freenet

Annual Report 2007

Group accounts of freenet AG

freenet AG – group overview

Results in € million	2007	2006	Q4/2007	Q3/2007	Q4/2006
Third-party revenue	1,863.3	2,054.8	473.9	470.0	530.2
Gross profit	582.4	465.8	146.1	137.1	112.5
EBITDA	252.8	147.0	56.5	60.3	24.8
EBIT	156.6	103.1	28.2	31.7	13.7
EBT	163.7	117.6	28.0	28.6	18.5
Group result	16.5	257.0	–50.6	–22.7	181.3

Balance	2007	2006	Q4/2007	Q3/2007	Q4/2006
Balance sheet total in € million	902.6	1,295.6	902.6	893.6	1,295.6
Shareholder's equity in € million	372.1	933.4	372.1	422.6	933.4
Equity ratio in %	41.2	72.0	41.2	47.3	72.0

Finances and investments in € million	2007	2006	Q4/2007	Q3/2007	Q4/2006
Cash flow from operating activities	285.1	144.8	49.8	82.0	28.2
Depreciation and amortisation	96.2	43.9	28.3	28.6	11.1
Investments	290.5	41.7	83.8	53.3	16.4
Net cash	–38.0	534.0	–38.0	–4.3	534.0

Share	2007	2006	Q4/2007	Q3/2007	Q4/2006
Closing prices (XETRA) in €	15.99	22.10	15.99	19.15	22.10
Number of ordinary shares in thousand	96,061	62,417	96,061	96,061	62,417
Market capitalisation in € thousand	1,536,025	1,379,409	1,536,025	1,839,580	1,379,409
Earnings per share in €	0.17	3.50	–0.53	–0.23	2.52

Business performance by sector	2007	2006	Q4/2007	Q3/2007	Q4/2006
Third-party revenue for the group in € million[1]	1,863.3	2,054.8	473.9	470.0	530.2
1. Revenue mobile telephony	1,184.8	1,331.7	301.0	301.7	348.7
2. Revenue broadband	272.3	195.1	77.4	72.2	53.8
3. Revenue portal	56.7	63.5	15.9	12.4	20.5
4. Revenue hosting	79.4	69.0	21.4	19.5	18.1
5. Revenue B2B	134.9	141.4	33.4	33.5	37.8
6. Revenue narrowband	149.3	281.7	27.8	33.9	59.5
Group gross profit in € million[1]	582.4	465.8	146.1	137.1	112.5
1. Gross profit mobile telephony	289.5	191.0	81.0	67.2	44.5
2. Gross profit broadband	67.6	2.2	14.9	16.0	0.9
3. Gross profit portal	40.7	50.7	11.3	8.4	16.1
4. Gross profit hosting	65.5	54.5	15.6	15.7	14.2
5. Gross profit B2B	31.2	28.4	6.9	9.7	7.2
6. Gross profit narrowband	88.9	145.4	16.7	20.3	33.3

Selected key data	2007	2006	Q4/2007	Q3/2007	Q4/2006
Total customer freenet group in million	11.69	12.68	11.69	11.81	12.68
Thereof contract customers in million	6.48	5.81	6.48	6.32	5.81
Mobile telephony					
Gross new customers in million	1.73	1.60	0.48	0.43	0.48
Net-additions in million	0.60	0.28	0.26	0.21	0.09
Mobile telephony customers in million	5.70	5.10	5.70	5.45	5.10
Thereof contract customers in million	2.99	2.75	2.99	2.90	2.75
Thereof prepaid customers in million	2.71	2.35	2.71	2.55	2.35
Monthly average revenue per user in €	15.03	16.93	14.05	15.36	16.50
Of which per contract customer in €	24.64	27.02	23.14	25.45	26.50
Of which per prepaid customer in €	4.13	5.00	3.85	3.65	4.76
Active narrowband customers (internet + telephony) in million	2.96	5.07	2.96	3.42	5.07
DSL customers in million	1.28	1.00	1.28	1.27	1.00
Active registered member in million	8.96	8.18	8.96	8.83	8.18
Paid service customers Hosting in million	1.20	1.05	1.20	1.17	1.05
Paid service customers Portal in million	0.54	0.46	0.54	0.51	0.46

Employees	2007	2006	Q4/2007	Q3/2007	Q4/2006
End of Period	3,838	3,646	3,838	3,822	3,646

1 Netting between segments is the reason behind the difference between the figures shown for sales and gross profits in the individual segments and the corresponding figures for the overall group.

List of contents

1. Letter to shareholders

1. Letter to shareholders

Eckhard Spoerr

Axel Krieger

Stephan Esch

Eric Berger

Dear shareholders, business partners, customers and friends of freenet AG,

It was with a great deal of optimism that we announced the dawn of a new era for freenet AG in the 2006 annual report. After a two-year transition period, almost endlessly prolonged by legal challenges, the desired merger of the 'old' freenet.de AG and moblicom AG was finally completed in March 2007, resulting in one of the leading telecommunications groups on the German market, with all key communications products in the field of Internet/telephony: broadband and narrowband Internet access, hosting, innovative DSL telephony, mobile and traditional fixed-line telephony, a comprehensive portal business and top-quality B2B solutions.

With according enthusiasm, at the start of CeBIT 2007 we served up a raft of new products, mainly bundled products involving all sorts of complete broadband packages and mobile Internet. They reflect the increasing fusion of mobile and fixed-line telephony and the Internet, and have great potential for growth. But then, just a few weeks later, several large shareholder groups appeared on the scene calling for the sale of the entire freenet AG or of individual parts of the business. The reasoning behind a possible break-up was the hypothesis that the sum of the parts of our company – mobile telephony, fixed line/Internet and web hosting – was worth more than freenet's overall strategy.

So, from the middle of last summer and with the help of investment bank Morgan Stanley, we undertook an exhaustive review of all possible strategic options for any consolidation of or with freenet. At the end of December, however, all talks with other companies about a sale of freenet or of any individual parts were terminated. It is true that, in light of the enormous competition in the sector, a consolidation would make sense, as only suppliers with a strong market position and corresponding customer numbers will be able to survive the price war with major international corporations over the long term. However, it was no longer acceptable – including and specifically in the interest of our company, our customers and our staff – for us to be largely putting the implementation of the strategy planned with the merger "on hold". Important projects, such as the new freenet AG's new brand image, the IT integration of the two merged companies, and negotiations on new contract models with mobile network operators had also unavoidably been set back by months.

Indeed, the current dramatic changes in the Internet/telecommunications market mean that all of the competing companies are facing major challenges which demand quick, clear decisions and swift, decisive action. While DSL business continues to grow strongly, volumes in the Internet narrowband sector are still dwindling. There is a clear shift taking place here in customers' Internet access preferences. The booming broadband business is also affecting traditional fixed-line telephony, as are the continually falling tariffs for mobile telephony, which are getting ever closer to call charges in the fixed-line sector. Meanwhile, in mobile telephony, service providers are losing market share above all to smaller, very competitive carriers and discounters. Therefore, it is hardly surprising that Federal Network Agency estimates indicate that revenues may well have dropped in 2007 among all competing companies – for the first time since the liberalisation of telecommunications began in the 1990s.

Even in such a difficult market environment, freenet once again looks back on a successful business year. Despite restrictions on our operations inflicted from outside the company, we showed a customer growth in the four most important of six trading areas, i.e. in mobile telephony, broadband, portal business and hosting. In B2B services we also came close to the excellent results of the previous year. We largely achieved our goals for 2007:

- Turnover declined slightly to €1.86 billion. In addition to the negative general market trends alluded to above, this figure is also affected by changes in accounting principles that, while showing lower sales, tend to result in rising gross yields and pre-tax profits.
- Despite continued high marketing expenditure and similarly substantial consultants' costs regarding a possible sale of freenet, our results have improved significantly – with gross profits of €582.4 million, EBITDA of €252.8 million and pre-tax profits of €163.3 million.
- To the benefit of our shareholders, we improved our capital structure in summer and distributed a total of €576 million in dividends, equating to a dividend of €6 per share.
- With just under 1.3 million DSL customers at the year-end, we kept our market share steady in this sector despite annoying processing problems and delays on the part of Deutsche Telekom AG in connecting "complete-package" customers.
- Even though the market for mobile telephony is becoming increasingly saturated, with a penetration level now of over 110%, we were able to increase customer numbers in this area to 5.7 million.
- With total customers numbers now at 11.7 million – including 6.5 million fixed contract customers – we continue to rank as one of Germany's leading telecommunications groups and as one of the two biggest network-independent providers of telecommunications services.

With growth rates generally declining and some markets saturated or on a downward trend, this strong customer base is increasingly gaining in strategic value. One of freenet's main objectives for the current year must and will therefore be to further cement and develop our customer base.

We have already made some key moves to this end. Late last summer, for instance, we signed a contract to cooperate with ElectronicPartner, a leading group of around 3,000 service-oriented specialist retailers, large-scale superstores and professional IT vendors. Since the start of the year, ElectronicPartner has significantly strengthened our sales channels by selling our DSL, bundled and mobile telephony products, plus our mobile Internet solutions. Our network of franchise shops, concessions and own stores has also been increased to 375 in recent months and quarters, while since the turn of the year our DSL convergence product "freenet*Komplett*" has been available in 900 cities and metropolitan areas. The year also brought excellent results once again in a wide range of tests run by the independent trade press – i.e. best portal site, web hosting company as well as very good rankings for our DSL- and DSL bundled products – which supported our multifaceted sales activities.

To more effectively manage our company's growth in the future and to improve our strategic flexibility, we are currently evaluating the formation of a holding group structure. Key steps in this process would include spinning off the DSL and portal operations into subsidiaries. A new segmentation into mobile telephony, broadband, portal business, hosting, B2B services and narrowband will give us maximum transparency in these areas of our business, which are at different stages in their lifecycle and thus require individual, targeted management.

Against this background – the company's outstanding market position, a highly motivated team at our six sites in Germany and the management's great experience and expertise – we are confident that we will be able to write the next chapter in freenet's success story in 2008!

Eckhard Spoerr

Axel Krieger

Stephan Esch

Eric Berger

2. Group management report

2. Group management report

Important note:

This group management report (management report) should be read in context with the group's audited financial data and appendices.

This report includes statements looking into the future, i.e. statements that are based not on historic facts but on current plans, assumptions and estimates. Forward-looking statements are valid only at the time that they are made. freenet AG accepts no obligation to modify these in the event that new information comes to light. Statements about the future are by their nature subject to risks and uncertainty. We therefore explicitly point out that a range of factors may influence actual results to such effect that they then differ appreciably from those forecast. Some of these factors are described in the "Risk Reporting" section and in other parts of this report.

2.1 Group structure

In the group management report for the 2006 financial year, we addressed the fact that the final significant change to the group structure in connection with the merger of mobilcom AG and freenet.de AG into telunico holding AG, renamed freenet AG in the meantime, was taking place. As a result of this merger, which became effective with its entry into the commercial registry on 2nd March 2007, freenet AG has taken the position of group parent company. Prior to this, MobilCom Holding GmbH had merged into mobilcom AG, thereby removing the intermediate holding company level from the group structure.

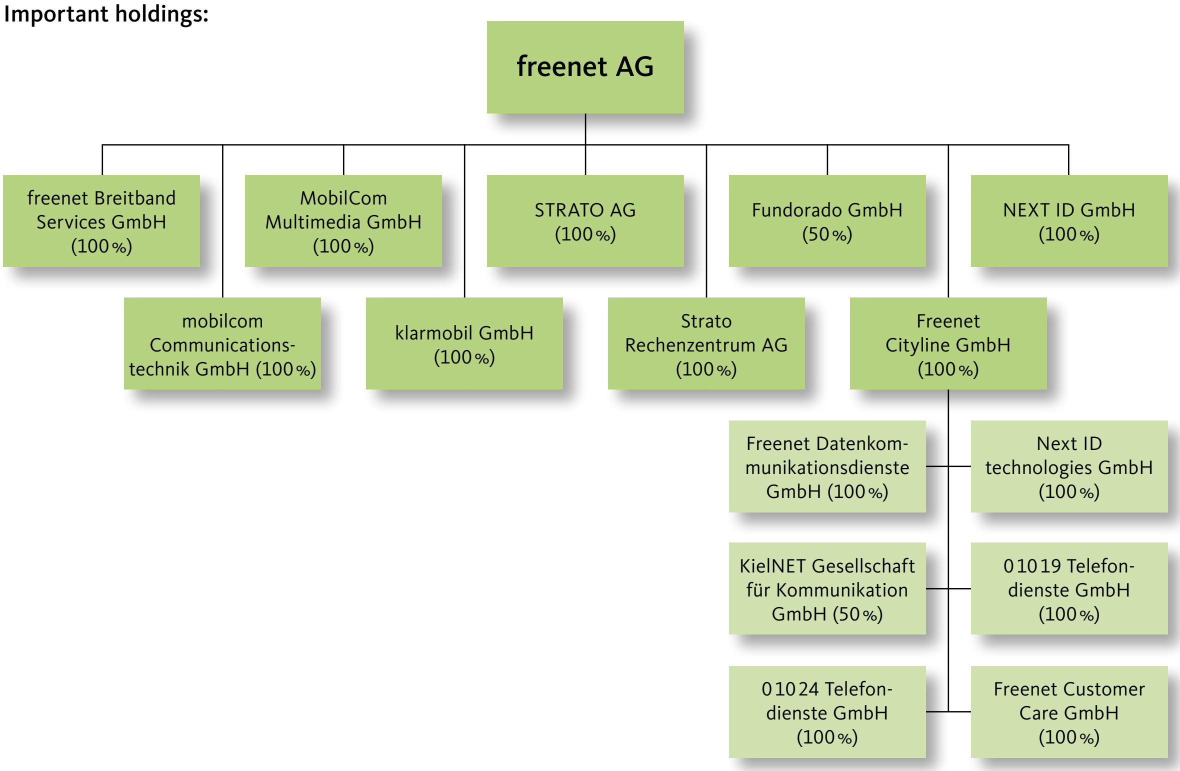
freenet AG's subscribed capital (ordinary share capital) is € 96,061,016, split into the same number of no-par-value shares in the name of holders. Each share carries the same rights, including one vote per share at general meetings.

The company has two shareholders with a direct or indirect interest in over 10 percent of the equity. These are Drillisch AG with a share of 25.24 percent of the ordinary share capital (24.51 percent via MSP Holding GmbH) and Mr. Robert Hersov (via Vatas International B.V.) with a share of 22.10 percent.

The process of appointment and removal of members of the freenet AG executive board is based on Clauses 84 and 85 of the German Companies Act (AktG) and Clause 31 of the Co-Determination Act (MitbestG) in conjunction with Clause 5, paragraph 1 of the company's Articles of Association. The definitive provisions for making any change to the Articles of Association are Clauses 133 and 179 of the German Companies Act and Clause 16, paragraph 1 of the Articles of freenet AG.

In accordance with Clause 4, paragraph 6 of the Articles of Association, and with the consent of the supervisory board, the executive board is authorised to issue 48,030,508 shares (2005 authorised share capital) not later than 18th August 2010. In accordance with the resolution of the Extraordinary General Meeting on 20th February 2007, the executive board is also authorised, with the consent of the supervisory board, to purchase, sell or call in shares in the company up to a total of 10 percent of the ordinary share capital.

Important holdings:



2.2 Overview of business trends in the freenet Group

freenet Group business trends

During the last business year, the paradigm change in the German Internet and telecommunications market continued and picked up speed. One characteristic of this was further growth of the broadband market, where very competitively priced bundled packages with DSL Internet access, DSL telephony and mobile telephony are increasingly being offered. On the other side of the coin, the industry is recording falling volumes in the high-margin areas of Internet narrowband access and traditional fixed-line telephony. Overall, service providers are also losing some market share in the mobile telephony sector to very competitive smaller carriers. Apart from this, the mobile telephony discount sector, which is populated by mobile service providers and various carrier brands as well as standalone discount vendors, shows high growth rates. The Federal Network Agency predicts falling revenues across the telecommunications market in 2007, for the first time since the market's liberalisation.

With competitive products and services, freenet AG is well positioned in the growth markets of broadband, portals and hosting, has been able to add significant customer numbers in mobile telephony, and has managed to maintain the previous year's good revenues in B2B services. At the same time, however, the company was affected by the downward trends in what were once its most important business areas: Internet narrowband access and fixed-line telephony. This trend is reflected in the figures for the past fiscal year. Group turnover fell by 9.3 percent year on year to € 1.86 billion, of which € 473.9 million was generated in the fourth quarter – a decline of 10.6 percent compared to the same quarter of 2006, but a slight improvement on the prior quarter's level of € 470.0 million.

In considering this drop in revenue it should be borne in mind that the way in which customer acquisition costs have been accounted for has changed, largely since the start of 2007. Having implemented new database structures which record the profitability of individual customer contracts, freenet now fulfils the requirement for obligatory capitalisation of elements of customer acquisition costs under IAS 38. As a result, there are lower sales to report, while at the same time gross profits and pre-tax profits increased year on year. Therefore, only limited direct comparisons with last year's figures are possible.

Gross profits therefore rose by 25.0 percent compared with the previous year, to € 582.4 million. € 146.1 million of this was generated in the fourth quarter – a rise of 6.6 percent on the previous quarter and of 29.9 percent compared to Q4/2006.

EBITDA rose to € 252.8 million – an increase of 71.9 percent compared to 2006 (€ 147.0 million). At € 56.5 million, fourth-quarter EBITDA was more than twice the € 24.8 million seen in 2006. EBIT rose by more than 50 percent to € 156.6 million. Compared to the previous year's figure, this reflects write-downs totalling nearly € 53 million, which came into effect due to the aforementioned mandatory capitalisation of elements of customer acquisition costs.

On the other hand, group operating profit for 2007 fell by 93.6 percent to € 16.5 million. This marked decline is explained primarily by the fact that the tax loss carryforwards resulting from the merger of freenet.de AG with mobilcom AG were first-time usable throughout the group in 2006. By contrast, in 2007 there were significant tax charges, from changes in the tax rate and from value adjustments to deferred income tax assets for loss carryforwards. The background to these effects from tax rate changes is the change in tax legislation effective from 1st January 2008 and the associated adjustment of the group's rate of tax for accounting for deferrals and accruals of tax liabilities. What is actually a positive reform of corporate taxation for the company has thus led in 2007 to a significant, one-off negative effect on group results. No actual outflow of liquid assets actually took place as a result of this accounting procedure.

Having distributed € 576 million to shareholders in the course of improving the capital structure in summer 2007, freenet AG's net cash and cash equivalents have dropped to minus € 36.4 million.

As at 31st December 2007 the group employed 3,838 employees including temporary staff (31st December 2006: 3,646). The average number of staff within the group during 2007 was 3,749 (previous year: 3,630). The new hires primarily serve to strengthen our sales and customer support operations, thereby forming a strong basis for freenet's future growth.

Locations:
Hamburg (left) and
Büdelsdorf (right)

Business performance by sector

With continual customer growth especially in the two high-sales sectors mobile telephony and broadband, increasing turnover on hosting and e-commerce/advertising in portal business and ongoing high revenues from B2B services, freenet AG is well positioned at this time of paradigm change in the Internet and telecommunications market. The group is successfully compensating for the market-wide downturn in its previous key business areas of narrowband access and fixed-line telephony (call-by-call and preselection) – now united in the narrowband division.

Mobile telephony

Since the introduction of liberalised mobile telephony at the start of the 1990s, this market has grown non-stop in Germany. According to Federal Network Agency figures, penetration passed the level of 110 percent by the middle of 2007. As a statistical average there is thus already more than one mobile telephony contract or mobile phone for every citizen, and estimates for the turn of the year 2007/08 assume around 96 million subscribers on the individual mobile phone networks. Already, one in ten German households are doing without a traditional fixed line connection and relying purely on mobiles for their telephone calls.

In the process, subscriber market shares have continued to shift in favour of the smaller network operators and, in particular, the mobile telephony discounters. And yet, despite increases in absolute numbers, the market shares of the service providers are on a slight downward trend, dropping now to below 25 percent. The experts at Forrester Research see new impetus for growth mainly in the area of mobile Internet, and are forecasting that in the year 2010, one in every two mobile telephony subscribers will be using mobile Internet services.

Immediately after the completion of the merger, freenet addressed this market segment with a number of new products. To coincide with CeBIT 2007, freenet then became the first provider in Germany to offer a genuine mobile phone flat rate, which covers all domestic calls to German mobile phone networks and to the national landline network for one fixed monthly price. The Full Range tariffs from “freenet*Mobile*” were also launched at this time with five package-price tariffs. freenet also presented an innovative milestone in terms of bundling mobile telephony and Internet serv-

Right:
At CeBIT 2007 freenet launched the flatrate tariff „freenet*Mobile* Mail & Surf“ including the high end smartphone Blackberry® Pearl™

ices in the form of “freenet*Mobile* Mail & Surf”. Via the BlackBerry® Pearl™ smartphone, this allows unlimited online surfing, management of freenet e-mails and standard telephone calls, all without any expensive data tariffs. In July, we then launched a value-for-money offensive based on the “freenet*Komplett*” product. This package of DSL and VoIP telephony was enhanced by adding in a mobile service which allows mobile calls at competitive rates with no basic fee or minimum charge.

During the course of the year, freenet was consequently able to increase its number of mobile telephony customers significantly – by nearly 12 percent, from 5.1 million at the start of 2007 to 5.7 million by the end of December. 260,000 of these were added in the fourth quarter. Contract customers, now numbering around 3 million, and pre-paid customers, at 2.7 million, both contributed to this growth. freenet was thus able to maintain its market share in mobile telephony. The success of klarmobil.de as a service-oriented discount offering made a not insignificant contribution to this.

Falling call charges and the previously mentioned mandatory capitalisation of elements of customer acquisition costs under IAS 38 resulted in lower revenues, yet increased gross yields and pre-tax operating profits year on year. Turnover in this sector declined by 11.0 percent year on year to € 1.18 billion, of which € 301.0 million was generated in the fourth quarter – a drop of 0.3 percent compared to the previous quarter and of 13.7 percent compared to the fourth quarter of 2006. Mobile telephony remains freenet AG’s strongest area of business in terms of revenue.

Gross profits went up considerably, rising year on year by 51.6 percent from € 191.0 million in 2006 to € 289.5 million in 2007, which translates to a 24.4 percent margin. € 81 million of the gross profits was produced in the fourth quarter, compared to € 44.5 million in the fourth quarter of 2006. The gross profits margin for full year in 2006 was 14.3 percent.

Broadband

Demand for broadband connections in Germany continues undiminished. As at the turn of the year 2007/08, the Federal Network Agency pegged the number of connections in Germany at close to 20 million. At around 95 percent, DSL continues to be the dominant connection technology, even if alternative channels, such as TV cables, have also increased slightly in importance recently. Growth rates will decline

slightly in the years ahead, but will remain in the double digits.

In the 2007 business year, the group acquired two new holdings whose business can mainly be assigned to the broadband segment: freenet Breitband Services GmbH and freenet Zugangsdienste GmbH.

The group has significant ongoing contracts with two suppliers with respect to purchasing broadband hardware for end customers.

During the course of 2007, freenet has further improved its positioning and competitiveness in the DSL market by bringing out new and attractive products. The telephony line including DSL “freenet*Komplett*” has, for example, been continually enhanced with a range of features, such as free, personally configurable voicemail, special numbers and around 240 international destinations. Then, for pure DSL connections, we brought in highly affordable flat-rate packages with additional speed options. At the same time, the availability of “freenet*Komplett*” also increased, reaching 900 cities across Germany by the end of 2007.

The number of DSL customers also increased over the course of the year, going up by 280,000 to 1.28 million by the end of December. This was achieved despite interruptions and delays in Deutsche Telekom AG's processing and switch-over procedures, especially in the 2nd half of the year, which significantly impeded freenet's growth and also led to a not insignificant number of cancellations by new customers. According to information provided in early February by the Association of Providers of Telecommunications and Value-Added Services (VATM), over 100,000 customers were waiting, in some cases for months, for their transfer away from Deutsche Telekom to a rival provider, because the former state-run business was failing to switch over connections promptly.

Broadband revenues increased by 39.6 percent, rising from €195.1 million in 2006 to €272.3 million in 2007. €77.4 million of this was generated in the fourth quarter – a rise of 43.8 percent compared to the same quarter of 2006 and an increase of €5.2 million on the previous quarter. Over the year, DSL thus developed into freenet's second-largest source of revenue. Gross profits also rose significantly, from €2.2 million in 2006 to €67.6 million in 2007, mainly due to the capitalisation of customer acquisition costs.. The fourth quarter produced earnings of €14.9 million, a €14.0 million increase on the same quarter in 2006. The gross profits margin for 2007 rose to 24.8 percent, having been 1.2 percent the previous year.

Portal business

The portal segment of freenet AG's business covers e-commerce/advertising and paid services. The ever-growing online advertising "pie" is being split between increasing numbers of websites, with the majority of advertising expenditure going to the large Internet portals.

In terms of e-commerce and advertising, freenet markets a variety of websites, including, for example, freenet.de, 4players.de, aktiencheck.de and fundorado. de. Using the surfing patterns of its anonymised users, freenet is able to offer advertisers "affinity profiles" for better-targeted advertising on these sites. This benefits everyone involved: the advertising industry is able to address its target groups more precisely, and users get information tailored to their particular interests.

In order to make its portal sites even more attractive, freenet further expanded and enhanced its all-round online offering during the last fiscal year. Particular attention was paid to the relaunch of the new, highly modern and user-friendly freenet.de site, the singles site and the launch of the mobile portal.

The mobile portal's main content, which is available without any manual settings to 4,000 mobile handsets from practically every manufacturer, initially included current news, a live sports ticker, share prices, TV and cinema listings and weather forecasts. During the further course of the year, heavily used services, such as Google, Wikipedia, ebay, Deutsche Bahn (German Rail) and the "The Örtliche" (White Pages) telephone directory were integrated into the mobile portal. Other features, such as freenet's dating and push e-mail services, are now also integrated in the portal. Furthermore, the company introduced a push e-mail service for consumers that pushes e-mails to BlackBerry's mobile devices in real-time and at flat-rate prices.

So sales and earnings from e-commerce and ad sales, as well as from paid services rose once again in 2007. However, as a result of a strong drop in inter-segment revenues and earnings from mobile phone marketing compared with 2006, the overall figures in the portal business have declined.

Accordingly, portal revenues dropped year on year, and are down by 10.7 percent to €56.7 million. Of this, €15.9 million was attributable to the fourth quarter – after €12.4 million in the prior quarter and €20.5 in Q4/2006. Gross yield for the segment including inter-segment settlements dropped to €40.7 million in 2007 from €50.7 million in 2006. Gross profits in Q4/2007 rose to €11.3 million after €8.4 million in the previous quarter, and declined by €4.9 million compared with Q4/2006.

The gross profits margin in this line of business was at over 70 percent both for all of 2007 and for Q4/2007.

Hosting

The web hosting division at freenet is covered by STRATO AG, which has been 100 percent owned by the group since the start of 2005. With an estimated market share of around 25 percent, STRATO is the number two in both the German and the European web hosting market. In the course of the business year, the company launched numerous new products and features on all matters related to publishing your own website. In addition to a new website builder, these included a video solution as a high-quality alternative to Youtube, and an initiative for mobile websites.

In 2007, STRATO also tapped new lines of business serving SMEs and in the field of "software as a service". The company launched a new version of the successful hosted web shop for small and medium-sized businesses, with new cross-selling functions and a complete order management system, including payment processing. Numerous other innovations, such as a high-quality security package, also further enhanced the fast-growing area of dedicated and virtual servers. Working in close partnership with Microsoft and Oracle, STRATO also made use of the high technical quality of its computing centre to expand the product portfolio by adding professionally hosted standard solutions for the SME market.

This Berlin-based freenet subsidiary has operations abroad in France, Spain, Great Britain, Italy and Holland, where it is able to gain new customers for its full-range web-hosting solutions without any capital expenditure on equipment. In the target markets Spain and Holland, STRATO managed to achieve double-digit percentage gains purely through organic growth. The success of its product strategy is incidentally underscored by countless prizes and awards won both in Germany and abroad. STRATO was, for instance, crowned Europe's best web-hosting company for Microsoft solutions in the Europe/Middle East/Africa region. In the January 2008 issue of trade journal "PC Praxis", STRATO also won "Web-Hosting Company of the Year", the foremost readers' award for web hosting in Germany.

Finally, STRATO really hit the headlines at the end of 2007 with the award of the "Berlin Environmental Prize" from Friends of the Earth Germany (BUND). The award recognised the company's commitment and pioneering role in matters of climate protection. Over the past year and a half, STRATO has achieved energy savings of 30 percent per customer. Since the start of 2008, the company's high-performance computing centre has been completely CO_2-neutral through the use of regenerative power. On an annual basis, this saves around 15,000 tons of carbon dioxide – at no additional cost to the customer. STRATO's environmental efforts are becoming an international model for the entire industry.

The trend in STRATO's numbers during the 2007 fiscal year has also been exemplary. Customer numbers increased by 14.5 percent, and the number of hosted domains by more than 3.5 million. Turnover rose to €79.4 million and gross profits to €65.5 million – a year-on-year rise of 15 and 20 percent respectively. Of this, €21.4 million of turnover and €15.6 million in gross profits were generated during the fourth quarter – again up a good 18 percent in terms of turnover and 9 percent in terms of gross profits compared with Q4/2006. Gross profits margins were around 80 percent both for the entire fiscal year of 2007 and for the fourth quarter.

B2B services

freenet's work in this field is primarily borne by group subsidiary NEXT-ID, one of the leading providers of interactive communications solutions for all things related to premium rate and other special phone numbers, mobile services and new media in Germany. With headquarters in Bonn and Hamburg, the company can avail itself of one of Germany's most powerful intelligent networks and possesses one of the country's largest audiotex platforms. Based on these, NEXT-ID develops innovative ideas for value-added services for mobile and fixed-line telephony and the Internet. The company's clients include major media players, brand-name manufacturers, call centre operators and entertainment businesses. NEXT-ID handles a large proportion of all calls for German interactive TV and radio programmes.

During the past fiscal year, NEXT-ID underpinned its strong market position with a series of important new contracts and rigorous diversification of the company's client portfolio. In the media field, for example, in addition to more intensive collaboration in the TV sector, NEXT-ID entered into an important strategic partnership with a leading provider of phone-in formats in the radio market. The aim of the company's media involvement is to extend the value chain in this sector and to continually evolve its interactive added-value services by creatively integrating voice, mobile and content applications.

This positioning helped NEXT-ID to contribute the lion's share of the group's B2B turnover last year. In addition to this came revenues from freenet Datenkom-

Server room of STRATO

munikations GmbH, which offers a variety of services to business clients, including the networking of premises across Germany, the integrating of field staff with company headquarters, and VPN networking of company clients via dedicated servers. Despite further legal restrictions on interactive TV and radio formats coming into force in NEXT-ID's field of business in the third quarter of 2007, revenues for B2B services were, at € 134.9 million, close to the high level of the previous year. € 33.4 million was accrued in the fourth quarter, almost exactly the level of the previous quarter, and an 11.7 percent decline compared to Q4/2006.

Gross profits, on the other hand, saw a year-on-year improvement, rising from € 28.4 million to € 31.2 million, which equates to a gross profits margin of 23.1 percent for the year 2007.

Narrowband

Traditional fixed-line telephony and narrowband Internet access, i.e. the segments that used to be the "old" freenet.de AG's best areas of business in terms of turnover, continued their market-wide downward trend last year, being increasingly replaced by DSL telephony, mobile telephony and DSL. As a result, the providers in this market saw their connection volumes go down once again in 2007, both for national and international calls.

freenet, too, is affected by this downward trend across the market, although the company's very attractive tariffs and terms keep it very well positioned within this sub-sector. Over the course of 2007, the number of active Internet narrowband customers fell by around 900,000, while the number of customers in fixed-line telephony dropped by nearly 1.2 million.

Turnover in this area is accordingly on the decline, falling by 47.0 percent in 2007, from € 281.7 million to € 149.3 million. € 27.8 million was the figure for the fourth quarter, after € 59.5 million in the same quarter of 2006 and € 33.9 million in the prior quarter. Gross profits in this area are also falling significantly, and are now at € 88.9 million after € 145.4 million in 2006, a drop of 38.9 percent. 18.8 percent of gross profits was generated in Q4/2007, a fall of 49.9 percent compared to Q4/2006. Meanwhile, at 59.5 percent, the gross profits margin showed a year-on-year improvement of nearly 8 percentage points.

In 2007 the mobile portal of freenet was launched

New freenet products

In **mobile telephony**, freenet became the first provider in Germany to offer a genuine mobile phone flat rate, which covers all domestic calls to German mobile phone networks and to the national landline network for one fixed price. Launched at the same time, coinciding with CeBIT 2007, were the Full Range tariffs from “freenet*Mobile*”, with five tariffs at all-in prices. In addition to these, “freenet*Mobile* Mail & Surf” also represented an innovative milestone in terms of bundling mobile telephony and Internet services. Via the BlackBerry® Pearl™ smartphone, this allows unlimited online surfing, management of freenet e-mails and standard telephone calls, all without any expensive data tariffs.

On the **broadband** front, freenet added several new features to its “freenet*Komplett*” broadband Internet/telephony product during 2007. These included personally configurable voicemail, special numbers and around 240 international destinations. For pure DSL connections, we also began selling highly affordable flat-rate packages with additional speed options.

The major new initiatives in our **portal business** during 2007 were the relaunch of the new, highly modern and user-friendly freenet.de portal, the single website and the launch of our mobile portal. Over the course of the past year, the company also further expanded and enhanced its all-round online offering, including, for instance, freenet.de, 4players.de, aktiencheck.de and fundorado.de.

The numerous new products launched in the field of **hosting** included a new website builder, a video solution as a high quality alternative to Youtube, and an initiative for mobile websites. The company also launched a new version of the successful hosted web shop for small and medium-sized businesses, with new cross-selling functions and a complete order management system including payment processing. Working in close partnership with Microsoft and Oracle, we also further developed professionally hosted standard solutions for the SME market.

Significant events at the freenet Group in 2007

- On **2nd March 2007** the merging of freenet.de AG and mobilcom AG into the freenet AG was officially entered in the commercial registry.
- Coinciding with **CeBIT 2007** – also in March – the new freenet AG corporate branding was unveiled and “freenet*Mobile*” and the mobile portal were launched. At the same time, the company enhanced its “freenet*Komplett*” offering with the addition of a low-cost mobile telephony component, making freenet now also a mobile telephony provider.
- In **April**, Professor Doctor Helmut Thoma was elected chairman of the freenet AG supervisory board.
- In **May**, sizable shareholder TPG sold its holding to the Vatas Group. Mr Eric Berger joined the freenet AG executive board.
- In **June**, freenet launched its market offensive in all areas related to the mobile Internet. At the same time, several large shareholders issued their first calls for the company to be broken up. freenet than engaged the investment bank Morgan Stanley to provide support for assessing appropriate strategic options (strategic review process).
- The freenet AG annual general meeting on **20th July 2007** approved the distribution of an ordinary and a special dividend, together amounting to 6 euros per share.
- In **August**, Drillisch AG, a mobile telephony rival, announced that it holds a purchase option over the Vatas shareholding.
- In **September**, ElectronicPartner and freenet announced a strategic partnership for the sale of freenet products.
- freenet, Drillisch and United Internet hold discussions in the autumn concerning a strategic partnership; the discussions are broken off without success at the end of **November**.
- In December, the strategic review process was concluded as well. freenet announced the continuation of the market strategy begun with the merger and with this in mind reviews the implementation of a holding structure for the company.

2.3 Group earnings, assets and financial position

Group earnings, assets and financial position

The merger of mobilcom AG and freenet.de AG to form freenet AG became effective by registration in the Register of Companies on 2nd March 2007. mobilcom AG and freenet.de AG thus no longer exist. Since this date, the two companies' previous shareholders have been shareholders of the new group parent company, freenet AG. The group assets and liabilities of the previous group parent company, mobilcom AG, were transferred upon the merger contract coming into effect to freenet AG. These consolidated financial statements can be fully compared with those of the previous year, as the merger process caused no changes in the areas of business that the consolidated report covers.

Key items of the consolidated financial statements

Sales revenues fell back in the fiscal year 2007 by 9.3 percent to € 1,863.3 million. However, this figure cannot be wholly compared with that of the previous year due to the following two facts: having begun to capitalise elements of customer acquisition costs for the "freenet*Komplett*" product from the 4th quarter of 2006, the company fulfilled the IAS 38 capitalisation requirements for contract customers in further significant product areas as of the first quarter of 2007. In connection with the period-based accruing of customer acquisition costs over the minimum term of customer contracts a number of revenue items relating to contract customers – primarily the connection bonuses on mobile telephony business due on contract signature from the network operators – could no longer be shown as immediate sales receipts. As of the first quarter of 2007, an appropriate accrual for these revenue items had instead to be made on the liabilities side. This is one significant reason for the drop of € 145.7 million in mobile telephony external revenue compared to the previous year. The level of consumer prices, which fell in 2007, also depressed sales revenues in this area.

In the third quarter of 2006 freenet.de AG had entered into a DSL wholesale contract with Deutsche Telekom AG in Bonn (DTAG), which superseded the DSL resale contract that had applied until then. The terms of the DSL wholesale contract have applied since 23rd May 2006. Compared to the DSL resale contract it no longer includes any accounting for bonuses for signing up new customers, which had previously been shown as revenue. On the other hand, one-off provisioning and the monthly transfer of connections are now purchased on more favourable terms with a corresponding impact on total expenditure for bought-in services. Despite the overall effect of this, the company was able to record revenues up € 77.2 million year on year thanks to increased customer numbers. This compensates in part for the significantly lower turnover from narrowband business, which fell by € 132.4 million.

Purchase expenditure reduced to € 1,280.9 million (2006: € 1,589.0 million). It was this that primarily led to an increase of € 116.6 million in the gross profit, which rose to € 582.4 million (2006: € 465.8 million). The total gross profit margin increased by 8.6 percentage points to 31.3 percent (2006: 22.7 percent). This reduction in material expenditure is connected mainly with the capitalisation of customer acquisition costs.

The average number of employees in the group rose compared to the previous year by 3.3 percent from 3,630 to 3,749. At € 134.6 million, the company was nevertheless able to show a 0.9 percent reduction in staffing costs. Of this figure, costs dependent on changes in the share price amounted during the fiscal year to € 11.0 million (prior year: € 8.7 million).

With other operating costs almost unchanged year on year, the company recorded an EBITDA in 2007 of € 252.8 million, exceeding the EBITDA of € 147.0 million achieved in the previous year by nearly 72 percent. The capitalisation of customer acquisition costs had the effect of increasing the 2007 EBITDA by € 147.8 million (prior year: € 7.3 million). If these figures are calculated out, it shows a year-on-year reduction in the EBITDA of € 34.7 million. This drop is largely caused by the fact that the fall in profits in the declining narrowband business was not made up for by profit improvement in other areas.

At € 96.2 million, depreciation is shown € 52.3 million higher than the previous year. Taking out the effect of depreciating capitalised customer acquisition costs of € 52.6 million (prior year: € 0.3 million), the level of depreciation has not changed year on year.

Group operating profit for the fiscal year 2007 amounted to € 16.5 million, having been € 257.0 million in 2006. The explanation for € 223.7 million of this appreciable drop comes from the deferred tax asset on carried forward losses. While in the fiscal year 2006 accounting for the first time since the merger of freenet.de AG and mobilcom AG to freenet AG for group-wide utilisation of carried forward tax losses had led to a clear increase in the group operating profit, the deferred tax asset for such losses was adjusted in 2007.

There were also tax charges in 2007 of around € 35 million arising from tax-rate changes. The background to this is the change in tax legislation effective from 1st January 2008 and the associated adjustment of the group's rate of tax for accounting for deferrals and accruals of tax liabilities.

As at 31st December 2007 the group's balance sheet assets totalled € 902.6 million, thus being € 393.0 million less than the total balance sheet assets at the end of the previous year (31st December 2006: € 1,295.6 million).

Long-term assets rose by 14.8 percent to € 533.3million (31st December 2006: € 464.4 million). This increase results largely from the capitalisation of customer acquisition costs, which leads to intangible assets rising to € 297.6 million (31st December 2006: € 103.7 million). Counteracting this was the 70.4 percent change in deferred claims in respect of tax on profits, which fell to € 52.3 million (31st December: € 176.7 million). For the one part, an adjustment had to be made in 2007 to the deferred tax asset for carried forward losses. For another, deferred claims in respect of tax on profits went down due to the change in the group's tax rate as a result of the 2008 corporation tax reform.

Short-term assets reduced by 55.6 percent to € 369.3 million (31st December 2006: € 831.2 million), which is largely attributable to the drop in liquid assets. These fell by 90 percent to € 53.7 million (31st December 2006: € 535.3 million), caused in the main by the dividend distribution in 2007 in the sum of € 576.1 million. The increase in long-term assets was more than compensated for by the fall in short-term assets, leading to an overall reduction in the total balance sheet assets.

The lower total for balance sheet liabilities comes largely from the reduction in share capital. As at 31st December 2007 group equity stood at € 372.1 million (31st December 2006: € 933.4 million). This drop of € 561.3 million results from the distribution of € 576.1 million in dividends and the achievement of a group annual net profit of € 16.5 million.

The equity-to-assets ratio thus fell to 41.2 percent, having been 72.0 percent at the end of the previous year. Long-term liabilities rose by € 28.9 million to € 39.3 million (31st December 2006: € 10.4 million). The increase results overwhelmingly from the accruals in connection with changed recording of customer acquisition costs. Short-term liabilities are made up predominantly of other payables (€ 280.5 million), trade payables (€ 103.0 million), borrowings (€ 90.3 million) and provision for other liabilities and charges (€ 15.4 million). The increase in short-term liabilities of € 139.4 million is due largely to the rise of € 90.2 million in finance debt – these bank liabilities were in turn taken on in connection with the financing of the dividend distribution.

In fiscal year 2007 the group generated cash flow from operating activities of € 285.1 million (2006: € 144.8 million).

Starting from a pre-tax profit (EBT) up € 46.1 million to € 163.7 million, increased depreciation and amortisation of fixed assets (up € 52.3 million to € 96.2 million), connected largely with the capitalisation of customer acquisition costs, had a positive effect on the cash flow from operating activities. The significant increase in operational liabilities of € 104.9 million also plays a large part in the positive trend in the inflow of funds. Counter effects came largely from payments of income taxes (€ 42.2 million), the reduction in provisions (€ 17.7 million) and the increase in current assets (€ 12.8 million).

The outflow of funds from investing activities increased year on year by € 246.3 million to € 273.5 million.

Key factors in the significant increase in the outflow of funds were above all the investments in intangible assets, and here in particular the expenditure attributable to the asset item "Customer base/relationships" for customer retention and acquisition in the contract customer sectors (€ 236.1 million). Further investments were accounted for by fixed assets (€ 22.4 million).

Additional income attributable to investment activity, largely from interest (€ 13.4 million), did not change exceptionally during the fiscal year.

Cash flow from financing activities reduced year on year by € 668.0 million. The outflow of funds from the group attributable to such activity was € 583.5 million.

While the main feature of the previous year's positive cash flow of € 84.5 million was the sale of a bonded loan (€ 85.0 million), the outflow of funds in the 2007 fiscal year was determined largely by a dividend payment of € 576.1 million or € 6.00 per share. Other outgoing payments were largely interest (€ 4.7 million).

The following summary shows some of the Group's key operating figures:

In € 000's	**2007**	**2006**	**Change**
Turnover	1,863.3	2,054.8	–191.5
Gross earnings	582.4	465.8	116.6
EBITDA	252.8	147.0	105.8
EBIT	156.6	103.1	53.5
EBT	163.7	117.6	46.1
Group profit / loss	16.5	257.0	–240.5

2.4 Risk reporting

freenet AG's executive board has set up an appropriate system within the Group to detect risks early on, monitor them and manage them. In a manual for risk management within the Group, which is regularly revised and updated, the executive board has defined the key risks, drawn up a strategy on how to handle risk and documented the distribution of tasks and responsibilities within the Group's risk management system. This manual, with which all employees are familiar, has further developed a culture of risk awareness within the Group.

At the same time, a department in our Group's organisation structure is in charge of summarising, at regular intervals, the risk reports from the parent company's departments and the subsidiaries. These risk reports, which describe specific identified risks, the probability of their occurrence, and the implications should they occur, are submitted to the executive board for review and assessment.

The management has set up a comprehensive monthly reporting system to manage and monitor ongoing business operations that extends to both the financial and the non-financial performance indexes in the Group. The executive board is kept informed about operational developments in a timely manner at regular "jour-fixe" meetings, which are held for all relevant lines of business. Recent developments and future measures are also discussed at these jour-fixe meetings. The heads of the various corporate divisions are also in constant communication with the executive board, ensuring timely notification of risks to the appropriate decision makers at all times.

The system set up at freenet AG for early detection, monitoring and management of risks serves to detect business risks and opportunities at an early stage while also enabling the company to respond to them actively and effectively. The system complies with statutory requirements for an early risk-detection system and follows the principles of German Corporate Governance.

The risks

Of all of the risks identified in relation to the freenet Group, we elucidate below on those areas of risk/individual risks that seen from the current perspective could significantly affect freenet AG's earnings, assets and financial position.

Market and competition risks

As in the previous year, the pace of growth in DSL as the technology for accessing the Internet was again high in 2007. Growth in the telecommunications market as a whole, however, is limited. There is a risk that as market volumes shift (e.g. from fixed-line telephony to mobile and/or Internet telephony and from narrowband to DSL broadband Internet access) freenet may not be able to compensate for losses that may arise in market share and revenues in one area with gains in turnover in other areas of the market with positive rates of growth.

The strong competition in telecommunications markets can lead at any time to shortfalls in sales revenues, to loss of market share and to pressure on margins in any given business field and/or can make it more difficult to gain market share. Such competition also leads to ever-higher expenditure on new customer acquisition, while at the same time revenues fall and customers are increasingly prepared to switch. Should this trend continue or even grow stronger, this will have a negative impact on the company's earnings, assets and financial position.

freenet has set itself ambitious targets in terms of developing the customer base. Customer acquisition and retention are both significant cost centres in the mobile telephony service provider and Internet business. If these costs turn out to be higher than anticipated, this can lead to substantial deficits in freenet's operating profits.

During the last fiscal year, Deutsche Telekom AG began strongly marketing its new "Call & Surf" bundled tariffs. These, in the company's view, break industry regulations and by committing customers for 24 months may cause a closing-off and monopolisation of the broadband market and lead to the company not achieving those of its marketing aims based on its upstream "Wholesale DSL" product.

In addition to this, the risk also exists that Deutsche Telekom AG will continue to be unwilling or unable to switch over the required number of access lines needed by competitors in a timely manner. This may lead to the failure concerning the marketing of complete packages.

The success of the company's business strategy is dependent on the regulator quickly intervening against Deutsche Telekom's practices in relation to the activation of customers switching supplier and against their unfair tariff models. Failing this, these would have a long-term negative effect on the company's business. In sum, these risks can have a negative impact on the company's earnings, assets and financial position.

Margins in the mobile telephony service provider business are dependent on how the network operators structure their tariff models. Changes in such tariff models can have a negative effect on freenet AG's earnings, assets and financial position.

The mobile phone network operators are increasingly moving over to marketing their products themselves and to forcing mobile telephony service providers out of the market. Due to their business structure, mobile phone network operators are able to a degree to offer better rates than mobile telephony service providers. This can lead to a loss of sales channels and customers, and can thus have a negative impact on the company's earnings, assets and financial position.

The development of a discount market for mobile telephony products continues to increase the pressure on prices and margins in the German consumer market for mobile telephony services. Due to competitors starting to market bundled packages, further risk factors have emerged since early 2007. In addition to generally increased competition, some of freenet's competitors have also begun offering their fixed line and/or DSL products with extremely cheaply priced mobile telephony components, thus putting the market prices for bundled packages under substantial pressure. It has now become apparent that these offers were not one-off promotions, as bundles of this kind have established themselves as firm parts of our key competitors' DSL offerings. As it can no longer be anticipated that market prices for bundled products are going to rise again, the earnings prospects for such products are permanently impaired.

In the Webhosting sector, the group offers paid services to their customers. It cannot be ruled out that these services may be made available to customers free of charge by competitors at some point in the future. Should this be the case, a negative impact on the company's earnings, assets and financial situation may be expected.

The revenue potential and profitability of the company's portal business depends essentially on the trend in advertising income. Negative trends in the ad sales market would produce a negative effect on the company's earnings, assets and financial situation. In its business activity, freenet AG is subject to a wide variety of regulatory and statutory requirements, in particular regulations arising from the areas of data, customer and consumer protection. These are subject to rapid change, which is likely to lead to further requirements and financial burdens.

To consumers, the freenet brand stands for Internet and not mobile telephony. In the event of the shops being rebranded, this lack of perceived expertise in mobile telephony could lead to a more than short-term dip in sales performance.

In the mass volume business of a telecommunications company particular attention has to be paid to the creditworthiness of customers and sales partners.

It is, however, unavoidable that a certain percentage of debt cannot be collected. Were this percentage to increase, it would have a negative impact on the company's earnings, assets and financial position.

freenet receives commission from network operators for procuring customers. If freenet's sales channels are abused by fraudulent third parties, this can lead to the network operators clawing back this commission, which can have a negative impact on the company's earnings, assets and financial position.

Some sales partners regrettably fail to act in compliance with contractual terms. This can have a detrimental effect on the company's image. It can also lead to customer dissatisfaction and ultimately to customer attrition.

The strategic review process conducted up until the end of 2007 meant that many projects could no longer be carried out or have had to be significantly scaled back. These include, for example, shop rebranding, the integration of IT infrastructures and negotiations on new contract models with the network operators. This is making it more difficult to overcome the disadvantages arising from the delayed completion of the merger. This has a negative impact on the company's medium and long-term trading prospects.

Technical infrastructure

Maintaining the operational availability and efficiency of the technical infrastructure, including the company's computer centres and billing systems, is of major importance to business continuity. Network outages or service problems caused by system faults or failures can lead to the loss of customers and result in financial losses for the company. As freenet uses the services of some third parties, these risks are not fully within the company's control. It is also the case that if the network infrastructure dimensioning is too small, this can lead to customer attrition, while if it is too large, this can cause disadvantages in terms of cost. There is also a risk that the drop in narrowband Internet traffic will make the company's own network infrastructure less competitive.

Insofar as the alternative network operators are not willing or able to make adequate investments in their network infrastructure, in particular in order to increase its geographical coverage, this limitation in coverage is already leading to an inability to satisfy customer demand for certain freenet products. This has a negative impact on customer numbers, turnover and profits. In such cases freenet is working as closely as possible with the network operators to remove these risks.

TV and radio cable network operators are increasingly equipping their cable networks with return channel capability, making the existing cables suitable not only for receiving TV and radio signals, but also able to be used for Internet access and telephony. The cable network operators are thus increasingly entering into competition with freenet.

Future developments in DSL technology and/or alternative broadband technologies, in particular DTAG's VDSL network, UMTS, WiMax and WiFi, may lead to losses in market share due to new competitors entering the market. If freenet fails to gain access to these technologies, possibly because there is no regulated claim to such access, or is only able to gain this on what for freenet are uneconomic terms, this may result in further losses in market share. Even if freenet does gain access to these technologies, this may require substantial further investment, the return on which is uncertain.

It is further to be anticipated that Internet access offers via mobile wireless technology will be increasingly marketed over coming years. This too could have a negative impact on the market shares achievable in the long term and thus impair freenet's earnings prospects

Dependency on suppliers

In order to be able to make use of the company's telecommunications services freenet AG's customers need special consumer hardware. If there are delays in the company being supplied with this hardware, this can lead to customer attrition and have a negative impact on freenet's earnings, assets and financial position.

The company's telephony and Internet access products are to a large part based on provisioning services, which it buys from network operators such as DTAG and alternative network operators. Collection of the majority of customer receivables is also via DTAG. freenet is therefore dependent in many areas on DTAG's efficiency and commitment. As the dominant telecommunications provider in Germany, DTAG can thus exert considerable pressure on freenet in terms of price and margins in both the provisioning and consumer markets.

Tax risks

For assessment periods that have not yet been finally audited, tax arrears payments can in essence still arise if the fiscal authorities come to different interpretations of tax regulations or to different assessments of the underlying facts in any given case.

The fiscal authority is of the opinion that, in connection with the discounted mobile phones sold to end customers upon the signing or renewal of mobile carriage contracts, for these items accrued income should be charged, in the amount of the discount, and released over the customer's contract period. The company disagrees and immediately deducts such discounts from taxable income. In the event that the company does not prevail with its opinion, this would result in the payment of back taxes.

The risk of divergent interpretations of contexts and valuations applies in particular also to any restructuring of corporate legal status. It cannot therefore be totally ruled out that the carried forward tax losses declared by the freenet Group, and also so far assessed by the fiscal authorities, could be wholly or partially inapplicable – as per Clause 8, paragraph 4 and/or Clause 8c (as of 2008) of the Corporation Tax Act (KStG) and Clause 12, paragraph 3, of the Reorganisation Tax Act (UmwStG).

Financial risks

The bank liabilities shown under financial debts result from overdraft credits with varying rates of interest. Risks of non-payment exist in connection with trade receivables and other assets shown on the balance sheet. The non-payment risk consists of any unexpected loss of currency or income. Provisions were made in the balance sheet for expected losses. Should these provisions turn out not to be sufficient, this would have a negative impact on the company's earnings, assets and financial position. In the opinion of the company, other financial risks such as those relating to foreign currency, liquidity, refinancing, exchange rate changes or cash flow can be classed as immaterial and are not therefore required to be shown separately in this annual report. There is a detailed review of the individual financial risks at point 32 in the appendix.

Legal risks

Former shareholders of mobilcom AG and freenet.de AG have applied for a court review of the share exchange ratio applied in the merger of mobilcom AG and freenet.de AG into what is now freenet AG.

If the court decrees that the exchange ratio was inappropriate, there difference will be settled in cash. The cash adjustment will be paid to all affected shareholders, even if they were not one of the plaintiffs in the compensation claim. This would have a negative impact on the earnings, assets and financial situation.

It is, however, the company's assumption that the share swap ratio was appropriate and that there will be no cash adjustments, as the exchange ratio was carefully calculated and was audited and confirmed by the court-appointed merger auditors.

In November 2002, mobilcom AG, being the company's legal predecessor, and a number of other former mobilcom group companies entered into a compromise agreement with France Télécom and several associated companies. The validity of this compromise agreement is being challenged by a number of individual shareholders. The company considers the agreement to be valid and has no indication that France Télécom does not feel bound by it. However, were the view of these shareholders to be legally upheld, it should be anticipated that France Télécom will claim from the company the sum of €7.1 billion, which it waived as part of the agreement, and will contest the grounds and amounts of any counterclaims the company may make.

Some individual shareholders are of the view that the increase in November 2002 in the real capital of mobilcom AG, being the company's legal predecessor, was flawed and/or that the assets in kind brought in were no longer of any value, with the consequence that on the one hand the company would still be entitled to compensation claims against France Télécom running into billions and further that the shares issued to France Télécom would have had no voting rights.

It is the company's understanding that the increase in real capital was performed in a valid manner. The company therefore likewise assumes that this will also have no impact on the share evaluation review proceedings.

2.5 Executive board remuneration

In accordance with the supervisory board's procedural rules, executive board remuneration is set by the freenet AG supervisory board's human resources committee. The executive board's remuneration is performance related and is made up of three components: A fixed element, a success-dependent element and a long-term element with an appropriate incentivising effect.

Total remuneration for the fiscal year 2007 for members of the executive board of the company and of its predecessor companies was € 9,315 thousand (2006: € 8,288 thousand). Of this total figure, € 1,467 thousand or 15.7 percent was accounted for by the fixed element and € 7,848 thousand or 84.3 percent by variable elements.

As at 31st December 2007, the provisions for share options and share appreciation rights for the executive board stood at € 8,230 thousand (2006: € 10,416 thousand). In the fiscal year 2007, a total sum arising from share options and share appreciation rights of € 9,428 thousand (2006: € 2,863 thousand) went to members of the executive board.

No share options or share appreciation rights were issued to members of the company's executive board nor those of it predecessor companies during the 2007 fiscal year. In the previous year, 3.4 million share appreciation rights were issued to executive board members.

Remuneration provisions for the event of a board member ceasing to be employed

Pension

In November 2004, all members of the freenet.de AG executive board were given a direct assurance of a pension from freenet.de AG.

When their period of service ends, freenet AG executive board members have a right to the benefits set out at point 33 of the group appendix.

Premature cessation of employment

All mobilcom and freenet.de service contracts in existence prior to the point at which the merger became effective, transferred at that point to freenet AG. The old contracts, which continued to be legally valid, were replaced by new ones. With the exception of the level of remuneration, including the number of share appreciation rights, the new contracts were the same as the old ones, including in terms of benefits in the event of the employment (prematurely) ending. No right exists to claim compensation for loss of office if an executive board member is responsible him/herself for the (premature) ending of his/her service contract.

The individual benefits provided by the company's service contracts for the event of cessation of employment are as follows:

- The right to payment of salary and bonuses (based on the assumption of 100 percent achievement of targets) for the remaining period of the contract where by mutual agreement the service contract is ended or notice to end it is served within, in either case, twelve months of a change of control of the company.
- From their 60th birthday, members of the executive board receive a pension equivalent to 2.5 percent of their final annual fixed salary for each year or part thereof that they served on the company's executive board or on that of its legal predecessor, freenet.de AG, totalling in any case not more than one third of their final annual fixed salary (guaranteed pension).
- A widow/widower's pension for the member's spouse/partner and an orphan's pension for any children up to the end of their education or vocational training, at the latest in any case up until their 27th birthday, amounting in total to not more than the guaranteed pension.
- Share appreciation rights, which have already become exercisable due to the expiry of the relevant vesting period and the respective objectives being achieved, remain in force. In the event of a member's service contract being terminated due to a change in control, all share appreciation rights remain in force and can be exercised regardless of the vesting period if the other exercise conditions are met within twelve months and in any case by not later than the end of the term. In the event of a executive board member terminating his/her service contract for any other good cause or due to a complete reduction in earnings capacity or invalidity, or in the event of death, all share appreciation rights remain in force and can be exercised, subject to the other contractual conditions, within a period of twelve months from the end of employment, not later however than by the end of the term. Where such termination is due to good cause, the 12-month restriction does not apply.

There are no service contracts with any of freenet AG's subsidiaries.

For further information please see point 33 of the group appendix. This covers, in particular, information on levels of remuneration, holdings of share appreciation rights, share ownership and other sundry details.

2.6 Supplementary report

No events subject to reporting requirements arose after the accounting date.

2.7 Opportunities and prospects

Opportunities report

Following the termination at the end of 2007 of the review of strategic options related to a consolidation of and with freenet, the company is now concentrating rigorously on implementing the strategy pursued through the merger of being a universal supplier in all areas of DSL, mobile telephony, bundled products, mobile Internet and associated services. To this end, the company is evaluating the formation of a holding structure and spinning off the DSL and portal business into subsidiaries, so that in future we shall be able to control mobile telephony, broadband, portals, hosting, B2B and narrowband in the best way possible in their six respective markets.

With the strategic sales cooperation agreement entered into in autumn 2007 with ElectronicPartner, the further developed chain of freenet shops, an attractive customer-focussed product portfolio and a total customer figure of now 11.7 million, freenet is well placed for further growth in 2008.

Sales performance on DSL connections is currently better in those regions in which “freenet*Komplett*” connections are available than it is in other regions. Geographic expansion of network coverage will thus also bring with it the opportunity to increase sales performance on DSL business as a whole.

The Federal Network Agency has at the same time ordered that Deutsche Telekom AG has to offer a stand-alone bitstream product not packaged with a telephone connection. At present, the company can only market “freenet*Komplett*” in areas where our alternative network partners have appropriately developed their networks. Should the Federal Network Agency stipulate competitive terms for this product, then further marketing opportunities may arise for “freenet*Komplett*” from the additional network coverage.

This would also increase the opportunities to generate further growth with newly developed broadband-based products and services and with mobile Internet.

Prospects report

All of freenet’s areas of business – mobile telephony, broadband, portals, hosting, B2B and narrowband – continue to feature very intense competition in markets with differing rates of growth and in some cases also declining user numbers:

- In **mobile telephony** the slight drop in growth experienced by the traditional service providers is likely to continue – as is the pressure on prices and margins, which comes not least from the discount suppliers, though also from the network operators. The success of the discount suppliers, which include strongly growing freenet subsidiary klarmobil, is also likely to be maintained in 2008.
- In the area of **DSL** we anticipate slightly falling rates of market growth with extremely intense competition. With attractive offers and bundled DSL-based products, freenet is well positioned in this market segment. The company is, however, dependent on the actions of Deutsche Telekom AG in relation to the disruptions described above in processing and switching over customers changing provider. Whether freenet will be able to maintain or even grow its market share, depends to a great extent on how much this situation improves.
- The market related to **portal business** is also likely to profit in 2008 from the growth of DSL, which aids innovative forms of advertising and e-commerce. At the same time, increasing numbers of Internet users are prepared to pay appropriately for high quality content. The company intends to participate accordingly in the market growth in this area in 2008.
- Via subsidiary STRATO AG, freenet is very well positioned in **hosting** as the number 2 in the German market. New impetus for growth in 2008 is likely to come primarily from other parts of Europe, where STRATO has been active since 2006.
- freenet is also well positioned in the **B2B** market, likewise essentially via a subsidiary. Future business in this area is, however, dependent to a significant extent on further development in the general legal and regulatory conditions.
- In the area of **narrowband**, i.e. narrowband Internet access and fixed-line telephony, the market-wide fall in users and volume that has persisted for several years is also likely to continue in 2008

Thus, the business performance is characterised by sometimes opposite trends in the segments, which accordingly affects the group’s revenues und earnings.

Büdelsdorf, 28th February 2008
The Executive Board

3. Consolidated financial statements

3. Consolidated financial statements

3.1 Overview

3.2 Consolidated income statement for the period from 1 January to 31 December 2007

In €'000s	Note	2007	2006
Revenues	1	1,863,284	2,054,835
Other operating income	2	59,672	73,126
Other own work capitalised		571	677
Costs of materials	3	−1,280,890	−1,589,007
Personnel expenses	4	−134,567	−135,764
Depreciation and impairment write-downs	5	−96,187	−43,921
Other operating expenses	6	−256,393	−257,989
Operating result		**155,490**	**101,957**
Share of results of associates		1,075	1,146
Interest receivable and similar income	7	14,510	15,103
Interest payable and similar expenses	8	−7,369	−589
Result before taxes on income		**163,706**	**117,617**
Taxes on income	9	−147,176	139,390
Group result		**16,530**	**257,007**
Group result attributable to shareholders of freenet AG		16,149	218,526
Group result attributable to minority interest		381	38,481
Earnings per share (undiluted) in €	10	**0.17**	**3.50**
Earnings per share (diluted) in €	10	**0.17**	**3.50**

3.3 Consolidated balance sheet as of 31 December 2007

Assets in €'000s	Note	31.12.2007	31.12.2006
Non-current assets			
Intangible assets	11, 12, 13	297,596	103,722
Goodwill	11, 12	110,304	110,303
Property, plant and equipment	11, 12	60,809	61,054
Investments accounted for using the equity method	15	3,174	3,501
Other investments	16	304	304
Deferred income tax assets	17	52,303	176,652
Trade accounts receivable	19	1,410	920
Other receivables and other assets	19	7,385	7,915
		533,285	**464,371**
Current assets			
Inventories	18	31,448	27,719
Current income tax claims	21	8,119	1,756
Trade accounts receivable	19	198,632	191,269
Other receivables and other assets	19	77,372	75,145
Cash and cash equivalents	20	53,744	535,337
		369,315	**831,226**
		902,600	**1,295,597**

Shareholders' equity and liabilities in €'000s	Note	31. 12. 2007	31. 12. 2006
Shareholders' equity			
Share capital	22	96,061	65,702
Capital reserves	22	390,144	254,561
Statutory revenue reserves		0	36
Retained earnings		–114,840	445,077
Capital and reserves attributable to shareholders of freenet AG		**371,365**	**765,376**
Minority interest in shareholders' equity		720	168,013
		372,085	**933,389**
Non-current liabilities			
Other payables	24	29,757	2,342
Borrowings	26	614	717
Deferred income tax liabilities	17	0	232
Retirement benefit obligations	28	829	538
Provisions for other liabilities and charges	29	8,133	6,555
		39,333	**10,384**
Current liabilities			
Trade accounts payable	24	103,004	94,649
Other payables	24	280,535	207,452
Current income tax liabilities	25	1,927	14,668
Borrowings	26	90,282	97
Provisions for other liabilities and charges	29	15,434	34,958
		491,182	**351,824**
		902,600	**1,295,597**

3.4 Schedule of changes in equity for the period from 1 January bis 31 December 2007

In €'000s	Note	Share capital	Capital reserves	Statutory revenue reserves	Retained earnings	Capital and reserves attributable to shareholders of freenet AG	Minority interest in shareholders' equity	Shareholders' equity
As of 1.1.2006		**65,702**	**255,648**	**36**	**226,551**	**547,937**	**129,532**	**677,469**
Stock-based compensation	4	0	–1,087	0	0	–1,087	0	–1,087
Group result		0	0	0	218,526	218,526	38,481	257,007
As of 31.12.2006		**65,702**	**254,561**	**36**	**445,077**	**765,376**	**168,013**	**933,389**
As of 1.1.2007		**65,702**	**254,561**	**36**	**445,077**	**765,376**	**168,013**	**933,389**
Stock-based compensation	4	0	857	0	0	857	0	857
Merger into freenet AG and purchase of minority interest from formerly freenet.de AG	22	30,359	134,726	–36	0	165,049	–167,255	–2,206
Dividend payment	31	0	0	0	–576,066	–576,066	0	–576,066
Cash-payments by subsidiaries to minority shareholders		0	0	0	0	0	–419	–419
Group result		0	0	0	16,149	16,149	381	16,530
As of 31.12.2007		**96,061**	**390,144**	**0**	**–114,840**	**371,365**	**720**	**372,085**

3.5 Consolidated statement of cash flows from 1 January to 31 Dezember 2007

In €'000s	Note	1.1.2007 – 31.12.2007	1.1.2006 – 31.12.2006
Result before tax		**163,706**	**117,617**
Adjustments:			
Depreciation and impairment on items of fixed assets	5	96,187	43,921
Decrease/Increase in provisions	28, 29	–17,655	10,342
Interest income	7	–14,510	–15,103
Interest expenses	8	7,369	589
Share of results of associates	15	–1,075	–1,146
Other non-payment components		857	–1,087
Loss on disposals of fixed assets		258	696
Increase/decrease of inventories, trade receivables and other assets not attributed to investing or financing activities		–12,754	52,207
Increase/decrease of trade payables and other liabilities not attributed to investing or financing activities		104,923	–12,473
Income taxes paid		–42,163	–50,726
Cashflow from operating activities		**285,143**	**144,837**
Purchase of property, plant and equipment		–22,422	–25,537
Purchase of intangible assets	11	–266,245	–16,052
Cash-proceeds from disposals of intangible and tangible fixed assets		435	283
Purchase of subsidiaries		0	–104
Return of capital from associates	15	1,402	1,157
Interest received		13,368	13,127
Cashflow from investing activities		**–273,462**	**–27,126**
Dividend payment		–576,066	0
Cash-payments for the acquisition of minority interest		–2,206	0
Cash-payments by subsidiaries to minority shareholders		–419	0
Cash-proceeds from disposals of promissory notes		0	85,000
Cash repayments of bonds and borrowings		–97	–171
Interest paid		–4,665	–306
Cashflow from financing activities		**–583,453**	**84,523**
Cash-effective change in cash and cash equivalents		**–571,772**	**202,234**
Value adjustments pertaining to attributable market values of securities included in cash funds		0	2
Cash and cash equivalents at 1.1.		**535,337**	**333,101**
Cash and cash equivalents at 31.12.		**–36,435**	**535,337**

3.6 Consolidatet statements of movements in non-current assets as of 31 December 2007

In €'000s	Costs of purchase or production					
	1.1.2007	Change in companies included in consolida-tion	Additions	Transfers	Disposals	31.12.2007
Intangible assets						
Internally-generated software	7,918	0	571	0	0	8,489
Software and licences	128,987	0	3,058	–151	859	131,035
Trademarks	17,833	0	0	0	0	17,833
Customer relationship	44,796	0	264,458	0	0	309,254
Goodwill	110,303	0	1	0	0	110,304
	309,837	**0**	**268,088**	**–151**	**859**	**576,915**
Property, plant and equipment						
Land, facilities on land and buildings	13,076	0	0	0	2	13,074
Switches and networks	177,180	0	7,034	598	0	184,812
Technical equipment and machinery	37,589	0	6,549	2,449	324	46,263
Other office equipment	110,684	0	8,806	–2,869	11,614	105,007
Payments on account and assets under construction	27	0	33	–27	0	33
	338,556	**0**	**22,422**	**151**	**11,940**	**349,189**
	648,393	**0**	**290,510**	**0**	**12,799**	**926,104**

Depreciation and impairment write-downs						Book values	
1.1.2007	Additions	Impairment write-downs	Transfers	Disposals	31.12.2007	31.12.2007	1.1.2007
5,779	1,463	0	–11	0	7,231	1,258	2,139
83,493	10,837	0	11	747	93,594	37,441	45,494
0	0	0	0	0	0	17,833	17,833
6,540	54,443	7,207	0	0	68,190	241,064	38,256
0	0	0	0	0	0	110,304	110,303
95,812	**66,743**	**7,207**	**0**	**747**	**169,015**	**407,900**	**214,025**
4,198	513	0	0	2	4,709	8,365	8,878
168,128	4,472	0	2	0	172,602	12,210	9,052
20,250	7,559	0	162	320	27,651	18,612	17,339
84,926	9,693	0	–164	11,037	83,418	21,589	25,758
0	0	0	0	0	0	33	27
277,502	**22,237**	**0**	**0**	**11,359**	**288,380**	**60,809**	**61,054**
373,314	**88,980**	**7,207**	**0**	**12,106**	**457,395**	**468,709**	**275,079**

Consolidatet statements of movements in non-current assets as of 31 December 2006

In €'000s	Costs of purchase or production					
	1.1.2006	Change in companies included in consolida-tion	Additions	Transfers	Disposals	31.12.2006
Intangible assets						
Internally-generated software	7,244	0	677	–3	0	7,918
Software and licences	138,816	0	7,049	3	16,881	128,987
Trademarks	57,714	0	0	0	39,881	17,833
Customer relationship	36,470	0	8,326	0	0	44,796
Goodwill	110,223	80	0	0	0	110,303
	350,467	**80**	**16,052**	**0**	**56,762**	**309,837**
Property, plant and equipment						
Land, facilities on land and buildings	13,071	0	5	0	0	13,076
Switches and networks	173,277	0	4,019	1,126	1,242	177,180
Technical equipment and machinery	28,728	0	3,596	6,320	1,055	37,589
Other office equipment	140,982	14	17,886	–7,180	41,018	110,684
Payments on account and assets under construction	266	0	31	–266	4	27
	356,324	**14**	**25,537**	**0**	**43,319**	**338,556**
	706,791	**94**	**41,589**	**0**	**100,081**	**648,393**

Depreciation and impairment write-downs						Book values	
1.1.2006	Additions	Impairment write-downs	Transfers	Disposals	31.12.2006	31.12.2006	1.1.2006
4,291	1,531	0	–43	0	5,779	2,139	2,953
88,694	11,324	0	43	16,568	83,493	45,494	50,122
39,881	0	0	0	39,881	0	17,833	17,833
2,919	3,621	0	0	0	6,540	38,256	33,551
0	0	0	0	0	0	110,303	110,223
135,785	**16,476**	**0**	**0**	**56,449**	**95,812**	**214,025**	**214,682**
3,684	513	1	0	0	4,198	8,878	9,387
160,285	9,082	0	0	1,239	168,128	9,052	12,992
13,900	7,376	0	2	1,028	20,250	17,339	14,828
114,841	10,071	402	–2	40,386	84,926	25,758	26,141
0	0	0	0	0	0	27	266
292,710	**27,042**	**403**	**0**	**42,653**	**277,502**	**61,054**	**63,614**
428,495	**43,518**	**403**	**0**	**99,102**	**373,314**	**275,079**	**278,296**

3.7 Notes to the consolidated financial statements of freenet AG for the period ended 31 December 2007

A. General information

freenet AG (also referred to in the following as "the Company"), the Group's parent company (also referred to in the following as "freenet"), is registered in Büdelsdorf, Germany. The Group provides telecommunications services in the segments Mobile Telephony, Broadband, Hosting, B2B as well as Narrowband.

As the legal successor of mobilcom AG (also referred to in the following as: mobilcom) and freenet.de AG (referred to in the following as: freenet.de), the Company as a result of the merger assumed the obligation on 2 March 2007 of preparing consolidated financial statements. In accordance with International Financial Reporting Standards (IFRS), assets were transferred from mobilcom AG and freenet.de AG to the Company as a result of the above-mentioned merger only at the point at which the transaction was entered in the commercial register on 2 March 2007 and only in conjunction with the acquisition of actual control over their assets and liabilities.

Because the merger between mobilcom and freenet.de to form the Company only became effective after 31 December 2006, the share capital of the former parent company of the Group mobilcom was still reported as €65,702 thousand in the previous year financial statements for the period ending 31 December 2006. In the previous year, earnings per share in accordance with IAS 33 were still determined on the basis of the 62,416,710 issued no-par value shares of mobilcom AG.

B. Accounting standards

The 2007 consolidated financial statements have been prepared in conformity with the IFRS of the International Accounting Standards Board (IASB) and the version approved in the EU, as well as in compliance with applicable provisions of commercial law in accordance with section 315a of the German Commercial Code (Handelsgesetzbuch – HGB). All standards prevailing as at 31 December 2007 were taken into account, as were the interpretations of the International Financial Reporting Interpretations Committee (IFRIC).

The consolidated financial statements have been prepared in Euros, the Company's functional currency. Unless otherwise specified, all figures are stated in thousand Euros (€'000s).

The consolidated financial statements have been prepared applying the historical cost convention – subject to the restriction that some financial assets are stated with their fair value. The annual financial statements of the companies included in the consolidated financial statements were based on uniform accounting and valuation principles and were prepared to the same balance sheet date as that applying to the consolidated financial statements.

The following table shows the new or modified IFRS and IFRIC, which are the subject of mandatory adoption with effect from 1 January 2007, or which have been the subject of early voluntary adoption since 1 January 2007, and the related impact on the Group:

Standard/Interpretation		Mandatory application	Adoption by EU Commission	Impact
IFRS 7	Financial Instruments: Disclosures	1.1.2007	Yes	Disclosures in notes
IFRS 8	Operating Segments	1.1.2009	Yes	Segment reporting
IAS 1	Presentation of Financial Statements: Information on Capital	1.1.2007	Yes	Disclosures in notes
IFRIC 7	Applying the Restatement Approach under IAS 29 Financial Reporting in Hyperinflationary Economies	1.3.2006	Yes	None
IFRIC 8	Scope of IFRS 2	1.5.2006	Yes	None
IFRIC 9	Reassessment of Embedded Derivatives	1.6.2006	Yes	None
IFRIC 10	Interim Financial Reporting and Impairment	1.11.2006	Yes	None

Adopted by EU Commission as of 31 December 2007.

The following table shows the new or modified IFRS and IFRIC which are not the subject of mandatory adoption, and which aer also not the subject of voluntary early adoption, in financial 2007 and their probable impact on the Group:

Standard/Interpretation		Mandatory application	Adoption by EU Commission	Impact
IAS 1 (rev.)	Presentation of Financial Statements	1.1.2009	Yes	Disclosures in notes
IAS 23	Borrowing Costs	1.1.2009	Yes	None
IAS 27	Consolidated and Separate Financial Statements under IFRS	1.7.2009	No	Still being reviewed by management
IFRS 2	Share-Based Payment	1.1.2009	No	None
IFRS 3	Business Combinations	1.1.2009	No	Still being reviewed by management
IFRIC 11	IFRS2 Group and Treasury Share Transactions	1.1.2008	Yes	None
IFRIC 12	Service Concession Arrangements	1.1.2008	Yes	None
IFRIC 13	Customer Loyalty Programmes	1.7.2008	Yes	None
IFRIC 14	IAS 19 Restriction for Surplus Cover of Plan Assets	1.1.2008	Yes	None

Adopted by EU Commission as of 31 December 2007.

C. Consolidated companies

The consolidated financial statements include all companies with respect to which the Company is directly or indirectly in a position to determine the Company's financial and business policies in such a way that the Group parent benefits from the activities of the company in question. For a complete list of all companies included in freenet AG's consolidated financial statements, please consult our disclosures in accordance with section 315a HGB in note 34.

A joint venture is a contractual agreement under which two or more partners carry out an economic activity which is subject to joint management.

Associated companies are defined as companies over which the Group exerts a significant influence but which are not controlled by the Group; normally involving a share of between 20 and 50 percent in voting rights.

01024 Telefondienste GmbH, freenet Customer Care GmbH, freenet Datenkommunikations GmbH, Next ID technologies GmbH, 01050.com GmbH, tellfon GmbH, 01083.com GmbH, new directions GmbH, freenet Direkt GmbH, MobilCom Multimedia GmbH as well as meOme GmbH will take advantage of the exemption regulations specified in section 264 (3) HGB for the annual financial statements for the period ending 31 December 2007.

MobilCom Products & Services GmbH was sold to Sycorax 1. Beteiligungsgesellschaft m.b.H (i.L.), Hamburg, on 20 December 2007 for a price of €1.00 for the purpose of liquidation. The company which was sold is a company without any active operations.

No business combinations in accordance with IFRS 3 took place in the course of the financial year.

D. Consolidation principles

Companies are included in the consolidated financial statements with effect from the date on which the Company assumes control. Minority interests in the companies are disclosed separately on the balance sheet.

The purchase method was applied to the consolidation of equity.

The historical cost of company acquisitions is determined by the sum of the fair values of the assets purchased, the liabilities acquired, any equity instruments issued for acquisition purposes and the costs directly attributable to the acquisition.

All of the acquired company's identifiable assets, liabilities and potential liabilities meeting the recognition criteria of IFRS 3.37 will be disclosed separately at their fair value, irrespective of the extent of any minority interests.

Goodwill is recognised as that portion of the asset value at the time of acquisition, as determined in the initial valuation, which is in excess of the purchaser's share of the fair value of the acquired company's identifiable assets, liabilities and potential liabilities. Any excess in the share of the fair net value of the acquired company over the costs of acquisition is immediately recognised as revenue.

Joint ventures are included in the consolidated financial statements using the proportional consolidation method. The Group's shares of the assets, liabilities, revenues and expenditure are summarised in the corresponding items on the consolidated balance sheet and revenue statement.

Investments in associates are disclosed in the consolidated financial statements according to the equity method, whereby the recognised values of the holdings are increased or reduced by the proportion of the changes in the joint venture's equity capital which is attributable to the freenet Group. Goodwill arising from the acquisition of associates is not disclosed separately.

Intra-group profits and losses, turnover, expenditure and revenue as well as existing receivables and liabilities between consolidated companies, are eliminated, and the same applies to associates in the case of elimination of intercompany results.

E. Accounting and valuation methods

The following accounting and valuation methods were applied when preparing the consolidated financial statements:

(a) Revenues

The Group predominantly provides services over a short performance period, and the revenues are collected after performance in full of the service. Services which atypically span the balance sheet date are shown according to the date on which reimbursement for the expenditure will in all probability be received. Services rendered but not yet invoiced are accrued separately in the annual financial statements. Revenues are disclosed net of value added tax and cash discounts.

Most of the sales of the Group are generated with a large number of end users; the remaining sales are attributable to business clients.

Supplementary notes on revenues:

The voice communication and data transmission fees are recognised as sales over the period during which the service is provided.

The Group receives commission revenues from the four mobile telephony networks principally for attracting new users and for contract extensions. Commission claims are determined on the basis of contractually agreed qualitative and quantitative factors such as the number of new users per quarter or the average revenue per user, and on top of this, advertising cost subsidies are granted for individual campaigns. Suppliers of mobile phones and accessories are also granted commission and advertising cost subsidies in return for achieving predefined turnover and/or volume targets. Where claims extend beyond the period in which the services were performed, commission revenues are accrued accordingly.

In the Hosting segment, revenues are also generated from the registration of names for Internet domains and web hosting. These involve entering into contracts with users whereby a range of services is offered in return for a registration fee plus regular monthly charges. The registration fee is recognised once registration has taken place and the service has been set up for the user, whereas the ongoing monthly charges are accrued over the term of the contract.

With regard to added value services, amounts are received for the Company's own account and also on behalf of third parties. Amounts which the Company charges for the account of the client do not constitute sales in accordance with IAS 18.

(b) Borrowing costs

Borrowing costs are recognised as expenses in the period in which they are incurred.

(c) Intangible assets

Goodwill is tested for impairment at least once every year, and is shown at original cost less cumulative impairments.

For this purpose, the goodwill is broken down over cash generating units. It is broken down over those cash generating units or groups of cash generating units which are expected to derive a benefit from the merger which gave rise to the goodwill. With regard to the specific breakdown, please refer to note 12 “Impairment test for non-monetary assets”.

The brand rights are assets with an undefinite economic service life which are not depreciated and instead are subject to an impairment test at least once every year. An indefinite useful life has been chosen because no steady loss of value is discernible with respect to this asset, nor could any time limit be set on its useful life.

Licences and software are shown at cost and are depreciated using the straight-line method over their probable economic service life, in general three years for software and three to ten years for licences. Within licences and software, a beneficial interest quota is amortised over 18 years in line with the minimum lease period for the underlying tenancy agreement.

Costs incurred in developing or maintaining software programs are usually recognised as expenses in the year they are incurred. Such costs are recognised as intangible assets falling under the heading internally generated software provided they relate to a clearly defined software product which can be used by the Company, and if the product’s expected overall economic benefit is greater than the costs incurred they are capitalised as intangible assets under the category “Internally produced software”. These costs include the personnel costs for the software development team as well as expenditure on services and fees incurred in creating the asset. Development costs are not capitalised until the point in time when their technical and economic feasibility can be proven. Capitalised software development costs are subjected to straight-line depreciation over the duration of their prospective useful life, usually three years.

As prescribed by IAS 38, the Group shows those parts of customer acquisition costs which are individually identifiable as intangible assets. The criterion of individual traceability was satisfied in 2006 exclusively for the “freenet*Komplett*” product range, so that only the costs for this product area were capitalised. Starting with the first quarter of 2007, the capitalisation criteria were satisfied for the first time for contract customers in the other main product areas of mobile telephony, broadband (excl. “freenet*Komplett*”), hosting as well as narrowband. In connection with allocating customer acquisition costs to specific periods over the minimum term of the customer agreements, various revenue components in the contract customer areas – mainly the connection premiums which become payable in mobile telephony when a contract is taken out and which are granted by the network operators – were also no longer recognisable immediately as sales; instead, starting with the first quarter of 2007, such revenues were for the first time to be recognised as liabilities. These revenue components are granted and calculated in return for part of the amounts which are now capitalised under customer acquisition costs. In line with the deferral of customer acquisition costs, these liability costs are reversed in sales in the specific periods over the legal term of the customer contracts of six to 24 months.

The main components of the customer acquisition costs in the individual contract customer areas are the provision costs, the customer hardware costs and the sales commissions. Mark-downs in relation to the costs of purchase are recognised for margins which do not cover costs over the legal term of the customer contracts. The intangible assets shown for customer acquisition costs are depreciated over the legal term of the customer contracts of six to 24 months. The costs of signing up new customers are allocated to the category “Customer relations” for presentation in the schedule of consolidated assets.

The figure of € 27.5 million recognised for customer relations is attributable to the purchase of broadband and narrowband customers from Tiscali S. p. A. which took place in financial 2007. Customer relations acquired from third parties are depreciated over a period of four to 14 years using the straight-line method.

One core technology which derives from the acquisition of the Strato-Group is depreciated over ten years using the straight-line method.

(d) Property, plant and equipment

Property, plant and equipment is valued at the cost of acquisition or production less straight-line depreciation. The useful lives assumed for the depreciation of assets reflect the assets’ expected useful lives within the Company. In calculating depreciation, the residual values at the end of the assets’ useful lives are disregarded on grounds of immateriality.

The depreciation of property, plant and equipment is generally based on the following useful lives:

Asset	**Useful life in years**
Buildings	25 years
Technical equipment and machinery	3 to 15 years
Motor vehicles	4 to 7 years
IT equipment	3 to 10 years
Telecommunications equipment and hardware	3 years
Leasehold improvements	3 to 10 years

(e) Impairment of non-monetary assets

Assets are always impaired if the carrying amount exceeds the recoverable amount. The recoverable amount is defined as the higher of the fair value of the asset less costs to sell and the value in use.

An impairment has to be carried out if triggering events indicate that the value of the asset might be impaired. Goodwill and assets with indefinite useful lives must be tested once a year in accordance with the provisions of IAS 36 for loss of value (impairment).

If the reason for an impairment is no longer applicable, the value of the asset is written up to a figure not exceeding the amortised cost of purchase.

(f) Leases

Leases where the Group is the lessee
The Group decides on a case by case basis whether assets are to be leased or purchased. For fixed assets, specific rules apply to motor vehicles (operating leases) and plant and equipment (purchase), but not to IT hardware and telecommunications equipment.

Leases which the Group enters into as the lessee are classified as either operating leases or finance leases, depending on whether all the significant risks and opportunities associated with the ownership of the leased property are assumed. In the case of operating leases, the lease instalments are shown in the income statement in a straight-line fashion over the term of the respective leases.

In the case of finance leases, IAS 17 specifies that the leased assets of which the Group is classified as the beneficial owner are capitalised and depreciated over their expected useful lives. Liabilities arising from the lease are correspondingly reduced by the capital portion of the lease instalments already paid, while the interest portion of the lease instalments is recognised as expenditure. The leases on technical data centre equipment are classified as finance leases. The original terms of the leases still running on the balance sheet date were estimated, taking the Company's existing option rights into account, at ten years, and the resultant debt is amortised over this period.

Leases where the Group is the lessor
If the beneficial ownership of a mobile telephone is transferred to the customer, in accordance with IAS 17 the Group recognises a receivable from the lessee in the amount of the net investment in the lease at the time the contract is entered into. Lease payments received are broken down into an interest portion and a capital (redemption) portion. The interest components are recognised as financial income spread over relevant periods. As of the reference data, finance leases can only be recognised in relation to mobile contracts in which the purchase price for the hardware component is spread over a contractually fixed period.

(g) Holdings in associates and other investments

Equity investments in associates continue to be recognised via an individual financial statement prepared for the various associates in accordance with IFRS and the Group's accounting and valuation methods. With regard to the procedure for accounting for holdings using the equity method, please refer to section D "Principles of consolidation".

(h) Financial instruments

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. For the purposes of measurement, financial assets are normally broken down into the following categories:
i. Financial assets measured at fair value through profit or loss
ii. Extended loans and receivables
iii. Held-to-maturity financial assets
iv. Available-for-sale financial assets.

i. Financial assets measured at fair value through profit or loss
This category contains two subcategories: Financial assets which are classified as held-for-trading right from the very beginning, and financial assets which are classified as "measured at fair value through profit or loss" right from the very beginning. A financial asset is assigned to this category if it is in principle acquired with the intention of being sold in the near future or if the financial asset is designated accordingly by management.

The financial assets measured at fair value through profit or loss which are held as of the balance sheet date are shown under liquid assets.

ii. Extended loans and receivables
Extended loans and receivables are non-derivative financial assets with fixed or determinable payments which are not listed on an active market. They arise if the Group provides money, commodities or services directly to a debtor without any intention of trading the receivables. They are included under current assets, with the exception of those which only fall due 12 months after the balance sheet date. The latter are shown under non-current assets. Loans and receivables are shown in the balance sheet under trade accounts receivable, other receivables and other assets. They also include services which have been provided but which have not yet been billed but for which a contractual claim exists.

iii. Held-to-maturity financial assets
Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed terms in relation to which Group management intends and is able to hold until final maturity. Held-to-maturity financial assets – with the exception of those which fall due within 12 months after the balance sheet date and which are shown correspondingly as current assets – have to be shown under non-current assets.

At present, the Group does not use this category for classifying any financial instruments.

iv. Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets which either have to be classified under this category or which have not been classified under any of the other categories shown. They are classified under non-current assets if management does not intend to sell them within 12 months after the balance sheet date.

Shares in affiliated companies and investments are considered to be available-for-sale financial assets. The available-for-sale financial assets which existed on the balance sheet date are shown under other financial assets.

Measurement of financial instruments

Regular purchases and sales of financial assets are shown as of the trade date, i.e. the day on which the Group enters into an obligation to buy or sell the asset. Financial assets which are not designated as "measured at fair value through profit or loss" are initially shown with their fair value plus transaction costs.

Financial assets which are designated as "measured at fair value through profit or loss" are initially shown with their fair value; corresponding transaction costs are expensed in the income statement.

On the occasion of subsequent measurement, financial assets measured at fair value through profit or loss are shown with their fair value. Any profit or loss resulting from the subsequent measurement of financial assets measured at fair value through profit or loss is taken to the income statement.

After initial recognition, loans and receivables are shown at amortised cost using the effective interest method less impairments for reductions in value. Profits and losses are shown in the result for the period if the loans and receivables are derecognised or impaired, and are also shown within the framework of amortisation.

After initial recognition, held-to-maturity investments are shown at amortised cost. Profits and losses are recognised in the result for the period if the held-to-maturity investments are derecognised or impaired, and also within the framework of amortisations.

After initial recognition, available-for-sale financial assets are shown with their fair value, whereby unrealised profits or losses are recognised directly in equity, under the reserve for unrealised profits. Dividend income arising from financial assets in this category has to be shown as other income in the income statement. Dividends attributable to available-for-sale equity instruments have to be shown in the income statement as other income at the point at which the legal claim of the Group for payment arises.

Shares in affiliated companies, investments and securities however are shown at cost, because it is not possible for their fair value to be reliably determined. The shares are not listed and an active market does not exist; moreover, there is no intention for these assets to be sold at present. If there are any indications of a lower fair value, these are recognised.

Cash and cash equivalents

Cash and cash equivalents consist of cash, sight deposits and other current highly liquid financial assets with an original term of max. three months.

Liabilities

Liabilities comprise the financial liabilities, trade accounts payable as well as other liabilities. When initially recognised, they are shown with the fair value of the consideration received less the transaction costs associated with borrowing.

In the following period, the financial liabilities are shown at amortised cost using the effective interest method. Profits and losses are recognised in the income statement when the liabilities are derecognised, and also within the framework of amortisations.

Non-current liabilities are shown at amortised cost. Any differences between historical cost and the repayment amount are recognised in accordance with the effective interest method.

Current liabilities are shown in the amount due for repayment or fulfilment. At this point, please also refer to the comments on the accounting and measurement of financial assets.

Financial liabilities arising from finance leases are shown with the present value of the minimum lease payments.

Impairment of financial assets

On every balance sheet date, a check is performed to determine whether there are any objective indications of an impairment of a financial asset or a group of financial assets. In the case of equity instruments which are classified as available-for-sale financial assets, a considerable or permanent decline in the fair value to a level below the costs of these equity instruments is considered to be an indication that the equity instruments are impaired. If there is such an indication for available-for-sale assets, the cumulative loss – measured as the difference between the cost of purchase and the current fair value less any impairment losses recognised in relation to the relevant financial asset – is derecognised from equity and shown in the income statement. Once impairments of equity instruments have been recognised in the income statement, they are not subsequently reversed to the income statement.

In the case of not listed equities which are categorised as available for sale, a major or permanent decline of the fair value of the securities to a level below their cost of purchase is considered to be an objective indication of an impairment. If no market prices are available, other valuation methods are used, e.g. the DCF method.

An impairment of trade accounts receivable is recognised if there are objective indications that the due amounts are not fully recoverable. Considerable financial difficulties of a debtor, an increased probability that the borrower will become bankrupt or will have to go through another restructuring process, as well as any breach of contract, e.g. default or late payment of interest and principal, are considered to be an indication of the existence of an impairment.

In the case of some categories of financial assets, for instance trade accounts receivable, assets for which no impairment has been determined on an individual basis are tested for impairment on a portfolio basis. Objective indications of an impairment of a portfolio of receivables might be the Group's experience with payment inflows in the past, an increase in the frequency of payment defaults within the portfolio over the average duration of a loan as well as evident changes in the national or local economic climate which are associated with defaults of receivables.

The carrying amount of the receivable is reduced by using an impairment account. If a receivable has become irrecoverable, it is derecognised from the impairment account. Subsequent payment inflows in relation to previously derecognised amounts are shown in the income statement under impairments of trade accounts receivable.

Derecognition of financial assets

The Group derecognises a financial asset only if the contractual right to cash flows attributable to a financial asset expires or if it transfers the financial asset and essentially all the risks and opportunities with ownership of the assets to a third party.

(i) Inventories

Inventories are shown at the lower of cost and the net realisable value on the balance-sheet date. The net realisable value is defined as the estimated recoverable proceeds less costs to sell. The acquisition or production costs are calculated using the first-in-first-out method (FIFO).

(j) Foreign currency transactions

The financial statements of foreign Group companies which do not prepare their accounts in the reporting currency are translated into Euro. The modified reference date method is used for translation purposes. Receivables and liabilities are translating using the exchange rate applicable on the date of the transaction.

The balances of the income statement are translated into Euros using average rates. Profits and losses arising from changes in exchange rates which occur by the balance sheet date are shown in the income statement

(k) Pension provisions

The pension provision shown in the balance sheet is equivalent to the present value of the defined benefit obligation on the balance-sheet date less the fair value of the plan assets adjusted by cumulative actuarial profits and losses which have so far not been shown in the income statement as well as subsequent service cost not shown in the income statement. The present value of the defined benefit obligation is calculated every year by an independent actuarial expert using the projected unit credit method. This method takes account not only of the pensions and acquired vested interests known on the reference date; it also includes likely future increases in pensions and salaries.

Actuarial profits and losses which are based on adjustments and changes to actuarial assumptions attributable to past experience are shown in the income statement if the balance of the cumulative actuarial profits and losses not shown in the income statement exceeds the higher of ten percent of the present value of the defined benefit obligation (before deduction of the plan assets) or ten percent of the fair value of the plan assets at the end of the previous reporting period. These profits or losses are realised over the expected remaining service years of the beneficiary.

Subsequent service cost is immediately taken to the income statement, unless the changes in the pension plan depend on the employee remaining with the Company for a defined period (period until entitlement becomes vested). In this case, the subsequent service cost is shown in the income statement using the straight-line method over the period until the rights become vested.

The service cost is shown under personnel expenses, and the interest portion of the allocation to provisions is shown in financial result.

(l) Other provisions

Provisions are recognised for legal or constructive obligations of uncertain timing or amount which arise as a result of past events, where it is probable that settlement of the obligation will lead to an outflow of Group resources and where a reliable estimate of the extent of the obligation can be made. The provisions are valued using a best-possible estimate of the obligation on the balance-sheet date, taking into account the discounting of non-current obligations.

According to IAS 16, the purchase costs of tenant fittings include costs expected for obligations to remove tenant fittings. In accordance with IAS 37, a provision is also created to cover the present value of obligations to remove tenant fittings for which an outflow of resources is likely; this provision is created at the point at which the obligations arise. Changes in the value of an existing provision, in other words changes in the fulfilment amount and/or the discount rate, are recognised by means of an adjustment to the carrying amount of the tenant fittings (upper limit: Recoverable amount; lower limit: Zero).

(m) Employee share option programmes

There are the following employee share option programmes in the Group:

- Stock appreciation rights of freenet AG
- Stock options of the former mobilcom AG

The accounting and valuation methods of the individual share option programmes are detailed in the following:

Stock appreciation rights of freenet AG
In 2006, stock appreciation rights were granted to the Managing Board of the Company as well as selected executives of the Group. They are valued at the fair value of the stock appreciation rights on the balance-sheet date. These rights are exercised in return for payment of a cash amount equivalent to the difference between the relevant stock price and the strike price less taxes and charges. For details, please refer to our explanations to note 23 “Employee participation programmes”.

Stock options of the former mobilcom AG
The former mobilcom AG had set up a stock-based compensation plan which is funded by equity instruments. The fair value of the work provided by the employees in return for the granting of options is recognised as an expense. The entire expense, which has to be recognised over the period until the point at which the options become vested, is calculated on the basis of the fair value of the options which have been granted. The estimate of the number of options which are expected to become exercisable is reviewed on every balance sheet day. The effects of any changes to original estimates which may have to be taken into consideration are recognised in the income statement and also by way of a corresponding adjustment in shareholders equity.

As part of the process of exercising options, the former mobilcom AG took advantage of the substitution right which it had been granted. The stock options are redeemed in the form of a cash settlement. Following revaluation using the parameters applicable for the corresponding reference date, allocations are paid into the provision via an entry in shareholders’ equity with no impact on the income statement.

(n) Deferred taxes on revenue

Deferred taxes are recognised for tax loss carry-forwards and using the liability method, for all temporary differences between the tax balance sheet values and the carrying amounts of assets and liabilities. Deferred tax assets are recognised for tax loss carry-forwards and allowable temporary differences only to the extent that it is probable that they can be used against future profits. Deferred tax assets are calculated using the tax rates prevailing under current tax law.

(o) Accruals and deferrals for public subsidies

Accounts receivable in the form of public subsidies are capitalised provided a corresponding claim exists and the amount thereof can be estimated with sufficient reliability. According to IAS 20, the item must be presented as deferred revenue and recognised in the income statement over a period of three to ten years, depending on the depreciation period applied. If at the time when the subsidy entitlement comes into being, the property, plant and equipment in question has already been depreciated either in whole or in part, it will be recognised immediately. For further details, please refer to note 24 “Trade accounts payable, other liabilities and accruals”.

(p) Exercise of management discretion

We provide the following details pursuant to IAS 1.113:

The statement and calculation of provisions depends on estimates. Provisions for passive legal disputes in particular are created on the basis of the assessment of the lawyers representing the Group companies.

An evaluation of the value of the receivables was carried out for establishing suitable valuation adjustments for trade accounts receivable. These assessments were based mainly on past experience as well as on the age structure and on the status of receivables in the dunning and collection process.

In the Broadband segment, for the purpose of defining the sourced services for provision costs, past experience is used as the basis for estimating the probability with which the order will subsequently become an active customer relationship. This probability is then used as the basis for accruing the provision costs which will be incurred once for activating and releasing the customer. These provision costs are capitalised as a component of customer acquisition costs.

In order to value the intangible assets for costs of signing up customers, an assessment is made to establish what percentage of the costs of signing up customers can be amortised within the original contractual term – only this percentage is capitalised.

In the “Domain-Hosting” segment, fees are generated from the registration and administration of top-level domains for users who are invoiced by DENIC Domain Verwaltungs- und Betriebsgesellschaft eG (“DENIC”), Frankfurt/Main. DENIC repays fees not needed as goods refunds. The amount of the goods refunds to be expected from DENIC is estimated on the basis of the payments on account made during the course of the year.

With regard to the accrual of purchased services from sales commissions for the various products of the Group, estimates are made on the basis of past experience to assess the probability with which final commissions (which can no longer be cancelled) become payable.

(q) Forward looking assumptions and margins of error

With regard to the most significant forward-looking assumptions and margins of error inherent in the consolidated financial statements, we hereby make the following observations pursuant to IAS 1.116:

As regards the forward looking assumptions made in the impairment tests for goodwill and intangible assets of indefinite useful life, please refer to note 12 “Impairment test for non-monetary assets”.

The deferred tax assets relating to losses carried forward are based on corporate planning which recognises forward-looking assumptions, for instance with regard to macro-economic developments as well as the development of the telecommunications market.

With regard to the assumptions and estimates made in the binomial model used for determining the provisions for outstanding stock options and stock appreciation rights according to IFRS 2 as of 31 December 2007, please refer to note 23 “Employee participation programmes”.

With regard to pension provisions and similar obligations, note 28 describes how forward-looking assumptions have been made for the valuation of the provisions for pensions and similar obligations. This involves the recognition of a discount rate, the trend in pensions, the assessment of the future development of the pensionable income of the beneficiary as well as an assessment of an expected return on the plan assets.

(r) Comparable figures and changes in the accounting policies

The items sales, cost of materials and depreciation are only comparable to a limited extent with the previous year figures. This is due to the accounting effects of the wholesale DSL agreement signed in the previous year with Deutsche Telekom AG, Bonn, and also the accounting effects of the capitalisation of customer acquisition costs in accordance with IAS 38.

Customer acquisition costs for the product area "freenet*Komplett*" were capitalised for the first time in 2006; the extended capitalisation of customer acquisition costs which took place in 2007 for the main product areas Mobile Telephony, Broadband, Hosting and Narrowband constitutes a change of method in accordance with IAS 8.14 billion; this change of method was essential as a result of the change in data availability. Because the database structures for these products are available for the first time, the individual costs can be traced back to the level of individual customers. This means that all criteria of IAS 38 with regard to mandatory capitalisation of customer acquisition costs have been satisfied. The previous year figures have not been adjusted in accordance with IAS 8 because the corresponding individual data for customer acquisition costs are not available and cannot be reconstructed.

The residual carrying amount of the capitalised customer acquisition costs was € 190,496 thousand as of 31 December 2007 (previous year: € 7,031 thousand). As a result of the capitalisation of customer acquisition costs, the deferred items shown under other liabilities and deferrals are € 89,732 thousand (previous year: 0) higher than would have been the case if this item had been recognised without the capitalisation of customer acquisition costs.

In addition, by way of comparison with recognition without the capitalisation of customer acquisition costs, sales would have been € 90,827 thousand lower (previous year: 0), costs of material would have been € 238,614 thousand lower (previous year: € 7,326 thousand), EBITDA would have been € 147,787 thousand higher (previous year: € 7,326 thousand), depreciation and impairments would have been € 52,617 thousand higher (previous year: € 292 thousand) and earnings before taxes would have been € 95,170 thousand higher (previous year: € 7,034 thousand). The figure reported for diluted as well as undiluted earnings per share is € 0.70 per share higher (previous year: € 0.07 per share).

F. Segment reporting

The Group adopted IFRS 8 (Operating Segments) before the point at which it came into force, with effect from 1 January 2007. In accordance with IFRS 8, and on the basis of internal management, operating segments have to be distinguished from group segments whose operating results are regularly reviewed by the main decision-making body of the Company with regard to decisions relating to the allocation of resources to this segment and the measurement of its profitability.

The Managing Board organises and manages the Company on the basis of the differences between the individual products and services offered by the Company. Because the Group exercises its business operations almost exclusively in Germany, there is no organisation and management based on geographical regions. The Group operated in the following operating segments in 2007:

- Mobile Telephony: Activities as a mobile service provider.
- Broadband: Range of broadband Internet connections and accesses, range of broadband voice services (Voice-over-IP).
- Portal: Portal services comprise E-Commerce/Advertising services, a range of payment services for end customers as well as the provision of sales services. E-Commerce/Advertising services comprise online shopping (for instance: the generation of sales commissions, monthly fees and customer acquisition premiums) as well as the marketing of advertising (banners and other forms of advertising) on web sites.
- Hosting: Registration of top level domains, provision of web space, implementation of related software solutions.
- B2B: Range of value added services for business customers, development of communication services, IT services and other services for business customers.
- Narrowband: Range of narrowband voice services (call-by-call, preselection).

The individual operating segments each also provide services to other operating segments. These services are charged on the basis of transaction prices which are the subject of commercial negotiation.

Income and expenses are allocated to the segments on the basis of selected criteria and economic relevance. In the case of sales, cost of materials and gross profit, this allocation can clearly be made on the basis of the dimensions of the cost centre; this means that the entire Group gross profit has been completely allocated to segments. All other positions of the income statement, including net assets, liabilities and asset additions and disposals, have not been allocated to segments in internal reporting which is available for the decision makers of the Group.

For purposes of segment reporting, the figures and measurements shown for the corresponding expenses and income do not differ from the figures and measurements shown in the consolidated balance sheet and the consolidated income statement.

Within the framework of mass business conducted by the freenet Group which focuses primarily on private customers, there is no reliance on individual customers. In added-value service business which belongs to the B2B segment, a significant percentage of sales is generated with a small number of large customers.

2007 **€'000s**	**Mobile Telephony**	**Broadband**
Third-party revenues	**1,183,594**	**272,302**
Intersegment sales	1,167	0
Sales, total	1,184,761	272,302
Cost of materials, third parties	**–893,630**	**–196,577**
Intersegment cost of materials	–1,673	–8,131
Cost of materials, total	–895,303	–204,708
Segment gross profit	**289,458**	**67,594**
Other operating income		
Other own work capitalised		
Personnel expenses		
Depreciation and impairment write-downs		
Other operating expenses		
Share of results of associates		
Consolidated result before financial result and taxes on income		
Consolidated financial result		
Taxes on income		
Group result		
Group result attributable to shareholders of freenet AG		
Group result attributable to minority interest		

Portal	Hosting	B2B	Narrowband	Elimination	Total
49,087	**75,034**	**133,979**	**149,288**	**0**	**1,863,284**
7,587	4,351	939	0	–14,044	0
56,674	79,385	134,918	149,288	–14,044	1,863,284
–13,892	**–13,046**	**–103,342**	**–60,403**	**0**	**–1,280,890**
–2,101	–821	–410	0	13,136	0
–15,993	–13,867	–103,752	–60,403	13,136	–1,280,890
40,681	**65,518**	**31,166**	**88,885**	**–908**	**582,394**
					59,672
					571
					–134,567
					–96,187
					–256,393
					1,075
					156,565
					7,141
					–147,176
					16,530
					16,149
					381

2006 **€'000s**	**Mobile Telephony**	**Broadband**
Third-party revenues	**1,329,335**	**195,076**
Intersegment sales	2,359	0
Sales, total	1,331,694	195,076
Cost of materials, third parties	**–1,134,902**	**–180,843**
Intersegment cost of materials	–5,839	–11,986
Cost of materials, total	–1,140,741	–192,829
Segment gross profit	**190,953**	**2,247**
Other operating income		
Other own work capitalised		
Personnel expenses		
Depreciation and impairment write-downs		
Other operating expenses		
Share of results of associates		
Consolidated result before financial result and taxes on income		
Consolidated financial result		
Taxes on income		
Group result		
Group result attributable to shareholders of freenet AG		
Group result attributable to minority interest		

Portal	Hosting	B2B	Narrowband	Elimination	Total
42,163	**66,626**	**139,938**	**281,697**	**0**	**2,054,835**
21,304	2,339	1,506	0	–27,508	0
63,467	68,965	141,444	281,697	–27,508	2,054,835
–10,654	**–13,224**	**–113,086**	**–136,298**	**0**	**–1,589,007**
–2,068	–1,192	0	0	21,085	0
–12,722	–14,416	–113,086	–136,298	21,085	–1,589,007
50,745	**54,549**	**28,358**	**145,399**	**–6,423**	**465,828**
					73,126
					677
					–135,764
					–43,921
					–257,989
					1,146
					103,103
					14,514
					139,390
					257,007
					218,526
					38,481

G. Notes to the consolidated income statement

1. Revenues

A breakdown of sales of € 1,863 million (previous year: € 2,055 million) is set out in section F. Segment reporting.

Of turnover generated in the Mobile Telephony segment, € 896 million (previous year: € 1,010 million) relates to rentals and fees, and € 100 million (previous year: € 115 million) relates to the sale of mobile telephony devices and accessories.

When the sales generated in financial 2007 are compared with the sales of the previous year, the following has to be borne in mind:

In the third quarter of 2006, freenet.de AG signed a Wholesale DSL agreement with Deutsche Telekom AG, Bonn (DTAG); this agreement replaced the previous agreement for resale DSL. The conditions of the Wholesale DSL agreement are applicable starting 23 May 2006. Compared with the Resale DSL agreement, the premiums for signing up new customers are no longer applicable (these used to be shown under revenues). On the other hand, the one-off provision and the monthly line leasing are now obtained on more favourable conditions, with a corresponding impact on the costs of purchased services.

The criteria applicable for capitalising parts of customer acquisition costs in accordance with IAS 38 were satisfied in the freenet Group for the first time starting in the fourth quarter of 2006 for the product area “freenet*Komplett*”; the conditions for capitalising customer acquisition costs for further major product areas will be satisfied starting in the first quarter of 2007. In connection with allocating customer acquisition costs to specific periods over the minimum term of the customer agreements, various revenue components in the contract customer areas – mainly the connection premiums which become payable in mobile telephony when a contract is taken out and which are granted by the network operators – were also no longer recognisable immediately as sales; instead, starting with the first quarter of 2007, such revenues were for the first time to be recognised as liabilities. Please refer to our comments on the accounting policies under section (c) Intangible assets.

2. Other operating income

Other operating income mainly includes income from the release of provisions and accrued liabilities, from late payment and charge-back charges, advertising cost subsidies and also income from the invoicing of payment in kind to employees in the form of the use of company cars.

Other operating income also includes € 6,777 thousand (previous year: € 2,301 thousand) in revenue from the leasing of business premises.

Other operating income also includes € 16 thousand (previous year: € 21 thousand) from foreign currency translations.

3. Costs of material

Costs of material are broken down as follows:

€'000s	2007	2006
Costs of purchased goods	200,082	259,840
Costs of purchased services	1,080,808	1,329,167
	1,280,890	**1,589,007**

Costs of purchased goods principally comprise the cost value of mobile telephones sold under term contracts and also bundles from prepaid business as well as DSL hardware which has been sold.

Costs of purchased services primarily include fees for mobile telephony services, commission payments to retail partners as well as fixed network interconnection fees for providing and leasing DSL lines.

For comparing cost of materials with the corresponding previous year figure, it is first of all necessary to consider the effects of the Wholesale DSL agreement of freenet AG with DTAG which has been applicable since 23 May 2006; please refer to our comments on note 1 "Sales".

In addition, it has to be borne in mind that most of the customer acquisition costs in the contract customer areas are shown under costs of material. Certain costs of material in the contract customer areas have been capitalised as customer acquisition costs in accordance with IAS 37 since the fourth quarter of 2006 (only in relation to the "freenet*Komplett*" product area) and since the first quarter of 2007 (in relation to further major contract customer areas). The capitalisation of customer acquisition costs has thus comparatively resulted in a reduction in costs of material and thus higher gross profits.

4. Personnel expences

Personnel expenses are broken down as follows:

€'000s	2007	2006
Wages and salaries	115,373	116,123
Social contributions	19,194	19,641
	134,567	**135,764**

The average number of people employed by the Group rose by 3.3 percent, from 3,630 to 3,749 compared with 2006.

In the course of the financial year, personnel expenses linked to the performance of the share price amounted to € 11,001 thousand (previous year: € 8,705 thousand).

€'000s	2007	2006
Stock appreciation rights	10,777	8,956
Stock options (former mobilcom AG)	224	161
Stock options (former freenet.de AG)	0	–412
	11,001	**8,705**

The Company's stock appreciation programme resulted in personnel expenses of € 10,777 thousand (previous year: 8,956 thousand). For an explanation of the stock option programme as well as the stock appreciation programme, please refer to our comments to note 23 "Employee participation programmes" as well as section (m) in "Accounting and valuation methods".

Personnel expenses also comprise an expense of € 566 thousand for defined benefit plans (previous year: € 233 thousand), see also note 28 "Pension provisions and similar obligations".

Personnel expenses include a figure of € 8,917 thousand as the employer's social insurance contribution as costs of defined contribution benefit plans (previous year: € 9,100 thousand).

5. Depreciation and impairments

The following table sets out the depreciation and impairments:

€'000s	2007	2006
Depreciation on intangible assets	66,743	16,476
Impairments on intangible assets	7,207	0
Depreciation on property, plant and equipment	22,237	27,042
Impairments on property, plant and equipment	0	403
	96,187	**43,921**

The depreciation of € 88,980 thousand relates to intangible assets (€ 66,743 thousand compared with € 16,476 thousand in the previous year) and property, plant and equipment (€ 22,237 thousand compared with € 27,042 thousand in the previous year).

Of the figure shown for impairments in financial 2007, € 7,207 thousand is attributable to capitalised customer acquisition costs for customer contracts which were terminated in the course of the financial year.

The increase in depreciation and impairments compared with the previous year is mainly due to the asset "customer relations", which accounted for a total of € 61,650 thousand (previous year: € 3,621 thousand) of the depreciation and impairments.

Of the figure shown in the previous year for impairments in the Mobile Telephony segment, € 303 thousand is attributable to tenant fittings which can no longer be used, and € 100 thousand is attributable to IT equipment.

6. Other operating expenses

Other operating expenses chiefly comprise advertising and trade fair costs, costs of premises, network costs, postage costs and legal and consultancy costs.

In the financial year, costs of impairments and the default of receivables totalling € 16,121 thousand (previous year: € 17,826 thousand) were incurred. Of this figure, trade accounts receivable accounted for € 15,142 thousand (previous year: € 17,618 thousand) and other assets accounted for € 979 thousand (previous year: € 208 thousand).

This item also includes leasing expenses of € 41,806 thousand for operating leases (previous year: € 40,946 thousand).

A figure of € 30 thousand (previous year: € 15 thousand) is shown for foreign currency translation under other operating expenses.

7. Other interest and similar income

This item comprises the following:

€'000s	2007	2006
Interest receivable from banks, debt collection and similar income	14,277	14,724
Interest of tax refund	121	0
Market valuation of money market investments	99	367
Interest income from finance leases	13	12
	14,510	**15,103**

8. Other interest and similar expenses

This item is broken down as follows:

€'000s	2007	2006
Interest on supplementary tax payments	5,144	0
Other interest and similar expenses	2,031	404
Interest on pension obligations	65	55
Interest on finance leases	45	89
Cumulative interest from compounding of liabilities	44	41
Market valuation of money market investments (write-down)	40	0
	7,369	**589**

9. Taxes on income

This item comprises paid and outstanding taxes on income as well as deferred taxes.

€'000s	2007	2006
Current tax expense for the financial year	–14,022	–21,850
Tax expense for previous years	–9,037	–2,923
Deferred tax expense (previous year: income) due to the write-down (previous year: write-up) of deferred tax assets	–39,109	184,590
Deferred tax expense for temporary differences	–49,564	–20,427
Deferred tax expense for tax rate changes	–35,444	0
	–147,176	**139,390**

For further details concerning deferred taxes, please refer to note 17 "Deferred tax assets and liabilities".

Applying the average tax rate of the consolidated companies to the consolidated result before taxes on income would result in anticipated tax expenses of € 63.2 million (previous year: € 45.3 million). The difference between this amount and the actual tax expense) of € 147.2 million (previous year: tax income of € 139.4 million) is shown in the following reconciliation.

€'000s	2007	2006
Result before taxes on income	**163,706**	**117,617**
Expected tax expense applying a rate of 38.6 % (previous year: 38.5 %)	–63,191	–45,283
Change in allowance for deferred tax assets	–39,109	184,590
Tax effect of non-allowable expenses and tax-free income	–429	4,448
Effects from changes in tax rate	–35,444	0
Tax expense from previous years	–9,037	–2,923
Other income (previous year: expenses)	34	–1,442
Actual tax expense (previoius year: tax income)	**–147,176**	**139,390**
Effective tax rate in percent	89.90	–118.51

The above tax rate includes the unchanged corporation tax rate of 25 percent for fiscal 2007, the solidarity surcharge of 5.5 percent and the Group's average municipal trade tax rate of 397.03 percent (previous year: 392.73 percent). The average trade tax levy rate of the Group has increased compared with the previous year, and is the reason behind the change in the Group tax rate (38.6 percent compared with the previous year figure of 38.5 percent).

In the third quarter of 2007, the Act on the Corporation Tax Reform 2008 was adopted and published in the Federal Gazette. As a result of the reduction in the tax rate for corporation tax and trade tax applicable in Germany, the tax ratio will tend to decline. For the accrual of deferred taxes, the corporation tax rate of 15 percent applicable in future had to be used for the first time in the interim financial statements for the period ending 30 September 2007 and also in these financial statements for the period ending 31 December 2007.

The deferred income tax assets and liabilities were calculated as of 31 December 2007 with a total tax rate of 29.7 percent (previous year: 38.5 percent) after due consideration had been given to the temporary differences in accordance with the liability method; this is the explanation for the effect of tax rate changes shown for 2007.

10. Earnings per share

Undiluted earnings per share

Undiluted earnings per share are calculated by dividing the result attributable to the shareholders by the weighted average number of shares in circulation during the financial year.

	2007	2006[1]
freenet AG shareholder interest in consolidated result in €'000s	16,149	218,526
Weighted average of shares in circulation	96,061,016	62,416,710
Earnings per share in € (undiluted)	**0.17**	**3.50**

1 In relation to the former mobilcom AG.

Diluted earnings per share

Diluted earnings per share are calculated by dividing the result attributable to the shareholders by the weighted average number of shares in circulation increased by potentially diluting shares.

The number of potentially diluting shares is calculated as the difference between the potential ordinary shares attributable to employee stock option programmes valued at the subscription price and the ordinary shares issuable at fair value.

	2007	2006[1]
Interest of shareholders of freenet AG in the consolidated result €'000s	16,149	218,526
Weighted average of shares in circulation	96,061,016	62,416,710
Potential number of diluting shares	15,148	4,594
Weighted average number of shares in circulation plus potential number of diluting shares	96,076,164	62,421,304
Earnings per share in € (diluted)	**0.17**	**3.50**

1 In relation to the former mobilcom AG.

H. Notes to the consolidated balance sheet

11. Intangible assets and property, plant and equipment

Movements in property, plant and equipment and intangible assets are shown in the schedule of fixed assets. Overall, the carrying amount of the technical equipment and machinery shown under property, plant and equipment as of 31 December 2007 includes a figure of € 2 thousand (previous year: € 40 thousand) for items which are the subject of an ongoing finance lease.

Intangible assets include a figure of € 190,496 thousand for the costs of signing up customers; this amount is written off over the legal contract term of six to 24 months. The depreciation on customer acquisition costs amounted to € 45,410 thousand. In addition, impairments of € 7,207 thousand were recognised in relation to customer contracts; these are due to premature contract terminations.

In addition, German narrowband and broadband customer arrangements were acquired from two other players by way of purchase agreements in 2007. These customer arrangements, most of which were acquired from the Italian Tiscali S. p. A., were shown with a residual carrying amount of € 22,446 thousand as of 31 December 2007. They are depreciated over an estimated actual service life of 48 months. The depreciation in 2007 for these customer arrangements amounted to € 5,934 thousand.

Research and development costs charged to the income statement were insignificant.

12. Impairment test for non-monetary assets

In accordance with the provisions of IAS 36, we hereby provide the following details on asset impairment testing:

The “Mobile Telephony” cash generating unit (CGU) was assigned goodwill totalling € 13,889 thousand. The CGU “Mobile Telephony” consists of the Service Provider segment represented mainly by mcc GmbH, as well as the “No Frills” segments in which klarmobil GmbH operates.

As part of a strategic review process carried out by freenet AG in 2007, the sale of service-provider business (incl. “No frills”) was reviewed as a strategic option. Offers for this business unit were obtained in this connection. The highest purchase price quoted for this business unit was used as the realisable amount of the “Mobile Telephony” CGU.

For the goodwill allocated to the “Mobile Telephony” CGU, the impairment test established that there is no need for an impairment.

Goodwill of € 88,025 thousand was allocated to the “Broadband” CGU. Goodwill of € 3,717 thousand as well as intangible assets with an indefinite service life (brand rights) of 17,704 thousand were allocated to the “Hosting” CGU.

The value in use of the “Broadband” and “Hosting” units was shown as the realisable value in each case. Planning which covers the period up to and including 2015 and which was approved by management was used for calculating the value in use of these two CGUs.

Planning of revenues in the “DSL” segment is influenced by various value drivers. One significant driver is the share of the DSL market. The Group offers DSL products on the basis of the network infrastructure of DTAG and also with “freenet*Komplett*” on the basis of the network infrastructure of alternative providers. The DSL line as well as the access (traffic) is marketed to the new customers in the entire planning period. Before the Group offered DSL lines to customers for the first time in 2004, as a result of the Resale contract which then existed with DTAG, only the access was offered to customers.

As a result of the expected market saturation, annual growth rates in the user portfolio are anticipated in the planning period up to 2015. Planning is based on the assumption that the percentage of customers to whom the line is also offered will continuously increase in relation to the total number of the Group DSL customers.

In the DSL segment, we are also planning those cash flows which are generated in connection with the marketing of DSL connections. These mainly comprise the one-off provision fees contractually agreed with DTAG and the alternative subscriber network operators. In addition, the cash flows attributable to the provision of hardware as well as hardware mail order and sales commissions on the basis of the development in user numbers.

The “Hosting” segment comprises two principal products: Shared hosting and dedicated hosting. In shared hosting, bandwidth and memory are shared with other users, whereas dedicated hosting provides sole use of a complete server. The target groups for dedicated hosting are professional users and businesses, which lease their own server and use it for hosting purposes. By way of contrast, shared hosting is chiefly designed for private individuals who have their own domain but not their own server, whether leased or owned. Future growth will be geared to the development of internet penetration. Sales planning is based primarily on two value drivers: The first of these, namely overall user numbers and user retention is important for future business, but careful attention has also been given to the second, namely average customer sales. Increasing sales have been assumed in the planning period.

The capitalisation rate used in determining the value in use for the two CGUs is to be divided into a base interest rate plus a market risk premium required by shareholders in return for the assumption of business risk.

A basic rate of 4.75 percent (previous year: 4.5 percent) has been used for the CGUs “Broadband” and “Hosting”. An average risk premium of 5.0 percent (previous year: 4.0 percent) has also been used, in line with the current IDW recommendations. This average risk premium has to be modified to take account of the special risk structure of the particular company or segment to be valued. This company- and sector-specific risk is expressed in the so-called Beta factor. This has resulted in a Beta factor of 0.96 (previous year: 1.0) being used. The average risk premium multiplied by the Beta factor has accordingly resulted in a market risk premium of 4.8 percent (previous year: 4.5 percent).

The attainable growth in the expected developments of cash flows is reflected in medium-term planning for the the CGUs “Broadband” and “Hosting” CGUs for the planning period up to 2015. An equity risk premium is accordingly not necessary for this period. The sustainable growth for the two CGUs specified above in the years following 2016 can be recognised by actuarial means as an equity risk premium in the capitalisation rate. This equity risk premium has been set at 2.0 percent (previous year: 2.0 percent).

The impairment test established that it is not necessary for any impairments to be recognised for the goodwill and intangible assets of indefinite useful life for the CGUs “Broadband” and “Hosting”.

One possible change in the significant assumptions for the “Broadband” CGU pursuant to IAS 36.134 f) could be that increasing competition in this segment might mean that the achievable gross margins might be lower than planned. Even if this assumption is made on the basis of market growth, this would not lead to any impairment of the assets assigned to this CGU.

Goodwill of € 4,674 thousand as well as intangible assets of indefinite useful life of € 129 thousand have been allocated to CGUs other than “Mobile Telephony”, “Broadband” and “Hosting”. The goodwill allocated to each of these other CGUs is not significant. The sum of the goodwill allocated to these other CGUs is also not significant in relation to the total goodwill of € 110,304 thousand as well as the intangible assets of indefinite useful life of € 17,833 thousand shown in the Group as of 31 December 2007.

The impairment costs of € 7,207 thousand recognised in financial 2007 consisted exclusively of impairments in relation to capitalised customer acquisition costs. Please refer to our comments on note 13 “Impairment test for the capitalised customer acquisition costs”.

No impairment costs were incurred in financial 2006 for the “DSL” and “Hosting” CGUs. Of the figure stated for impairments recognised, € 403 thousand was attributable to the CGU “Mobile Telephony” for property, plant and equipment (of which € 303 thousand relating to tenant fittings which can no longer be used as well as € 100 thousand relating to IT equipment).

13. Impairment test for the capitalised customer acquisition costs

In accordance with the requirements of IAS 38, the Group capitalises some of its customer acquisition costs in the main contract customer areas. The carrying amount of the customer acquisition costs capitalised as of 31 December 2007 € 190,496 thousand (previous year: € 7,034 thousand).

An impairment test was carried out at the end of financial 2007 to assess whether the residual carrying amount in each of the units for which customer acquisition costs have been capitalised (Mobile Telephony, Broadband, Hosting, Narrowband) is at least covered by the margin which can probably be achieved in the remaining months until the end of the legal contract term of the individual customers to which the capitalised customer acquisition costs relate. The margin includes the income and expenditure items which can be almost completely and individually allocated to the various customers.

The test did not identify any impairment requirement for all units.

In addition, an impairment test was also carried out at the individual customer level.

The carrying amount includes the impairments of € 7,207 thousand recognised in the course of the fiscal year in relation to the capitalised customer acquisition costs. An impairment became necessary in the case of the termination of customers for whom the customer acquisition costs had been capitalised at the time of the termination; the process of calculating the impairment took into consideration the income which can probably still be generated with these customers after their termination.

14. Joint ventures

The consolidated financial statements include an investment in three joint ventures, namely FunDorado GmbH, Hamburg, (FunDorado), which was established in financial 2001 and in which the freenet Group holds a 50.0 percent stake (previous year: 50.0 percent). FunDorado operates a fee-based internet portal.

The following assets, liabilities, income and expenditure are shown as of 31 December 2007 or in financial 2007:

€'000s	**FunDorado GmbH**	**Attributable to Group**
Current assets	2,580	1,290
Non-current assets	614	307
	3,194	**1,597**
Current liabilities	2,076	1,038
Non-current liabilities	104	52
	2,180	**1,090**
Income	7,624	3,812
Expenses	7,100	3,550

The following assets, liabilities, income and expenditure are shown as of 31 December 2006 or in financial 2006:

€'000s	**FunDorado GmbH**	**Attributable to Group**
Current assets	2,232	1,116
Non-current assets	744	372
	2,976	**1,488**
Current liabilities	1,798	899
Non-current liabilities	104	52
	1,902	**951**
Income	6,142	3,071
Expenses	5,522	2,761

As was the case in the previous year, no contingent liabilities or capital obligations existed in connection with the Group's holding in this joint venture as of 31 December 2007. In financial 2007, FunDorado GmbH employed an average of 28 persons (previous year: 25).

Effective 13 October 2006, FunDorado GmbH acquired a 50 percent stake in NetCon Media s.r.o. based in Hlucin, the Czech Republic (referred to in the following as NetCon). The Company produces content which is designed primarily to be used in the fee-based internet portal of FunDorado. NetCon in turn owns a 100 percent stake in its sales company siXXup new Media GmbH, Pulheim (referred to in the following as siXXup). NetCon as well as siXXup are both included as joint ventures in the consolidated financial statements. For the sake of simplicity, 1 November 2006 has been chosen as the date of initial consolidation.

Including the balances of its subsidiary siXXup, NetCon shows the following assets and liabilities as of 31 December 2007, and the following assets, liabilities, income and expenses for 2007:

€'000s	**NetCon Media s.r.o.**	**Attributable to Group**
Current assets	160	40
Non-current assets	238	60
	398	**100**
Current liabilities	52	13
Non-current liabilities	0	0
	52	**13**
Income	1,405	351
Expenses	1,383	346

Including the balances of its subsidiary siXXup, NetCon shows the following assets and liabilities as of 31 December 2006, and the following assets, liabilities, income and expenses for the months of November and December 2006:

€'000s	**NetCon Media s.r.o.**	**Attributable to Group**
Current assets	124	31
Non-current assets	417	104
	541	**135**
Current liabilities	74	19
Non-current liabilities	0	0
	74	**19**
Income	157	39
Expenses	169	42

NetCon, including its subsidiary, employed 57 (previous year: 5) persons on the balance sheet date.

As of 31 December 2007, there were no contingent obligations or capital commitments in connection with the Group interest in these joint ventures.

15. Investments accounted for using the equity method

The carrying amount of companies accounted for using the equity method as of 31 December 2007 was € 3,174 thousand (previous year: € 3,501 thousand); as was the case in the previous year, this related to KielNET GmbH Gesellschaft für Kommunikation, Kiel (referred to in the following as “KielNET”). The Group owns a 50 percent stake in this company. If voting in the case of resolutions is tied, the deciding vote is held by Stadtwerke Kiel AG, Kiel. KielNET supplies telecommunication services within the license area in the Kiel region.

In financial 2007, KielNET generated sales of € 20,666 thousand (previous year: € 20,823 thousand) as well as net income of € 2,072 thousand (previous year: € 2,292 thousand). As of 31 December 2007, the assets of this company amounted to an aggregate € 19,585 thousand (previous year: € 19,647 thousand), and the liabilities amounted to an aggregate € 13,289 thousand (previous year: € 12,696 thousand).

The € 327 thousand decline in the carrying amount from the companies accounted for using the equity method compared with 31 December 2006, in conjunction with earnings of € 1,075 thousand generated by the companies accounted for using the equity method in 2007, is due to the fact that a dividend payment of € 1,402 thousand was received from KielNET; this has to be treated as a reduction in the equity participation.

16. Other investments

Other investments reported as of the balance sheet amounted to an unchanged € 304 thousand, and related to the investment in Libri.de GmbH, Hamburg. This investment is shown at cost.

No impairments had been recognised in relation to the other financial assets as of the balance sheet date and also as of the previous year reference date. Moreover, no disposals have taken place.

17. Deferred income tax assets and liabilities

After temporary differences were taken into consideration, deferred tax assets and liabilities were calculated using the liability method with a total tax rate of 29.7 percent (previous year: € 38.5 percent).

The following amounts are shown in the consolidated balance sheet:

€'000s	**31.12.2007**	**31.12.2006**
Deferred tax assets	52,303	176,652
Deferred taxes liabilities	0	–232
	52,303	**176,420**

Of the figure shown for deferred income tax assets, € 24,241 thousand (previous year: € 30,122 thousand) are classified as current and € 28,062 thousand (previous year: € 146,530 thousand) are classified as non-current. In the previous year, the income tax liabilities shown in the balance sheet were entirely of a non-current nature.

Changes in the disclosed deferred income tax assets and liabilities for financial 2007 and 2006 are shown in the following two tables:

Changes in deferred income tax assets and liabilities in 2007 (€'000s)	**1.1.2007**	**Income and expenses from taxes on income**	**31.12.2007**
Fixed assets from finance leases	–16	16	0
Other property, plant and equipment	–717	319	–398
Intangible assets	–29,116	–45,620	–74,736
Financial assets	–978	–42	–1,020
Loss carry-forwards	207,080	–104,596	102,484
Provisions	584	–614	–30
Other liabilities and accruals	–418	26,368	25,950
Other	1	52	53
	176,420	**–124,117**	**52,303**

Movements during 2006:

Changes in deferred income tax assets and liabilities in 2006 (€'000s)	**1.1.2006**	**Income and expenses from taxes on income**	**31.12.2006**
Fixed assets from finance leases	–675	659	–16
Other property, plant and equipment	–92	–625	–717
Intangible assets	–28,813	–303	–29,116
Financial assets	–845	–133	–978
Loss carry-forwards	43,000	164,080	207,080
Provisions	328	256	584
Other liabilities and accruals	–566	148	–418
Other	–80	81	1
	12,257	**164,163**	**176,420**

The summarised net development of deferred taxes is shown in the following:

€'000s	**2007**	**2006**
As of 1.1.	176,420	12,257
Tax expense (previous year: income)	–124,117	164,163
As of 31.12.	**52,303**	**176,420**

The existing tax loss carry-forwards exceed the sum of the forecast cumulative result of the following financial years. Accordingly, a deferred tax asset has also only been recognised in the consolidated balance sheet to the extent that the realisation of that asset is evaluated as probably. The expected results are based on a Company's forecast for pre-tax. As of 31 December 2007, deferred taxes relating to tax loss carry-forwards amounted to € 102,484 thousand (previous year: € 207,080 thousand). Of this figure, € 54,520 thousand (previous year: € 118,816 thousand) is attributable to corporation tax losses carried forward and € 47,964 thousand (previous year: € 88,264 thousand) is attributable to trade tax losses carried forward. Other losses carried forward for which no deferred tax asset has been shown in the consolidated balance sheet are as follows: € 2.9 billion (corporation tax) and € 2.4 billion (trade tax) (previous year: € 2.8 billion corporation tax and € 2.4 billion trade tax).

18. Inventories

Inventories are broken down as follows:

€'000s	**31.12.2007**	**31.12.2006**
Mobile telephones/accessories	12,360	8,909
DSL hardware	8,618	8,214
Bundles and vouchers	4,709	5,963
SIM cards	3,881	3,290
Other	1,880	1,343
	31,448	**27,719**

An impairment of € 120 thousand (previous year: € 1,188 thousand) has been recognised in relation to year-end stocks of inventories.

19. Receivables and other assets

This item is broken down as follows:

€'000s	31.12.2007	31.12.2006
Trade accounts receivable	200,042	192,189
Other assets	53,040	67,193
Advance payments	31,717	15,867
	284,799	**275,249**

Trade accounts receivable are due exclusively from external parties, and comprise mainly receivables attributable to fees, equipment sales and fixed network and internet services.

The total of trade accounts receivable and the other non-derivative financial assets, less impairments which had been recognised, amounted to € 253,082 thousand as of 31 December 2007 (previous year: € 252,639 thousand). In the freenet Group, the most significant item in this category are trade accounts receivable. These are due mainly from end customers, and to a lesser extent they are due from business customers as well as dealers and sales partners.

Invoices are issued by the Group itself in the segments Mobile Telephony, Broadband, Portal and Hosting. In the segments B2B and Narrowband, some invoices are issued by the Group itself, and the collection facility of Deutsche Telekom AG (DTAG) is used for some other invoices.

Where invoices are issued to end customers by the Group itself, they are mostly due immediately after the invoice is raised. The invoices submitted to DTAG have a payment term of 30 days.

Last year, in the case of trade accounts receivable which were not impaired and which were not overdue, no renegotiations were held in relation to existing receivables.

As of 31 December 2007, trade accounts receivable in the amount of € 156,437 thousand (31 December 2006: € 160,626 thousand) are neither impaired nor overdue.

Trade accounts receivable in the amount of € 12,500 thousand (31 December 2006: € 7,869 thousand) are overdue but not impaired. These receivables are due from various customers who have not defaulted in the past.

The maximum default risk as of the balance sheet date corresponds to the carrying amount of the above-mentioned trade accounts receivable.

The Group does not have any securities which have been provided to it.

In the course of fiscal 2007, fully impaired overdue receivables were sold for a price of € 3,754 thousand. All major risks and opportunities associated with ownership of these receivables were transferred to the buyer.

The following information relates to the age structure of this category of trade accounts receivable and non-derivative financial assets.

€'000s	Carrying amount 31.12.2007	Thereof: On reference date neither impaired nor overdue	Thereof: Not impaired on reference date and overdue by		
			Fewer than 90 days	Between 91 and 180 days	More than 180 days
Trade accounts receivable	200,042	156,437	4,925	2,709	4,866
Other non-derivative financial assets	53,040	51,738	0	18	1,113
	253,082	**208,175**	**4,925**	**2,727**	**5,979**

€'000s	Carrying amount 31.12.2006	Thereof: On reference date neither impaired nor overdue	Thereof: Not impaired on reference date and overdue by		
			Fewer than 90 days	Between 91 and 180 days	More than 180 days
Trade accounts receivable	192,189	160,626	1,264	2,756	3,849
Other non-derivative financial assets	60,450	51,990	0	0	2,042
	252,639	**212,616**	**1,264**	**2,756**	**5,891**

The following table sets out information concerning the movement in imparments for the category of trade accounts receivable as well as non-derivative financial assets:

€'000s	
Impairments created as of 31 December 2006	83,783
Impairments created as of 31 December 2007	94,911
Net allocation to impairments in financial 2007	**11,128**

€'000s	
Impairments created as of 31 December 2005	104,023
Impairments created as of 31 December 2006	83,783
Net reversal of impairments in financial 2006	**–20,240**

Trade accounts receivable include receivables attributable to finance leases based on the following anticipated payment streams:

€'000s	31.12.2007	31.12.2006
Within one year	3,939	1,850
Between one year and five years	1,404	844
	5,343	**2,694**
As yet unrealised financing income (discounting)	–221	–119
Present value of receivables attributable to finance leases	**5,122**	**2,575**

A risk rate of 6.0 percent has been chosen for discounting the receivables attributable to finance leases, so that the present value which is shown corresponds to the market value. For further information, please refer to the disclosures relating to the accounting and valuation methods, section E. Accounting and valuation methods, (f) Leases – the Group as lessor. An impairment test was not carried out because there are no indications of the existence of any impairments.

The other assets include accounts due from fiscal authorities as well as network operator commissions. As a result of the sale of a subsidiary, the receivables attributable to this company and corresponding impairments of € 23,807 thousand included in the figure were reclassified as other assets. For further comments, please refer to C. Consolidated companies.

Of the figure stated for receivables and other assets, € 203 thousand (previous year: € 160 thousand) are attributable to related parties, see note 33 "Transactions with related parties".

20. Cash and cash equivalents

Cash and cash equivalents are broken down as follows:

€'000s	31.12.2007	31.12.2006
Cash in hand and cash at banks	53,034	529,838
Securities (money market paper)	710	5,499
	53,744	**535,337**

The following is a reconciliation of liquid assets with cash and cash equivalents in accordance with IAS 7, consisting of cash at banks, cash in hand, cheques and current money market paper and stocks which can be liquidated at any time as well as current financial liabilities with an original term of up to three months:

€'000s	31.12.2007	31.12.2006
Liquid assets	53,744	535,337
Liabilities as part of current finance scheduling due to banks	–90,179	0
	–36,435	**535,337**

Of the total figure stated for liquid assets, the Group was not able to access € 6,450 thousand as of the balance sheet date as a result of the provision of security and funds which had not been definitively released.

21. Current tax assets

The current tax assets essentially comprise receivables attributable to corporation tax and trade tax.

22. Share capital and additional paid-in capital

	Number of shares 000	Share capital €'000s	Additional paid-in capital €'000s	Retained earnings €'000s	Total €'000s
As of 1. 1. 2006	**62,417**	**65,702**	**255,648**	**36**	**321,386**
Recognition of stock-linked compensation	0	0	–1,087	0	–1,087
As of 31. 12. 2006	**62,417**	**65,702**	**254,561**	**36**	**320,299**
As of 1. 1. 2007	**62,417**	**65,702**	**254,561**	**36**	**320,299**
Recognition of stock-linked compensation	0	0	857	0	857
Merger with freenet AG and acquisition of minority interests in the former freenet.de AG	33,644	30,359	134,726	–36	165,049
As of 31. 12. 2007	**96,061**	**96,061**	**390,144**	**0**	**486,205**

The issued share capital of the Company amounted to € 96,061 thousand on the balance sheet date, and consisted of 96,061,016 no-par value shares with a theoretical value of € 1.00 in the share capital. The entire share capital is fully paid up. All shares have been issued with equal rights.

50 thousand of these shares are held by MobilCom Logistik GmbH, Schleswig, and the shares of the latter company are in turn wholly owned by the Company. These shares are shown at acquisition cost of € 50 thousand.

The figure shown for the share capital as of 31 December 2006 was the same as that shown for the share capital of the former mobilcom AG.

When the merger between freenet.de and the Company became effective on 2 March 2007, additional paid-in capital increased by € 134.7 million to € 390.1 million. Because the minority shareholders of the former freenet.de now own a direct equity participation in the Company, minority interests are now no longer shown in relation to the consolidated result because the former external shareholders of freenet.de have become direct shareholders as a result of the merger between freenet.de and the Company.

Authorised capital increase

In accordance with the resolution of the shareholders' meeting of 19 August 2005, there is an authorised capital increase of € 48,030,508.00 (authorised capital increase 2005) at freenet AG; this empowers the Managing Board, subject to the consent of the Supervisory Board, to increase the share capital on one or more occasions before 18 August 2010 by a total of up to € 48,030,508.00 by way of issuing new shares.

Contingent capital

In accordance with the resolution of the shareholders' meeting of 20 July 2007, the contingent capital of the Company was increased by up to € 318,447.00.

As a result of the merger in accordance with section 23 of the German Transformation Act (Umwandlungsgesetz), the Company is obliged to grant equivalent rights to holders of stock options of the former mobilcom AG. In accordance with section 4 of the merger agreement of 8 July 2005, this was achieved by the Company converting the former subscription rights for shares in mobilcom AG into subscription rights for shares of the Company in accordance with the ratio of 1:1 defined in the merger agreement for converting the shares of mobilcom AG into shares of the Company.

In order to be in a position to issue new shares of the Company to the option holders in accordance with the regulations set out in the option conditions if the above-mentioned stock options are exercised, contingent capital of € 318,447.00 was created. The contingent capital increase is only carried out to the extent that the holders of the option rights actually exercise their right to subscribe for shares of the Company and only to the extent that the Company does not grant any of its own shares or pay cash in order to fulfil the option rights. The new shares participate in profits from the beginning of the fiscal year in which they are issued.

23. Employee participation programmes

The Group offers the following employee participation programmes:

- Stock appreciation rights of freenet AG
- Stock options of the former mobilcom AG

The stock option programme of the former freenet.de AG was terminated in financial 2007 by way of payment.

Stock appreciation rights of freenet AG

In the course of 2006, freenet AG introduced a so-called stock appreciation programme by issuing a total at present of 5,145,000 stock appreciation rights (Aktienwertsteigerungsrechte – SARs) to senior executives, including members of the Managing Board. No other stock appreciation rights were issued in the course of the fiscal year 2007. The stock appreciation programme does not confer any rights to purchase shares; instead, it comprises a cash payment for each stock appreciation right equivalent to the difference between the share price of the Company applicable at the point at which the rights are exercised (capped however at € 27.00) and a fixed strike price of € 11.16.

The value of dividend payments to the shareholders and other benefits for the shareholders are deducted from the strike price in accordance with recognised methods for the total shareholder return approach. On the assumption that the employment contract of a senior executive is still in existence, 20 percent of the stock appreciation rights to which a senior executive is entitled become exercisable on 7 November of each year if certain targets are attained.

For the stock appreciation rights which became exercisable starting on 7 November 2006, the relevant target is that the price of the Company's shares must exceed the strike price (under the total shareholder return approach) by at least 5 percent at least on one occasion in the period starting immediately before the corresponding stock appreciation rights become exercisable and ending with the expiry of the term in February 2012. For the stock appreciation rights which become exercisable in subsequent years, the percentage increases by five percent in each case, in other words to a figure of ten percent for the stock appreciation rights for the waiting time ended on 7 November 2007, to a figure of 15 percent for the stock appreciation rights becoming exercisable on 7 November 2008, etc.

If a change of control takes place at the Company, the above waiting periods are no longer applicable; however, the targets are retained.

The term of all stock appreciation rights is due to end on 2 February 2012. The exercise period in each instance is defined as the period which commences 31 stock exchange trading days on the stock exchange in Frankfurt am Main after the end of the first ordinary shareholders' meeting of the Company after the end of the corresponding waiting period until the end of the term.

Details of stock appreciation rights which have so far been issued are set out in the following table:

Stock appreciation rights	**Strike price €**	**Target price €**	**Maturity**	**Balance SARs 31.12.2006**	**Issued**	**Exercised**	**Disposals**	**Balance SARs 31.12.2007**
Tranche 1	11.16	11.72	2.2.2012	1,029,000	0	1,020,000	0	9,000
Tranche 2	11.16	12.28	2.2.2012	1,029,000	0	0	5,000	1,024,000
Tranche 3	11.16	12.84	2.2.2012	1,029,000	0	0	5,000	1,024,000
Tranche 4	11.16	13.40	2.2.2012	1,029,000	0	0	5,000	1,024,000
Tranche 5	11.16	13.95	2.2.2012	1,029,000	0	0	5,000	1,024,000
				5,145,000	**0**	**1,020,000**	**20,000**	**4,105,000**

As of 31 December 2007, 9,000 SARs were exercisable; the intrinsic value of each SAR was € 4.83.

The obligation arising from the stock appreciation rights programme was determined in accordance with IFRS 2 using an option price model (binomial model). In the course of fiscal year 2007 this programme resulted in personnel expenses of € 10,777 thousand; of this figure, € 7,281 thousand was paid in cash, and € 3,496 thousand comprised expenses resulting from the net allocation to the provision. In 2007, the SARs were exercised at an average share price of € 18.41. A sundry provision of € 12,452 thousand, including € 5,099 thousand current provisions and € 7,353 thousand non-current provisions, was shown for the outstanding stock appreciation rights as of 31 December 2007.

The valuation parameters of the option price model were defined as follows: The reference date price of the Company of € 15.99 was used as the stock price. The expected volatility was defined as 44.0 percent – it was determined using an estimate of the future performance of the share price of the Company taking account of a mean value between the historical volatility as well as the implied volatility of the shares of freenet AG or the shares of the former parent company of the Group mobilcom AG. The risk-free interest rate was determined on the basis of the yield structure curve of German Federal Bonds as of the balance sheet date. As of 31 December 2007, this resulted in a risk-free rate of between 4.04 and 4.11 percent for the individual tranches. For each of the measured tranches, the expected remaining term of the stock appreciation rights was determined as the remaining waiting time as of the valuation reference date plus half of the remaining term after the end of the waiting time is attained.

Stock options of the former mobilcom AG

The former mobilcom AG granted stock options to the Managing Board, the executive bodies of the subsidiaries and selected employees of mobilcom AG and the following companies affiliated with mobilcom AG. In accordance with section 4 (1) of the merger agreement of 8 July 2005, which was signed by the Company as well as mobilcom AG and freenet.de AG, freenet AG grants identical rights to all holders of options in accordance with section 23 UmwG, because the mobilcom shares were converted in a ratio of 1:1 into shares of freenet AG.

All stock options are subject to the following issue conditions: The options are not permitted to be exercised before the expiry of two years after the point at which they are issued (shut-out period). After the shut-out period, up to 50 percent of the granted option rights can be exercised; a further 25 percent can initially be exercised after a period of three years, and the remaining option rights can only be exercised after a period of four years after the point at which they were issued. After the expiry of the corresponding shut-out period, a further period of three years is defined as the period in which the rights can be exercised.

Details concerning the options which have been issued so far are set out in the following table:

Stock options	**Exercise price €**	**Term until**	**Date of issue**	**1.1.2007**	**Expiry**	**Exercised**	**Disposals**	**31.12.2007**
Tranche 2001	24.40	Nov. 2008	12.11.2001	18,700	8,600	0	1,500	8,600
Tranche 2004	20.51	Mar. 2011	31.3.2004	304,116	0	162,490	13,932	127,694
				322,816	**8,600**	**162,490**	**15,432**	**136,294**

Movements in the stock options in the previous year are shown in the following:

Stock options	**Exercise price €**	**Term until**	**Date of issue**	**1.1.2006**	**Expiry**	**Exercised**	**Disposals**	**31.12.2006**
Tranche 2001	24.40	Nov. 2008	12.11.2001	54,400	23,700	0	12,000	18,700
Tranche 2004	20.51	Mar. 2011	31.3.2004	400,778	0	393	96,269	304,116
				455,178	**23,700**	**393**	**108,269**	**322,816**

The 136,294 (previous year: 322,816) share options which had not been exercised as of the balance sheet date are dated options which are linked to the employee's relationship within the Group. At the end of the financial year, 104,371 (previous year: 170,758) option rights were exercisable in total.

Only stock options of the tranche 2004 were exercised during last year. The difference to be granted for each option is defined as the difference between the average XETRA closing price of the shares of the Company on the last ten trading days before the exercise date and the exercise price of € 20.51. For the 162,490 exercised option rights, the average share price was € 23.88.

The options recognised as disposals (1,500 options) were issued to employees whose employment contract at a Group company had been terminated before the end of the exercise period. In addition, the fiscal year saw the expiry of 8,600 stock options for which the contractually defined exercise period ended.

In the previous year, starting with a balance of 455,178 stock options as of 1 January 2006, 393 options were exercised with an average share price of € 20.83. After deducting 23,700 expired options for which the contractually fixed exercise period ended, and 108,269 disposals, this resulted in a final balance 322,816 outstanding stock options as of 31 December 2006.

The stock options are valued by means of a binomial model. In these models, possible developments of a stock price are modelled using a binomial decision tree. The valuation is based on the following assumptions: With the exercise price of € 20.51, the closing price of freenet shares on the Frankfurt stock exchange (XETRA) on 28 December 2007 was used (€ 15.99). The expected volatility was set at 44.0 percent – it was estimated using an estimate of the future performance of the share price of freenet AG in XETRA trading of the Frankfurt stock exchange, including historical volatility. The no-risk interest rate for matching maturities was determined separately for the exercisable options as well as for options subject to a shut-out period of one and two years respectively. The expected remaining terms of the stock options, broken down over the corresponding shut-out periods, are defined as the corresponding periods to the expiry date. The expected dividend yield is specified as 1.51 percent.

Stock options of the former freenet.de AG

The former freenet.de AG granted stock options of freenet.de AG to the Managing Board, the executive bodies of the subsidiaries and selected employees of freenet.de AG and the following affiliated companies. All stock options related to the purchase of new ordinary shares in freenet.de AG and were granted subject to the following conditions: The options cannot be exercised before the expiry of a period of two years after the point at which they were issued. After a waiting period of two years, 40 percent of the granted options can be exercised, and a further 20 percent can be exercised on each occasion after three, four and five years. Options which are not exercised expire six years after the point at which they are issued or at the point at which the employee ceases to be employed in the freenet Group.

Details of the options issued under this programme are set out in the following table:

Stock options freenet.de AG	**Exercise price €**	**Term until**	**Date of issue**	**1. 1. 2007**	**Unwinding**	**31. 12. 2007**
Tranche 2001/02	9.79	July 2007	1. 7. 2001	1,200	1,200	0
Tranche 2002	2.97	July 2008	11. 7. 2002	174,000	174,000	0
Tranche 2003	3.49	June 2009	19. 6. 2003	359,992	359,992	0
				535,192	**535,192**	**0**

Within the framework of the merger which was completed in the course of the financial year, agreement was reached with all option holders with regard to the dated options, according to which the beneficiaries waived their entitlement to their stock options and all related rights in return for cash compensation. This agreement was conditional on the merger of freenet.de AG and mobilcom AG with the Company becoming effective. For each stock option, the compensation is equivalent to the difference between the unweighted average of the XETRA closing prices of freenet shares on the last 30 market trading days before the shareholders' meeting of freenet.de AG on 25 August 2005 (€ 23.09) and the exercise price of the corresponding stock option.

The provision of € 10,678 thousand which existed as of the end of the previous year (which was created in 2005) was fully utilised for paying cash compensation.

24. Trade accounts payable, other liabilities and accruals

The trade accounts payable as well as other liabilities and accruals are broken down as follows:

€'000s	31.12.2007	31.12.2006
Other liabilities and accruals	244,931	150,939
Trade accounts payable	103,004	94,649
Advance payments received	65,361	58,855
	413,296	**304,443**

The other liabilities and accruals include public sector subsidies. These relate to accrued income for investment subsidies in accordance with the Investitionszulagengesetz (Investment Subsidy Act) as well as subsidies from the Gemeinschaftsaufgabe Ost programme.

In financial 2007, new subsidies of € 412 thousand (previous year: € 1,622 thousand) were granted, and a figure of € 1,399 thousand (previous year: € 1,184 thousand) was recognised as income in the income statement from the pro-rata reversal of deferred liabilities, as described in E. Accounting and valuation methods, note (o). Deferrals of € 1,632 thousand for public subsidies (previous year: € 2,541 thousand) were shown as of 31 December 2007.

Liabilities due to related parties amount to € 94 thousand (previous year: 0). Please refer to note 33 “Transactions with related parties”.

Of the overall figure stated for liabilities, € 383,539 thousand (previous year: € 302,101 thousand) is due during the next 12 months. Liabilities in the amount of € 29,672 thousand (previous year: € 2,342 thousand) have a maturity of between one year and five years; all other liabilities are due after more than five years.

Other liabilities which are due to mature after 31 December 2008 are discounted using a normal market rate of 4.5 percent, and the capitalised carrying amount accordingly is equivalent to the current market value.

Of the figure shown for the liabilities in the categories trade accounts payable and other non-derivative financial liabilities, € 310,612 thousand (previous year: € 236,440 thousand) are due within one year, € 29,672 thousand (previous year: € 2,342 thousand) are due between one year and five years and € 85 thousand (previous year:0) are due more than five years after the balance sheet date.

25. Current income tax liabilities

Current income tax liabilities mainly show the liabilities due to the fiscal authorities resulting from ongoing tax audits for the years 2000 to 2004 and corporation tax, solidarity surcharge and trade tax relating to financial 2005 and 2006.

26. Debt

Debt is structured as follows:

€'000s	31.12.2007	31.12.2006
Non-current		
Liabilities from finance leases	614	717
	614	**717**
Current		
Liabilities to banks	90,179	0
Liabilities from finance leases	103	97
	90,282	**97**
	90,896	**814**

With regard to the maturity of the finance lease liabilities shown in the category of liabilities from finance lease, please refer to our comments on note 28 “Finance leases”.

Liabilities due to credit institutions are of a short-term nature. With regard to liabilities due to banks, the Group has not taken on any obligations as a result of providing securities.

27. Finance leases

The minimum lease payments are due as follows:

€'000s	31.12.2007	31.12.2006
Minimum lease payments		
Within one year	142	142
Between one year and five years	568	565
More than five years	142	283
	852	**990**
Interest content of future leasing payments		
Within one year	39	45
Between one year and five years	91	115
More than five years	5	16
	135	**176**
Present values of the total liabilities from finance leases	**717**	**814**

The maturities of the total liabilities of finance leases are shown in the following:

€'000s	31.12.2007	31.12.2006
Within one year	103	97
Between one year and five years	477	450
More than five years	137	267
	717	**814**

As was the case in the previous year, the finance lease obligations shown as of the balance sheet date relate to a rental agreement for technical fittings in a data centre of the Strato-Group. The value shown in the balance sheet is equivalent to the present value of the contractual minimum lease payments, including the first option right for extension in favour of the Strato-Group, which is expected to be exercised. The interest rate used as the basis for recognising the resultant finance lease obligations is unchanged at 5.5 percent.

28. Pension provisions and other obligations

The pension obligations are a consequence of direct pension commitments. The pension benefit provided in each case is the payment of a lifetime retirement pension upon reaching the age of 60 or 65. The pension benefits are financed by a reinsured benevolent fund. The direct pension commitments are always determined by the amount of salary and the time of service at the Company.

The amount of the provision in the consolidated balance sheet is calculated as follows:

€'000s	31.12.2007	31.12.2006
Present value of funded obligation	1,632	1,531
Fair value of plan assets	–829	–699
Actuarial profits/losses	26	–294
Provision shown in balance sheet	**829**	**538**

It is expected that these obligations will be fulfilled in the long term.

The following table sets out the development in the present value of the funded obligation:

€'000s	2007	2006
As of 1.1.	**1,531**	**1,357**
Subsequent service costs	359	0
Current service cost	242	253
Interest expense	65	55
Actuarial gains	–565	–134
As of 31.12.	**1,632**	**1,531**

The plan assets consist of a reinsurance policy concluded by the benevolent fund set up for this purpose with a fair value of € 829 thousand (31 December 2006: € 699 thousand). The following table sets out the development in fair value:

€'000s	**2007**	**2006**
As of 1.1.	**699**	**400**
Expected income from plan assets	36	20
Difference between expected and actual income from plan assets	–255	–22
Employer contribution to plan assets	349	301
As of 31.12.	**829**	**699**

In 2008, there are plans for employer contributions of € 349 thousand to be allocated to plan assets.

The following items are recognised in the consolidated income statement:

€'000s	**2007**	**2006**
Current and subsequent service cost[1]	601	253
Interest expense	65	55
losses (realised)	9	13
Anticipated income from plan assets	–35	–20
Total cost of defined benefit plans	**640**	**301**
Thereof amount recognised in personnel expenses (note 4)	566	233
Thereof recognised in other operating expenses	9	13
Thereof recognised in interest and similar expenses (note 8)	65	55

1 Of the figure shown for service costs in financial 2007, €242 thousand is attributable to current service costs, and € 359 thousand is attributable to subsequent service costs.

Movements in the amounts recognised as provisions are shown in the following:

€'000s	**2007**	**2006**
As of 1.1.	**538**	**539**
Total expense recognised in the consolidated income statement	640	300
Payments into plan assets	–349	–301
As of 31.12.	**829**	**538**

The main actuarial assumptions are as follows:

In percent	31.12.2007	31.12.2006
Discount rate	5.70	4.50
Anticipated income from plan assets	5,0	5,0
Future salary increases	0,0	0,0
Future pension increases	2,0	2,0

29. Other provisions

Other provisions are broken down as follows:

€'000s	1.1.2007	Consumption	Release	Cumulative interest	Allocation	31.12.2007
Outstanding stock options and stock appreciation rights	20,881	18,538	612	0	10,777	12,508
Litigation risks	17,314	9,780	2,702	0	2,123	6,955
Restructuring	862	501	361	0	0	0
Contingent losses	993	866	127	0	0	0
Dismantling obligations	1,463	0	0	44	0	1,507
Interest expense due to tax audit	0	0	0	0	2,597	2,597
	41,513	**29,685**	**3,802**	**44**	**15,497**	**23,567**

Further details concerning the creation of provisions for outstanding stock options and stock appreciation rights are documented under note 23 “Employee participation programmes”.

The provisions for litigation risks primarily concern the presumed costs from various legal actions against group companies. The greater part is a consequence of litigation with former trading partners and customers, challenges against resolutions of the shareholders’ meeting and actions relating to unfair trade practises. The Group expects that the majority of the disputed questions will be settled during financial 2008. More information is not given here so that the legal and negotiating position is not announced ahead of time, thereby creating a risk for the position.

The restructuring provision created in the course of fiscal year 2006 was completely reversed within the fiscal year in line with the restructuring plan.

The provisions for anticipated losses mainly comprised obligations arising from the premature termination of a rental agreement. Of the total amount of € 993 thousand, a figure of € 127 thousand had not been consumed by the end of the financial year; this figure was reserved because there were no further financial obligations.

Of the figure stated for dismantling obligations, € 533 thousand relate to the present value of costs of obligations for dismantling tenant fittings in data centres of STRATO. As was the case in the previous year, a rate of 4.25 percent has been used for discounting purposes. The outflow of funds is expected after the presumed expiry of the long-term leases on which they are based in 2012 or 2013. Of the figure stated for the provision for dismantling obligations,

€ 975 thousand relates to obligations for dismantling tenant fittings and various technical and administration locations of the Group. After the probable expiry of the underlying tenancy agreements, the outflow of funds for this part of the provision is expected to be € 736 thousand in 2008 and € 239 thousand in the years 2009 to 2014. The provisions have again been discounted with a rate of 4.25 percent.

The tax audit for the assessment periods 2000 to 2004 which was ongoing for major companies of the freenet Group was completed at the end of 2007. Please refer to our comments on note 25 "Current income tax liabilities". A provision of € 2,597 thousand was created for the expected interest charges resulting from this tax audit, with due consideration being given to advance payments which have already been made. Because the definitive tax notices are to be issued in 2008, the Group expects to utilise this provision in 2008.

I. Other details

30. Other financial obligations

At the end of the financial year, there are operating lease obligations (which cannot be terminated) from leases and leasing agreements as well as maintenance, support and other obligations and order commitments in the following amounts:

€'000s	31.12.2007	31.12.2006
Rent and leasing obligations		
Due within one year	39,997	43,784
Due between one and five years	28,946	27,163
Due term greater than five years	8,487	3,949
	77,430	**74,896**
Maintenance support and other obligations		
Due within one year	4,706	7,546
Due between one and five years	7,356	6,767
Due term greater than five years	6,785	9,360
	18,847	**23,673**
Acceptance obligations from orders		
Regarding intangible assets	789	39
Regarding property, plant and equipment	4,573	9,118
Regarding inventories, expenses and services	29,290	31,856
	34,652	**41,013**
	130,929	**139,582**

The liabilities from leases and leasing agreements result essentially from the leasing of fixed network lines and the leases for office space and shops and from hardware leasing. As of the balance sheet date, there were options for extending the majority of leases and leasing agreements. The conditions of these extension options are in all cases freely negotiable or identical to the current conditions of the agreements. The liabilities from maintenance, support and other agreements are based primarily on contracts for the network infrastructure in the "Fixed Network/Internet" segment.

The acceptance obligations from orders at the end of the financial year amounted to € 34,652 thousand (previous year: € 41,013 thousand). € 5,362 thousand (previous year: € 9,157 thousand) of this figure is attributable to the procurement of fixed assets – it includes, among other items, the obligation agreed between the Group and TELES AG, Berlin, in December 2004 concerning the acceptance of technical equipment and services valued at € 3,752 thousand net resulting from the acquisition of the Strato-Group. This liability is shown in the table under the acceptance obligations from orders relating to property, plant and equipment. The obligation has to be fulfilled by 31 December 2008. The other acceptance obligations relate primarily to merchandise, e.g. mobile telephony devices and accessories.

Other liability obligations exist primarily with regard to guarantees for shop rents and amounted to € 4,304 thousand (previous year: € 3,683 thousand) as of the balance sheet date.

31. Notes to the consolidated cash flow statement

Cash and cash equivalents consist of cash at banks, cash in hand, checks and short-term money market papers and financial securities which can be liquidated at any time and current financial liabilities, each with an original maturity of less than three months.

The payment flows are broken down according to ongoing business operations, investment activities and financing activities. The indirect-calculation method was chosen for presenting the cash flow from ongoing business activities.

Cash flow from operating activities

Compared with the corresponding previous year period, the cash flow from operating activities increased by € 140.3 million to € 285.1 million.

On the basis of earnings before taxes which increased by € 46.1 million to € 163.7 million, the depreciation and impairments on fixed assets which increased by € 52.3 million to € 96.2 million and which related primarily to the capitalisation of customer acquisition costs, in particular had a positive impact on the cash flow from operating activities. In addition, the significant increase in operating liabilities of € 104.9 million was one of the major factors behind the positive development in cash inflows. Opposite effects were seen primarily in payments of income taxes (€ 42.2 million), the decline in provisions (€ 17.7 million) and the increase in current assets (€ 12.8 million).

Cash flow from investing activities

During the financial year, the outflow of cash attributable to investment activities increased € 246.3 million compared with the previous year to € 273.5 million.

The main factor behind the strong increase in the outflow of funds were investments in intangible assets, and in particular the spending for customer retention and acquisition in the contract customer areas (€ 236.1 million) attributable to the asset “customer base”. Other investments included property, plant and equipment (€ 22.4 million).

There were no unusual movements in income attributable to investing activities, primarily attributable to interest (€ 13.4 million) during the course of the fiscal year.

Cash flow from financing activities

Compared with the corresponding previous year period, cash flow from financing activities declined by € 668.0 million. In 2007, there was thus an outflow of € 583.5 million in the cash flow from financing activities.

Whereas the positive cash flow of € 84.5 million in the previous year mainly reflected the sale of a borrower’s note loan (€ 85.0 million), the cash outflow of fiscal 2007 was mainly attributable to a dividend payment of € 576.1 million or € 6.00 per share. Further payments mainly comprised interest (€ 4.7 million).

32. Additional information concerning financial instruments

Disclosures in accordance with IFRS 7

This section provides an overview of the significance of financial instruments for the Group, and provides additional information on balance sheet items which include financial instruments.

We have provided the following information for presenting the financial instruments which existed within the Groupsas of 31 December 2007 and as of 31 December 2006, the corresponding allocation to categories as well as reconciliation in the various valuation categories in accordance with IAS 39:

Financial instruments by class as of 31 December 2007 (€'000s)	Valuation category according to IAS 39	Carrying amount 31.12.2007	Approach			Fair value 31.12.2007
			Amortised cost	Costs of purchase	Fair value through profit or loss	
Assets						
Cash and cash equivalents	KF	53,034	53,034			53,034
Financial instruments measured at market value	EFVM	710			710	710
Total liquid assets		**53,744**	**53,034**		**710**	**53,744**
Other financial assets	ZVF	304		304		–
Trade accounts receivable	KF	200,042	200,042			200,042
Other non-derivative financial assets	KF	53,040	53,040			53,040
Non-financial assets		31,717				
Total other receivables and other assets		**84,757**				
Liabilities						
Trade accounts payable	FV	103,004	103,004			103,004
Debt (liabilities to banks)	FV	90,179	90,179			90,179
Liabilities from finance leases	FV	717	717			717
Other non-derivative financial liabilities	FV	237,365	237,365			237,365
Non-financial liabilities		72,927				
Total other payables		**310,292**				
Thereof aggregated by valuation categories according to IAS 39:						
Available-for-sale financial instruments	ZVF	304		304		–
Loans and receivables	KF	306,116	306,116			306,116
Financial assets, measred at fair value through profit or loss	EFVM	710			710	710
Financial liabilities, measured at amortised cost	FV	–431,265	–431,265			–431,265

Financial instruments by class as of 31 December 2006 (€'000s)	**Valuation category according to IAS 39**	**Carrying amount 31.12.2006**	**Approach**			**Fair value 31.12.2006**
			Amortised cost	**Costs of purchase**	**Fair value through profit or loss**	
Assets						
Cash and cash equivalents	KF	529,838	529,838			529,838
Financial instruments measured at market value	EFVM	5,499			5,499	5,499
Total liquid assets		**535,337**	**529,838**		**5,499**	**535,337**
Other financial assets	ZVF	304		304		–
Trade accounts receivable	KF	192,189	192,189			192,189
Other non-derivative financial assets	KF	60,450	60,450			60,450
Non-financial assets		22,610				
Total other receivables and other assets		**83,060**				
Liabilities						
Trade accounts payable	FV	94,649	94,649			94,649
Debt (liabilities to banks)	FV	0	0			0
Liabilities from finance leases	FV	814	814			814
Other non-derivative financial liabilities	FV	144,133	144,133			144,133
Non-financial liabilities		65,661				
Total other payables		**209,794**				
Thereof aggregated by valuation categories according to IAS 39:						
Available-for-sale financial instruments	ZVF	304		304		–
Loans and receivables	KF	782,477	782,477			782,477
Financial assets, measred at fair value through profit or loss	EFVM	5,499			5,499	5,499
Financial liabilities, measured at amortised cost	FV	–239,596	–239,596			–239,596

The non-financial assets constitute that part of the balance sheet item “Other receivables and other assets” which is not covered by the scope of IFRS 7.

The non-financial liabilities constitute that part of the balance sheet item “Other liabilities and deferrals” not covered by the scope of IFRS 7.

The market value of cash and cash equivalents, trade accounts receivable, other current financial assets, trade accounts payable and other current financial obligations is roughly equivalent to the carrying amount. This is due to the short remaining terms of these financial instruments.

The market values of the non-current receivables and other financial assets with remaining terms of more than one year correspond to the carrying amounts of the payments associated with the assets, with due consideration being given to the current interest parameters. Accordingly, the carrying amounts of these financial instruments are approximately equivalent to the market values.

For those financial instruments measured at market value, the Group uses the price in an active market as the market value.

The other financial assets are normally measured at cost because it is not possible to reliably determine the fair value. The shares are not listed on a stock exchange, and no active market exists for them. There are no plans at present to sell these assets. If there are any indications of lower fair values, these are recognised.

The market value of the financial debt is equivalent to the carrying amount as a result of the short remaining terms involved.

The Group determines the market value of liabilities arising from finance leases by discounting the expected future cash flows with the rates applicable for similar debt with an equivalent remaining term.

Trade accounts payable and other financial liabilities and accruals normally have short remaining terms; the recognised figures are approximately equivalent to the market value.

In the fiscal year 2007 as well as in the previous year, the following net results were shown for the individual categories of financial instruments in accordance with IAS39:

Net results by valuation categories 2007 (€'000s)	**From interest**	**From subsequent measurement**		**From disposal**	**Net result**
		At fair value	**Impairment/ receivable losses**		
Valuation category					
Available-for-sale financial instruments (ZVF)	0	0	0	0	0
Loans and receivables (KF)	0	0	–19,875	3,754	–16,121
Financial assets, measured at fair value through profit or loss (EFVM)	14,277	59	0	0	14,336
Financial liabilities, measured at amortised cost (FV)	–2,063	0	0	0	–2,063
	12,214	**59**	**–19,875**	**3,754**	**–3,848**

Net results by valuation categories 2006 (€'000s)	**From interest**	**From subsequent measurement**		**From disposal**	**Net result**
		At fair value	**Impairment/ receivable losses**		
Valuation category					
Available-for-sale financial instruments (ZVF)	0	0	0	0	0
Loans and receivables (KF)	0	0	–17,826	0	–17,826
Financial assets, measured at fair value through profit or loss (EFVM)	14,724	367	0	0	15,091
Financial liabilities, measured at amortised cost (FV)	–481	0	0	0	–481
	14,243	**367**	**–17,826**	**0**	**–3,216**

Net gains and losses from loans and receivables include changes in the impairments, gains and losses attributable to derecognition as well as payment inflows and increases in the value of loans and receivables which had originally been written off.

Net profits and losses in the category of held-for-sale financial instruments comprise impairments and profits and losses attributable to derecognition.

Net gains and losses attributable to financial liabilities at cost comprise profits or losses of derecognition.

In addition, information is provided with regard to interest income and interest expenses of financial assets and financial liabilities not measured at fair value through profit or loss using the effective interest method.

Principles and objectives of financial risk management

With its assets, liabilities and planned transactions, the freenet Group is exposed in particular to market risks, liquidity risks and default risks.

The objective of financial risk management is to constantly monitor these risks and to limit them by operational and finance-oriented activities.

No derivative financial instruments are used within the Group.

The fundamental aspects of financial policy are defined by the Managing Board. In addition, certain financial transactions require the prior approval of the Managing Board.

The Group Treasury department provides services to the operating segments and co-ordinates access to the financial markets. In addition, it monitors and manages the market and liquidity risks associated with the operating segments of the Group by way of regular internal risk reporting which analyses the risks on the basis of degree and extent. The Group Treasury department considers that one of its main tasks is to optimise the net interest income of the Group.

The Debtor Management department is responsible for monitoring the default risks as well as regular internal risk reporting in relation to these risks. One of its main objectives is to minimise the costs attributable to the failure or impairment of receivables due from end customers and sales partners.

Market risks

The activities of our Group mean that it is primarily exposed to financial risks attributable to changes in interest rates and currency exchange rates.

i. Interest rate risk

The Group is exposed to interest rate risks because the Group companies take on debt with fixed and variable interest rates. The risk is managed by the Group by ensuring an appropriate relationship between fixed and variable investments and borrowings.

The Group Treasury department constantly monitors the various opportunities available for investing the liquid assets and debt on the basis of the daily liquidity planning at its disposal. Demand for and the investment of liquid funds in the Group are managed centrally on the basis of an existing internal cash pooling agreement in which the main companies of the freenet Group participate.

All the short-term bank borrowings taken out as of the balance sheet date were subject to interest at a variable rate, and had been invested on the basis of EONIA subject to daily conditions.

Changes in market interest rates for the net interest income of financial instruments which were originally subject to interest at a variable rate might have an impact on net interest income and are included in the process of calculating the result-related sensitivities.

In order to present the market risks, the Group uses a sensitivity analysis which shows the effects of theoretical changes in relevant risk variables on the result and shareholders' equity.

The periodic effects are determined by relating the theoretical changes in the risk variables to the financial instrument holdings as of the closing reference date.

The balance sheet also includes a figure of € 90.2 million for bank borrowings under current debt as of 31 December 2007. However, it has to be borne in mind that this figure is opposed by current liquid funds of € 53.8 million on the assets side of the balance sheet as of the reference date. Interest in a range of 4.5 to 4.8 percent was charged on the bank borrowings as of the reference date.

It is expected that the above-mentioned bank borrowings will be repaid completely within one year. After the dividend payment, the bank borrowings netted with liquid funds in financial 2007 amounted to an average of € 33 million.

If net bank borrowings again turn out to be € 33 million on average in 2008, this would result in an interest charge of € 1.53 million for 2008 on the basis of an assumed interest rate of 4.65 percent (based on the average rate as of 31 December 2007). A change of 0.5 percentage points in the level of market interest rates would result in a corresponding change of € 0.17 million in results.

Money market funds are subject to marginal interest rate fluctuations so that there is always a possibility of price losses. However, the risk is not significant as the moneys have been invested in funds on a very short-term basis (held for trading). There are no contractually defined maturity dates or interest adjustment dates; a return results from the change in the price of the instrument and any dividend payments.

The risk of interest rate changes is negligible for the other interest-bearing assets and liabilities.

ii. Foreign currency/exchange rate risk

Foreign currency trades are conducted to a minor extent within the Group. If necessary, foreign exchange hedging takes place by way of cash holdings in foreign currency.

Overall, the Group considers that the foreign currency risk is of negligible significance.

Liquidity risk

The liquidity risk of the Group is defined as the risk that the Company might not be able to meet its financial obligations, for instance it might not be able to repay debt, pay purchase obligations and obligations arising from finance leases.

Comprehensive financing planning instruments are used throughout the Group to monitor and control liquidity. Different planning horizons are considered in this respect, ranging up to one year. The short-term liquidity planning and control are done on a daily basis for the following three months. The planning is updated daily by the Group Treasury department following liaison with Accounting and Controlling on the basis of current data.

The Group also manages liquidity risks by holding appropriate reserves, credit lines at banks and also by constantly monitoring the forecast and actual cash flows. Reconciliations are also performed for the maturity profiles of the financial assets and liabilities.

The Group anticipates that it will be able to meet its other obligations out of operating cash flows and the proceeds of maturing financial assets.

Securities (money market funds) can be liquidated at short notice. There are no plans to sell any of the holdings. If it became necessary to sell these holdings, their sale at short notice would possibly be more difficult as there is no organised capital market for these interests.

In the Group, there are contingencies arising from warranties for liabilities of a subsidiary provided to business customers; these amounted to € 16.0 million as of the balance sheet date (previous year: € 15.3 million).

The following table shows the contractually agreed undiscounted interest and redemption payments of the original financial liabilities of the Group:

Financial liabilities (€'000s)	**Carrying amount 31.12.2007**	**Cash flows 2008**		
		Interest (fixed)	**Interest (variable)**	**Repayment**
Trade accounts payable	103,004			103,004
Debt (liabilities due to banks)	90,179		1,530[1]	90,179
Liabilities from finance leases	717	39		142
Other non-derivative financial liabilities	237,365			207,608

1 Interest charge relating to debt, netted with holdings of liquid assets. The interest payments of € 4,193 thousand expected in relation to the bank borrowings of €90,179 thousand were netted with expected interest income of € 2,663 thousand in relation to expected liquid funds of € 57,179 thousand

If it is expected that a figure of € 28,901 thousand will be repaid in 2009 for other non-derivative financial liabilities; the remaining € 856 thousand of the other non-derivative financial liabilities will probably be repaid in 2009; no interest is occured in either case.

Default risk

A credit risk is defined as the unexpected loss of cash or revenues. This risk materialises if the customer is not able to meet his obligations within the agreed period.

Trade accounts receivable from end customers are the main item in the freenet Group with regard to default risks. In the mass business of our Group, particular attention is devoted to the creditworthiness of customers and sales partners. Credit checks are carried out for major contract customer areas before a contract is taken out with the customer.

Once a contract has been entered into, the performance of a rapid and regular dunning and collection process with several collection companies in benchmarking and long-term collection monitoring as well as high-spender monitoring are key measures for minimising the default risk in our Group.

An ongoing dunning and collection process also takes place for accounts due from dealers and franchise partners; credit limits are also defined and monitored. Where appropriate, a delivery restriction is imposed if the limit is reached.

In order to determine an impairment of trade accounts receivable, due account is taken of any change in creditworthiness between the point at which the terms of payment were granted and the balance sheet date. There is no significant concentration of credit risk because the customer base is broad and because there are no correlations.

An appropriate creation of impairments takes account of default risks. Receivables and other assets are derecognised if the Group considers the receivable is irrecoverable.

Securities and liquid assets are essentially deposited with large German banks and their money market funds. There is no significant risk of default. The Group Treasury department constantly monitors the current and expected future yields of the investments.

With regard to those trade accounts receivable which are neither impaired nor overdue for payment, there are no indications as of the reference date that the debtors will not meet their payment obligations.

With regard to the other financial assets of the Group, such as cash and cash equivalents and available-for-sale investments, the maximum credit risk in the case of counterparty default is equivalent to the carrying amount of these instruments.

33. Transactions with related parties

The following major transactions have taken place between the Group and related parties:

€'000s	2007	2006
Sales and income attributable to services and onward charging		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	1,698	820
FunDorado GmbH, Hamburg	237	162
LGB & Vogel GmbH, Düsseldorf	4	8
Mr. Prof. Dr. Helmut Thoma, Hürth-Berrenrath	0	5
Purchased services and onwarding charging		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	682	502
Jaschinski Biere Brexl, Berlin	236	26
FunDorado GmbH, Hamburg	210	12
Notariat Ballindamm, Hamburg	65	n. A.
siXXup new Media GmbH, Pulheim	49	0
NetCon Media s.r.o., Hlucin, Czech Republic	7	0
Sale of assets		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	0	48
Purchase of assets		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	0	5

The following major receivables due from and liabilities due to related parties existed as of the end of the fiancial year:

€'000s	2007	2006
Receivables		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	190	149
FunDorado GmbH, Hamburg	13	11
Liabilities		
KielNET GmbH Gesellschaft für Kommunikation, Kiel	34	0
Jaschinski Biere Brexl, Berlin	60	0

If the parties were not to be classified as related in accordance with IAS 24, no comparison was made (n. a.). All transaction prices were negotiated under commercial terms.

Managing Board compensation

Compensation paid to the members of the Managing Board of the Company and its predecessors is broken down as follows:

Compensation for financial 2007 (€'000s)	Salary	Variable compensation from stock option and stock appreciation rights[1]	Other variable compensation	Total
Eckhard Spoerr	642	3,408	358	4,408
Axel Krieger	357	2,130	142	2,629
Stephan Esch	257	1,065	53	1,375
Eric Berger	211	639	53	903
	1,467	**7,242**	**606**	**9,315**

1 Incl. non-cash compensation for 2007 valued in accordance with IFRS 2.

Compensation for financial 2006 (€'000s)	Salary	Variable compensation from stock option and stock appreciation rights[1]	Other variable compensation	Total
Eckhard Spoerr	641	2,785	410	3,836
Axel Krieger	336	1,741	180	2,257
Stephan Esch	282	870	22	1,174
Eric Berger[2]	160	522	43	725
Michael Grodd[3]	138	0	158	296
	1,557	**5,918**	**813**	**8,288**

1 Incl. non-cash compensation for 2006 valued in accordance with IFRS 2.
2 Member of the Managing Board of the former freenet.de AG.
3 Stepped down from the Managing Board of the former mobilcom AG on 15 November 2006.

As of 31 December 2007, the provision for stock options and stock appreciation rights for Mr. Spoerr amounted to € 3,873 thousand (previous year: € 4,737 thousand); the corresponding figures for Mr. Krieger were € 2,421 thousand (previous year: € 3,693 thousand), for Mr. Esch were € 1,210 thousand (previous year: € 1,167 thousand) and for Mr. Berger were € 726 thousand (previous year: € 819 thousand).

In financial 2007, the following amounts were paid out of stock options and stock appreciation rights: € 4,272 thousand (previous year: € 1,233 thousand) to Mr. Spoerr, € 3,402 thousand (previous year: € 1,233 thousand) to Mr. Krieger, € 1,022 thousand (previous year: € 187 thousand) to Mr. Esch as well as € 732 thousand (previous year: € 210 thousand) to Mr. Berger.

No new stock appreciation rights or stock options were issued to members of the Managing Board of the Company.

In November 2004, a direct pension commitment was granted to Mr. Spoerr, Mr. Krieger, Mr. Esch and Mr. Berger. As of 31 December 2007, the defined benefit obligation (DBO) amounted to € 835 thousand (previous year: € 809 thousand) for Mr. Spoerr, € 442 (previous year: € 422 thousand) for Mr. Krieger, € 137 thousand (previous year: € 105 thousand) for Mr. Esch and € 136 thousand (previous year: € 117 thousand) for Mr. Berger.

Total current and subsequent service time expenses of € 597 thousand (previous year: € 249 thousand) are shown in personnel expenses for the members of the Managing Board as a result of the pension commitments.

No loans were extended to any of the members of the Managing Board, and no guarantees or other warranties were issued for any of the members of the Managing Board.

Supervisory Board compensation

The compensation of the Supervisory Board is defined in the articles of association. Until the merger between mobilcom AG and freenet.de AG to form the Company became legally effective on 2 March 2007, the articles of association of the legal predecessors, in other words, mobilcom AG and freenet.de AG, were applicable for the compensation of the Supervisory Board up to that time. Accordingly, the compensation in 2007 consisted of three components:

- Basic compensation
- Fees for attending meetings
- Profit-linked compensation

The Supervisory Board members receive basic compensation of € 12,000 for each full fiscal year of membership on the board. The chairperson of the Supervisory Board receives double this amount, the vice chairperson one and a half time this amount.

Every Supervisory Board member receives in addition an attendance fee of € 1,000 for each Supervisory Board meeting he/she attends. Supervisory Board members who belong to a Supervisory Board committee – with the exception of the committee formed in accordance with section 27 (3) of the German Codetermination Act – receive in addition an attendance fee of € 1,000 for each meeting of the committee. The committee chairperson receives double this amount.

The Supervisory Board members also receive, after the end of each fiscal year, variable compensation in the amount of € 500 for each € 0.01 in dividends in excess of € 0.10 per share of the company stock which are distributed to the shareholders for the previous fiscal year. The extent of the variable compensation is limited to that amount which is payable in the form of basic compensation. The chairperson of the Supervisory Board receives double this amount, the vice chairperson one and a half times this amount.

For their activity during the financial year 2007, the members of the Supervisory Board of the Company and of the legal predecessors, i. e. mobilcom AG and freenet.de AG, received basic compensation of € 150.5 thousand as well as fees of € 150 thousand for attending meetings. In addition, profit-linked compensation of € 150.5 thousand (calculated on the basis of the next dividend payment of the Company) was recognised as an expense. The total compensation paid for Supervisory Board activities was thus € 451 thousand.

Individual figures for the last two financial years are shown in the following tables. Please note that rounding differences may result from the format used for presenting subtotals and final totals, because the figures have been rounded to one decimal point.

Compensation for 2007 €'000s	**Basic compensation**	**Attendance fees**	**Profit-linked compensation**	**Total**
Active members				
Prof. Dr. Helmut Thoma	22.3	23.0	22.3	67.6
Birgit Geffke[1]	15.5	19.0	15.5	50.0
Oliver Brexl	12.0	14.0	12.0	38.0
Thorsten Kraemer	5.4	4.0	5.4	14.8
Dr. Dieter Leuering	5.4	5.0	5.4	15.8
Sascha Lucht[1]	10.4	15.0	10.4	35.7
Andreas Neumann[1]	10.4	10.0	10.4	30.7
Franziska Oelte[1]	10.4	14.0	10.4	34.7
Kai Petersen[1]	10.4	8.0	10.4	28.7
Prof. Dr. Hans-Joachim Priester	10.0	10.0	10.0	30.0
Richard Roy	5.4	7.0	5.4	17.8
Ulrike Scharlach[1]	10.4	7.0	10.4	27.7
	127.8	**136.0**	**127.8**	**391.6**
Former members				
Christian Burger[2]	1.0	0.0	1.0	2.1
Andrew John Dechet	5.5	2.0	5.5	13.1
Bastian Frederik Lueken	4.7	3.0	4.7	12.3
Prof. Klaus-Dieter Scheurle[2]	1.6	0.0	1.6	3.1
Prof. Dr. G. Konrad Schmidt	6.4	4.0	6.4	16.8
Prof. Dr. Dieter H. Vogel[3]	3.5	5.0	3.5	12.0
	22.7	**14.0**	**22.7**	**59.4**
	150.5	**150.0**	**150.5**	**451.0**

1 Employee representatives in accordance with section 7 (1) sent. 1 no. 1 MitbestG of 4 May 1976.
2 Mermber in the Supervisory Board of the former freenet.de AG.
3 Member of the Supervisory board of the former mobilcom AG.

Compensation for 2006 €'000s	**Basic compensation**	**Attendance fees**	**Profit-linked compensation**	**Total**
Active members				
Prof. Dr. G. Konrad Schmidt	12.0	11.0	7.5	30.5
Birgit Geffke[1]	18.0	14.0	11.3	43.3
Oliver Brexl	1.3	1.0	0.8	3.1
Christian Burger[2]	6.2	0.0	6.2	12.4
Andrew John Dechet	12.0	11.0	7.5	30.5
Sascha Lucht[1]	12.0	13.0	7.5	32.5
Bastian Frederik Lueken	12.0	14.0	7.5	33.5
Andreas Neumann[1]	12.0	13.0	7.5	32.5
Franziska Oelte[1]	12.0	15.0	7.5	34.5
Kai Petersen[1]	12.0	10.0	7.5	29.5
Ulrike Scharlach[1]	12.0	9.0	7.5	28.5
Prof. Klaus-Dieter Scheurle[2]	9.3	0.0	9.3	18.6
Prof. Dr. Helmut Thoma	24.4	11.0	19.9	55.3
	155.2	**122.0**	**107.5**	**384.7**
Former members				
Klaus Thiemann	10.0	8.0	6.2	24.2
Prof. Dr.-Ing. Dieter H. Vogel	24.0	19.0	15.0	58.0
	34.0	**27.0**	**21.2**	**82.2**
	189.2	**149.0**	**128.7**	**466.9**

1 Employee representatives in accordance with section 7 (1) sent. 1 No. 1 MitbestG of 4 May 1976.
2 Mermber in the Supervisory Board of the former freenet.de AG.

Furthermore, Supervisory Board members are reimbursed for expenses incurred as a result of exercising their office as well as for VAT.

34. Disclosures in accordance with section 315a HGB

The list of the companies included in the consolidated financial statements in accordance with section 313 (2) to (3) HGB is shown in a separate list of shareholdings, instead of in the notes, in accordance with section 313 (4) HGB. This separate list is submitted to the electronic Federal Gazette.

The average number of employees in the Group (section 314 (1) no. 4 HGB) has been shown in note 4 “Personnel expenses”.

With regard to the disclosures concerning compensation of the executive bodies of the Company (section 314 (1) No. 6 HGB), please refer to note 33 “Transactions with related parties”.

In accordance with section 314 (1) no. 8 HGB, we hereby declare that the declaration of conformity in accordance with section 161 AktG was submitted by the Managing Board and Supervisory Board of the Company in December 2007 . It has been made permanently available to shareholders on the Company’s web site at

http://www.freenet.ag/investor-relations/entsprechenserklaerung.html

A total of € 1,919 thousand in fees was paid to the auditor in accordance with section 314 (1) no. 9 HGB during the fiscal year. Of this figure, € 614 thousand was paid for the audit of the annual accounts and consolidated annual accounts, € 508 thousand for other certification or assessment services (thereof: advanced insurance premium of € 327 thousand), € 13 thousand for tax accountant services and € 784 thousand for other services.

35. Significant events occurring after the balance sheet date

No reportable events have occurred after the balance sheet date.

Büdelsdorf, 28th February 2008
freenet AG

The Managing Board

Eckhard Spoerr

Axel Krieger

Stephan Esch

Eric Berger

3.8 Auditor's report

We have audited the consolidated financial statements prepared by the freenet AG, Büdelsdorf, comprising the balance sheet, the income statement, statement of changes in equity, cash flow statement and the notes to the consolidated financial statements, together with the group management report for the business year from 1 January to 31 December2007. The preparation of the consolidated financial statements and the group management report in accordance with the IFRSs, as adopted by the EU, and the additional requirements of German commercial law pursuant to § (Article) 315a Abs. (paragraph) 1 HGB ("Handelsgesetzbuch": German Commercial Code) are the responsibility of the parent Company's Board of Managing Directors. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with § 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institut der Wirtschaftsprüfer (Institute of Public Auditors in Germany) (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the Group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of the entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Company's Board of Managing Directors, as well as evaluating the overall presentation of the consolidated financial statements and the group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion based on the findings of our audit the consolidated financial statements comply with the IFRSs as adopted by the EU and the additional requirements of German commercial law pursuant to § 315a Abs. 1 HGB and give a true and fair view of the net assets, financial position and results of operations of the Group in accordance with these requirements. The group management report is consistent with the consolidated financial statements and and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Kiel, 2nd March 2008
PricewaterhouseCoopers
Aktiengesellschaft
Wirtschaftsprüfungsgesellschaft

(Dr. Andreas Focke)	(ppa. Marko Schipper)
German Public Auditor	German Public Auditor

3.9 Responsibility statement

To the best of our knowledge, and in accordance with the applicable accounting principles, the consolidated financial statements give a true and fair view of the assets, liabilities, financial position and profit or loss of the Group, and the Group management report includes a fair review of the development and performance of the business and the position of the Group, together with a description of the principal opportunities and risks associated with the expected development of the Group.

Büdelsdorf, 28th February 2008

Eckhard Spoerr

Axel Krieger

Stephan Esch

Eric Berger

4. Reports

4. Reports

4.1 Supervisory board report

The supervisory board would like to report here on their activities during the 2007 fiscal year. We shall elucidate on key areas considered by the full board, the work of our sub-committees, personnel changes on the management and supervisory boards and on the annual and group audit.

Overview of supervisory and advisory work

During the 2007 business year, the supervisory board regularly provided the executive board with advice on corporate governance and oversaw its management of the business. The executive board involved the supervisory board directly in all decisions material to the governance of the company and regularly reported to us on the company's business progress, corporate planning, strategic development and current situation both in verbal and written form. The orderliness, appropriateness and efficiency of the executive board's management of the company gave us no cause for complaint.

In particular, we discussed in detail with the executive board the deviations taken by the business from the original plans and goals and reviewed these on the basis of the documentation provided. The executive board agreed with us the company's strategic direction following the merger with mobilcom AG and freenet.de AG. All business events of material significance for the company were discussed in full by the supervisory board based on the executive board's reports.

Based likewise on the executive board's reports and after careful scrutiny and deliberation, we also took formal decisions where necessary. Where current business events required our consideration, we called meetings at short notice and dealt with strategic requirements in a very timely manner. The executive board also maintained regular contact with us outside of formal meetings and kept us informed of the latest business developments. Furthermore, the supervisory board chairman also discussed the company's prospects and future strategic direction in separate meetings with the executive board and was kept informed of current issues and events at all times.

During the 2007 fiscal year, a total of eight physical board meetings took place, plus one telephone meeting prior to the merger of the company with mobilcom AG and freenet.de AG. In one case the supervisory board also took a number of decisions by means of written correspondence. With the exception of two meetings, to which one member in each instance sent their apologies, supervisory board meetings were all fully attended.

Any conflicts of interests that members of the management or supervisory board may have must be declared to the supervisory board without delay and be reported to the annual general meeting. No such conflicts of interest have been declared to the supervisory board.

At its meeting on 9th May 2007, the supervisory board agreed pursuant to clause 114, paragraph 1 of the German Companies Act (AktG) that the group's legal advisors be the law firm Jaschinski Biere Brexl, a partner of which, Mr. Oliver Brexl, is a member of the supervisory board.

Issues discussed by the supervisory board

In their full meetings, the members of the supervisory board regularly discussed the group's turnover, the financial position, bottom-line trends and individual business divisions based on reports from the executive board members, who attended all meetings.

During the supervisory board meeting held by telephone on 23rd February 2007, Professor G. Konrad Schmidt was elected chairman until the new elections in April 2007, the previous chairman having stepped down.

The first meeting after registration of the merger with mobilcom AG and freenet.de AG took place on 24th April 2007. The employees' supervisory board representatives legally appointed on 20th April 2007 took part here for the first time. Professor Doctor Helmut Thoma was elected supervisory board chairman at this meeting.

We also dealt at this meeting with reviewing and approving the annual and group accounts for 2006. The auditors expanded at this meeting on their audit findings. Based on our own review, we have no objections to the auditors' audit results and followed the audit committee's recommendation in approving the annual and group accounts.

At two meetings on 9th and 30th May 2007, the supervisory board dealt with preparations for the 2007 ordinary general meeting. This included dealing with the new election of shareholders' representatives to the supervisory board, agreeing two controlling and profit transfer agreements with Next ID GmbH and meOme GmbH respectively and, in particular, with the proposal to the general meeting to issue a special dividend. In addition to this, we also worked in depth on corporate planning for 2007. Based on a comprehensive report from the executive board, we also debated the group's future strategic development. Another focus of the discussion was on expanding the executive board, as a consequence of which we appointed Mr. Eric Berger as executive board member for the area of online services. We also ratified the company's stock appreciation programme.

On 20th July 2007, the day of the ordinary general meeting, we held two meetings. Prior to the general meeting, the supervisory board looked at election proposals and counter motions from differing shareholders and dealt initially with the resolutions it would propose to points on the general meeting agenda. As a result of the new election of shareholders' supervisory board members at the general meeting it was necessary thereafter to hold a constitutional meeting, at which we carried out the elections for the positions of chair and vice-chair and also determined the composition of the board's sub-committees.

We used the meeting on 20th September 2007 to deal exhaustively with the group's business development. Taking into account expert opinion from external advisors, we also held intensive discussions on strategic options with the executive board. This theme was also the key focus of the two supervisory board meetings on 29th October and 19th December 2007. In its deliberations on strategic options the board at times involved and sought advice from the company's external legal advisors. On 29th October 2007 the board also dealt with the withdrawal of the claims for reimbursement of sales tax arising from the acquisition of the former mobilcom's UMTS licence.

At our final meeting of the fiscal year, on 19th December 2007, we gave our particular attention to the recommendations of the German Corporate Governance Codex and took a decision on the declaration of compliance pursuant to clause 161 of the German Companies Act (AktG). Another key area of discussion was the termination of the strategic review process. Further we charged the executive board with looking into a holding structure for freenet AG and spinning off the DSL and portal business. Our deliberations on implementing the executive board's convergence and brand strategy were closely linked with this decision.

After the end of the reporting year, we held a further meeting on 2nd March 2008, where discussions centred very much on the annual and group audit.

Work of the supervisory board committees

In order to deal efficiently with its duties the supervisory board has set up one executive committee and four sub-committees. The sub-committees prepare the issues and draft supervisory board resolutions to be discussed by the full board. They also dealt with duties transferred to them as a result of the recommendations of the German Corporate Governance Codex. To the extent that legislation permits, the supervisory board's decision-making authority was also delegated to sub-committees in some individual cases. We regard this division of duties as sensible, as it has proven itself in practice. The supervisory board chairman chairs all of the committees, except the audit committee. The respective committee chairmen reported to the full supervisory board on the matters discussed at their sub-committee meetings. The executive board was represented at all sub-committee meetings.

The executive committee met two times and had one conference call during the reporting year. The executive committee dealt largely at its meetings with strategic matters. At the core of its deliberations in this respect were the consequences for the company of the merger of mobilcom AG and freenet.de AG. Another key area of focus was dealing with the strategic review process, in the course of which a break-up of the company through partial sales to different buyers was examined and ultimately rejected. Another topic was the implementation of the recommendations of the German Corporate Governance Codex. The members of the executive committee are Professor Doctor Helmut Thoma (chairman), Mrs Birgit Geffke, Mrs Franziska Oelte (both since 24th April 2007) and Mr. Richard Roy (since 20th July 2007).

The audit committee met twice in 2007. The focus of its work was on the annual and group accounts and the auditors' audit reports. The committee also dealt with risk management and the actions decided upon in relation to this by the executive board. It also discussed company compliance issues. The audit committee obtained the auditors' declaration of independence pursuant to clause 7.2.1 or the German Corporate Governance Codex, monitored the auditors' independence, commissioned the audit and defined its key areas of focus. The auditors took part in both audit committee meetings, reporting on the one hand in detail on how the audit was going and on the other on planned audit actions and events that arose while the audit was being conducted. The audit committee is made up of Professor Hans-Joachim Priester (chairman), Mr. Sascha Lucht, Mr. Andreas Neumann (both since 24th April 2007) and Dr Dieter Leuering (since 20th July 2007).

The personnel committee is responsible for the contracts of employment with members of the executive board and for their remuneration. This committee held four meetings and discussed the level of remuneration for executive board members, ratification of share appreciation rights and increasing the size of the executive board through the addition of Eric Berger. In one case the personnel committee also took one decision by means of written correspondence. Since 24th April 2007 the personnel committee has consisted of Professor Doctor Helmut Thoma (chairman), Mrs Birgit Geffke, Mr. Oliver Brexl and Mr. Sascha Lucht.

The mediation committee pursuant to clause 27, paragraph 3 of the German Co-Determination Act (MitbestG) was not convened during the 2007 fiscal year. Since 24th April 2007 the members of this committee have been Professor Doctor Helmut Thoma (chairman), Mrs Birgit Geffke, Mrs Ulrike Scharlach and Mr. Oliver Brexl.

The nominations committee, newly formed in December 2007, which for future new elections will suggest suitable candidates to the supervisory board to propose to the general meeting, did not meet during the reporting year. Since 19th December 2007 its members have been Professor Doctor Helmut Thoma (chairman), Mr. Richard Roy and Mr. Thorsten Kraemer.

Annual and group audit for the fiscal year 2007

The annual accounts for the fiscal year 1st January to 31st December 2007 prepared by the executive board in accordance with the rules of the German Commercial Code (HGB) and the freenet AG annual report were audited by PricewaterhouseCoopers AG WPG of Frankfurt am Main. The audit was commissioned by the supervisory board's audit committee in accordance with the resolution of the ordinary general meeting passed on 20th July 2007. The auditors issued an unqualified audit report.

The freenet AG group accounts were produced in accordance with clause 315a of the German Commercial Code (HGB) based on the IFRS international accounting standards. The auditors gave these group accounts too an unqualified audit report.

The audit committee had defined the key areas of focus for this reporting year as being examination of the after-effects of the merger and of capitalising client acquisition costs. The reports on this as well as all other audit reports and final accounts documents were sent promptly to all supervisory board members. They were discussed in depth at the audit committee meeting on 2nd March 2008 and the supervisory board meeting on 2nd March 2008, in which the executive board was also involved. The auditors took part in the discussion of the annual and group accounts at both meetings. They reported on the material findings of the audits and made themselves available to the audit committee and supervisory board to answer any supplementary questions or provide further information. The auditors also reported on the audit of the company's early risk-detection system.

After our own review of the annual accounts, the final group accounts, the annual report and the group annual report, we agreed to the audit findings produced by the auditors with no objections and in accordance with the recommendation of the audit committee approved the annual and group final accounts at our meeting on 2nd March 2008. The final annual accounts are thus formally adopted.

Supervisory and executive board changes

There were several personnel changes on the freenet AG supervisory board during the reporting year. Board chairman Professor Dieter Vogel stepped down from his post on 22nd February 2007. The extraordinary general meeting on 23rd February 2007 voted Professor Hans-Joachim Priester onto the supervisory board in his place. Mr. Oliver Brexl was also voted onto the supervisory board at this general meeting. Professor G. Konrad Schmidt was chairman of the supervisory board from 23rd February 2007 until the election to this position of Professor Doctor Helmut Thoma at the meeting on 24th April 2007. Pursuant to its resolution of 20th April 2007, the district court of Kiel appointed Mrs Birgit Geffke, Mrs Franziska Oelte, Mrs Ulrike Scharlach, Mr. Sascha Lucht, Mr. Andreas Neumann and Mr. Kai

Petersen to the supervisory board as representatives of the workforce. These court-appointed members had previously performed this function on the supervisory board at mobilcom AG. On 24th April 2007, Mrs Birgit Geffke was voted vice chair of the supervisory board. Mr. Andrew Dechet had held this office until that date.

Following the resignations on 21st May 2007 of Professor G. Konrad Schmidt, Mr. Andrew Dechet and Mr. Bastian Lueken, the supervisory board consisted of nine members until the ordinary general meeting on 20th July 2007. In addition to the previous shareholders' representatives, this general meeting voted Mr. Richard Roy, Mr. Dr. Dieter Leuering and Mr. Thorsten Kraemer onto the supervisory board for the first time. Mr. Olaf Schulz was also elected by the general meeting as an alternate for the shareholders' representatives.

The supervisory board appointed Mr. Eric Berger a member of the executive board with effect from 1st June 2007 until 31st December 2010. Mr. Berger is responsible for the area of online services.

The supervisory board expresses its appreciation to the executive board for its achievements and success during the reporting year and thanks all employees for their commitment throughout 2007.

Büdelsdorf, 2nd March 2008
The Supervisory Board

Professor Doctor Helmut Thoma
Chairman

4.2 Corporate Governance Report

The company identifies with the aims of the German Corporate Governance Codex and the principles of transparent, responsible management and control of the business, designed to increase value. The freenet Group management board, supervisory board, all managers and members of staff are committed to these objectives.

Since its market listing on 5th March 2007, freenet AG has, with the exceptions listed below, complied with the recommendations contained in the German Corporate Governance Codex (as issued on 12th June 2006/as contained from 14th June 2007 in the current version) and intends also to comply in future with the recommendations of the 14th June 2007 version, except in cases where there is a declaration to the contrary from the company below.

1. The company has taken out D&O insurance for its directors and officers. This insurance includes no excess for members of the management or supervisory boards (clause 3.8, sentence 3 of the Codex). The terms of the D&O insurance policy are subject to ongoing review, especially in respect of the excess, as there is no visible benefit to the company associated with this. Acting responsibly is a given duty for all board members.
2. The structure of the remuneration system and a regular review of management board remuneration is undertaken not by the full supervisory board, but, pursuant to clause 11, paragraph 2 of the supervisory board's procedural rules, by the freenet AG supervisory board's personnel committee (clause 4.2.2, sentence 1 of the Codex). The supervisory board is of the view that operating in this way helps to make its work more efficient.
3. No age limit is currently set either for members of the management board or of the supervisory board. In the supervisory board's opinion it makes no sense that well-qualified people with great professional and personal experience should not be considered as candidates simply due to their age (clause 5.1.2, sentence 6 and clause 5.4.1, sentence 2 of the Codex).
4. The company did not publish the group annual accounts to 31st December 2006 within 90 days of the end of the fiscal year (clause 7.1.2, sentence 3 of the Codex). Production of the group accounts was delayed due to the merger with mobilcom AG and freenet.de AG recorded in the companies register on 2nd March 2007. It is the company's intention to adhere to this recommendation in future.

The management and supervisory boards made this declaration in December 2007 and published it on the company's website at *http://www.freenet.ag/investor-relations/entsprechenserklaerung.html*

Remuneration report

Management board remuneration
In accordance with the supervisory board's procedural rules, management board remuneration is set by the freenet AG supervisory board's human resources committee. The management board's remuneration is performance related and is made up of three components: A fixed element, a success-dependent element and a long-term element with an appropriate incentivising effect based on changes in the share price.

Total remuneration for the fiscal year 2007 for members of the management board of the company and of its predecessor companies was €9,315,000 (2006: €8,288,000). Of this total figure, €1,467,000 or 15.7% was accounted for by the fixed element and €7,848,000 or 84.3% by variable elements.

As at 31st December 2007, the provisions for share options and share appreciation rights for the management board stood at €8,230,000 (2006: €10,416,000). In the fiscal year 2007, a total sum arising from share options and share appreciation rights of €9,428,000[1] (2006: €2,863,000) went to members of the management board.

No share options or share appreciation rights were issued to members of the company's management board nor those of it predecessor companies during the 2007 fiscal year. In the previous year, 3.4 million share appreciation rights were issued to management board members.

1 €4,498,000 of which arising from the settlement of freenet.de AG's old share option scheme.

Pension

In November 2004, all members of the freenet.de AG management board were given a direct assurance of a pension from freenet.de AG, which freenet AG continues to honour.

When their period of service ends, freenet AG management board members have a right to the benefits set out at point 33 of the group appendix.

Remuneration provisions for the event of a board member ceasing to be employed

Premature cessation of employment

All mobilcom and freenet.de service contracts in existence prior to the point at which the merger became effective, transferred at that point to freenet AG. The old contracts, which continued to be legally valid, were replaced by new ones. With the exception of the level of remuneration, including the number of share appreciation rights, the new contracts were the same as the old ones, including in terms of benefits in the event of the employment (prematurely) ending. No right exists to claim compensation for loss of office if a management board member is responsible him/herself for the (premature) ending of his/her service contract.

The individual benefits provided by the company's service contracts for the event of cessation of employment are as follows:

- The right to payment of salary and bonuses (based on the assumption of 100% achievement of targets) for the remaining period of the contract where by mutual agreement the service contract is ended or notice to end it is served within, in either case, twelve months of a change of control of the company.
- From their 60th birthday, members of the management board receive a pension equivalent to 2.5 percent of their final annual fixed salary for each year or part thereof that they served on the company's management board or on that of its legal predecessor, freenet.de AG, totalling in any case not more than one third of their final annual fixed salary (guaranteed pension).
- A widow/widower's pension for the member's spouse/partner and an orphan's pension for any children up to the end of their education or vocational training, at the latest in any case up until their 27th birthday, amounting in total to not more than the guaranteed pension.
- Share appreciation rights, which have already become exercisable due to the expiry of the relevant vesting period and the respective objectives being achieved, remain in force. In the event of a member's service contract being terminated due to a change in control, all share appreciation rights remain in force and can be exercised regardless of the vesting period if the other exercise conditions are met within twelve months and in any case by not later than the end of the term. In the event of a management board member terminating his/her service contract for any other good cause or due to a complete reduction in earnings capacity or invalidity, or in the event of death, all share appreciation rights remain in force and can be exercised, subject to the other contractual conditions, within a period of twelve months from the end of employment, not later however than by the end of the term. Where such termination is due to good cause, the 12-month restriction does not apply.

The remuneration for members of the company's management board and of those of its predecessor companies was made up for the fiscal year as follows:

Management board remuneration 2007 (In €'000s)	Basic remuneration	Variable earnings from share options and share appreciation programme[1]	Other variable remuneration	Total remuneration
Eckhard Spoerr	642	3,408	358	4,408
Axel Krieger	357	2,130	142	2,629
Stephan Esch	257	1,065	53	1,375
Eric Berger	211	639	53	903
	1,467	**7,242**	**606**	**9,315**

1 Including cash-effective compensation and valued in accordance with IFRS 2.

In the previous year, the remuneration of members of the company's management board and of those of its predecessor companies was made up as follows:

Management board remuneration 2006 (In €'000s)	Basic remuneration	Variable earnings from share options and share appreciation programme[1]	Other variable remuneration	Total remuneration
Eckhard Spoerr	641	2,785	410	3,836
Axel Krieger	336	1,741	180	2,257
Stephan Esch	282	870	22	1,174
Eric Berger[2]	160	522	43	725
Michael Grodd[3]	138	0	158	296
	1,557	**5,918**	**813**	**8,288**

1 Including cash-effective compensation and valued in accordance with IFRS 2.
2 Executive director of the former freenet.de AG.
3 Left the management board of the former mobilcom AG on 15th November 2006.

As at 31st December 2007, the provisions for share options and share appreciation rights for Mr. Spoerr stood at € 3,873,000 (prior year: € 4,737,000), for Mr. Krieger € 2,421,000 (prior year: € 3,693,000), for Mr. Esch € 1,210,000 (prior year: € 1,167,000) and for Mr. Berger € 726,000 (prior year: € 819,000). At this date, the following number of share appreciation rights were held by members of the management board: Mr. Spoerr 1.28 million, Mr. Krieger 0.8 million, Mr. Esch 0.4 million and Mr. Berger 0.24 million.

In the fiscal year 2007, a sum arising from share options and share appreciation rights of € 4,272,000 (prior year: € 4,737,000) went to Mr. Spoerr, € 3,402,000 (prior year: € 1,233,000) to Mr. Krieger, € 1,022,000 (prior year: € 187,000) to Mr. Esch and € 732,000 (prior year: € 210,000) to Mr. Berger.

No new share options or share appreciation rights were issued to members of the company's management board during the 2007 fiscal year.

In November 2004, Messrs Spoerr, Krieger and Berger were each given a direct assurance of a pension from freenet.de AG, which freenet AG continues to honour. As at 31st December 2007 the defined benefit obligation (DBO) for Mr. Spoerr stood at € 835,000 (prior year: € 809,000), for Mr. Krieger € 442,000 (prior year: € 422,000), for Mr. Esch € 137,000 (prior year: € 105,000) and for Mr. Berger € 136,000 (prior year: € 117,000).

A total of € 597,000 (prior year: € 249,000) of service period costs, both current and due to be retrospectively charged, arising from the pension awards was included for members of the management board in the 2007 staffing costs.

No members of the management board were granted any loans and the company took on no sureties or other warranties on their behalf.

Supervisory board remuneration

The supervisory board's remuneration is governed by the articles of association. In the 2007 fiscal year the remuneration is made up of three components:

- A fixed remuneration
- Meeting fees
- Success-based remuneration

Supervisory board members receive a basic remuneration in the sum of € 12,000 for each full fiscal year of their board membership. The supervisory board chair receives double and the vice chair one and a half times this figure.

For each supervisory board meeting that they attend all board members also receive a meeting fee of € 1,000. All supervisory board members belonging to any supervisory board sub-committee – with the exception of the committee constituted in accordance with clause 27, paragraph 3 of the German Co-Determination Act – receive an additional meeting fee of € 1,000 for each committee meeting. The committee chair receives double the figure.

Following the end of each business year, the members of the supervisory board further receive a variable emolument in the sum of € 500 for every € 0.01 over € 0.10 per company share distributed in dividends to shareholders. This variable element of remuneration may not exceed the sum due as fixed remuneration. The supervisory board chair receives double and the vice chair one and a half times this figure.

The remuneration for members of the company's supervisory board and of those of its predecessor companies was made up for the fiscal year as follows:

Remuneration for the fiscal year 2007 (In €'000s)	**Basic remuneration**	**Meeting fees**	**Success-based remuneration**	**Total**
Active members				
Prof. Dr. Helmut Thoma	22.3	23.0	22.3	67.6
Birgit Geffke[1]	15.5	19.0	15.5	50.0
Oliver Brexl	12.0	14.0	12.0	38.0
Thorsten Kraemer	5.4	4.0	5.4	14.8
Dr. Dieter Leuering	5.4	5.0	5.4	15.8
Sascha Lucht[1]	10.4	15.0	10.4	35.7
Andreas Neumann[1]	10.4	10.0	10.4	30.7
Franziska Oelte[1]	10.4	14.0	10.4	34.7
Kai Petersen[1]	10.4	8.0	10.4	28.7
Prof. Dr. Hans-Joachim Priester	10.0	10.0	10.0	30.0
Richard Roy	5.4	7.0	5.4	17.8
Ulrike Scharlach[1]	10.4	7.0	10.4	27.7
	127.8	**136.0**	**127.8**	**391.6**
Former members				
Christian Burger[2]	1.0	0.0	1.0	2.1
Andrew John Dechet	5.5	2.0	5.5	13.1
Bastian Frederik Lueken	4.7	3.0	4.7	12.3
Prof. Klaus-Dieter Scheurle[2]	1.6	0.0	1.6	3.1
Prof. Dr. G. Konrad Schmidt	6.4	4.0	6.4	16.8
Prof. Dr. Dieter H. Vogel[3]	3.5	5.0	3.5	12.0
	22.7	**14.0**	**22.7**	**59.4**
	150.5	**150.0**	**150.5**	**451.0**

1 Workers' representatives as per clause 7, para. 1, sentence 1, point 1 of the Co-Determination Act of 4th May 1976.
2 Member of the supervisory board of the former freenet.de AG.
3 Member of the supervisory board of the former mobilcom AG.

In the previous year, the remuneration of members of the company's supervisory board and of those of its predecessor companies was made up as follows:

Remuneration for the fiscal year 2006 (In €'000s)	**Basic remuneration**	**Meeting fees**	**Success-based remuneration**	**Total**
Active members				
Prof. Dr. G. Konrad Schmidt	12.0	11.0	7.5	30.5
Birgit Geffke[1]	18.0	14.0	11.3	43.3
Oliver Brexl	1.3	1.0	0.8	3.1
Christian Burger[2]	6.2	0.0	6.2	12.4
Andrew John Dechet	12.0	11.0	7.5	30.5
Sascha Lucht[1]	12.0	13.0	7.5	32.5
Bastian Frederik Lueken	12.0	14.0	7.5	33.5
Andreas Neumann[1]	12.0	13.0	7.5	32.5
Franziska Oelte[1]	12.0	15.0	7.5	34.5
Kai Petersen[1]	12.0	10.0	7.5	29.5
Ulrike Scharlach[1]	12.0	9.0	7.5	28.5
Prof. Klaus-Dieter Scheurle[2]	9.3	0.0	9.3	18.6
Prof. Dr. Helmut Thoma	24.4	11.0	19.9	55.3
	155.2	**122.0**	**107.5**	**384.7**
Former members				
Klaus Thiemann	10.0	8.0	6.2	24.2
Prof. Dr.-Ing. Dieter H. Vogel	24.0	19.0	15.0	58.0
	34.0	**27.0**	**21.2**	**82.2**
	189.2	**149.0**	**128.7**	**466.9**

1 Employee representatives pursuant to Section 7 paragraph 1 sentence 1 No. 1 of the MitbestG dated 4 May 1976.
2 Member of the supervisory board of the former freenet.de AG.

Members of the supervisory board are also reimbursed for expenses incurred in the exercise of their duties and for any sales tax incurred.

5. Further information

5. Further information

5.1 Glossary

ADSL	ADSL technology enables data to be transmitted at a speed of up to 8 mbps over a telephone line, and thus permits broadband use of the telephone line (ADSL = Asymmetrical Digital Subscriber Line)..
ADSL2+	The extension of the ADSL standard permits a maximum data speed of 25 mbps in the receiving direction and 3.5 mbps in the transmission direction. Such a data speed enables HD/SD TV channels to be transmitted (ADSL2+ = Asymmetrical Digital Subscriber Line 2+).
ARPU	Average Revenue Per User..
Directory enquiries	This facility is an information service with nationwide availability at all times without the need for any prefix; it is used for providing information concerning the number, name and address and additional details of telecommunication users. Such services are reached via a number 118xy.
B2B	Business with business customers (B2B = Business to Business)..
BNetzA	Bundesnetzagentur für Elektrizität, Gas, Telekommunikation, Post und Eisenbahnen (Federal Network Agency for Electricity, Gas, Telecommunication, Posts and Railways).
Broadband	Digital data transmission with a speed of more than 128 kbps.
Call-by-Call	Choice of network operator for a specific connection on a call-by-call basis.
CFA	Cooperation agreement between mobilcom, FT and Gerhard Schmid from the year 2000 (CFA = Cooperation Framework Agreement).
DSL	A Digital Subscriber Line is used by households and companies for transmitting and receiving data at high transmission speed (up to 50,000 kbps). This is a major increase in speed compared with modem or ISDN connections of up to 128 kbps
DSL line	The DSL line between the subscriber network operator (TNB) and the user.
DSL-Resale	The process of reselling DSL lines under a separate name.
DTAG	Deutsche Telekom AG.
EBIT	Earnings before interest and taxes less depreciation and amortisation plus the result of companies accounted for using the equity method.
EBITDA	EBIT (see above) plus depreciation and amortisation.
Earnings per share	This ratio specifies that portion of consolidated net profit or loss which is attributable to an individual share. It is calculated by dividing the consolidated net income/net loss by the weighted average number of issued shares.

Fixed network	In general language, this concept is used to describe a telecommunications network which is used for providing line-borne services.
freenet IP Netz	The core network for IP-based services connects the central technology locations (also known as IP backbone).
FT	France Télécom S.A., Paris, France.
GSM	Pan-European standard for second generation digital mobile telephony in the 900 and 1800 MHz range (GSM = Global System for Mobile Communication).
IFRS	International Financial Reporting Standards
Intelligent Network	An Intelligent Network (IN) is not a separate physical network, but a services-oriented central system built on an existing phone network (e.g. ISDN). An IN adds intelligent network components and additional service features to a phone network, primarily value-added services for fixed-line and mobile calling, and faxing. IN operators don't necessarily have to be network operators (carriers) at the same time; they can implement their product on existing networks.
Interconnection	Interconnection of switching telephone networks.
Internet	The Internet is a worldwide network of computers based on the Internet Protocol (IP) without any central network management.
IP	Internet Protocol; a data interchange protocol which is widespread in computer networks.
IP Backbone	This core network for IP-based services connects the central technology locations of a network. Depending on the particular type, these networks can assume international and even international dimensions.
ISDN	ISDN integrates services such as telephony, fax or data communication in the fixed network. Digital technology improves transmission quality and increases transmission speed compared with analogue connections. ISDN also permits packet-switched data transmission (ISDN = Integrated Services Digital Network).
ISIN	International Securities Identification Number.
Value-add service	A value-add service is an independent range of services within a telecommunications service, which is characterised by special connection treatment, virtual connections, independent charging or content services.
MNO	Mobile Network Operator.
mobilcom	mobilcom Aktiengesellschaft, Büdelsdorf.

Mobile telephony network A public mobile telephony network offering mobile telephony services in accordance with the GSM 900 or GSM 1800 standard, or for the third generation range of mobile telephony services (UMTS/IMT 2000).

Mobile telephony service provider Provider of mobile telephony services without their own mobile telephony network; they sell mobile telephony minutes, SIM cards and mobile telephones as well as value-add services, such as SMS in their own name and for their own account.

Naked DSL If only the DSL connection is offered to the end user on a twin copper wire, this arrangement is known as naked DSL.

Page impressions Page impressions describe the number of hits of any users on a web site, and are used as an important criterion in the range of analysis of Internet services.

Penetration rate (mobile telephony market) Total number of issued SIM cards expressed as a percentage of the total number of inhabitants.

Portal Central web site which generally comprises a comprehensive range of navigation functions, aggregated content and additional services, such as email.

Prepaid Mobile telephony service paid in advance.

Preselection Permanent default setting of the subscriber line to a specific connection network operator

PwC PricewaterhouseCoopers Aktiengesellschaft Wirtschaftsprüfungsgesellschaft.

Roaming Feature of cellular radio networks which ensures that activated mobile stations, irrespective of location, can be reached in all radio cells of the entire area of coverage of a network. Roaming can also cover equivalent networks of various network operators (national roaming) and also cover cross-border networks (international roaming).

Narrowband Analogue or digital data transmission with a speed of up to 128 kbps.

Server Hosting Presentation of the services of an Internet server, such as memory and email functionality, e.g. for installation of a website.

Server Housing Service for which the servers required for a web site are not operated on the premises of the owner of a website, and instead are operated on the premises of a service provider specialising in this service.

SIM card Subscriber Identity Module; chip card with a processor and memory of GSM telephones, storing various information, including the user number allocated by the network operator, and which identifies the user in the mobile network.

SMS Digital short message via mobile telephone (SMS = Short Message Service).

TAL	Describes the twin copper wire between the main distributor of DTAG and the end user; TAL = Teilnehmeranschlussleitung (subscriber access line).
Triple Play	This normally describes the bundling of three services on one broadband line, e.g. the bundling of mobile telephony, voice and data services on one broadband line.
UMTS	UMTS is a new high-performance standard which permits all types of communication and multi-media applications via mobile telephones; also known generally as 3G mobile phones (UMTS = Universal Mobile Telecommunications System).
VATM	Verband der Anbieter von Telekommunikations- und Mehrwertdiensten e.V., comprising competitors of DTAG.
VDSL	High-speed DSL connection which permits higher transmission speeds as a result of increasing the fibre content of the transmission channel (VDSL = Very High Bit Rate Digital Subscriber Line).
VoIP	Telephony via a computer network (e.g. the Internet) based on the Internet Protocol (IP) (VoIP = Voice over IP).
Web Hosting	Hosting of web sites on the server of an Internet service provider (provider or web hoster).
Wholesale DSL	Agreement with DTAG for selling on broadband DSL access lines (DSL lines) of DTAG.
xDSL	Generic term of various types of DSL, such as ADSL, ADSL 2+, VDSL.

5.2 Contact, publications

freenet AG
Investor Relations
Hollerstraße 126
24782 Büdelsdorf

Andreas Neumann
Phone: +49 (0) 40/51306778
Fax: +49 (0) 40/51306970
E-mail: investor.relations@freenet.ag
Internet: www.freenet.ag

The annual report and our interim reports are also available in the Internet at

www.freenet.ag
heading: Investor Relations.

In the event of any doubt, the German version shall prevail.

Current information concerning freenet AG and your shares is available on our website.

5.3 Financial calender

9 May 2008[1]
Publication of interim report I/2008

May 2008[1]
Annual shareholders‘ meeting

8 August 2008[1]
Publication of interim report II/2008

8 November 2008[1]
Publication of interim report III/2008

1 Probable dates

freenet AG
Hollerstraße 126
24782 Büdelsdorf

6102636