees, senior management and members of the Supervisory and Advisory Boards. A second stock option plan ("SOP2000A") was implemented in 2000.

SOP2000A provides for the issuance of stock options allowing eligible employees and executive officers to acquire shares. QSC has been authorized to issue 3,338,970 convertible bonds each having a nominal value of EUR 0.01. Each bond is convertible into one share of QSC's common stock. The allocation period ended on December 31, 2000. The bonds attract annual interest of 3.5% and have a five year term. The plan is funded through a conditional capital increase (see Note 10). The conversion price is:

(a) if allocation and subscription of the bond was made prior to the price fixing of the initial public offering on a German Stock Exchange: EUR 5.54 less the par value of EUR 0.01 already paid to the issuer and accrued interest;

(b) if allocation and / or subscription of the bond is made after the initial public offering on a German Stock Exchange: the closing price quoted on the German "Neuer Markt" Stock Exchange on the date the bond was allocated or subscribed, whichever occurs later.

Shares acquired through the exercise of convertible bonds are subject to a three year retention period commencing on the issue or subscription date of the bonds, whichever occurs later:

(a) 20% of the shares so acquired may be sold from the commencement of the second year after grant or subscription of the bonds, whichever occurs later;

(b) a further 30% of the shares may be sold from the commencement of the third year; and

(c) from the commencement of the fourth year, the remaining 50% may be sold

with the right to retain the full sale price. Should any bond holder terminate his employment or renounce his designation or appointment during the retention period or should such employment be terminated during this period for cause or should such designation or appointment be withdrawn, the conversion rights shall be forfeited. Should such forfeiture occur after the convertible bonds have been converted into shares, such shares are to be transferred to QSC against payment of the conversion price of the shares.

The following table summarizes activity under QSC's stock option plans for the years ended December 31, 1999 and December 31, 2000:

	Number of shares subject to option	Weighted average exercise price in EUR
Issued and subscribed, below market value for accounting purposes	2,975,076	0.74
Exercised	(2,880,774)	0.74
Outstanding at December 31, 1999	94,302	0.74
Issued and subscribed, below market value for accounting purposes	1,182,547	5.54
Issued and subscribed, at market value for accounting purposes	1,292,186	4.22
Exercised	(993,293)	5.47
Forfeited	(59,319)	4.80
Outstanding at December 31, 2000	**1,516,423**	**4.19**

QSC accounts for its stock option plans under the provisions of Accounting Principles Board No. 25 (APB 25), "Accounting for Stock Issued to Employees" 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 SOP2000, the measurement date is the date of grant. In the case of SOP2000A, the conversion price of 483,169 convertible bonds was reduced. The re-pricing took effect in November 2000. The 483,169 convertible bonds were therefore accounted for using variable plan accounting. All other convertible bonds and shares exercised under SOP2000A have a measurement date equal to the grant date. As at December 31, 2000 QSC had deferred compensation totaling TEUR 21,515 in accordance with APB No. 25. This amount is yet to be amortized as a charge to operations over the remaining vesting period of the options. QSC amortized TEUR 9,132 and TEUR 1,870 in the years ending December 31, 2000 and 1999 respectively. QSC did not record any compensation expense in connection with the 483,169 convertible bonds subject to variable plan accounting. These bonds have a weighted average exercise price of EUR 4.23. QSC's stock closed at EUR 3.75 on the last trading day of 2000 at the Frankfurt Neue Markt stock exchange.

Had compensation expense for share options granted under the plans been determined in accordance with SFAS 123, QSC's net loss and loss per share for the year ending on December 31, 2000 would have been reduced to reflect a compensation cost of TEUR 7,322 (1999: TEUR 2,393), being TEUR 6,556 (1999: TEUR 2,393) for SOP2000, TEUR 98 (1999: TEUR 0) for those conversion rights under SOP2000A that were re-priced in November 2000 and TEUR 668 (1999: TEUR 0) for all other conversion rights subject to compensation under SOP2000A. The pro-forma amounts are as shown below:

	Dec. 2000 in TEUR*	Dec. 1999 in TEUR*
Approximate net loss after distribution to preferred shareholders		
as reported	(89,150)	(128,398)
pro forma	(87,340)	(128,921)
Basic eamings per share		
as reported	(1.15)	(4.22)
pro forma	(1.12)	(4.24)
Diluted loss per share		
as reported	n/a	n/a
pro forma	n/a	n/a

* except for per share amounts

The weighted average fair value of options granted in the period ended December 31, 2000 was estimated at EUR 7.97 (SOP 2000A) and EUR 10.15 (SOP 2000). The following weighted average assumptions were used: dividend yield of 0% (1999: 0%), expected life of 4 years (1999: 3 years) and a risk free interest rate of 6% (1999: 2.75%). A volatility of 82.62% (1999: 83%) was used in valuing options.

12. Income taxes and deferred taxes

The effective tax rates for 2000 and 1999 are as follows:

	2000	1999
Corporate income taxes	20.3%	32.7%
Trade tax on income	18.8%	18.4%
Surcharge	1.1%	1.8%
	40.2%	**52.9%**

Differences between German statutory and US books:

Temporary differences between book basis and tax basis of assets and liabilities result from declining balance depreciation used in the tax balance sheet, lump-sum allowances for accounts receivable, valuation differences for pension reserves, direct offering expenses, investments in equity method investees and non-cash compensation expenses.

The reconciliation of the tax benefit is as follows:

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Net loss before taxes	**(89,174)**	**(7,526)**
Income tax benefit based on the enacted tax rate	35,848	3,970
Share of post acquisition losses	562	0
Valuation allowance for treasury stock	403	0
Deferred revenues	(94)	(2)
Pension accruals	(23)	(33)
Non-tax deductible stock compensation expense	(3,671)	(989)
Changes based on the enacted taxe rate	(1,415)	(4)
	31,610	2,942
Less: Valuation Allowance	(31,586)	(2,940)
	24	**2**

As at December 31, 2000, QSC's accumulated losses for taxation purposes amounted to TEUR 112,404 (1999: TEUR 11,234). The tax effect from these losses is capitalized for US-GAAP purposes based on a tax rate of 40.2%, net of which TEUR 35,379 (1999: TEUR 2,940) relates to trading losses and TEUR 9,807 (1999: TEUR 2.991) relates to tax deductions for offering expenses.

Based on the recent formation of QSC and its limited operating history, it is unlikely that QSC will generate sufficient taxable income during the carry-forward period to utilize the tax loss carry-forwards. As a result, a valuation allowance of TEUR 45,186 (1999: TEUR 5,931) has been provided against all of the tax loss carry-forwards. Any reduction in the valuation allowance attributable to the offering expenses will be credited to equity rather than the statements of operations. There is no current or deferred tax income expense. The initial public offering expenses were offset against the additional paid-in capital raised regarding the initial public offering of shares of QSC.

In 2000 QSC made an initial public offering of shares. In connection with the initial public offering QSC had expenses of offering of TEUR 18,728 (1999: TEUR 5,667 expenses of offering in connection with a private placement). These expenses of offering are deducted directly from the gross proceeds of the offering and charged against additional paid-in capital. Because the realization of the benefit of the tax loss carry-forward related to the offering expenses is uncertain, the tax benefit is not taken into account.

The reconciliation of the components of the deferred tax assets and liabilities is as follows:

	Dec. 2000 in TEUR	Dec. 1999 in TEUR
Deferred tax (asset)/liability		
Declining method depreciation	4	8
At equity consolidation	(562)	0
Lump-sum allowance	0	3
Deferred revenues	(96)	(2)
Pension reserve	(29)	(6)
Other	0	21
Tax loss carry-forward	(44,503)	(5,931)
	(45,186)	(5,907)
Less: Valuation allowance	45,186	5,931
	0	**24**

13. Debt

QSC entered into a vendor guaranteed financing agreement with Deutsche Bank AG on December 29, 1999. Under the agreement QSC has at its disposal a credit facility of TEUR 168,571 to finance network equipment purchases.

As at December 31, 2000 QSC had no borrowings under the vendor guaranteed financing agreement.

14. Litigation

QSC was accused by a prominent individual in Germany of allegedly unlawfully using that individual's name in an advertisement. The matter was settled out of court with QSC agreeing to pay compensatory damages in the amount of TEUR 112.

QSC requires licenses of class 3 to be able to operate transmission lines in Germany. The German regulatory authority awards these licenses. QSC, together with other German license holders, is involved in litigation against the German regulatory authority appealing the authority's license fee directive.

In November 2000 one of QSC's executive directors left the Management Board. The validity of the termination of the service agreement is subject to litigation.

15. Commitments and contingencies

QSC has entered into leased line agreements with several carriers in Germany. QSC uses leased lines to connect its Metropolitan Service Centers to the co-location rooms within Deutsche Telekom's central offices and to its sales partners.

QSC leases co-location space within Deutsche Telekom central offices from the incumbent and it has entered into rental agreements for its Metropolitan Service Centers. QSC rents office space under various operating leases and leases its company vehicles. As at December 31, 2000 QSC's commitments from leases with a non-cancelable lease term in excess of one year were as follows:

Year ending December 31	in TEUR
2001	35,270
2002	13,850
2003	6,876
2004	4,821
2005	3,123

Rental expenses on operating leases totaled TEUR 30,360 in 2000 and TEUR 445 in 1999.

QSC signed a sponsorship agreement with the German soccer club Werder Bremen. As long as Werder Bremen remains in the German first division, this agreement will be in effect until June 30, 2001 with sponsorship payments totaling TEUR 4,218. QSC shall make contingent payments if Werder Bremen wins certain championships or cups. These commitments will be reduced if Werder Bremen relegates from the first division. Payments under the sponsorship agreement with Werder Bremen are amortized over the period of each soccer season.

As at December 31, 2000 QSC had open purchase orders in a total amount of TEUR 12,320. TEUR 2,399 (1999: TEUR 14,828) thereof represent open purchase orders with Lucent under the Equipment Supply Agreement of November 8, 1999. TEUR 9,921 (1999: 5,624) represent open purchase orders with Deutsche Telekom AG for building out co-location spaces in its central offices for QSC.

As at December 31, 2000 QSC had contingent liabilities in the amount of TEUR 1,884 principally being rental bonds.

16. Events subsequent to the balance sheet date

In March 2001, QSC took out insurance coverage against bad debts to further improve its credit management. QSC will purchase credit insurance for all significant accounts.

On February 23, 2001 QSC signed contracts to acquire a 65% share in COMpoint Network Consulting GmbH, Vellmar, Germany ("COMpoint"), the sale being economically effective as of January 1, 2001. COMpoint is a limited liability company with a registered capital of TEUR 26. COMpoint is an Internet service provider. QSC has a call option on the remaining 35% of COMpoint exercisable between June 1, 2002 and May 31, 2004.

QS COMMUNICATIONS AG, COLOGNE

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS (Euro amounts in thousands ("TEUR"), except for per share amounts)

The following discussion and analysis of QSC's financial condition and results of operations should be read in conjunction with the audited financial statements and the related notes thereto.

Overview

We commenced operations in January 1997 as a consulting company providing services in telecommunications and information technology to German and international clients. We phased out our consulting business by the end of December 1999.

We were the first company to publicly announce plans in Germany for a nationwide rollout of symmetric digital subscriber line services, known as DSL, on November 10, 1999. Since then we have built-out and deployed more than 800 central offices and the relevant Metropolitan Service Centers in the forty largest German cities with nearly full coverage at the end of 2000. Our network addresses more than twenty million potential users.

We provide high-speed Internet and corporate network access, known as broadband access service, to the German market using DSL technology. Currently, we distribute our DSL services through sales partners, who are mainly Internet service providers. As at December 31, 2000, we had signed contracts with 89 sales partners.

We give our customers a high-capacity local connection to the Internet and to private, local and wide area networks over standard copper lines. As at December 31, 2000, we had sold more than 9,000 lines.

Factors Affecting Future Operations

Revenues

We derive the following types of revenues from our DSL business:

- monthly recurring service charges for connections from the end-user customer to our facilities;
- monthly recurring charges for providing sales partners with broadband capacity at our Metropolitan Service Centers and on our backbone;
- non-recurring charges for installation;
- monthly recurring charges for providing equipment housing to our sales partners within our Metropolitan Service Centers;
- monthly recurring charges for the leased-line fiber connection from our sales partners to our Metropolitan Service Centers.

We expect prices for both recurring and non-recurring services to decrease each year due to increased competition and future volume discounts.

We generate revenues under our service agreement with IN-telegence GmbH & Co. KG. We expect that these revenues will be a diminishing percentage of our revenues in the future.

Operating expenses

The following factors comprise our operating costs:

- Network expenses: We pay Deutsche Telekom monthly rental costs for lines between end-users and Deutsche Telekom's central offices including non-recurring installation costs for such lines. Network expenses also include monthly rental costs for space within Deutsche Telekom's central offices and for our Metropolitan Service Centers. We pay Deutsche Telekom and other telecommunications companies monthly recurring and non-recurring costs for lines between Deutsche Telekom's central offices and our Metropolitan Service Centers and for lines between our Metropolitan Service Centers and our distribution partners. Other network expenses we incur are for repairs and maintenance of our network, for the operation of our network and for the design and deployment of our network. Network costs may vary in the future due to regulatory intervention regarding the monthly rental for co-location space in Deutsche Telekom's central offices. We expect leased line costs for lines between central offices and Metropolitan Service Centers and for lines between Metropolitan Service Centers and our distribution partners to decrease in the future due to increased competition and future volume discounts.

- Other operating expenses include costs for selling and marketing activities, research and development costs as well as general and administrative expenses.

EBITDA

In addition to other measurements, which are reflected in our statement of operations, we measure our financial performance by EBITDA. EBITDA consists of net loss excluding interest, taxes, share of post-acquisition losses, amortization of deferred stock compensation and depreciation and amortization of non-current assets. We believe that EBITDA is a meaningful measure of performance because it is commonly used in the telecommunications industry. However, other companies may calculate it differently from us. We present EBITDA to enhance your understanding of our operating results. You should not construe it as an alternative to operating income as an indicator of our operating performance or as an alternative to cash flows from operating activities as a measure of liquidity. For the financial year 1999, we calculated negative EBITDA of TEUR 5,818. For the financial year 2000 we calculated negative EBITDA of TEUR 79,395, primarily due to increased operating expenses in connection with the development of our DSL business.

Capital expenditures

The development and expansion of our business will require significant expenditures. When we enter a market, we primarily incur the following types of capital expenditures:

- expenditure for procurement, design and construction of space within Deutsche Telekom's central offices;
- purchase and installation of DSL access multiplexing equipment and asynchronous transfer mode switches;
- purchase and installation of equipment for our Metropolitan Service Centers;
- purchase and installation of our network management systems;
- demand-based expenditures for purchasing end-user DSL line cards and customer premises equipment.

Currently, the average cost to deploy our facilities in a central office, excluding end-user line cards, is approximately TEUR 60 and the average cost to deploy our facilities in a Metropolitan Service Center is approximately TEUR 130. Expenditures may vary in future periods due to the quantity and type of equipment we initially deploy in a co-location room or in a Metropolitan Service Center. Following the build-out and initial deployment of our equipment in a central office, the major portion of our capital expenditures is for the purchase of line cards and customer premises equipment to support customer and end-user growth. We expect that the average cost of both line cards and customer premises equipment will decrease in the next few years.

Results of Operations (year ended December 31, 2000 and year ended December 31, 1999)

Revenues

In financial year 2000, we recorded revenues of TEUR 4,971. Compared with revenues of TEUR 1,595 in financial year 1999, this represents an increase of 212%.

Close to 90% of our revenues in 1999 were generated by the consulting business, our core business until early 1999. We started to phase out the consulting business at the beginning of 1999 and changed our focus to building up our new DSL business. By the end of 1999 we had successfully terminated the consulting business.

Our new DSL business generated 95% of our revenues in financial year 2000. As at December 31, 2000 we had contracts to provide more than 9,000 lines for Internet access to end-user customers. Close to 65% of these lines were contracted in the fourth quarter of 2000. After finishing the deployment of our network in Germany's main metropolitan centers and with increased sales and marketing efforts, we expect revenues from our DSL business to further increase in future periods.

The Securities and Exchange Commission ("SEC") issued Staff Accounting Bulletin SAB 101 "Revenue Recognition in Financial Statements" in December 1999. SAB 101 requires that, in certain circumstances, revenues received in the first month of a contract be recognized over an extended period of time instead of in the first month of the contract. QSC has adopted the provisions of SAB 101. Accordingly, we do not recognize revenues from non-recurring installation charges in the month they are invoiced, but we recognize them over the estimated average contract life of 12 months. For the period ended on December 31, 2000, we recognized TEUR 4,971 in revenues. TEUR 239 in installation charges are deferred to be recognized in future periods.

Network expenses

Network expenses totaled TEUR 62,783 for the financial year 2000. During the equivalent period in 1999, we recorded network expenses of TEUR 2,937.

Currently, network expenses represent approximately 60% of our total operating expenses reflecting the rapid progression of our network roll-out and the building of our operating infrastructure. We have increased the number of co-location rooms in service from 17 at the beginning of January to more than 800 at the end of December. As at December 31, 2000 Deutsche Telekom had provided us with co-location spaces in a total of 949 of their central offices. Eight hundred sixty-two of these co-location spaces had been equipped with the required technical equipment. We expect increasing network expenses in future periods due to intensified sales activity and expected revenue growth.

Selling and marketing expenses

We recorded selling and marketing expenses of TEUR 17,281 for the financial year 2000 and TEUR 2,297 for the equivalent period of 1999, representing an increase of 652%. Selling and marketing expenses increased significantly reflecting our efforts to market and sell our DSL services.

The largest part of selling and marketing expenses in financial year 1999 related to the consulting business which was phased out by the end of 1999. Selling and marketing expenses in the financial year 2000 consist primarily of salaries, costs incurred for promotional and advertising campaigns and the development of corporate identity. We established six sales regions during the financial year 2000. We expect selling and marketing expenses to further increase as we continue to promote our services.

General and administrative expenses

General and administrative expenses were TEUR 20,771 in financial year 2000 and TEUR 4,232 for financial year 1999, representing an increase of 391%.

The increase in general and administrative expenses is mainly attributable to growth in headcount in all areas of our company. Additionally, we entered into a lease agreement for additional office space to move all our employees in Cologne to one building and to accommodate further organizational growth. We expect our general and administrative expenses to further increase in future periods as we continue to expand our business and manage our organizational growth.

Research and development expenses

We recorded research and development costs of TEUR 2,097 in financial year 2000 and TEUR 381 in 1999, representing an increase of 450%.

Research and development costs primarily consist of development costs for advanced solutions and applications for our DSL business. We expect our research and development expenses to further increase in future periods as we continue to develop value added services.

Other income (deductions)

Other income (deductions) consists primarily of interest income on our cash balance and interest expense associated with short-term borrowings. Interest income for financial year 2000 was TEUR 10,213 in comparison to TEUR 649 in financial year 1999. Interest expense for financial year 2000 was TEUR 20 consisting mainly of interest expense on our loan in connection with the vendor guaranteed financing agreement with Deutsche Bank AG. For financial year 2000 we recorded a share of post-acquisition losses of TEUR 1,398. This net loss represents our 50% share of the net losses of QS Communications Benelux B.V. (“QSC Benelux”) and the 30% share of the net losses of ALCHEMIA S.p.A. (“Alchemia”) for the period ended December 31, 2000. There was no share of post-acqusition losses during 1999 as there were no investments in other entities.

Liquidity, Capital Resources and Investments

Our operations have required substantial capital investment for the network roll-out. We financed our operations through equity. From 1999 through to December 31, 2000 we raised total net proceeds of TEUR 428,871 through private placements, our public share offering in April 2000 and our employee equity incentive programs. In addition, we entered into a vendor guaranteed financing agreement with Deutsche Bank AG in December 1999, securing a credit facility of TEUR 168,571.
As at December 31, 2000, we had no borrowings. Cash and cash equivalents on December 31, 2000 were TEUR 294,780.

The accumulated deficit of TEUR 217,532 contains TEUR 120,873 in dividends from a beneficial conversion feature in connection with our private placement in December 1999 and TEUR 11,002 deferred compensation resulting from the issuance of convertible bonds. The non-cash beneficial conversion feature is the result of our private placement in December 1999, where we sold shares in series B preferred stock at a price per share deemed below the fair value per share for accounting purposes. We recognized the difference between the deemed fair value per share and the actual price per share as a non-cash dividend of TEUR 120,873 in connection with the beneficial conversion feature. The non-cash deferred compensation amount is the result of the issuance of our stock option plans, where we sold convertible bonds at a price per share deemed below the fair value per share for accounting purposes. From October 1999 to December 2000, we incurred TEUR 11,002 in compensation expense.

From January 1 through to December 31, 2000, net cash outflow from operating activities was TEUR 45,704. This was due to net losses of TEUR 89,150 and increases in assets of TEUR 26,057, offset by non-cash expenses of TEUR 19,972 and increases in accounts payable and accrued liabilities of TEUR 49,531. We used TEUR 78,967 net cash for investing activities due to purchases of intangible assets, plant and equipment. We paid TEUR 6,825 for our investments in QSC Benelux and Alchemia. Net cash provided by financing activities during the twelve months ended on December 31, 2000 amounts to TEUR 289,079, which primarily relates to the net proceeds from our public offering in the second quarter.

We expect to experience significant negative cash flow from operating and investing activities in future periods due to our expanding business and the continued build-out of our network. We may also make investments in entities that are complementary in order to further support the growth of our business and to expand our geographic presence through partnerships. We believe that the credit facility and our existing cash will be sufficient to fund those investments.

Recent Developments and Outlook

In the financial year 2000 we concentrated on building our network and increasing our network coverage. From January to December 2000 we increased the number of operational co-location rooms to more than 800. As at March 10, 2001 Deutsche Telekom had provided us with co-location spaces in a total of 1,093 of their central offices. Eight hundred ninety-four of these co-location spaces had been upgraded with DSL equipment. We have completed our first roll-out phase which was designed to open up Germany's most densely populated metropolitan centers. The second roll-out phase addresses regions of medium population density. We have developed a set of selection criteria which allow us to identify those regions offering the highest potential for our services. By only addressing the markets identified by our stringent selection process, we expect our network expenditures for the second roll-out phase to be significantly lower than those for the first roll-out phase.

We expect to further increase our operational costs as we continue to expand our business. At the same time we expect to further increase our expenditures on sales and marketing activities to promote our services to end-user customers jointly with our distribution partners.

We expect our decision to build a backbone interconnecting our Metropolitan Service Centers to further improve our sales: Sales partners can connect to only one Metropolitan Service Center, yet will be able to offer our services nationwide.

Currently QSC develops a residential product that will directly compete with the residential offers of our competitors, especially Deutsche Telekom.

Since the beginning of 2000 we have hired additional personnel. As at December 31, 2000 we had 194 employees in total. We expect the number of employees to further increase in future periods.

On March 10, 2000 the Supervisory Board appointed Messrs James G. Cosgrove and Claus Wecker as further members to QSC's Advisory Board. On the same date, Mr Markus Metyas was appointed as Chief Financial Officer of the Company. On March 11, 2000 the general meeting elected Messrs John C. Baker, Gerd Eickers, Herbert Brenke, David Ruberg, Manjit Dale and Ms Ashley Leeds as members of the Supervisory Board. On September 16, Messrs Bernd Wilhelm and Hans-Peter Kohlhammer were appointed to the Advisory Board. On November 16, 2000 Mr Gerd Eickers resigned from the Company's Supervisory Board. On the same day, Mr Gerd Eickers was appointed to the Management Board as Chief Operating Officer, the appointment becoming effective on January 1, 2001. Mr Torsten C. Scheuermann no longer serves on the Management Board as of November 16, 2000.

Members of the Supervisory Board receive compensation in the amount of TEUR 5 per annum, payable after the end of each fiscal year. The Chairman receives TEUR 10 and his deputy TEUR 7.5 in compensation per year. In addition, members of the Supervisory Board are eligible to receive up to 9,130 convertible bonds each under the second employee equity incentive program. Five members of the Supervisory Board have subscribed to their allocation of convertible bonds with one member having converted the bonds into shares.

Forward Looking Statements

The statements contained in this report that are not historical facts are forward looking statements. We have based these forward looking statements on our current expectations and projections of future events. Actual results could differ materially from those anticipated in these forward looking statements as a result of the risks facing us or faulty assumptions on our part. Assumptions that could cause actual results to vary materially from future results include, but are not limited to:

- our ability to successfully market our services to current and new customers;
- our ability to generate customer demand for our services in our target markets;
- the development of our target markets and market opportunities;
- market pricing for our services and for competing services;
- the extent of increasing competition;
- the ability of our equipment and service suppliers to meet our needs; and
- trends in regulatory, legislative and judicial developments.

GLOSSARY

ADSL
Asymmetric Digital Subscriber Line; asymmetric data transmission technology with downstream rates between 1.5 Mbps and 8 Mbps and upstream rates between 16 Kbps and 640 Kbps.

ASP
Application Service Provider; service providers that host, manage, support, and deliver software applications and database to customers from a remote data center over the Internet or wide area networks.

ATM
Asynchronous Transfer Mode; network technology that subdivides data into evenly sized packages for transportation, the so-called cells. “Asynchronous”, in this context, means: data of different logical relations can be mixed on a single physical connection.

Backbone
High-speed network that interconnects networks with lower speeds/capacities.

Broadband
Data transmission capacity in excess of 128 Kilobit per second.

Bandwidth
The transmission capacity of a line.

CO
Central office or co-location room; local access switching facility of Deutsche Telekom, where the last mile begins.

ISDN
Integrated Services Digital Network; digital switching technology allowing the transmission of any and all forms of telecommunication through a single line.

ISP
Internet service provider. They facilitate customer data communication by provision of Internet access and related services, e.g. e-mail management.

Last Mile
The distance from the telephone outlet to the nearest local switching centre (central office).

Mbps
Megabit per second; measuring unit of data transmission speed.

MSC
Metropolitan Service Center; QSC's local access network mode where local broadband traffic is bundled and connected with the Internet and/or the PoTS (Plain old Telephony System) world. The MSCs also house broadband application servers.

QoS
Quality of Service; in order to ensure an agreed transmission service level, the transport protocol, e.g. ATM, must support Quality of Service. Quality of Service for instance, ensures that a video transmitted via QSC speedw@y-DSL will reach the user without distortions.

SDSL
Symmetric Digital Subscriber Line; symmetric transmission technology, allows for data transfer into both directions at equal speeds of up to 2.3 Megabit per second.

Leased Line
Any permanently available connection; no time lost due to dialling in and the setting up of a connection.

Video-on-Demand
The future of home entertainment. Via the Web, movies can be ordered and copied almost "live" through the telephone line. Due to QSC's SDSL technology, the virtual video library as well as countless other multimedia services will grow from a technical concept stage to real consumer availability.

Web-Hosting
Service providers offer server capacities mainly to business subscribers for their Internet applications.

Voice over DSL
The possibility to transmit voice and data simultaneously within the framework of DSL technology.

CALENDAR/CONTACTS

CALENDAR

Shareholders' Meeting
May 17, 2001

Quarterly Reports
May 29, 2001
August 28, 2001
November 27, 2001

CeBIT
March 22-28, 2001

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