# ANNUAL REPORT FREENET AG

# 2016

freenet GROUP

MOBILCOM-DEBITEL / KLARMOBIL.DE / GRAVIS / FREENET.DE / MEDIA BROADCAST / FREENET DIGITAL / FREENET ENERGY / MOTION TM

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# OVERVIEW KEY FINANCIALS[1]

# GROUP

## Result

| In EUR million/as indicated | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Revenue | 3,362.4 | 3,117.9 | 938.3 | 867.2 | 826.8 |
| Gross profit | 898.7 | 790.4 | 253.0 | 234.1 | 215.6 |
| EBITDA | 438.8 | 370.2 | 127.1 | 118.2 | 97.8 |
| EBIT | 298.8 | 298.8 | 87.1 | 81.2 | 78.9 |
| EBT | 244.0 | 254.7 | 73.7 | 67.2 | 64.0 |
| Group result | 216.4 | 221.5 | 54.4 | 58.0 | 48.4 |
| Earnings per share in EUR (diluted and undiluted) | 1.78 | 1.73 | 0.48 | 0.47 | 0.38 |
| Dividends paid per share in EUR for the financial year | 1.60[2] | 1.55 | - | - | - |

## Balance Sheet

| In EUR million/as indicated | 31.12.2016 | 31.12.2015 | 31.12.2016 | 30.9.2016 | 31.12.2015 |
|---|---|---|---|---|---|
| Balance sheet total | 4,284.8 | 2,724.0 | 4,284.8 | 4,194.0 | 2,724.0 |
| Shareholders' equity | 1,402.3 | 1,379.0 | 1,402.3 | 1,329.5 | 1,379.0 |
| Equity ratio in % | 32.7 | 50.6 | 32.7 | 31.7 | 50.6 |

## Finances and investments

| In EUR million | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Free cash flow | 341.5 | 284.5 | 78.8 | 71.3 | 67.1 |
| Depreciation and amortisation | 124.3 | 71.4 | 35.0 | 31.9 | 18.8 |
| Net investments[3] (CAPEX) | 48.1 | 30.4 | 13.9 | 9.5 | 10.7 |
| Net debt | 725.8 | 369.2 | 725.8 | 787.7 | 369.2 |
| Pro forma net debt | 1,416.0 | 369.2 | 1,416.0 | 1,473.8 | 369.2 |

## Share

| | 31.12.2016 | 31.12.2015 | 31.12.2016 | 30.9.2016 | 31.12.2015 |
|---|---|---|---|---|---|
| Closing price Xetra in EUR | 26.76 | 31.32 | 26.76 | 26.03 | 31.32 |
| Number of issued shares in '000s | 128,061 | 128,061 | 128,061 | 128,061 | 128,061 |
| Market capitalisation in EUR million | 3,426.9 | 4,010.2 | 3,426.9 | 3,332.8 | 4,010.2 |

## Employees

| | 31.12.2016 | 31.12.2015 | 31.12.2016 | 30.9.2016 | 31.12.2015 |
|---|---|---|---|---|---|
| Employees | 4,886 | 4,367 | 4,886 | 4,928 | 4,367 |

# OVERVIEW KEY FINANCIALS[1] MOBILE COMMUNICATIONS SEGMENT

## Customer development

| In million | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Mobile Communications customers/cards[4] | 12.06 | 12.24 | 12.06 | 12.06 | 12.24 |
| Thereof Customer Ownership | 9.53 | 9.30 | 9.53 | 9.47 | 9.30 |
| Thereof Postpaid | 6.51 | 6.31 | 6.51 | 6.43 | 6.31 |
| Thereof No-frills | 3.02 | 2.99 | 3.02 | 3.04 | 2.99 |
| Thereof Prepaid | 2.53 | 2.94 | 2.53 | 2.59 | 2.94 |
| Gross new customers/cards | 2.82 | 2.88 | 0.78 | 0.73 | 0.78 |
| Net change | -0.17 | -0.49 | 0.00 | -0.03 | -0.04 |

## Result

| In EUR million | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Revenue | 3,126.0 | 3,061.2 | 867.4 | 793.5 | 811.6 |
| Gross profit | 744.1 | 742.8 | 203.2 | 187.3 | 203.6 |
| EBITDA | 420.4 | 382.8 | 118.8 | 112.3 | 99.1 |

## Monthly average revenue per user (ARPU)

| In EUR | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Postpaid | 21.4 | 21.4 | 21.2 | 21.6 | 21.3 |
| No-frills | 2.4 | 2.5 | 2.5 | 2.5 | 2.4 |
| Prepaid | 3.1 | 3.0 | 3.1 | 3.2 | 3.1 |

# TV AND MEDIA SEGMENT

## Result

| In EUR million | 2016 | 2015 | Q4/2016 | Q3/2016 | Q4/2015 |
|---|---|---|---|---|---|
| Revenue | 218.9 | 0.0 | 70.8 | 70.1 | 0.0 |
| Gross profit | 110.8 | 0.0 | 38.3 | 35.7 | 0.0 |
| EBITDA | 28.0 | 0.0 | 9.6 | 8.3 | 0.0 |

1 Unless otherwise indicated, we refer to the section “Definition of alternative performance measures” for the definition of the key figures.
2 The dividend will be paid subject to resolution at the Annual General Meeting in June 2017. Further information on the dividend can be found in the section “freenet AG and the capital markets”.
3 Investments in property, plant and equipment and intangible assets, less the proceeds from the disposal of intangible assets and property, plant and equipment.
4 At the end of period.

# ANNUAL REPORT
# FREENET AG

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# DIGITAL LIFESTYLE, MOBILE COMMUNICATIONS, TV AND MEDIA

# ACQUISITIONS ARE THE FOUNDATION OF THE NEW "TV AND MEDIA" SEGMENT

At the end of 2015 and in the first quarter of 2016, freenet AG succeeded in breaking into digital TV business with two fundamental acquisitions and equity participations, thus extending its strategic focus to include an attractive growth field.

- Firstly, freenet acquired all shares of the Media Broadcast Group. This company is based in Cologne, and is the sole commercial provider of DVB-T2 HD in Germany. This new standard is due to start at the end of March 2017, and permits the terrestrial broadcasting of a comprehensive station package in full HD quality, and in particular addresses millions of German TV households who are already using DVB-T. In addition to the public sector programmes, this will enable customers to additionally receive approximately 20 private stations in full-HD quality – although this will still only be possible in encrypted form. For this purpose, viewers will require not only an internal or external antenna but also a CI+ module (to be retrofitted) with new TVs with DVB-T2-HD capability; on the other hand, a small set-top box is necessary for all other devices.
- This also includes access to the catch-up services of the various stations. The acquired business also includes radio (VHF and DAB) as well as network services for TV production; the satellite operations of Media Broadcast were spun off before the acquisition.
- Secondly, freenet has acquired an initial starting investment of 24.99 per cent in EXARING AG, and secured the distribution rights to that company's closed IP platform for innovative entertainment services. This company is based in Munich, and has its own 12,000 km fibre-optic network; in this way, it provides the possibility of motion image entertainment for currently approximately 23 million German households with transmissions of up to 8K – thus also covering future innovations such as virtual reality and holography/3D.

In this way, freenet has laid the foundation for using its significant retail expertise and distribution capability to market TV with excellent image quality to private customers. With its participation in EXARING, the company also addresses the rapidly expanding market of streaming and video-on-demand services in Germany. In the further course of the year, freenet then intensively prepared the market launches of the new products in the TV and Media segment – "freenet TV" in DVB-T2 and "waipu.tv" in the field of digital motion picture entertainment.

On 31 May 2016, the pilot operation of DVB-T2 HD started as planned in several major German cities. In this first test phase of the new broadcasting standard, viewers in the respective core regions will be able to receive (via antenna) high-resolution TV images of ARD and ZDF as well as the private stations RTL, Sat.1, ProSieben and VOX. For this purpose, freenet (or the new subsidiary Media Broadcast) initially licenced approximately a dozen of these set-top boxes. At the same time, in conjunction with advertising activities of the public sector stations and the intensive reporting regarding the new terrestrial HD-TV, the company started various marketing measures, exhibition appearances and talks with the private stations – for instance about future PR cooperations.

The interest of consumers as well as TV stations in the new standard are documented by various figures and developments. For instance, the new freenet brand reported approximately 10,000 subscribers for its online newsletter concerning the subject a few weeks after the start of the PR activities concerning the web site freenet.tv. In addition, at the end of August 2016, 14 production licences for set-top-boxes had been issued to manufacturers who currently offer the devices required for freenet TV. At the same time, the technical change-over measures had also been implemented at 38 of a total of 61 transmitter stations, and the station portfolio now covers 97 per cent of TV programmes which are currently consumed.

In the third quarter of 2016, freenet boosted the strong demand for this product with a series of specific marketing activities. One of the main activities in this respect was the company's own stand at the IFA in Berlin in the first week of September; it met with strong interest among consumers as well as representatives from the public sector and also private stations, the press and investment companies. The company also presented a PC dongle with a small DVB-T2 antenna, which freenet TV has been offering since the beginning of 2017 for full-HD TV reception for PCs and MacBooks.

In addition, in the second half of the year, separate TV spots concerning the subject as well as specific online advertising ran on mobilcom-debitel.de; the cross-media end-of-year campaign provided information concerning the disconnection of the old DVB-T standard which was due to expire at the end of March 2017 as well as the advantages of freenet TV. Since mid-September 2016, all affected programmes have been providing information about the imminent change of technology by way of inserts. mobilcom-debitel also started to equip most of its shops with freenet TV; potential clients and mobile communication customers of the company are thus able to obtain detailed information and advice concerning the benefits of the new TV offering in their local store.

In the somewhat more advanced IPTV field of EXARING, intensive test runs were commenced at the beginning of April 2016 (initially with 100 participants) regarding linear TV, video-on-demand, online games and streaming services. In May, the test series were extended with continuous questions to 500 participants in the first instance; during the third quarter, the test series were extended to 1,000 beta testers. In the course of two questionnaires, they provided a total of more than 70,000 progress reports, evaluations as well as further suggestions which were included in the customer-oriented configuration of waipu.tv at the product start on 30 September 2016. waipu.tv is available in two options: as an advanced version with 10 hours memory for 4.99 euros per month and as a perfect version with 50 hours memory for 14.99 euros per month – both versions can be terminated monthly and come with a free test month. At the same time, two data centres necessary for waipu.tv commenced operations in Karlsruhe and Leipzig.

The waipu.tv app has been available free-of-charge in Google Play Store and also in the Apple App Store since 30 September 2016; with the aid of this app, and on the basis of the latest EXARING fibre-optic infrastructure, brilliant video and audio quality can be transferred quickly and easily to the user's smartphone and from there to the user's existing TVs at home. Right from the very beginning, the product supplied by waipu.tv provided more than 50 TV channels on the user's mobile phone and at home via Google Chromecast, and the offering was extended continuously in subsequent months. In time for the Christmas season, mobilcom-debitel also put together a low-cost package with a discounted streaming dongle as well as free use of waipu.tv and maxdome for three months.

# NEW OFFERINGS TO EXTEND THE DIGITAL LIFESTYLE PORTFOLIO

mobilcom-debitel has set new accents in recent years in the segments of energy, entertainment and security – in particular with innovative SmartHome solutions. In the first quarter of 2016, the company succeeded in launching a further field with a range of products, namely e-health: Under the bracket “SmartCare”, digital technologies for disease prevention as well as physical and mental well-being are now available via www.md.de/smartcare.

The well-being offerings started with “Withings aura” at the beginning of the year: The digital wellness oasis comprises individually controllable light and sound options to enable the user to relax when going to sleep and waking up, and also provides bolt-on options of sensor-driven sleep monitoring. This was followed by the “Withings smart body analyser”: The multi-functional scale monitors the user’s weight, body-mass index as well as body fat percentage by means of an app, and also provides differentiated information for a range of body types, automatic heart frequency measurement as well as additional features such as room air quality and daily weather report. SmartCare activities were concluded at the end of October with “asina”, a tablet-PC solution which addresses in particular technology beginners, senior citizens, people with handicaps and their relatives; they can configure the product individually for their specific needs and can thus use it as assistance for nursing care and support – with three applications for health tracking, for instance for blood sugar, blood pressure and weight.

In the field of fitness, the company also offers the leading portal for online training with “Gymondo”; this is a low-cost subscription which can be terminated monthly, for charges starting at 4.99 euros per month. It contains more than 20 programmes and 250 courses, at can be used to turn the user’s own four walls into a sports studio. The fitness tracker “Jawbone UP2” is the ideal complement in this respect: The slim bracelet checks the fitness of its user, suggests activity plans, supports a balanced diet and provides convincing features with a long battery operating time and an integrated alarm clock function with a vibration alarm. And “NeuroNation” has rounded off the health offering: Starting at 8 euros per month, this enables the user to analyse brain fitness, create customised exercise programmes and improve concentration and cognitive performance with targeted memory training.

In the hardware field, mobilcom-debitel has continued the “Sonntagskracher“ (Sunday Stunner) which were launched in November 2015. The company has offered a range of highlights under the terms of these weekly bargain actions enabling users to acquire devices for a low price:

- In February, the Samsung Galaxy S6 in the 32 GB version for approximately 400 euros – a saving of 150 euros compared with the official sales price,
- Mid-March: the Galaxy Tab A LTE 9.7 for approximately 235 euros instead of the official 340 euros,
- As an „Easter Sunday Stunner“: the Bluetooth body analysis scale Medisana BS 444 connect for approximately 25 euros instead of 70 euros as RRP,
- As a special „Pfingstkracher“ (Whitsun Stunner): the very successful iPhone 5s (for which there continues to be strong demand) in the 16 GB version for 300 euros,
- In the summer months, a range including the fitness tracker Fitbit Zip (reduced by 80 per cent), the Samsung Galaxy S6 in the 32 GB version with a reduction of 190 euros, and the iPad Air 2 Wifi with 32 GB for 379 euros as well as the smartphone Xperia Z5 Compact of Sony for a price of 355 euros, as well as
- In the autumn weeks and in the run-up to Christmas: for instance the iPhone SE in the 64 GB version for 465 euros.

In the field of security, the product range of mobilcom-debitel has for several years included Norton Mobile Security, which is security software for protecting smartphones and tablets. In July, the main brand of freenet extended its portfolio to include two additional digital security solutions for protecting PCs and Macs: “Norton Security Online” from Symantec is available in one version with three licences for a price of 2.99 euros per month and one version with five licences for 3.99 euros per month.

At the same time, the company started a new app-based magazine flatrate with “Readly”. For a monthly price starting at 9 euros, this provides five users with simultaneous access via PC, smartphone or tablet to more than 1,600 magazines from ten countries; this is available not only in relation to the current editions, but also to the corresponding archives.

The freenet subsidiary GRAVIS also carried out various special actions in the course of the year. For instance, on the occasion of the European Football Championship, there was the Sonos PLAYBAR with a 100 euro voucher: The WLAN sound system with nine loudspeakers provided an app-driven facility for genuine stadium sound in HiFi quality – and subsequently also for a perfect party atmosphere with music services such as Apple Music, Spotify or Deezer.

This was followed in August by the “summer sale” of the company; it comprised 75 discounted products with reductions of up to two thirds and more in certain cases. The main beneficiaries were Apple products such as MacBooks, iPads and iPhones incl. attractive protective covers and smart covers. Further highlights included the app-driven mood light Avea of Elgato (reduced by 50 per cent) or the Misfit Ray for a price of approximately 99 euros: The fitness bracelet records not only all major activity data, incl. swimming, but also the duration and quality of sleep.

On the occasion of the “Black Friday sale”, GRAVIS offered hardware and software subject to conditions which in certain cases featured considerable reductions, including MacBooks, wearables and SmartHome products. And within the framework of its “advent weeks”, the freenet subsidiary discounted numerous products on a weekly basis – with a focus on Apple and considerable (in certain cases three-digit) discounts.

# CUSTOMER GROWTH BOOSTED BY TARIFF ACTIONS

In the traditional mobile communications segment, freenet AG covers all major areas of activity with its subsidiaries – with a focus on private customers: The main brand mobilcom-debitel focuses on high-quality contractual relations with its Allnet tariff world, thus extending the various digital lifestyle offerings of the Group to include transparent low-cost flatrates for a wide range of user profiles and all German mobile networks. At the same time, the various discount brands of freenet address the no-frills market. In addition to the company's own tariffs, the original tariffs of the network operators are also available – in general with discounts of 10 per cent.

As was the case last year, the freenet brands set additional accents in competition in the course of the financial year 2016, with a range of specific discount and tariff offerings; once again, this contributed to the continuous growth of customer ownership which is of considerable importance for freenet. The temporary actions of the various discount providers within the Group ran via the company's own deal platform www.crash-tarife.de or via neutral online platforms. The following selection of offerings reflects the variety of tariffs and network options for the customer – and underlines the excellent competitive position of freenet as an independent service provider in the mobile communications market.

- At the end of January 2016, mobilcom-debitel offered the smart surf in the Vodafone network for an official price of 9.99 euros per months; including two credits for a total of 144 euros, this price reduced to 3.99 euros per month over the two-year contract period. In return, the user received a data volume of 1 GB with a speed of 14.4 Mbps and an additional 50 free minutes as well as 50 free texts to all German networks.
- In mid-March, the subsidiary halved the Comfort Allnet to also approx. 10 euros, using a starting credit of 120 euros. The tariff in the network of O2 comprised a mobile-Internet flatrate with an unthrottled inclusive volume of 1 GB in conjunction with a maximum bandwidth of 21.6 Mbps as well as a flatrate for calls to all German networks.
- At the beginning of July, the freenet main brand introduced the LTE standard for new customers for its O2 and E-Plus tariffs. This was matched by three new LTE smartphone tariffs with free calls to all German networks and data volumes of 1 GB, 2 GB or 5 GB – with monthly charges ranging from approximately 10 to approximately 20 euros and maximum bandwidth of up to 50 Mbps. And in August, the company offered an LTE data flatrate with a volume of 10 GB and a maximum speed of 150 Mbps for approximately 16 euros per month; versions with 3 GB and 6 GB were also available for even lower monthly charges.
- And in the fourth quarter, the new O2 Free tariffs were available in the online shop of mobilcom-debitel with a discount of 10 per cent. The offerings comprised a call and text flatrate to all German mobile and landline networks, an EU roaming option as well as a mobile data flatrate with 1 GB, 2 GB or 4 GB; the maximum data rate in the LTE network is 225 Mbps.
- At the beginning of June 2016, the discount subsidiary klarmobil upgraded its tariff family: It restructured its usually temporary offerings into a fixed Allnet tariff group, generally offering more performance for the same money – in particular a higher data volume and higher surfing speeds. New and existing customers are able to choose between three new tariff options: For 14.85 euros per month during the minimum two-year contract period, the Allnet Flat 1000 comprises a call flatrate to all German networks, an Internet flatrate with a high-speed data volume of 1 GB and max. 21 Mbps in downstream; with the Allnet Flat 2000 for 17.85 euros per month, the Internet flatrate doubles to 2 GB high-speed data volume with max. 42 Mbps in downstream and otherwise identical features; and finally, the Allnet Flat 4000 costs 22.85 euros per month, offering a call flatrate as well as a text flatrate to all German networks as well as a high-speed data volume of 4 GB also with max. 42 Mbps.

- In addition, in the second half of the year, klarmobil reduced various tariffs in the course of attractive special actions. For instance, at the end of October, the smart flatrate was available in the network of Deutsche Telekom in three options between 2.95 euros and 9.95 euros. And in November, the company reduced the Allnet-Spar flatrate S to 14.96 euros, combined with a middle-class smartphone.

In this context, mobilcom-debitel and the discount subsidiaries of freenet again achieved several dozen test victories, recommendations and awards in independent comparison tests in the specialist and industry press in the course of 2016. And as was the case in previous years, many offerings comprised the low-price acquisition of corresponding smartphones and tablets of all relevant manufacturers such as Apple, Huawei, LG, Nokia, Samsung and Sony.

# MARKETING CAMPAIGNS ADDRESSING NEW AREAS OF OPERATION AND CUSTOMERS

In the financial year 2015, mobilcom-debitel commenced an umbrella campaign with the Greek “Costa Fast Gar Nix” (i.e. costs virtually nothing) and “Costa Gans Wenig” (i.e. costs very little) as a new provocative face. With this emotionalising presenter, the campaigns, which comprised traditional marketing measures as well as online communication and a range of PoS activities, became one of the most effective series in recent years: All relevant measuring criteria as well as the delivery of new customers to the involved shops subsequently increased significantly.

“Costa Fast Gar Nix” was again the focus of the three major marketing campaigns in the financial year 2016. In the spring campaign between the beginning of February and the beginning of May, Costa advertised attractive digital lifestyle and mobile communications offerings, in the course of two four-weekly TV flights with more than 2,000 spots on high-coverage private stations. There was also online advertising, various PoS measures, extensive promotions, bulk mailings involving several million items as well as social media and PR. On Valentine’s Day, regional promotion actions were aired on the social media channels of mobilcom-debitel with “watch-out flyers” incl. competitions and other game and prize opportunities. The highlights among the offerings included hardware such as the Samsung Galaxy Grand Prime, the LED Sengled Pulse Solo, various smartphone tariffs and digital lifestyle options of Gymondo, Zattoo, mobilcom-debitel audio books as well as accessories reduced by up to 50 per cent.

To celebrate its 25th birthday at the beginning of June, the company also started a three-month anniversary campaign with offerings relating to smartphones, tariffs and digital lifestyle products. The campaign was again aired on numerous marketing channels with TV spots, online advertising, out-of-home posters as well as various below-the-line measures at the PoS. For this purpose, high-coverage stations such as ProSieben and Sat.1 broadcast two four-weekly TV flights with more than 2,000 spots; extensive online advertising and out-of-home posters in more than 20 major German cities, additional social media and PR activities as well as several million supplements in the Bild-Zeitung rounded off the 360-degree campaign.

In addition, during the summer months, mobilcom-debitel again went on the traditional tour covering a total of 30 German cities. The roadshow focussed mainly on major events such “Bochum Total” or the “Out4Fame Festival” in Bottrop and the positioning of the company as a digital lifestyle provider. Visitors were able to immerse themselves in virtual worlds, test new smartphones as well as additional products and applications, become drone pilots or obtain information regarding the new freenet TV.

In the autumn campaign between 1 October and 31 December, the focus was for the first time on the new TV offerings of mobilcom-debitel. Acting as a TV show master, Costa presented freenet TV and waipu.tv, as well as TV hardware in the form of receivers, antennae and CI+ modules and also, in the digital lifestyle field, the Samsung Galaxy S5 mini, various accessories of Networx and Google Chromecast. As part of the extensive above-the-line activities, more than 2,500 TV spots were aired in two versions and numerous online advertising materials on highly frequented web sites, as well as an out-of-home flight in 22 cities as well as digital out-of-home. In addition, the Bild-Zeitung issued a supplement with three million copies, and 7 million bulk mailings were sent to households in Germany in October and November. At the PoS, the advertising activities comprised Costa pavement signs, posters, flyers, various posters as well as Instore TV, and high-attention social-media actions rounded off the PR offensive.

# FREENET ENERGY EXTENDING ITS PORTFOLIO OF OFFERINGS

In 2013, freenet acquired MFE Energie GmbH, the leading high-street energy marketer in Germany. The portfolio comprises 30 nationwide and regional energy utilities – including the main brands such as E.ON, EnBW, E WIE EINFACH, eprimo and Yello as well as various municipal operations and well-known eco-providers such as Lichtblick, primastrom and Sauber Energie. As the first service-certified energy distributor in Germany, the company addresses private as well as business customers with its high-quality products and services.

In the third quarter of 2016, MFE Energie GmbH was renamed freenet Energy GmbH; the purpose of the new name is to strengthen the image of the company and simultaneously to unlock further synergy in conjunction with other brands of the freenet Group. freenet Energy is able to access the sales ability and expertise of approximately 600 of the Group's own shops, contractually committed retailers and 400 major electronic stores as partners; the freenet subsidiary is one of the most efficient specialist energy distributors and is one of the marketers with the highest level of sales of energy products at the PoS in Germany. The products are also available via a wide-range online distribution network which is achieving continuous growth, and are also available via direct sales with various partners.

In the further course of the year, the company expanded its utility portfolio to include further attractive co-operation partners:

- MAINGAU Energie started at the end of September; it is now a nation-wide supplier of electricity and gas, with more than 100 years of experience in the energy sector, with constantly low tariffs and more than 250,000 private and business customers.
- This was followed in mid-October by the MONTANA Group, which has been operating in the energy field for the past 55 years. With also approximately 250,000 customers in Germany and Austria and annual revenue of more than 550 million euros, this provider which is based in Grünwald near Munich is one of the largest SME energy suppliers in Germany; it specialises in trading with gas and electricity, mineral oil products and renewable energy as well as technical services related to heating.
- The beginning of November saw the start of a co-operation with the municipal operations of Flensburg, with which freenet Energy additionally strengthens the regional energy marketing of gas and electricity in Northern Germany.
- And in mid-November, the company also extended its regional energy marketing activities to the south of Germany via a co-operation with erdgas schwaben, and has thus set further accents in the marketing of renewable energies. This Augsburg-based provider has been supplying Swabia and the neighbouring parts of Upper Bavaria with climate-friendly natural gas for almost 60 years – with an increasing content of domestic bio-natural gas, heat and electricity. As a pioneer in the field of bio-natural gas, erdgas schwaben is currently the only energy service provider in Germany to have three operating bio-natural gas installations, thus achieving annual savings of more than 60,000 tons of $CO_2$.

# WIDE RANGE OF MEASURES WITH A POSITIVE IMPACT ON EMPLOYEES, CORPORATE CULTURE AND LOCATIONS

A key element of the corporate culture of freenet is a philosophy which focusses strictly on the interests of the company's stakeholders. This is applicable for the customers, shareholders, business partners and – last but not least – the employees as well as the social environment at the respective locations.

In 2016, these stakeholder values once again involved a wide range of corresponding activities – beyond operations. In the course of the year, freenet advertised 811 new jobs, thus complying with its social responsibility as a major and successful employer. In addition, 138 young people commenced their training in commercial/technical areas and in logistics, and ten students commenced their studies at professional academies, with the aim of achieving a qualification as Bachelor of Science or Bachelor of Arts.

A fixed element of the programme for promoting future executives are the continuous staff development programme, as well as the "freenet entrepreneurs" as a group-wide development programme, the "annual development talks" which were implemented for the first time in 2016 and finally three bursaries for a masters course (in parallel with ongoing employment) at the well-known MCI Management Center Innsbruck:

- A total of 249 qualification measures was held as part of the staff development programme; more than 1,000 permanent employees in the Group took part in these measures. An internal team of trainers also supported the specific qualification of the more than 2,000 employees in the mobilcom-debitel shops as well as in customer service.
- The "freenet entrepreneurs" entered the second stage in 2016. Key staff is considered to be multipliers within the Group, and take part in a special development programme over a period of eight months, focussing on entrepreneurial action, leadership and management.
- For the first time since last year, the "annual development talks" form a further key element in personnel development, with a view to implementing continuous improvement processes in the company. At the same time, they make a significant contribution towards expanding the group-wide feedback culture.
- For the first time, the company has awarded three bursaries for English masters studies at the MCI in parallel with ongoing employment. These bursaries are considered to be an investment in the social future and economic/entrepreneurial thinking, and freenet bears 25 per cent of the course fees in each case. In addition to a wide range of management and leadership skills, this also involves communicative and intercultural contents.

Communication and transparency have always been key issues for freenet – this would seem to be obvious for a telecommunications and media Group, but is by no means an automatic feature within the sector. For instance, the CEO blogs about his business impressions and significant events and takes time himself to immediately respond to questions of employees directed to "Frag Christoph (ask Christoph)" – also anonymously. And the familiar form of address (the familiar "Du" form as opposed to the less personal "Sie" form) – ranging from the trainees right through to the directors – makes a significant contribution to the specific freenet culture of flat hierarchies, efficient processes and rapid decisions.

As has been the case in recent years, freenet in 2016 again demonstrated a high degree of social commitment at its various locations. This is for instance demonstrated in donations running to high five-digit figures to

- the Kinderhilfsfonds (children's aid fund) Rendsburg-Eckernförde,
- the Katholische Hospizstiftung (Catholic hospice foundation) St. Martin in Stuttgart,
- the Hospiz-Initiative (hospice initiative) as well as the campaign "Mach Mittag" for school lunches in Kiel,
- the "Gutenachtbus (goodnight bus)" for homeless persons in Düsseldorf – a Sprinter van as a mobile dining room and consulting room,
- the "Krämer Kids" daycare centre in Berlin/Oberkrämer,
- the project "Straßenkids" (street kids) in Hamburg and
- the drug aid programme "Knackpunkt" as well as the project "Bemmen (Stullen) für die Schule" (sandwiches for school) in Erfurt.

The fact that the subsidiary and main brand mobilcom-debitel outsourced its customer service with foresight to Capita Customer Services at the end of 2016 does not contradict its multi-faceted commitment for the respective locations. On the contrary: For the specialised outsourcing service provider, optimum service for the customer is the sole business model and core competence. In this way, freenet makes a significant contribution towards ensuring that the relevant employees, taking account of the increasing digitising of the economy and customer contacts, will in the long term continue to be deployed in line with their skills, thus ensuring that their jobs are safe; the respective employment agreements have been retained subject to comparable conditions.

# TO OUR SHAREHOLDERS

*From left to right: Joachim Preisig, CFO; Christoph Vilanek, CEO; Stephan Esch, CTO*

# LETTER TO SHAREHOLDERS

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

Right from the very beginning, the history of our company, which has now been in existence for 25 years, has been characterised by particular momentum and significant entrepreneurial virtues: The ability to identify and address attractive markets, to constantly acquire market shares by way of organic growth as well as the ability to take on crucial and careful acquisitions in order to break into new and exceedingly promising areas of business.

Last year, we opened a further exciting chapter in this story of success of freenet AG – and we thus initiated a new era for our company: With the acquisition of all shares of the Media Broadcast Group and an equity participation in EXARING AG of initially approximately 25 per cent, which has now increased to more than 50 per cent, we have broken into the TV business and home entertainment of the future.

- As the sole commercial provider of DVB-T2 HD, Media Broadcast is offering a new station package in full-HD quality with the second generation of terrestrial antenna broadcasting due to start at the end of March 2017: up to 18 free-to-air public sector TV broadcasters and approximately 20 high-coverage private stations such as RTL, Sat. 1, ProSieben and VOX. The latter encrypted for a monthly payment of 5.75 euros – as the new brand freenet TV. The programmes which are included will in the medium term cover at least 96 per cent of the overall audience market.
- EXARING in turn has its own approximately 12,000 kilometre fibre-optic network which reaches more than 23 million German households with a broadband connection of more than 16 Mbps. With our majority holding, we have secured the distribution rights for this closed IP platform; our corresponding new product waipu.tv permits app-driven use of streaming services on the user's TV at home and, if required, on the user's smartphone for an additional charge. waipu.tv replaces the previous TV reception technologies satellite and cable, and is the only full-service offering of linear TV in Germany which operates without a set-top box. In the medium term, and in combination with the fibre-optic infrastructure, the platform will also permit future motion image innovations such as 4K, 8K, virtual reality and holography/3D.

These strategic decisions and investments have to be viewed within the context of remarkable figures in the new areas of operation and also in our core mobile communications division. A selection of the most import developments is set out in the following:

- In the summer of 2016, the Swedish network equipment provider Ericsson published an analysis concerning the global use of mobile phones, smartphones and data volumes. According to this analysis, the penetration of the global population with mobile communication contracts increased to 100 per cent at the beginning of the year: Approximately 7.4 billion people are now opposed by more than 7.4 billion contracts, and four out of five mobile phones which are sold are now smartphones; sales of smartphones are expected to virtually double in five years, from 3.2 to 6.3 billion.
- There has also been a corresponding increase in data consumption; according to a prediction of the Scandinavian experts, data consumption will rise from 1.4 GB (global average in 2015) to 18 GB per user per month in Western Europe during the next five years. This growth will be driven primarily by consumption of motion pictures particularly among young people; in five years, this is expected to account for 70 per cent of mobile data traffic, and is expected to feature annual growth rates of 55 per cent.
- These forecasts are confirmed by further studies. The US streaming service Netflix for instance has increased the number of its world-wide subscribers for films and TV series from 0.5 to almost 75 million during the past ten years.
- This trend is also applicable for Germany. On average, Germans today spend 223 minutes every day in front of the TV screen; the corresponding figure in 1988 was 144 minutes. According to the consumer electronics association GFU, the TV is increasingly becoming the central device for motion picture entertainment as well as home entertainment/automation, and volume sales of high-resolution UHD devices in Germany are currently rising strongly.
- In addition, according to a study of the market research company Nielsen, 16 per cent of the surveyed German users now use a video-on-demand service in the Internet. According to analyses of PricewaterhouseCoopers, online revenues in this still recent market in Germany will rise from 181 million euros in 2015 to 410 million euros in 2019.
- For video streaming, 94 per cent of local users use Internet-capable TVs, 52 per cent use their laptop and 26 per cent use a tablet; on the other hand, more than 80 per cent of the approximately 62 million German Internet users now surf the web with their smartphone. Overall, nine out of ten Germans above the age of ten currently use the Internet; almost everybody in the age range up to 44 years uses the Internet, whereas only approximately half of the over 65s use the Internet, albeit with the strongest growth of six percentage points recently compared with 2015.
- In addition, the smartphone enables a digital lifestyle which is increasingly comprising key daily functions. According to a study of the credit card provider VISA, 54 per cent of European consumers use their mobile devices for making payments; and they do so as naturally as with cash.
- In addition, 28 per cent of Germans use their smartphone for operating a health app for jogging, walking or on their way to work, in addition to special fitness bracelets or smart watches.

The technological merging of digital linear HD-TV and catch-up services, cloud-based streaming and PC services, online games and video-on-demand services is giving rise to new dimensions of information, entertainment and other services – we are firmly convinced of this. This process is driven by apps on smartphones or tablets in the resolutions HD, 4k and 8k – at home or on mobile devices; the smartphone in particular is thus increasingly becoming the key focal point of our modern life. We are firmly convinced that we will be able to successfully transfer our subscription model which has demonstrated its value over a period of two and a half decades, with currently approximately 12 million customers in the field of mobile communications/mobile Internet, to the new areas of operation. In this way, in addition to the sound mobile communications market (which however is to a large extent saturated) and the long-term digital lifestyle growth field, we are creating a third and strong earnings pillar for our company in the medium and long term.

Recent months and quarters have also been characterised by intensive work for preparing the market launch of freenet TV and waipu.tv. With the start of pilot operation and the test phases of DVB-T2 HD at the end of May 2016 in several major German cities, we began to licence the necessary set-top boxes and also started to carry out co-ordinated marketing measures – partially in co-operation with the public sector and private stations. In the second half of the year, these activities were accompanied by trade fair appearances at the IFA in Berlin and the media symposia in 2016, own TV spots concerning the subject, targeted online advertising on mobilcom-debiltel.de as well as a cross-media end-of-year campaign. At the same time, we increasingly equipped our mobilcom-debitel shops with the new TV products and corresponding presentation areas. In these shops, the visitor is now able to encounter the areas of mobile communications, digital lifestyle and innovative TV. The customer closely experiences the increasing merging and networking of the services – and we consistently take advantage of the corresponding cross-selling potential when advising the customer.

By the change-over date on 29 March 2017, Media Broadcast will have to upgrade 61 transmitter stations, and up to 3.5 million users will have to change over to new set-top boxes. The aim of Media Broadcast is to use newsletters and online campaigns to ensure that a maximum number of the previous users register so that they can subsequently be directly and personally converted to the pay service.

The beginning of the fourth quarter of 2016 saw the start of marketing of waipu.tv with two options for the customer: The Comfort version with ten hours memory for 4.99 euros per month and as the Perfect version with 50 hours memory for 14.99 euros per month – both with the option of being terminated monthly and with a free test month. The start was preceded since the beginning of April with intensive test series with up to 1,000 participants and two surveys – with a total of more than 70,000 responses, evaluations and further suggestions regarding the customer-oriented configuration of the offerings. At the end of 2016, EXARING already had approximately 50,000 registered users of its app – even without relevant marketing investment.

Using the same consistency and intensity, we also devoted our attention to the two other business areas of the freenet Group last year – our core mobile communications segment and the digital lifestyle growth market which we have been addressing for several years. The latter activities were extended in the first quarter to include innovative e-health solutions, complementing the existing areas of energy, entertainment, security and SmartHome. Under the "SmartCare" heading, they comprise digital technologies for disease prevention as well as physical and mental well-being. The main product starts were as follows:

- "Withings aura" with individually controllable light and sound options to enable users to go to sleep and wake up relaxed, as well as bolt-on options of sensor-driven sleep monitoring,
- The multi-functional scale "Withings smart body analyser" with differentiated information regarding weight, body mass index, body fat percentage, heart frequency, room air quality and daily weather report,
- The tablet-PC solution "asina", particularly for technology beginners, senior citizens, people with handicaps and their relatives – to assist support and with three applications for health tracking, for instance for blood sugar, blood pressure and weight,
- In the field of fitness, the leading portal for online training ("Gymondo"), which is a low-cost subscription which can be terminated monthly for payments starting at 4.99 euros per month – and ideally complemented by
- The fitness tracker "Jawbone UP2", a slim bracelet for monitoring fitness with activity plans, diet suggestions and tips for improving concentration and cognitive performance.

In the hardware field, our main brand mobilcom-debitel and also the subsidiary GRAVIS continued their regular shop activities and also their special actions which were carried out in 2015 – some activities taking place as part of a weekly cycle in the form of "Sunday Stunners", as "summer sales" or "Black Friday sales" or within the framework of the "advent weeks". They mainly comprised smartphones and tablets of various manufacturers with up to three-digit discounts, also including offerings and accessories from the fields of e-health and entertainment. These included Bluetooth loudspeakers and headsets, smart watches and fitness bracelets and the latest app-based games, film, music and audio book options. And last but not least, as a result of its excellent position as a long-standing exclusive Apple dealer partner, GRAVIS was one of the first retailers in Germany which was able to offer the latest Apple devices very soon after the initial launch in its 43 stores – for instance the very popular iPhone 7.

mobilcom-debitel also extended its security segment for protecting smartphones and tablets to include two digital security solutions for PCs and Macs: "Norton Security Online" from the house of Symantec is now available in one version with three licences for a price of 2.99 euros per month and one version with five licences for 3.99 euros. In addition, the company has also started a new app-based magazine flatrate in the form of "Readly"; for a monthly payment starting at 9 euros, this enables up to five users to gain access with their PC, smartphone or tablet to more than 1,600 magazines from ten countries; this is applicable not only for the current issues but also for the corresponding archives.

In mobile communications, the fact that the market has been saturated for several years means that our main brand mobilcom-debitel has been focussing on high-quality contract relations with its range of Allnet tariffs, thus extending the respective digital lifestyle offerings of the Group to include transparent and low-cost flatrates for a wide range of user profiles and all German mobile networks. At the same time, the various discount brands of freenet address the no-frills sector. In addition to our own tariffs, we also offer the original tariffs of the network operators – in general with discounts of 10 per cent in relation to the monthly basic charge. As has been the case in previous years, we have been able to gain additional points against the competition in the course of 2016 with our brands, by means of a range of specific discount and tariff offerings; in general, these run via the company's own deal platform www.crash-tarife.de or via neutral online platforms, and made a significant contribution to the continuous growth in customer ownership which is of great significance for freenet.

This strategy which is based on sustainable profitability in conjunction with careful growth was again successful last year, as demonstrated by the following figures for 2016:

- Customer ownership is a key management parameter for our company, and has now reported growth for more than five years in a row: In the course of the year, the number of postpaid and no-frills customers increased by 232,000 to 9.53 million as of the end of December 2016; the number of particularly valuable contract customers with two-year contracts included in this figure increased by 203,000 to 6.5 million.
- The important postpaid ARPU of 21.4 euros continued to be very stable – compared with 21.4 euros in the two previous years.
- Compared with the previous year, revenue has increased by 7.8 per cent to 3.36 billion euros; this was attributable to the sound mobile communications segment and in particular to significantly higher digital lifestyle revenue as well as the acquisitions and equity participations seen at the end of 2015 and the beginning of 2016.
- Gross profit has also increased to the current figure of 898.7 million euros; this corresponds to a gross profit margin of 26.7 per cent.
- In consequence, EBITDA has improved by 68.6 million euros compared with 2015 to the current figure of 438.8 million euros – despite the increase in the number of customers which has involved significant sales expenses.
- The free cash flow of 341.5 million euros is above the previous years' level.

This means that freenet AG has met or even exceeded its targets for the financial year 2016; as has been the case in previous years, we have again proved to be more than a very reliable player on the capital markets, and have simultaneously laid the foundation for our constant dividend policy which focusses on shareholder value; this aims to pay out between 50 and 75 per cent of the free cash flow. It has to be noted that our forecast increased somewhat as a result of the acquisition of the Media Broadcast Group and the equity participation in EXARING AG – to an EBITDA of slightly more than 400 million euros and free cash flow of approximately 300 million euros.

The latter increased by approximately 30 million euros following the receipt of the dividend payment of Sunrise Communications Group AG in April 2016; however, this did not form part of guidance. In March 2016, freenet signed a contract (in the form of a financial investment) for the acquisition of up to 11,051,578 ordinary shares of the largest private telecommunication provider in Switzerland. Sunrise has more than three million customers in the fields of mobile communications, landline, Internet and digital TV. On the basis of our good figures for 2016, and together with the supervisory board, we are proposing to the next annual general meeting that a dividend of 1.60 euros should be paid out for each dividend-bearing share; this corresponds to around 60 per cent of the free cash flow, and comprises a total of 204.8 million euros.

In this way, we are continuing our course which has demonstrated its value in a phase which represents a major opportunity and a minor paradigm change for our company. We do so in the firm conviction that, with the recent acquisitions and the associated quantum leap, we are taking very important steps in the direction of securing a prosperous long-term future for freenet AG. With the development of new and fascinating markets – in the interest of our shareholders, our employees and the other stakeholders.

The outsourcing of the customer service of mobilcom-debitel to Capita Customer Services as of 1 March 2017 does not represent a contradiction in this respect. On the contrary: We are engaging an outsourcing service provider for whom optimum customer service is the sole business model and core competence; the employment agreements of the affected employees will be retained subject to equivalent conditions, and will be provided with maximum security.

We as the freenet Group in turn can devote ourselves to the major challenges in the course of the next few months and years to an even greater extent and with all our ability and expertise – as a lean, efficient and successful provider of attractive solutions relating to mobile communications/mobile Internet, digital lifestyle and innovative TV.

Christoph Vilanek | Joachim Preisig | Stephan Esch

# A RÉSUMÉ OF MANAGEMENT AND EMPLOYEES

## “The digital quantum leap requires local identity and intensive support for people!”

If we now look at the smartphone on the occasion of its tenth birthday, there can only be one conclusion: “Never before in history have there been such radical changes in daily professional work and leisure-time behaviour”. We of course appreciate the virtually unlimited variety and extreme speed which accompany the process of digitising daily operations and in particular business processes – this is also the case at freenet. And in our capacity as a company we have repeatedly been a catalyst behind this momentum – currently taking place with the merging of smartphones, Internet and TV and the associated quantum leap in the TV world; the smartphone is thus increasingly becoming the focal point of our daily operations across all areas and structures.

However, we must take care to ensure that, in conjunction with the process of digitising our life, we do not neglect the need to face the conflicts posed by new challenges and products and also focus on personal communication. This is because many people feel disoriented and even threatened in view of the world-wide Anglicisation of language, the predominance of American and Eastern Asian hardware, media, TV series, browsers, search engines, software and technological innovations from the USA – even in the USA itself. The responses to the above also include nationalist movements, votes and election results – accompanied by recollections of a separate regional and social identity.

At freenet, we consider that it is one of our main tasks to ensure that our customers and also our employees are not afraid of these, in the final analysis, irrevocable changes to their professional and private lives. How will we achieve this? For instance by offering our customers clear new products which focus on their specific needs, such as freenet TV and waipu.tv. But also by means of maximum personal proximity and support, which we guarantee by means of our extensive nation-wide network of our own shops – and which we are currently focussing on people to an even greater extent. We provide our employees with maximum security in view of the changes which are taking place: We provide them continuously with further training in the new subject areas, and provide them with the corresponding technical equipment. We also ensure pronounced digital transparency in the company across all structures; within this framework, employees can for instance address questions to me directly (also anonymously). I answer these questions myself immediately. Or I report mainly impressions and experiences to employees in my blog, for instance at exhibition appearances or visits to product manufacturers relating to digital lifestyle. “We understand digital life” – we not only propagate our new claim, we also implement it in our daily work with full commitment and consequence!

Within the freenet Group, we have maintained the special corporate culture of SMEs by using Group subsidiaries with flat hierarchies which operate essentially under their own responsibility; each individual counts in such a structure. And last but not least, we are strengthening our unmistakeable identity by means of joint celebrations. As on the occasion of our anniversary, when we invited all employees of our 11 locations spread over the whole of Germany to attend the giant summer party at the Babelsberg studios in Potsdam. We are proud of our employees – and are proud of our special identity as a successful company in Germany!

Christoph Vilanek,
Chief Executive Officer, freenet AG

# "freenet has now obtained very favourable refinancing – with flexible scope for strategic decisions!"

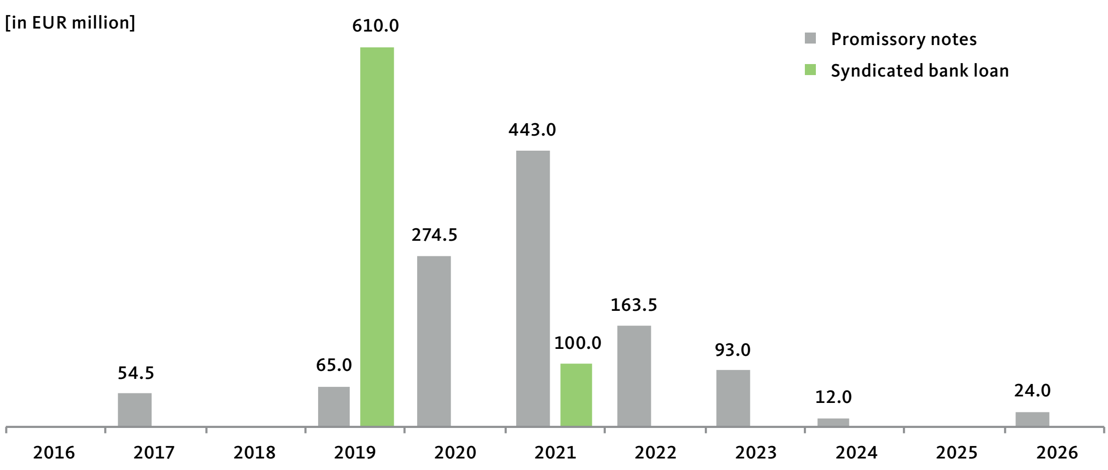
The strategic decisions taken last year have resulted in new challenges for us in the field of financing, particularly as decisions had in some cases already been taken in relation to the acquisitions and equity participations at the end of 2015/2016, although some of them were still open. In addition, we also aimed to take optimum advantage of the currently low interest rate climate to secure long-term refinancing for the company. We have once again succeeded with this balancing act – in close co-operation based on principles of mutual trust with our partner banks and the capital markets.

Accordingly, in the first quarter of 2016, we raised external funds totalling up to 1.7 billion euros. To finance the transactions – all shares of the Media Broadcast Group, approximately 25 per cent of EXARING AG and also approximately 25 per cent of Sunrise Communications Group AG – and for refinancing the corporate bond which fell due upon final maturity in April 2016, we used a borrower's note loan and a syndicated bank loan: We successfully placed the borrower's note loan of 560.0 million euros at the end of February 2016 with domestic and international institutional investors – in a total of five tranches with maturities of between five and ten years and with an average interest rate over these maturities of 1.12 per cent per annum. The syndicated bank loan has a total volume of 1.14 billion euros, and allows freenet AG to draw funds for possible further acquisitions and current operations in three different tranches. The purpose of the first two tranches is to provide bridge financing for any such additional purchases: An initial tranche, with a variable interest rate, with a maturity of twelve plus six months and an initial margin of 0.8 per cent, and the second tranche with a three-year maturity, variable interest rate and an initial margin of 2.1 per cent. The third tranche with a volume of 100.0 million euros is also provided with a variable interest rate – with an initial margin of 1.8 per cent and designed specifically as a revolving credit facility.

This means that freenet AG has not only obtained virtually complete and sustainable refinancing in the current low interest rate climate – for average financing rates of less than 2 per cent per annum we have thus also established an excellent position for further strategic activities in the course of the next few months and years!

Joachim Preisig,
Chief Financial Officer, freenet AG

## Financing and maturity structure of freenet AG (as of January 2017)



# “Digitising 4.0 is our next step!”

The history of our Group is one of permanent challenges and constant innovation over the past successful 25 years. This begins with our original brands mobilcom and debitel at the pioneering time of mobile communications at the beginning of the 1990s: At that time for instance, there was no billing software for this new market. We therefore had to develop such software ourselves, and have expanded it continuously in line with our growth into the extremely modern IT systems for increasingly diverse applications and customer groups.

Our capacities have also experienced corresponding growth: When freenet was originally established, we only had to manage a fraction of the locations and data. Today, our IT team manages approximately 700 micro-locations and handles more data per hour than in a whole day in the past; and following the integration of Media Broadcast and EXARING, the fully utilised capacity of our three datacentres will be one hundred times that applicable in the initial years following our initial establishment.

Our next challenges will be to connect private and business customers to our internal systems: Third parties should be able to use them externally so that, for instance, they will be able to develop their own apps on the basis of our clouds for managing their mobile communication contracts. In addition, we intend and will have to further digitise our business processes. The aim is to constantly offer our customers services and we also aim to offer our employees optimum working conditions. For instance with regard to digitising our human resources: When recruiting new staff, the employees in the Personnel department will no longer need a long time to process and forward hard-copy forms, and instead they will be able to decide and complete such decisions within a single day in a fully digitised manner. The aim is not to prepare the ground for the much-discussed robots. On the contrary, the aim is to enable them to devote their valuable time to their new colleagues.

In this way, we have underlined our excellent positioning as one of the best-digitised companies in Germany. And at the same time, we will retain our special pioneering spirit which has remained unchanged over 25 successful years. These aspects are mutually beneficial: Without change, there is no tradition, no survival!

Stephan Esch,
Chief Technical Officer, freenet AG

# "We bring full-HD-TV easily and inexpensively to your home!"

**Wolfgang Breuer on…**

… the history and current situation of Media Broadcast: Our company is able to look back on decades of successful co-operation with the broadcasting companies. This is because, before privatisation of the federal companies, we were the radio element at Deutsche Bundespost and were still owned by Deutsche Telekom until 2008. In our sector, staff fluctuation levels have always been comparatively low – and there have been correspondingly close personal networks and long-standing business relations. And this is still true today! And today, we are still in the fortunate position of having long-term contracts with the public sector and major private stations of Germany. This means that most of the revenues of the next few years are assured – with very little downside risk, but with major upside potential with freenet TV.

… the potential market for DVB-T2: Although the TV stations never really advertised DVB-T as the predecessor of DVB-T2, they have so far been able to sign up a total of approximately 7 million viewers in Germany; of this number, approximately 3 million have been using this standard as the sole source of their TV reception at home – without any alternative source in their home.

… the success potential for freenet TV: When DVB-T is shut down at the end of March 2017, these customers will have to respond if they do not wish to be confronted with a blank screen. And they will not find any product on the market which provides such excellent quality and, at 5.75 euros per month without a minimum contract period, with such favourable conditions as those available with freenet TV; cable TV is generally twice as expensive. In addition, the installation of freenet TV is extremely simple and customer-friendly: No engineer is required for connecting the equipment, and you also do not need a new satellite dish on your roof. If at all, you only require a corresponding low-cost receiver from the shop or electronic store if the TV at home is not already fully HD-capable – that is all that is required. We are thus in an extremely comfortable competition situation – and are therefore also very optimistic for freenet TV.

Wolfgang Breuer is Chief Executive Officer of Media Broadcast GmbH in Cologne. Until 2011, the electrical engineer was employed in senior management positions at Deutsche Telekom AG, Romtelecom, Comstar-UTS Russia and recently as Director of T-Mobile Croatia.

## Brief portrait: Media Broadcast in facts and figures

- 750 national and international customers – in addition to the public sector and private stations in Germany, also radio and TV production companies, international radio organisations, event managers, telecommunications providers and companies in all sectors with audio-visual content for addressing customers/employees
- More than 350 DVB-T stations, 110 DAB stations, 1,675 VHF stations
- Approx. 500 m² datacentre space for hosting media and telecommunication applications
- Nation-wide service throughout the whole of Germany

# “We maintain and repair TV and radio transmitters!”

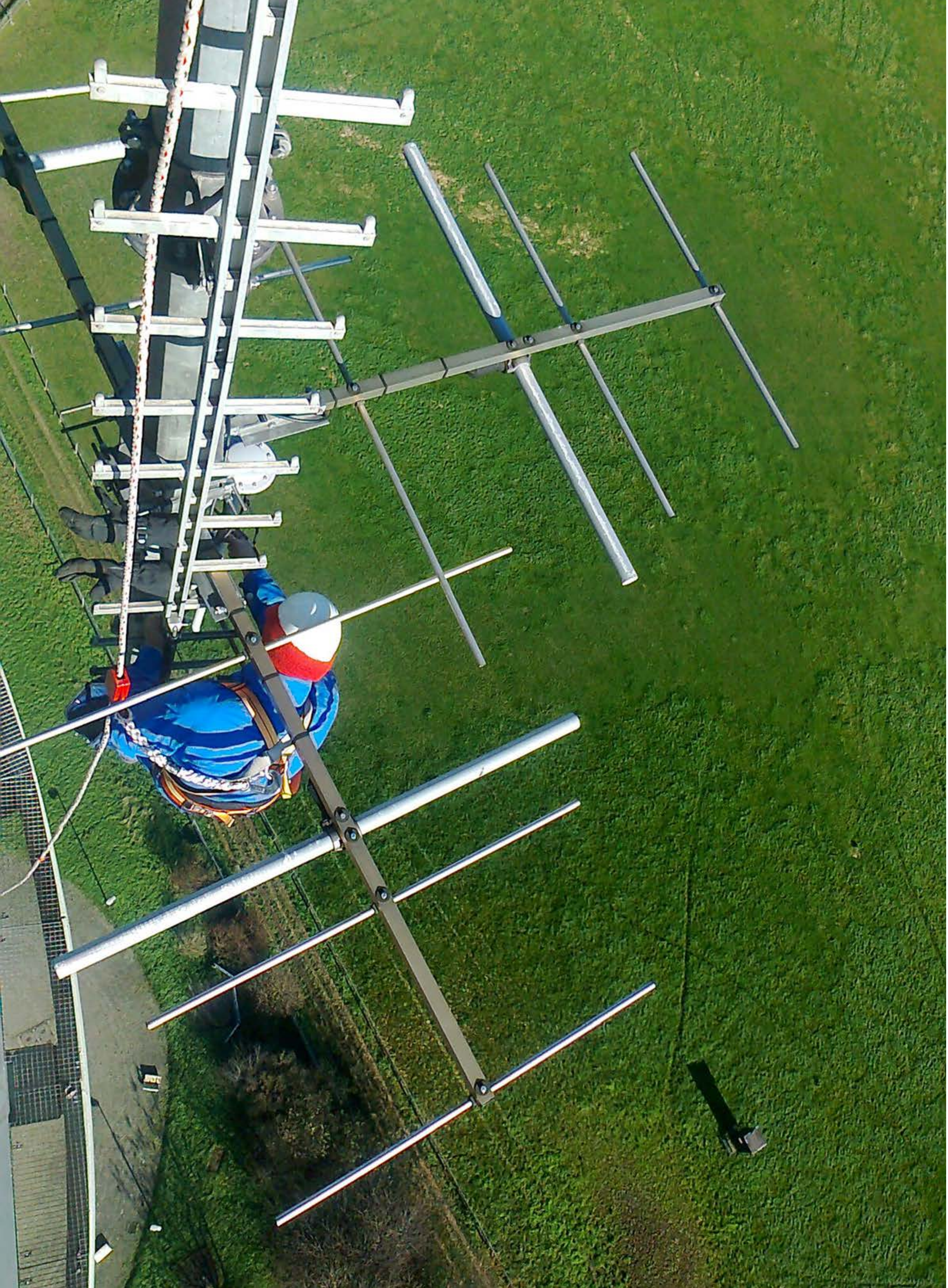
**Wilhelm Trella about…**

… his job: Our service activities cover the entire technical equipment of Media Broadcast with approximately 260 employees. Maintenance and repair of the antennae on radio towers and masts pose genuine challenges for our operation service teams each comprising eight to ten employees: A main inspection is mandatory every six years, and minor annual inspections are also necessary. The members of the team therefore regularly have to climb the towers and masts, on average every two weeks, and with teams comprising at least three members for safety reasons – where possible not in the winter. I have been an amateur mountaineer since I was a child, and I am therefore generally given responsibility for the “monster towers”, i.e. radio towers and masts which are several hundred metres high, such as the Alex in Berlin and the Colonius in Cologne.

… the special difficulties: When maintenance and repair work is being carried out, the stations have to shut down the affected transmitter: Because of the viewers and advertising revenues, they prefer to do this in the middle of the night and only for a few hours. This makes our work all the more difficult: We initially sit for many hours in our car – on the way to our work locations which are spread throughout the whole of Germany. This is generally followed by top sporting performance under time pressure and against our bio-rhythm: If the towers and masts do not have a lift, or if any such lifts are defective, we sometimes have to climb several hundred metres inside the towers and masts. In a stuffy atmosphere, with safety equipment weighing several kilos on our body and with additionally approximately 25 kilos of equipment – ropes, torque wrenches and screwdrivers, hammers, cameras, lamps, measuring equipment. Dripping in sweat, we then go out onto the platforms to inspect the antennae – sometimes in heavy rain, snow or frost, where ladders and locking slides are covered in ice. Even in the summer, we generally encounter strong or even stormy winds, so that it is virtually impossible to talk to each other. And there is also the risk of suddenly occurring thunderstorms.

… unpleasant events: In the Uckermark for instance, a jet fighter had evidently used our mast as a target – with us right at the top: He initially flew towards us in low-level flight and then pulled up the jet almost vertically along the mast only a few metres away from us – with a jet of fire and ear-splitting noise such as that heard during the start of a rocket or an explosion. The mast swayed backwards and forwards for several minutes, and we thought it would fall over, taking us with it!

Wilhelm Trella had his first climbing job 28 years ago, still as an employee of Deutsche Telekom at that time; the photos on the desk of the mountaineering tours of the graduate civil engineer had come to the attention of his colleagues responsible for tower and mast operations which were not particularly popular among engineers. Today, he is Professional of Tower Check, region North/West of Media Broadcast.

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# "We broadcast sport and the world live into the TV!"

**Josef Rade about...**

... his broadcasting van: Media Broadcast has a total of nine broadcasting vans which are almost permanently deployed for hundreds of national and international customers; three of these vans permit HD-live broadcasts, including mine, which I also helped to design. The van is absolutely autonomous, right through to having its own generator for supplying electricity, and contains the latest equipment worth approximately 1.5 million euros: A simple HD camera alone costs 50,000 euros, the lens, stand and monitor together cost a further 44,000 euros. Inside the van, there are three workplaces for video, production and audio direction – which I however frequently operate on my own if the particular customer wishes to save costs.

... his jobs: My van is almost my second home: I handle approximately one hundred live broadcasts or recordings every year, covering mainly Western Germany, the Netherlands, Belgium as well as Northern France, and on average spend two days on each job. Every year, this is equivalent to approximately 70,000 kilometres on the road. We broadcast a lot of sport, in particular Bundesliga football, the Champions League and Europa League, horse racing for the betting offices, athletics; there are also all types of TV shows and programmes for the public sector and private stations, for instance reporting on the US elections – as well as royal weddings such as that of Felipe VI. and Letizia of Spain.

... his longest journey: The Football World Cup 2010 in South Africa, where I had to drive seemingly endless distances between the venues – with the legendary victory of our team against England in Durban and the final involving Holland against Spain, these were two absolute highlights of the World Cup.

... the most critical moments: For instance the Ski-Jumping World Championships 2002 in Harrachov in the Sudeten Mountains in the Czech Republic, where Sven Hannawald won a gold medal. There was a severe storm which lasted for several days and which buffeted the broadcasting van like a ship in heavy seas and almost tore off the satellite antenna. Then there was a situation in 2006 in Poznań/Poland: We had been engaged by the BBC on the occasion of the fairy tale summer and were due to broadcast images among our neighbours on the occasion when Germany played against Poland. We were subject to massive attacks by Polish hooligans, who almost took apart the entire van – until finally the police arrived. And finally in 2010, the final "Wetten, dass...?" of Thomas Gottschalk, when Samuel Koch injured himself so severely when attempting to jump over a moving vehicle.

... and the most moving events of his professional career: There have been several: For instance also in Poland on the occasion of the funeral of Pope John Paul II; the handshake of Bill Clinton when he was awarded the Karlspreis in Aachen; then the meetings with Helmut Schmidt – for instance on the occasion of the World Economic Summit in Bonn, when he came to us and personally ensured that we were given plenty to eat and drink in view of endless waiting times. Or the thanks of Helmut Kohl on the occasion of the funeral of his wife Hannelore, who I had broadcast on several occasions personally in her vacation on the banks of Wolfgangsee. However, the most moving occasion was when Elton John sang his song "Good bye England's Rose" on the occasion of the funeral of Lady Diana in Westminster Abbey: I will never forget this moment my entire life!

Josef Rade has now been working with Media Broadcast and its predecessors as an engineer for approximately 40 years. He drives one of the high-performance broadcasting vans of the company, covering mainly Western Germany, the Netherlands, Belgium and Northern France, as well as major international events.

# "We are opening up new TV dimensions with waipu.tv!"

**Christoph Bellmer about…**

**… different TV behaviour of the YouTube generation:** "Who watches TV nowadays?" is what I frequently hear from young people. And indeed, they generally no longer spend a lot of time in front of the "first screen" i.e. the traditional TV at home at the beginning of a favourite programme; instead, they stream their own individual programme onto their smartphone or tablet – namely the "second screen", as TV people say. They do so whenever and wherever they want, with pauses and repeats in line with their own personal schedule, from the catch-up services of the stations, from Netflix, amazon Prime, maxdome or other providers. For the YouTube generation, the smartphone is the focal point of life – and the second screen has long since become their first screen.

**… the fascination of waipu.tv:** With waipu.tv, we combine the best of two worlds: The smartphone becomes an intelligent TV remote control unit and via Chromecast or Amazon Fire the user streams his own specific programme onto the TV screen. When surfing the various channels, he draws the images with a simple wipe onto the TV – which in particular as a large screen still provides the optimum viewing experience; IPTV accordingly consistently combines the trend of present-day use options with the traditional TV as the projection surface. In addition, I can view the latest episode of my favourite series – for instance CSI:NY – and have an extremely flexible recording function.

**… the fibre-optic cable of EXARING:** When building our own fibre-optic network covering approximately 12,000 kilometres in Germany, we enjoyed the "blessing of late arrival": Unlike our competitors, we did not have to integrate existing and outdated technologies, and instead we were able to implement our own ideas in the design. In this way, we not only have one of the most powerful networks in Europe but also probably the only network of this dimension in the world which serves only this single purpose: namely the highest speed optimum transmission of motion pictures.

**… the location Germany:** We not only operate the highly modern fibre-optic network; due to considerations of copyright, we also maintain individual memory for each individual customer for the programme which he has selected – in a system which has been optimised for this requirement. In addition, software development for IPTV is based in Germany; the crucial factors in this respect are the proximity to the developers and the very high quality of the product.

Christoph Bellmer has been a shareholder and Chief Executive Officer of EXARING AG since 2013. He has many years of experience in managing companies in the technology and media fields; he was accordingly responsible

- as CEO since 2006 for the satellite platform arena with the Bundesliga games,
- between 2006 - 2009 as COO for operations of the cable network operator Unity Media,
- since 2010 in the ProSiebenSat.1 group as CEO for maxdome and New TV.

## Brief portrait: EXARING AG in facts and figures

- Fibre-optic network infrastructure of 12,000 kilometres in Germany, exclusively for the transmission of motion pictures
- 20 per cent metropolitan area, 80 per cent backbone
- Hundreds of coupling points with DSL and cable networks possible
- Capacity for approximately 100 million parallel HD streams
- Ultra-HD/8k delivery
- Low-latency architecture
- 23 million German households within reach at the product start


HUAWEI
Technik-Tools
Hören
Technik-Tools


freenet TV
Zubehör
Schützen
Hier
testen!

# "We are presenting innovative TV worlds, digital lifestyle and mobile communications products!"

**Sebastian Neumeier about…**

… his job as branch manager: I enjoy working with and for people. At mobilcom-debitel, I appreciate the very pleasant and free working atmosphere, the flat hierarchies as well as the extensive freedom for designing the relevant procedures – also in my shop. Of course there are objectives, but we to a large extent determine the route to these objectives ourselves. Performance is recognised and rewarded – I am now 28 years old, and I'm already a manager in a store which is running very well.

… his service philosophy: In principle, I treat customers in the same way as I would like to be treated as a customer myself. This comprises a wide range of small aspects but also very important services – welcoming and taking leave of customers with a handshake, ensuring that the customer's smartphone is quickly recharged free-of-charge while receiving advice right through to processing which is as complete as possible when the customer decides to buy a more complex product – for instance for a change of contract for mobile communications, electricity or now TV. I am also permanently inspired by good service aspects in other sectors; in this way, we gain many loyal customers – of whom many also specifically ask for their favourite advisor.

… the new shop concept of mobilcom-debitel: Products related to digital lifestyle and innovative TV are becoming more and more important for our customers. This is reflected in the new store concept with three areas which we have now implemented on the Karlsplatz in Munich and which means that the buying process is a genuine experience: To the right of the entrance, there is the "digital lifestyle wall", which invites the customer to try out the products and be inspired – from the smartphone and audio products right through to seasonal products. Opposite the entrance, there is the "campaign wall" with digital displays concerning the current offers and campaigns. And to the left, there is the "commercial wall", which presents a wide selection of products – ranging from the smartphone right through to accessories. A four metre consultation desk forms the centre of the shop – also in the figurative sense: We focus on the customer and the personal discussion with him.

… the new TV products: They are presented prominently in the shop and are extremely well received by the customers: waipu.tv which started at the end of September 2016 has enjoyed a particularly good reception among our young customers, who have a high affinity with the smartphone and streaming – it is developing into a genuine trump in our hand. And we are also optimistic for freenet TV once the old DVB-T standard is disconnected at the end of March 2017 and millions of existing customers will be virtually compelled to react.

At 28 years of age, Sebastian Neumeier manages the first redesigned digital lifestyle shop of mobilcom-debitel. Following the refurbishment in November 2016, an innovative store concept with a new design was implemented in the heavily frequented store on the Karlsplatz in Munich; it focusses to an even greater extent than before on shopping as an experience, inspiration and the customer, and combines traditional product offerings relating to mobile communications with the new innovative solutions.

# SUPERVISORY BOARD REPORT

Dear Ladies and Gentlemen,

Below, the Supervisory Board reports on its activities in the financial year 2016.

## Supervision and advice in continuous dialogue with the Executive Board

In the financial year 2016, as in the previous years, the Supervisory Board diligently performed the monitoring and advisory duties incumbent upon it under the law and the articles of association. As well as numerous issues that were discussed and decided upon at the Supervisory Board's meetings, the plenum's deliberations in the first half of 2016 were focused primarily on:

- The acquisition of the Media Broadcast Group and a holding in Sunrise Communications Group AG,
- the auditing of and making of resolutions for the annual financial statements as at 31 December 2015 and
- the preparations for the Annual General Meeting on 12 May 2016.

In the second half of the year, the Supervisory Board then concerned itself primarily with:

- the outsourcing of customer support activities of mobilcom-debitel GmbH and other group companies as well as
- financing considerations for the Group.

The Supervisory Board continuously advised, supported and supervised the Executive Board in its management duties and regularly advised it in connection with its decisions pertaining to the management of the company. The Executive Board included the Supervisory Board at an early stage in all of its decisions of a fundamental nature relating to the company's management and reported regularly and extensively in written and oral form about the business performance, corporate planning, strategic development and situation of the company. In connection with this, the Executive Board provided the Supervisory Board with reports and documents, both without having to be asked and when requested on the occasion of Supervisory Board discussions. In addition, the Executive Board provided extensive explanations of its activities in the plenum and at meetings of the Supervisory Board's committees.

In particular, the Supervisory Board held detailed discussions with the Executive Board about divergences in the business performance compared to the plans and targets, and examined these with the help of the documents that it had received. In addition, the Executive Board continued with the company's strategic alignment – with its concentration on the Mobile Communications segment and simultaneous restructuring as a digital lifestyle provider, as well as its expansion of the business areas to include the TV segment – in close consultation with the Supervisory Board. All of the commercial transactions with significance for the company were discussed in detail on the basis of the Executive Board's reports. Likewise on the basis of the Executive Board's reports, the Supervisory Board made resolutions after examining the subject matter in question, as and when required. Outside of the meetings, too, the Executive Board kept the Supervisory Board members informed about current business developments.

*Dr Hartmut Schenk, Chairman of the Supervisory Board*

Furthermore, the chairman of the Supervisory Board held regular discussions with the Executive Board on the company's strategy, planning, business development, risk situation and management as well as compliance and informed itself about current topics and events.

The propriety, expediency and efficiency of the Executive Board's management were unobjectionable.

In the financial year 2016, the Supervisory Board held three meetings requiring personal attendance as well as three telephone meetings. A further meeting requiring personal attendance planned for the first half of 2016 was cancelled, and no further day set for this planned meeting requiring personal attendance in view of the number of telephone meetings. The presence at the Supervisory Board meetings in the year under review was again exemplary: With the exception of one meeting, which was attended by eleven of the twelve Supervisory Board members, the meetings of the Supervisory Board were always attended by all twelve members. Accordingly, no member of the Supervisory Board participated in just half of the meetings or fewer. In 2016, the meetings of the committees were always attended by all members.

Table 1: **Individualised disclosure of attendants of the Supervisory Board members at Supervisory Board and committee meetings**

| Name of the Supervisory Board member | Attendance at Supervisory Board and Committee meetings | Percentage of Attendance (%) |
|---|---:|---:|
| Dr Hartmut Schenk (Chairman) | 10/10 | 100 |
| Claudia Anderleit | 9/9 | 100 |
| Sabine Christiansen | 7/7 | 100 |
| Birgit Geffke | 9/9 | 100 |
| Thorsten Kraemer | 9/9 | 100 |
| Knut Mackeprang | 6/6 | 100 |
| Ronny Minak | 10/10 | 100 |
| Michael Stephan | 10/10 | 100 |
| Prof Dr Helmut Thoma | 6/6 | 100 |
| Gesine Thomas | 5/6 | 83 |
| Marc Tüngler | 11/11 | 100 |
| Robert Weidinger | 10/10 | 100 |

No circumstances that might constitute conflicts of interest involving Executive or Supervisory Board members which must be disclosed to the Supervisory Board and about which the Annual General Meeting must be informed were disclosed to the Supervisory Board.

# Supervisory Board meetings

Regular topics for discussion in the plenum were
- current business developments,
- the market and competitive situation and
- the financial position and results of operations as well as the financing situation of the company.

In the telephone meeting of 15 February 2016, the Executive Board provided information concerning the status of negotiations regarding the acquisition of the Media Broadcast Group as well as the acquisition of shares in Sunrise Communications Group AG. The Supervisory Board was involved in detail with both acquisitions. The financing of both acquisitions and refinancing of the expired corporate bond also formed a considerable part of the plenary discussions and the resolutions which were adopted. In addition, following the preparatory work and at the recommendation of the personnel committee, the Supervisory Board also adopted a resolution regarding clarifying regulations concerning the impact of acquisitions on the variable remuneration of the members of the Executive Board.

On 1 March 2016, the Supervisory Board continued deliberations by telephone regarding the acquisition of shares in Sunrise Communications Group AG and the related financing, and granted its approval for this purpose.

In the meeting requiring personal attendance on 22 March 2016, the main subject matter of the audit and discussion was the annual and consolidated financial statements as at 31 December 2015. The findings of the annual financial statements audit were discussed together with representatives of the auditor, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft. After completing its own audit, the Supervisory Board raised no objections to the auditors' audit findings and followed the audit committee's recommendation by approving the annual and consolidated financial statements. The annual financial statements were thereby adopted. Another central point brought up at this meeting were the agenda for the Annual General Meeting on 12 May 2016 and the corresponding proposed resolutions from the Supervisory Board to the Annual General Meeting. At this meeting, the Supervisory Board also passed a resolution on the target agreements with the members of the Executive Board for the year 2016. The Supervisory Board also adjusted its rules of procedure and the rules of procedure of the Executive Board in order to specify in detail the responsibilities of the audit committee and in order to transfer to it the responsibility for non-audit services of the auditor.

On 12 August 2016, the members of the Supervisory Board consulted jointly by telephone with the Supervisory Board of mobilcom-debitel GmbH regarding the outsourcing of Customer Service of mobilcom-debitel GmbH. Following extensive discussions, the Supervisory Board approved the sale and transfer of Customer Service at the locations in Erfurt and Büdelsdorf to Capita Customer Services (Germany) GmbH.

In its next meeting requiring personal presence on 22 September 2016, the Supervisory Board considered the product planning of EXARING and Media Broadcast. In the context of the current situation on the financial markets, the Supervisory Board also deliberated on the refinancing of the company and approved the issuing of a borrower's note loan and other financing instruments.

At its meeting requiring personal attendance on 8 December 2016, the Supervisory Board discussed the plans submitted by the Executive Board for the financial year 2017 of which it consensually took note afterwards. The main subject of the meeting were further considerations concerning the strategic positioning of the Group with regard to an equity participation in Sunrise Communications Group AG. The Supervisory Board also passed a resolution on the submission of the annual declaration of compliance with the German Corporate Governance Code. And finally, it made changes to the rules of procedure applicable for the Executive Board and the Supervisory Board which had become necessary as a result of the Market Abuse Directive coming into force.

After the financial year 2016 had come to an end, a plenum meeting was held on 21 March 2017, mainly for the purpose of discussing the annual and consolidated financial statements as at 31 December 2016. The details concerning this matter are the subject of the separate section "Audit of the annual and consolidated financial statements for the financial year 2016" in this report. A further topic was the agenda for the 2017 Annual General Meeting, including the resolutions proposed to the Annual General Meeting by the Supervisory Board.

## The work of the Supervisory Board's committees

In order to perform its duties efficiently, the Supervisory Board has set up a steering committee and four other committees. The general duties, the working method and the composition of the individual committees are described in greater detail in the corporate management statement.

## Steering committee

The steering committee was not convened in 2016.

# Personnel committee

In 2016, the members of the personnel committee got together for three meetings, two of which were telephone conferences at its meetings, the committee dealt with questions regarding the impact of acquisitions and the variable remuneration for Executive Board members. It also investigated the system governing insurance contracts concluded by the company regarding the Executive Board's retirement benefits, and the extent to which it falls into line with the agreements concluded. And finally, the committee established whether and to what extent the parameters for the variable remuneration of the Executive Board members for 2015 were reached, set new parameters for the target agreements for the financial year 2016 and proposed these to the Supervisory Board for a resolution.

# Audit committee

In four meetings requiring personal attendance, the committee concerned itself regularly with the current audit focal points and discussed them with the auditors. The committee's members dealt intensively with the annual report, the six-month report and the quarterly reports. One highly significant topic in the committee in the first six months of 2016 was the dividend recommendation, which the committee members discussed in depth with the Chief Financial Officer. The committee obtained reports directly from the managers responsible in Compliance and Internal Audit as well as reports regarding risk management and fraud management. The committee also concerned itself with the process of approving non-audit services provided by the auditor in accordance with the requirements of the Auditor Reform Act. For this purpose, it defined a catalogue of generally approved non-audit services.

The main emphasis of the audit committee's work was to guide and support the auditing of the annual financial statements. For this purpose,

- the committee obtained the statement of independence of the auditor,
- the committee monitored the auditor's independence and the implementation of the audit assignment,
- the committee determined the focal points of the financial statements audit and
- the committee prepared the Supervisory Board's resolutions on the annual and consolidated financial statements, the proposal for the appropriation of profits and the agreements with the auditor.

# Mediation committee

As in the previous years, the mediation committee did not have to be convened in 2016.

# Nomination committee

The nomination committee held one meeting requiring personal attendance in 2016, and started with the preparations for the election of new and reelection of existing shareholder representatives in the Supervisory Board due to take place at the Annual General Meeting on 1 June 2017.

# Annual and consolidated financial statements for the financial year 2016

The annual financial statements prepared by the Executive Board in accordance with the rules of the German Commercial Code (HGB) for the financial year from 1 January 2016 to 31 December 2016 and the freenet AG management report were audited by PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, Frankfurt. The audit assignment had been awarded by the chairman of the audit committee in accordance with the resolution passed by the Annual General Meeting on 12 May 2016. The auditor awarded an unqualified audit opinion. The consolidated financial statements of freenet AG as at 31 December 2016 were prepared in accordance with section 315a HGB on the basis of the international accounting standards IFRS. The auditor granted these consolidated financial statements and the Group management report an unqualified audit opinion.

The auditor's report of the auditor, PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft, has been signed by Dr Andreas Focke in his capacity as the responsible auditor. Dr Andreas Focke has been responsible for auditing the company and the Group since PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft was appointed as auditor for the financial year 2014.

The audit was reported on and discussed in the audit committee on 1 March 2017 and at the Supervisory Board meeting on 21 March 2017. The auditors participated in the discussion of the annual and consolidated financial statements in both committees. They reported on the most significant results of the audits and were at the disposal of the audit committee and the Supervisory Board for supplementary questions and information. As a result of its own final audit of the annual and consolidated financial statements, the management report and the Group management report, the Supervisory Board raised no objections and approved the result of the audit conducted by the auditor.

The Supervisory Board followed the audit committee's recommendation and approved the annual and consolidated financial statements at its meeting on 21 March 2017. The annual financial statements are thereby adopted. At its meeting on 21 March 2017, the Supervisory Board also examined the Executive Board's proposal for the appropriation of the net profits and discussed it with the auditor. Subsequent to this, the Supervisory Board – following the audit committee's recommendation – gave its consent to the Executive Board's proposal.

# Changes on the Executive Board and the Supervisory Board

In the financial year 2016, there were no changes in the composition of the Executive Board and the Supervisory Board.

The Supervisory Board would like to express its thanks and appreciation to the members of the Executive Board as well as to the employees at all of the Group companies for their personal commitment and their good work.

Büdelsdorf, 21 March 2017
For the Supervisory Board

Dr Hartmut Schenk
Chairman of the Supervisory Board

# FREENET AG AND THE CAPITAL MARKETS

## Capital market environment

The stock market made a volatile start to 2016, suffering considerable losses. In the first quarter, the uncertainty regarding the state of the Chinese economy as well as the continuing low prices of oil were the main factors resulting in a negative development on the European financial markets. Despite the expansionary monetary policy of the central banks in the euro zone and the continuing weakness of the euro compared with the US dollar, there was insufficient impetus in Europe to compensate for these negative effects. The markets calmed down from mid-February onwards, and gained slightly in March following the European Central Bank's (ECB) announcement of further monetary policy easing. Thanks to this recovery in the second half of the quarter, the DAX ended the first quarter at 9,966 points, a loss of 7 per cent compared with the beginning of the year. The TecDAX index also reported a negative performance in the first quarter, declining by 11 per cent to 1,626 points.

At the beginning of the second quarter, the stock markets posted a positive performance, mainly as a result of the recovery in the oil price, improved economic indicators in China as well as improved US labour market data. Up to the Brexit vote on 23 June 2016, the stock markets moved sideways in conjunction with severe fluctuations. Finance- and export-oriented stocks in particular fell sharply following the surprising result of the referendum. This was reflected in the performance of the DAX which, at the end of the first half, closed 10 per cent down compared with the beginning of the year. Similar losses were also reported for the benchmark index which is relevant for the freenet Group: The TecDAX gave up 13 per cent in the first half of the year.

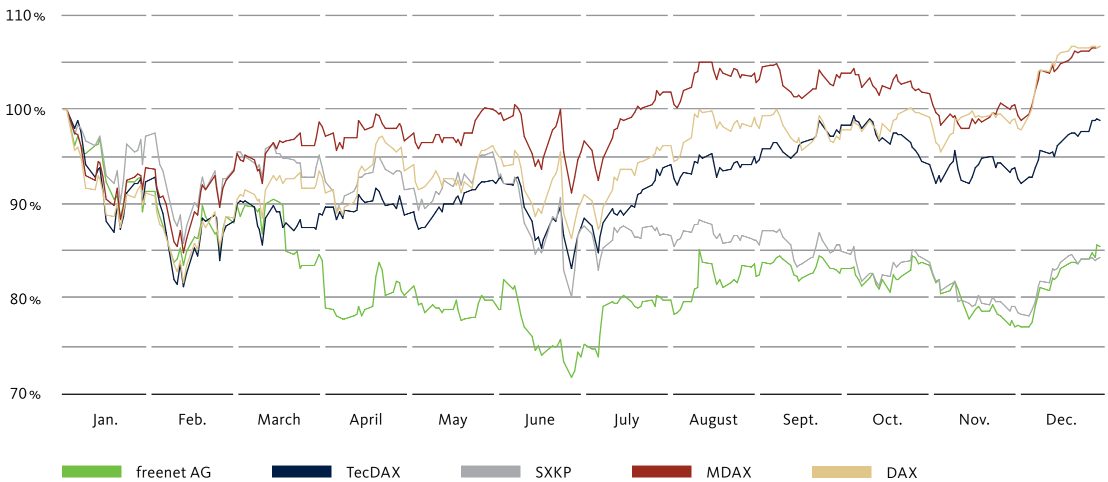
Following the weak performance since the beginning of the year, the international markets started to advance in the course of the summer months. Weakening uncertainty regarding the possible negative impact of the Brexit vote, robust economic data from the USA and more optimistic economic prospects for China supported the turnaround. Accordingly, the DAX was able to reduce its losses to -2 per cent by the end of the third quarter. The TecDAX also fell by 2 per cent during the nine-month period.

Despite the considerable turmoil experienced at the beginning of the year, the overall record for 2016 was reasonable. The surprising election of Donald J. Trump as the US president resulted only briefly in lower prices on the stock markets. In addition, at the beginning of December, the ECB extended its programme of spending billions on buying government bonds and other securities until the end of 2017. The German DAX reported a gain of 7 per cent over the twelve-month period, and this was also the case for the MDAX. The technology stock index TecDAX closed with a slightly negative performance of -1 per cent.

# The freenet share

Following a period of gains which were considerably above average in the years 2013 to 2015, the shares of freenet AG made a negative start to the new year in a weak market climate. The low point of the past 12 months was reached on 27 June at 22.35 euros. The shares subsequently set off on a positive trend, closing at an end-of-year price of 26.76 euros. Compared with the beginning of the year, the share price fell by approximately 15 per cent. The TecDAX fell by 1 per cent in the same period. On average, approximately 475 thousand freenet shares were traded every day in 2016 on the electronic trading platform Xetra, compared with approximately 506 thousand in 2015. Regarding the trading volume via the platforms of Deutsche Börse AG, there was a slight decline to 54 per cent of the total trading volume last year (previous year: 59 per cent), whereas the volume traded via alternative markets ("dark pools") accounted for approximately 46 per cent (previous year: 41 per cent).

Figure 1: **Performance of the freenet share in 2016 (indexed; 100 = Xetra closing price on 31 December 2015)**




Whereas the freenet share price ended the financial year 2015 positively, it moved essentially in line with the overall market in the course of the first quarter of 2016. In the first three months of the last financial year, the share price declined by 16 per cent. Whereas the closing price at the end of 2015 amounted to 31.32 euros, it amounted to 26.29 euros at the end of the first quarter. The freenet shares posted their lowest daily closing price in the first quarter on 23 March (26.00 euros). The benchmark index TecDAX also reported a weak start to the year in line with the international markets. The technology index fell by 11 per cent in the course of the first quarter; the European telecommunications stock index SXKP fell by approximately 6 per cent. The average daily trading volume of freenet shares on Xetra amounted to approximately 519 thousand in the first three months of 2016, compared with 375 thousand in the previous quarter. The dark-pool content increased slightly in the first quarter by 1 per cent, to approximately 46 per cent of the overall trading volume.

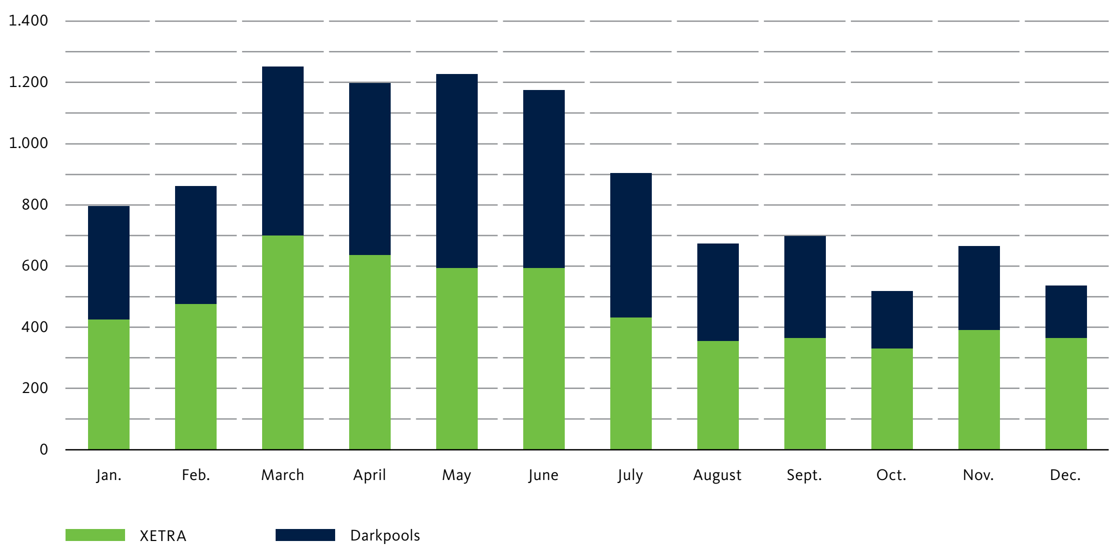
At the beginning of the second quarter, the stock markets reported a positive performance, and freenet shares also posted initial gains. On 1 April, the opening price of freenet shares amounted to 24.69 euros, and the highest price in the second quarter of 2016 was seen on 20 April at 26.20 euros. Following the Brexit vote on 24 June, the world-wide indices tumbled at the end of the first half. freenet shares followed the considerable downward trend on the European stock markets, falling to a year's low of 22.35 euros on 27 June, before ending the second quarter three trading days later with a price of 23.08 euros. On the other hand, trading with freenet shares recovered somewhat in this period. On average, approximately 594 thousand shares were bought and sold every market day, compared with approximately 595 thousand in the previous year. The volume traded via dark pools increased in the second quarter to 50 per cent of the overall trading volume.

Whereas freenet AG shares reported losses in the first half of 2016, they recovered significantly in the third quarter of 2016. Starting from a six-month closing price of 23.08 euros, the shares fell to their low in the third quarter on 6 July at 23.07 euros. On 11 August, they posted a quarterly high of 26.64 euros. Overall, freenet shares in the third quarter rose by approximately 11 per cent to 26.03 euros. Accordingly, during this period, the shares outperformed the TecDAX (+13 per cent) and considerably outperformed the SXKP index (which declined by -3 per cent). The average daily trading volume of freenet shares on Xetra amounted to 383 thousand, and was accordingly lower than the figure for the corresponding previous-year period of approximately 453 thousand. The proportion of the aggregate traded volume accounted for by darkpools fell again slightly against the previous quarter by 1 per cent and came to 49 per cent.

The fourth quarter was again affected by uncertainty on the capital market. Nevertheless, the price of freenet shares increased by approximately 3 per cent from 26.03 euros at the beginning of October to 26.76 euros at the end of the year. The average daily volumes in the fourth quarter amounted to approximately 356 thousand, and were thus slightly lower than the corresponding previous-year figure (375 thousand). The dark-pool content amounted to 37 per cent in the final quarter, and was significantly lower than the level reported for the three previous quarters.

Overall, the market capitalisation of freenet AG declined from approximately 4.0 billion euros to approximately 3.4 billion euros in the period from January to December 2016. According to the index system of Deutsche Börse, the shares accordingly occupied fourth position in the TecDAX ranking, in line with the corresponding previous-year figure. Also in terms of market turnover, freenet confirmed its previous-year placing in fifth position.

Figure 2: **Average daily trading volume of the freenet share in 2016 in thousands**




# Shareholder structure at freenet AG

freenet AG's share capital totals 128,061,016 euros and is divided into 128,061,016 registered no-par value shares. Each share represents 1.00 euros of the share capital.

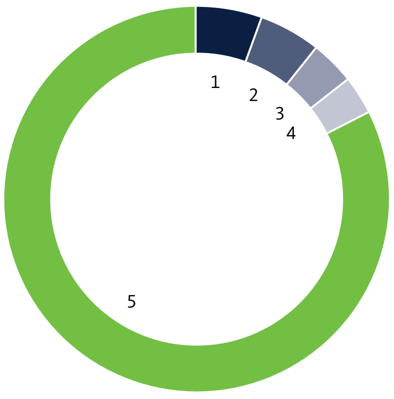
# Voting rights disclosures

According to the voting rights disclosures received pursuant to Section 21 of the German Securities Trading Act (WpHG), freenet AG's shareholder structure changed as follows during the financial year 2016:

- In February, Flossbach von Storch AG (Germany) informed us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 8 February amounted to 3.025 per cent (3,873,898 voting rights).
- In February, Allianz Global Investors Fund (Luxembourg) informed us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 20 April amounted to 3.07 per cent (3,936,052 voting rights).
- In February, Flossbach von Storch SICAV (Luxembourg) notified us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 22 February amounted to 3.06 per cent (3,927,881 voting rights).
- In February, BNP Paribas Asset Management S.A.S. (France) informed us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 5 February amounted to 3.01 per cent (3,850,077 voting rights).
- In March, Capital Income Builder (USA) informed us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 11 March amounted to 2.93 per cent (3,751,148 voting rights).
- Flossbach von Storch AG (Germany) notified us in March of the acquisition of shares with voting rights by the special funds managed by the subsidiary Flossbach von Storch SICAV. This revealed that its share of the voting rights in freenet AG on 21 March amounted to 4.997 per cent (6,398,624 voting rights).
- BNP Paribas Asset Management S.A.S. (France) notified us in March that its share of voting rights fell below the 3-per cent threshold. This revealed that its share of the voting rights in freenet AG on 22 March amounted to 2.985 per cent (3,822,430 voting rights).
- In March, Deutsche Asset Management Investment GmbH (Deutschland) notified us that its holding had fallen below the 5 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 23 March amounted to 4.89 per cent (6,261,015 voting rights).
- Flossbach von Storch AG (Germany) notified us in March of the acquisition of shares with voting rights by the special funds managed by the subsidiary Flossbach von Storch SICAV, and also notified us that the share in voting rights had exceeded the 5 per cent threshold. This revealed that its share of the voting rights in freenet AG on 23 March amounted to 5.55 per cent (7,111,663 voting rights).
- In May, Deutsche Asset Management Investment GmbH (Deutschland) notified us that its holding had fallen below the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 10 May amounted to 2.65 per cent (3,392,465 voting rights).
- In May, Flossbach von Storch SICAV (Luxembourg) notified us that it had exceeded the 5 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 10 May amounted to 5.23 per cent (6,701,755 voting rights).
- In June, BlackRock Inc. (USA) notified us that its holding had fallen below the 3 per cent reporting threshold. On 17 June, its share of the voting rights in freenet AG amounted to 2.98 per cent (3,811,336 voting rights).
- In September, Deutsche Asset Management Investment GmbH (Deutschland) notified us that it had exceeded the 3 per cent reporting threshold. This revealed that its share of the voting rights in freenet AG on 9 September amounted to 3.05 per cent (3,901,949 voting rights).

The shareholder structure at the end of 2016 was therefore as follows:

Figure 3: **Shareholder structure of freenet AG on 31 December 2016**




| | | |
|---|---|---|
| 1 | **5.55 %** | Flossbach von Storch AG* |
| 2 | **5.16 %** | Allianz Global Investors GmbH* |
| 3 | **3.70 %** | The Capital Group Companies, Inc.* |
| 4 | **3.05 %** | Deutsche Asset & Wealth Investment GmbH* |
| 5 | **82.54 %** | Other shareholders/fee float** |

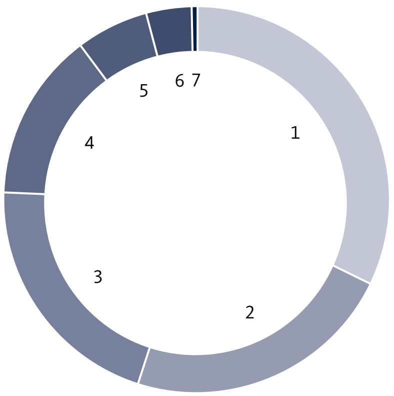
* *incl. attributions according to German Securities Trading Act.*
** *The free float according to Deutsche Börse AG amounts to 89.29%.*

The institutional investors in 2016 again constituted the main group of investors of freenet AG (73 per cent compared with 77 per cent in the previous year). As of the reporting date, the blocks of shares held by institutional investors were again pure financial investments. As was the case in previous years, approximately half of all invested financial institutions adopted a value-oriented investment approach. The percentage of growth-oriented financial investors increased for the first time in two years. The remaining financial investors were index- and/or returns-oriented or pursued specialised investment strategies.

# Geographical distribution

An analysis of the shareholder structure carried out in October 2016 demonstrated that Germany accounts for the largest regional group of investors (55 per cent). At 32 per cent, approximately one third of the shares are held by German institutional investors, and the remaining 23 per cent are held by German private shareholders. The second most significant percentage of our outstanding shares (almost 21 per cent) is held by financial investors from the USA and Canada, followed by the financial investors from the rest of Europe (14 per cent). Institutional investors from Great Britain and Ireland hold around 6 per cent of freenet shares, and a further 4 per cent of the capital is held by private shareholders from the rest of Europe. The financial investors from other countries constitute an absolute minority (0.3 per cent).

Figure 4: **Geographical distribution of the freenet AG shareholder structure on 31 December 2016**




| | | |
|---|---|---|
| 1 | **32.2 %** | German institutional investors |
| 2 | **22.8 %** | German retail investors |
| 3 | **20.7 %** | Financial investors USA and Canada |
| 4 | **14.1 %** | Financial investors rest of Europe |
| 5 | **6.1 %** | Financial investors UK and Ireland |
| 6 | **3.8 %** | Retail investors rest of Europe |
| 7 | **0.3 %** | Financial investors rest of the world |

*Source: Retail investors according to share register; institutional and financial investors according to shareholder identification.*

# Earnings per share

The undiluted/diluted earnings per share of 1.78 euros in the reporting year exceeded the previous years' level (1.73 euros). The basis for calculating the earnings per share is the weighted average of shares outstanding.

Table 2: **Earnings per share**

| In EUR/as indicated | 2016 | 2015 |
|---|---|---|
| **Undiluted earnings per share** | **1.78** | **1.73** |
| **Diluted earnings per share** | **1.78** | **1.73** |
| Weighted average of shares outstanding in thousand (undiluted) | 128,011 | 128,011 |
| Weighted average of shares outstanding in thousand (diluted) | 128,011 | 128,011 |

# Dividend

On 12 May 2016, freenet AG's Annual General Meeting decided to pay a dividend of 1.55 euros per eligible no-par-value share for the financial year 2015, representing a pay-out ratio of 69.7 per cent of free cash flow. The dividend was distributed to the shareholders on 13 May 2016 through Clearstream Banking AG, Frankfurt am Main, by way of the respective custodian banks and financial institutions. The pay-out was made from the tax-specific contribution account in accordance with Section 27 of the German Corporation Tax Act (KStG). This means that the dividend was again paid out without any deduction of capital gains tax and the solidarity surcharge.

The Executive Board and Supervisory Board are standing by their current dividend policy and intend to propose to the Annual General Meeting on 1 June 2017 the payment of a dividend for the 2016 financial year in the amount of 1.60 euros per no-par-value share from the cumulative profit. This corresponds to a payout ratio of around 60 per cent of free cash flow.

# Analysts' recommendations

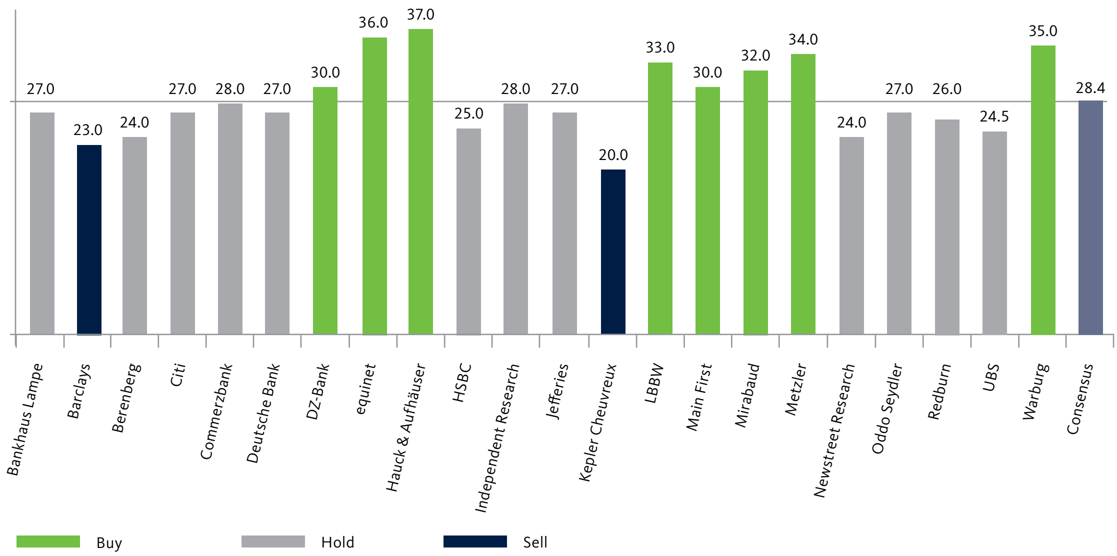
In the financial year 2016, 21 (previous year: 18) internationally operating investment houses regularly published analyses and recommendations regarding the current development of the freenet Group.

The New Street Research Institute included freenet in its coverage in March; Barclays published an initial report in November. Two banks and research houses followed the development of freenet AG in July and August, although they discontinued coverage at the end of the year. Overall, analysts published approximately 110 comments or rather recommendations in the course of the year. This corresponds to an increase of approximately 24 per cent compared with the previous year, with approximately 90 comments and recommendations. The number of published reports increased at ten analysts, whereas eight analyst houses published fewer comments than was the case in 2015. In total, 17 analysts participated in the quarterly consensus estimates last year (previous year: 14 analysts). The median of all publications concerning freenet shares doubled from two and a half comments in 2015 to five comments per broker in the financial year 2016.

Most analyst estimates concerning the freenet shares were positive in the course of the year: Most of the 21 stock analysts issued a hold recommendation for the shares (50 per cent compared with 38 per cent in the previous year), 35 per cent issued a buy recommendation (previous year: 54 per cent) and 15 per cent issued a sell recommendation (previous year: 8 per cent).

Overall, seven investment specialists issued a buy recommendation for freenet shares at the end of 2016, twelve analysts issued a hold recommendation, and two issued a sell recommendation. The analysts' average target price for the share as at 31 December 2016 was 28.39 euros.

Figure 5: **Current recommendations for the freenet share (target prices in euro)**




As per 31 December 2016

# Investor Relations

Last year, our IR work concentrated on the TV and Media segment and thus the equity participation and acquisition of EXARING AG and the Media Broadcast Group announced at the end of 2015/beginning of 2016. In the course of the year, discussions with capital market participants were also dominated by questions following the acquisition of a stake as a major shareholder of Sunrise Communications Group AG. In March, a capital market day was held in this connection for analysts and investors in Frankfurt am Main. Members of the Executive Board also visited the financial locations Frankfurt, London, Paris and New York as well as Switzerland within the framework of roadshows in 2016. Members of the Executive Board and the IR team also presented freenet at numerous European capital market conferences. In this way, interested capital market participants had the opportunity to inform themselves comprehensively and at first-hand about the current development of business and the market as a whole, as well as about freenet AG's strategic orientation. Overall, approximately 300 investor talks were held in the course of the year (previous year: approximately 220 talks). In addition, the IR department maintained regular contact with private and institutional investors, as well as with analysts, by telephone and email.

Last year, the Executive Board and the IR team again placed major emphasis on communicating regularly and transparently with the shareholders and stakeholders of freenet AG and on informing them continuously of the development of the company. In the current financial year, we want to intensify our IR activities further and stabilise our financial communication so that we can continue to ensure a reliable and prompt supply of information in the future.

# Information about the freenet share

| **Master data** | |
|---|---|
| Name | freenet AG NA |
| Type of share | No-par-value share |
| ISIN | DE000A0Z2ZZ5 |
| WKN | A0Z2ZZ |
| Sector | DAXsector Telecommunication, DAXsubsector Wireless Communication |
| Transparency standard | Prime standard |
| Market segment | Regulated market |

| **Information on the security** | |
|---|---|
| Class | Registered shares without par value |
| Index | TecDAX, Midcap Market Index, CDAX, HDAX,<br>STOXX Europe 600 Telecommunications (SXKP),<br>Prime All Share, Technology All Share |
| Share capital | 128,061,016 euros |
| Quantity of shares | 128,061,016 |
| Stock exchanges | Regulated market/Prime Standard: Frankfurt<br>Open Market: Berlin, Hamburg, Stuttgart, Düsseldorf, Hannover, Munich |

| **Trading parameters** | |
|---|---|
| Symbol | FNTN |
| Reuters instrument code | FNTGn.DE |
| Trading model type | Continuous trading |
| Designated sponsors | Oddo Seydler Bank AG, equinet Bank AG |

Further information on the freenet share is available at www.freenet-group.de/investor

# Redemption of the corporate bond from 2011 and the credit facility from 2013

In April 2011, freenet AG placed a five-year corporate bond with a volume of 400.0 million euros and an annual coupon of 7.125 per cent on the capital market as some of the instruments for repaying private equity financing. The bond was repaid in full, including interest, on time on 20 April 2016.

In addition, freenet AG had concluded a credit facility for up to 300.0 million euros in December 2013. This facility was not utilised in 2016; it was terminated by the company in March 2016 and was replaced by a more extensive syndicated bank loan.

# Syndicated bank loan and two borrowers‘ note loans

At the beginning of the reporting period, freenet AG took advantage of the favourable interest rate climate and raised debt totalling up to 1.7 billion euros. The company issued a borrower's note loan and raised a syndicated bank loan for financing the transactions carried out in the first quarter of 2016 and for refinancing the corporate bond which fell due upon final maturity in April 2016.

The borrower's note loan of 560.0 million euros was successfully placed with domestic and international institutional investors at the end of February 2016 – in a total of five tranches with maturities of between five and ten years and with an average rate of 1.12 per cent per annum over these maturities.

The syndicated bank loan has a volume totalling 1.14 billion euros and enables the company to draw funds in three different tranches for possible acquisitions and current operations. The purpose of the first two tranches was to provide bridge financing for the two acquisitions and equity participations carried out at the end of 2015 and in the first quarter of 2016 and also to provide refinancing of the corporate bond which expired in April 2016.

- The first tranche with a volume of 240.0 million euros had a maturity of twelve plus six months; it was issued with variable interest and an initial margin of 0.8 per cent. This tranche was completely redeemed with the issuing of a second borrower's note loan in the autumn of 2016.
- The second tranche has a maturity of 3 years; it comes with variable interest and an initial margin of 2.1 per cent. The second tranche, which provides for max. 800.0 million euros, has been utilised to the extent of 720.0 million euros (nominal) for the acquisition of Sunrise Communications Group AG. The remaining 80.0 million euros line was not utilised. After the issuing of a second borrower's note loan in the autumn of 2016, a total of 110.0 million euros was redeemed, so that this tranche comprised a volume of 610.0 million euros at the end of 2016.
- The third tranche with a volume of 100.0 million euros is also provided with variable interest and an initial margin of 1.8 per cent, and is designed specifically as a revolving credit facility. This means that the funds can be drawn and repaid at any time during the five-year maturity. As at the end of 2016, this tranche was completely unused.

For funding the syndicated bank loan, freenet AG successfully placed a borrower's note loan due to be repaid upon final maturity with five tranches for 350.0 million euros at the end of October 2016. The transaction which was carried out on an arm's-length basis was handled by Bayerische Landesbank, Landesbank Baden-Württemberg, Norddeutsche Landesbank and ING Bank. It was taken up over the entire volume at the lower end of the respective marketing range with an initial average rate of 1.11 per cent p.a. and maturities of between four and eight years. The borrower's note loan comprises two four-year tranches with one fixed coupon and one variable coupon of 1.00 per cent p.a. respectively, a six-year tranche with a fixed coupon of 1.28 per cent p.a., a six-year tranche with a variable coupon of 1.20 per cent p.a. as well as an eight-year tranche with a fixed coupon of 1.68 per cent p.a. With this transaction, freenet was able to confirm its investment grade rating.

# Financial information online

Shareholders and other interested members of the public can find detailed information about the freenet share on our website at www.freenet-group.de/investor-relations.

In addition to company announcements, financial reports and capital market presentations, the information on offer includes Annual General Meeting documentation and a financial calendar. Regardless of the type of terminal being used, the website also features a variety of services and dialogue offers, including a contact and order form and an interactive share analysis tool.

Interested users can also learn more about the company and about freenet AG's press relations at www.freenet-group.de/en.

# GROUP MANAGEMENT REPORT

# CORPORATE PROFILE OF THE GROUP

## The business model

In its core business of mobile communications and mobile Internet, the freenet Group operates as an independent service provider without own network. In order to meet the needs and demands of various customer groups, the company distributes mobile communications tariffs and options throughout Germany, using a subscription agreement and a multi-brand strategy. In addition to its own tariff worlds, the freenet Group also offers the original tariffs of the German mobile network operators Deutsche Telekom, Vodafone and Telefónica Deutschland. The mobile communications services of the freenet Group are marketed under the company's own name and for its own account via a wide range of distribution channels and with a pronounced focus on service. With its high-street model, the freenet Group has established a nation-wide presence in Germany with approximately 590 shops which can be directly managed and which are operated under the premium brands mobilcom-debitel and GRAVIS, as well as numerous additional retail distribution outlets for mobile communications. Among other things, this includes an exclusive distribution right for tariffs in the T-Mobile and Vodafone networks in the approximately 400 electronics stores of Media-Saturn-Deutschland GmbH. The company also uses various online distribution capabilities across all brands.

The product portfolio of the freenet Group comprises mobile tariffs as well as current devices such as smartphones, tablets and notebooks as well as attractive accessories. Ever since the clear competitive positioning of the freenet Group as a digital lifestyle provider in 2013, the company has been continuously expanding its offering to include innovative digital applications relating to home automation and home security, health, data security, entertainment and infotainment. As a result of breaking into the new TV and Media segment, the product portfolio has since 2016 also included two technological versions of high-resolution digital TV.

Mobile communications marketing activities of the freenet Group essentially focus on end customer business with private customers in Germany, an area which is split up into three customer sectors. The contract customers who are acquired predominantly via high-street sales outlets and the no-frills customers generated almost exclusively via online channels jointly comprise the non-financial performance indicator known as customer ownership, which is used as an internal control parameter. There is also a relevant number of prepaid customers.

In the company's view, the key factors for its commercial success are customer development and the average monthly revenue per user in mobile communications as well as the development of digital lifestyle and TV activities.

# Corporate strategy

Of the mobile communications providers operating without their own network, the freenet Group is the leader in the German mobile communications market. It was again able to maintain its leading competitive position as a service provider in the financial year 2016.

In a saturated market with a slightly contracting overall market volume, the company's core business of mobile communications and mobile Internet continue to focus on high-quality contract relations with regard to signing up new customers and also with regard to managing existing customers. The company's strategic focus continues to be on further boosting its customer base in the valuable customer segments of postpaid customers and no-frills (together: customer ownership) as well as the profit-oriented expansion of high-street service-oriented sales. Besides on continuous optimisation of the shops operated under the main brand mobilcom-debitel in respect of location, product and service portfolio and sales support, the further development of the GRAVIS stores as a premium supplier of so-called digital lifestyle products from a variety of manufacturers at the forefront. The resultant cross-selling potential is to be strategically used mainly in customer ownership, for instance by way of the increasing marketing of integrated lifestyle product worlds.

A further key element of the corporate strategy is the expansion of digital lifestyle business focussing on added value by way of continuously optimising and extending the corresponding product and service portfolio. The freenet Group positioned itself at an early stage as a digital lifestyle provider in this market segment, and thus transfers existing skills such as sales strength, service orientation and long-standing experience in subscription business to new markets closely related to its core business.

As a result of breaking into the new TV and Media segment, the company has consistently continued its strategic alignment as an extensive digital lifestyle provider. The reason for breaking into TV business is the need to develop new growth potential and revenue sources in the rapidly expanding motion picture content market within the context of previous marketing successes of video-on-demand and streaming products via partnerships. With the investments in an innovative start-up company and an established digital terrestrial provider in Germany, the freenet Group has secured access to TV infrastructures and has thus established a competitive advantage. On this basis, the company in 2016 launched two very promising TV products on the market which address different customer groups and which permit modern high-resolution digital TV in a new form. In this way, the freenet Group has laid the foundation for a comprehensive and innovative TV experience and simultaneously prepares the way for TV of the next generation. On this basis, the company considers that the new TV and Media segment provides an opportunity for it to establish a further relevant mainstay in addition to its core business of mobile communications.

In the course of the next few years, the freenet Group will continue to evaluate additional strategic areas of operation apart from its pure mobile communications operations and the retailing of mobile communications products in line with precisely defined profitability and investment requirements and taking account of demand patterns and market momentum.

In implementing its strategy, the freenet Group devotes equal attention to the varied requirements and expectations of all interest groups. While the shareholders expect a reasonable and reliable overall return on their invested capital, the company's creditors are mainly concerned not just with an attractive interest rate on borrowed capital that is commensurate with the risks involved, but also with lasting assurance of adequate capacity for debt repayment. The freenet Group's customers are interested in up-to-date services and products with specific additional benefits, plus expert advice. The employees expect a far-sighted management that provides long-term job security with reasonable working conditions. That is why the freenet Group attaches special strategic importance to an open, respectful and appreciative corporate culture in the competition for qualified employees.

# Group structure and acquisitions

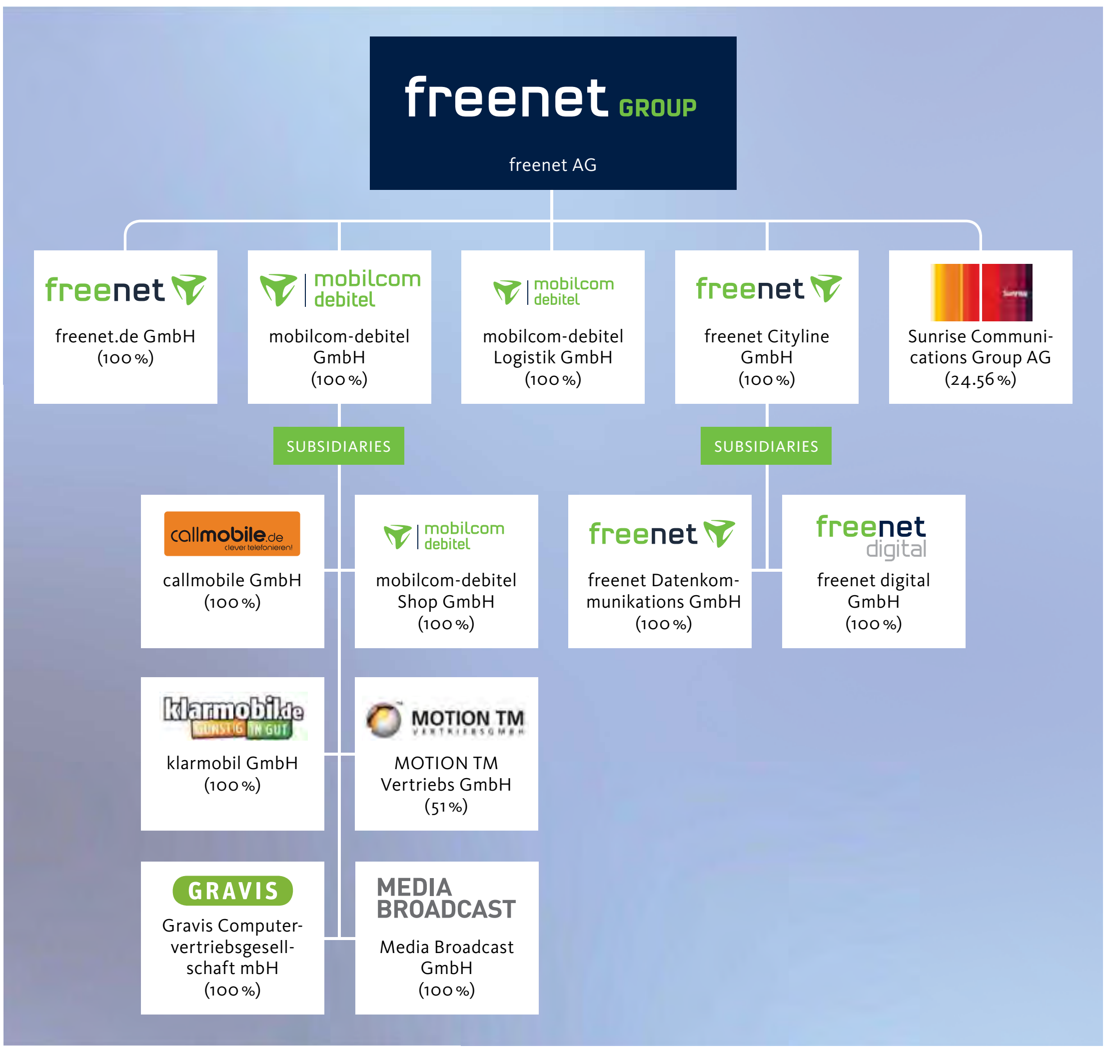
With a view to further developing its digital lifestyle business activities and correspondingly extending its product portfolio for private households, the freenet Group made further acquisitions in the financial year 2016.

In March 2016, the Group completed the acquisition of 100 per cent of shares of the Media Broadcast Group, the sole commercial provider of DVB-T2 and DAB+ in Germany. The Media Broadcast Group consists of a holding company as well as the major operating company Media Broadcast GmbH with its headquarters in Cologne, and also other subsidiaries and equity participations. The acquisition, in conjunction with the holding in EXARING AG acquired in the previous year, represents an important addition to the strategic development of freenet AG towards becoming the leading digital lifestyle provider in Germany. The entry into the new field of terrestrial and internet-based TV („IPTV“) is providing the company with the opportunity of achieving further diversification in the digital lifestyle field and of developing new growth potential and sources of revenue.

In the first half of 2016, freenet AG also acquired a 24.56 per cent stake in Sunrise Communications Group AG ("Sunrise") with registered offices in Zurich. As the largest private telecommunications provider in Switzerland, Sunrise accounts for more than 3 million customers in the fields of mobile communications, landline, internet and digital TV.

The main Group companies as of 31 December 2016, measured in terms of their contribution to the main financial performance indicators of the Group are set out in the following:

Figure 6: **Material Group companies of freenet AG as at 31 December 2016**



# Segment specific disclosures

The organisation and management of freenet AG are not conducted along the lines of customer sectors or geographical territories. In line with internal management of freenet AG, a distinction was made between the "Mobile Communications" and "Other/Holding" segments up to the first quarter of 2016.

Since the equity participation in EXARING AG and the acquisition of the Media Broadcast Group, the freenet Group has been operating in the new TV and Media growth segment. This means that, since the second quarter of 2016, there has been a changed reporting structure, according to which EXARING AG (with retroactive effect as of 1 January 2016) as well as the Media Broadcast Group (with retroactive effect as of 18 March 2016) are reported separately as "TV and Media" segment.

The "TV and Media" segment comprises all services relating to IPTV (mainly to end users), the planning, project management and establishment, operation, service and the marketing of broadcast-related solutions for business clients in the radio and media sector as well as DVB-T2 services to end users.

The "Mobile Communications" segment comprises not only the original mobile communications activities but also the still recent growth area of internet-based mobile applications (digital lifestyle products). For the purpose of assessing the net assets, financial position and results of operations of freenet AG, the "Other/Holding" segment is only of minor importance.

# Management system

To implement the operative and strategic objectives of the Group, a standardised management system is used at the highest Group level and in the freenet Group's individual companies, where it draws on financial and non-financial control parameters. Taking account of the ongoing expansion of our digital lifestyle activities and in view of the planned development of the new area of TV operations in connection with the acquisition of the Media Broadcast Group and our equity participation in EXARING AG, we constantly monitor the composition of all internal control parameters. If a corresponding need for adjustment is identified, we may adjust our internal control parameters. The following financial and non-financial performance indicators are relevant for management purposes.

# Financial performance indicators

In order to measure the short-, medium- and long-term success of our strategic alignment and its operational implementation, we currently use the following financial performance indicators:

- Revenue,
- EBITDA,
- Free cash flow,
- Postpaid ARPU.

The financial performance indicator free cash flow is not used for management purposes in relation to specific segments; instead, it is used exclusively in relation to the Group. Postpaid ARPU is used as a management parameter only in the Mobile Communications segment.

A schedule of the so called non-GAAP measures (also known as "alternative performance measures") EBITDA and free cash flow is set out in the section "Definition of alternative performance measures" at the end of this chapter.

## Revenue

The freenet Group's traditional field of business is determined by products and services covering all aspects of mobile communications and mobile internet. The revenue generated here is shown in the Mobile Communications segment. The German mobile communications market is saturated and characterised by a small number of providers. As a result, there has long been a situation of predatory competition on the market with increasing pressure on prices, which tends to lead to a decrease in service revenue in the market.

In this environment, the Executive Board's strategy is geared towards the generation of additional sources of income to complement the Mobile Communications segment. This applies in particular to the digital lifestyle business activities and the TV business which is currently being developed. In addition to EBITDA, the success of activities in digital lifestyle as well as in TV and Media will be reflected primarily in the company's future revenue trend.

## EBITDA

In general, EBITDA is therefore regarded as the operational viability of a company both in the assessment of corporate developments over a number of periods and when comparing companies in the same market sector with one another.

While the mobile communications network operators post high capital expenditures every year for the expansion and maintenance of their networks, the freenet Group restricted itself to a comparatively low level of annual investment within the scope of its corporate planning and management. As EBITDA focuses on the operating efficiency ascertained by the accounting process, however, this performance indicator makes comparability possible even independently of the structurally conditioned different capital costs in the respective business models. Accordingly, EBITDA is also used for valuation purposes within the framework of corporate acquisitions and disposals.

With regard to a precise definition of EBITDA, please refer to the section "Definition of alternative performance measures" in this chapter.

## Free cash flow

Free cash flow as a group-wide liquidity-oriented key performance indicator is an important supplement to the results-oriented assessment of a company's performance.

The free cash flow is of equal importance for the procurement of equity and borrowed capital. While the Annual General Meeting decides on the amount of the dividend distribution as part of freenet AG's retained profits in accordance with the German Commercial Code, the dividend payout ratio is disclosed in relation to the free cash flow. This creates a direct link to the cash inflow that was actually generated in the respective period. To improve shareholder orientation, the Executive Board has determined a distribution corridor of currently 50 to 75 per cent of free cash flow within the framework of its corporate management.

At the same time, the free cash flow is significant for providers of outside capital because it contains all of a company's operational payment obligations and as such is a benchmark for potential interest and redemption payments.

For a precise definition of free cash flow, please refer to the section "Definition of alternative performance measures" in this chapter.

## Postpaid ARPU

We define postpaid-ARPU as the monthly average revenue in the business segment Mobile Communications, generated by the distribution of 24-month contracts. ARPU generally depicts the willingness of customers to pay appropriate monthly remuneration for the respective mobile communications services. Therefore, the revenue generated via the "mobile option" from the sale of mobile phones and/or smartphones does not flow into ARPU. Changes in the market and competitive situation in Germany have a significant impact on the development of ARPU.

# Non-financial performance indicator

Given the company's strategic position as a digital lifestyle provider, both the financial performance indicators and customer ownership as a key non-financial performance indicator are used for control purposes in the freenet Group.

## Customer ownership

The measurement of customer ownership, consisting of the valuable postpaid and no-frills sectors in Mobile Communications, is particularly significant for medium- and long-term corporate management. The control parameter exclusively relevant in the Mobile Communications segment, is in combination with the average revenue generated per user (ARPU) a significant pillar of business.

In addition, customer ownership makes it possible to address customers in an individualised way with a view to cross-selling and up-selling. The media disruptions that result from multichannel selling are being overcome thanks to a variety of marketing measures. The successful launch of the click-and-collect system, in other words the payment and for collection of online orders in mobilcom-debitel shops must likewise be seen against this background.

In the interests of its strategic commercial alignment as a digital lifestyle provider, freenet focuses on high-quality customer relations when acquiring new customers and managing existing customers.



# Other control parameters

For managing the Group, freenet AG uses further control parameters in addition to the main financial and non-financial performance indicators. These parameters are used as an additional measure for the development of the freenet Group, and mainly cover the following areas:

- Product brands, new products,
- Partnerships,
- Sales activities,
- Research and development,
- Employees.

## Product brands, new products

The freenet Group is increasingly also addressing the digital lifestyle growth market. In mobile communications/mobile internet, the company puts its faith in a multi-brand strategy so that it can serve all sectors of this market in a target-group-specific manner. Under its main brand mobilcom-debitel, the company markets the postpaid and prepaid tariffs for all German mobile communications networks, focusing on high-calibre contractual relationships. The major strengths of the brand include demand-oriented and independent customer advice relating to mobile communication products and services as well as maximum proximity to customers. This is achieved primarily by the approximately 590 shops operating under the main mobilcom-debitel brand, the company's presence in approximately 400 major electronics stores and also via a wide range of further high-street distribution outlets and retail partners.

In addition, the discount brands of the Group – klarmobil, freenetmobile, callmobile and debitel light – focus on the no-frills segment: customers in this segment are interested primarily in inexpensive tariffs and to a lesser extent in subsidised terminals or special services; the discount tariffs are sold largely via company-own online trading platforms.

For many years, mobile data services have been one of the areas of telecommunication which have been achieving the strongest growth. Accordingly, for the freenet Group, these services constitute a focal point of marketing the company's portfolio of products and services. In this context, in 2016, the company further enhanced its existing portfolio of flatrates and data tariffs for smartphones and other devices within the framework of numerous limited seasonal and special promotions; these generally comprised additional services or discounts in the individual tariffs.

The discount subsidiary klarmobil has also upgraded its tariff family: It restructured its mostly temporary offerings to form a fixed Allnet tariff group – with increased data volumes and higher surfing speeds subject to equivalent conditions. New and existing customers are able to choose between three new tariff options: For 14.85 euros per month during the minimum two-year contract duration, the Allnet Flat 1000 offered a flatrate for calls to all German networks, an internet flat rate with 1 GB data volume and max. 21 mbps in downstream. For 17.85 euros per month, the Allnet Flat 2000 doubled the internet flat rate to 2 GB high-speed data volume with max. 42 mbps in downstream, and otherwise offers the same benefits. And finally, the Allnet Flat 4000 cost 22.85 euros per month, offering in addition to the flat rate for calls a flat rate for text messages to all German networks as well as a high-speed data volume of 4 GB with also max. 42 mbps.

At the same time, in its digital lifestyle division, freenet Group has been continuously expanding its range of innovative products and applications via the mobilcom-debitel and GRAVIS brands. In the first quarter of 2016, the company started further operations (e-health) with a range of products: Under the concept of "SmartCare" digital technologies for disease prevention as well as personal and mental well-being are now available via www.md.de/smartcare. E-health complements the existing portfolio of digital lifestyle products in the fields of entertainment, data security, home automation and security.

In the course of the third quarter and following intensive preparatory work, freenet AG started the first IPTV product in the TV and Media segment in co-operation with EXARING AG: namely waipu.tv. waipu.tv is available in two options: as an advanced version with ten hours memory for 4.99 euros per month and as a perfect version with 50 hours memory for 14.99 euros per month – both versions can be terminated monthly and come with a free test month. At the same time, two data centres necessary for waipu.tv commenced operations in Karlsruhe and Leipzig. The corresponding waipu.tv app has been available free-of-charge in Google Play Store and also in the Apple App Store since 30 September 2016; with the aid of this app, and on the basis of the EXARING fibre-optic infrastructure, brilliant video and audio quality can be transferred quickly and easily to the user's smartphone and from there to the user's existing TVs at home. Right from the very beginning, the product supplied by waipu.tv provided more than 50 TV channels on the user's mobile phone and on the TV screen at home via Google Chromecast, and the offering was extended continuously in subsequent months. In time for the Christmas season, mobilcom-debitel also put together a low-cost package with a discounted streaming dongle as well as free use of waipu.tv and maxdome for three months.

In the DVB-T2 HD field of the Media Broadcast Group, pilot operation of the new broadcasting standard started on 31 May 2016 in several major German cities: During the "soft launch", high-resolution TV images of ARD and ZDF as well as the private stations RTL, Sat.1, ProSieben and VOX can be received via antenna in the respective core regions.

At the end of the "soft launch" on 29 March 2017, freenet TV will start as a new brand and commercial provider following previous intensive advertising: From this date onwards, up to 20 private stations will be available in full-HD quality – although the services will still be encrypted. For this purpose, in addition to an internal or external antenna, a CI+ module of freenet TV for upgrading new DVB-T2 HD-capable TVs is required; and a small set-top box will be required for all other TVs. Up to the end of June 2017, viewers will initially be able to use the full-HD offering of the private stations free-of-charge in a three-month starting phase, followed by a monthly payment of 5.75 euros.

The tremendous interest of consumers and TV stations in the new standard is among other things shown in the 14 product licences for set-top boxes issued already by the end of August 2016 to the manufacturers who currently offer the devices required for freenet TV.

## Partnerships

In September 2016, mobilcom-debitel and SH Telekommunikation Deutschland GmbH entered into a long-term strategic exclusive partnership for digital lifestyle sales. Within the framework of the co-operation, SH Telekommunikation will in future market the digital lifestyle services of the freenet subsidiary – particularly in the fields of entertainment and online games, fitness, e-books and security. The Cologne-based company operates the home shopping station Sparhandy TV in addition to the end user portal Sparhandy.de, and is also responsible for purchasing, sales and logistics of the mobile communications hardware and cardware of ElectronicPartner and the associated specialist retail partners as well as its own retail partners.

Also in September 2016, the freenet subsidiary klarmobil started a marketing partnership with THW Kiel, which has been a flagship of German Handball for many years. In future, klarmobil will be present at all Bundesliga and DHB cup games in the home arena of the Kiel-based club – including an advertising space in the TV-relevant area on the floor of the stadium next to the two goals and with spots on the video cube on the roof of the stadium. There are also plans for klarmobil to offer its own smartphone tariff exclusively for fans of the German Handball record champion, three-time winner of the Champions League, European Club Champion and World Cup Champion. The aim is to provide a mutually positive image for both brands with strong links to Schleswig-Holstein.

In 2013, freenet acquired MFE Energie, the leading high-street energy marketer in Germany. The portfolio comprises more than 30 nation-wide and regional energy utilities – including the major brands such as E.ON, EnBW, E WIE EINFACH, eprimo and Yello as well as various municipal operations and well-known eco-providers such as Lichtblick, primastrom and Sauber Energie. With its first-class products and services, the company is the first service-certified energy distributor in Germany to address private as well as business customers.

In the third quarter of 2016, MFE Energie GmbH changed its name to freenet Energy GmbH; the new name is intended to strengthen the image of the company and also to unlock further synergies in connection with other brands of the freenet Group. freenet Energy is able to access the sales ability and expertise of approximately 600 of the Group's own shops, more than 5,600 retailers and 400 major electronics stores as partners; the freenet subsidiary is thus one of the most powerful energy distributors in the retail market and is one of the marketers of energy products generating the highest revenues at the point of sale in Germany. The products are also available via a wide-range continuously expanding online distribution network as well as in direct sales with various partners.

In the course of the following months, the company expanded its utility portfolio to include further attractive co-operation partners:

- The start was made at the end of September 2016 with MAINGAU Energie, now a nation-wide electricity and gas utility with more than 100 years of experience in the energy sector, with permanently low tariffs and more than 250,000 private and business customers.
- This was followed in mid-October 2016 by the MONTANA Group, which has been operating in the energy field for 55 years. With also approximately 250,000 customers in Germany and Austria and recent annual revenue of more than 550 million euros, this multifaceted provider based in Grünwald/Munich is one of the largest SME energy suppliers in Germany; it specialises in trading with gas and electricity, mineral oil products and renewable energy as well as technical heating-related services.
- The beginning of November 2016 saw the start of a co-operation with the municipal operations of Flensburg, with which freenet Energy additionally strengthens the regional marketing of gas and electricity in Northern Germany.
- And in mid-November 2016, the company also extended its regional energy marketing activities to include the south of Germany by way of a co-operation with erdgas schwaben, thus setting further accents with regard to the marketing of renewable energies. For almost 60 years, this Augsburg-based provider has been supplying climate-friendly gas to the region of Swabia and the neighbouring parts of Upper Bavaria – with an increasing content of domestic biogas, heat and electricity. As a pioneer in the field of biogas, erdgas schwaben is currently the only energy service provider in Germany with three operating biogas installations, thus achieving annual savings of more than 60,000 tons of $CO_2$.

## Sales activities

In the course of the financial year 2016, mobilcom-debitel carried out the preliminary work for introducing a new concept for its nation-wide shops, and opened the first flagship store in Munich at the end of the year. The aim is to impart a more emotional flavour to customer contact at the point of sale in future, and to position itself even more clearly as a digital lifestyle specialist. The natural ambience of wooden furniture, created by a Danish designer in the fashion/lifestyle field, forms a counterpoint to the technology products on offer. The following are examples of major new elements in the shops:

- the DLS power wall with the currently four digital lifestyle issues which are presented: SmartHome, entertainment, smartphone camera and fitness/ health,
- The campaign wall consisting assembled screens, playing the current campaign by means of digital signage to attract strong attention,
- A honeycomb-shaped white wall consisting of square boxes for presenting products in a flexible and modular manner – as in a boutique – and with wooden draws which the customer can open,
- a consultation table in the centre of the store, eight metres long, and with sockets for recharging equipment, at which the customer and sales representatives can sit together and discuss questions relating to products and contracts in a relaxed atmosphere.

## Research and development

As a service provider without its own network infrastructure, freenet AG does not maintain its own research and development department. In view of the rapid technological progress being made in telecommunications and in mobile voice and data services, however, the company concerns itself intensively with current developments in this area. The major objective in this context is to maintain the company's competitive positioning in this dynamic market environment in the long-term. In this context, freenet AG in 2016 addressed the continuously changing market and customer requirements with its own portfolio of products and services relating to mobile communications, mobile Internet and digital lifestyle.

The income statement has not recognised significant costs of research and development in the financial year or in the previous year.

In the digital lifestyle growth market, the freenet Group expanded its product offensive in 2016 to include new offerings; focussing on the existing fields of entertainment, data security and home automation and security as well as the new E-health segment. In the case of some products, the company is involved in the final phase of their development in order to guarantee maximum customer friendliness. At the same time, this also enhances the added value of the company achieved with the relevant products.

In addition, within the framework of IT and strategy projects, the Group also carried out cash-effective investments totalling 18.7 million euros in 2016 (previous year: 11.5 million euros).

## Employees

freenet AG employs a wide range of basic and further training measures to satisfy its demand for specialists and suitably qualified young professionals, and also meets its social responsibility as a major and successful employer.

Once again, freenet AG was very much in demand as an employer in 2016: For instance, 18,958 applications were received in relation to 811 job advertisements. In addition, the company recruited 138 trainees for commercial and technical operations as well as for logistics, and also recruited ten students for studies combining theory and practice to obtain qualifications as a Bachelor of Science of Bachelor of Arts at universities offering studies combining theory and practice.

A further fixed element of the Group-wide training concept is the trainee programme which has been in existence for four years. As part of this programme, the trainees, over a period of twelve months, undergo a wide range of qualification measures and training sessions, attend network symposia in order to get to know other locations, working procedures and colleagues – and are thus given optimum preparation for their position in a predefined area.

freenet AG considers that staff promotion and development in line with the company's specific needs is a further key task. In 2016, the Group therefore carried out a total of 249 qualification measures; 1,050 permanent employees participated in these measures. In addition, an internal team of trainers is responsible for ensuring the specific qualification of the more than 2,000 employees of the shops and customer support.

The Group-wide development programme "freenet entrepreneurs" which started in 2015 provides specific opportunities of qualification and further development to key staff in various areas of the Group: The eight-month programme is intended to strengthen the initiative, commitment and entrepreneurial spirit of the relevant employees and to serve as a platform for experience, reflection and the interchange of information with each other as well as with internal and external experts concerning a wide range of subjects. Issues such as entrepreneurship, leadership, management and disruptive thinking are addressed. The participants are encouraged to shape developments in the company, to implement changes, to act as multipliers within the Group – and their loyalty to freenet AG is accordingly strengthened.

A further key foundation for the future development of the company and the continuous improvement processes was laid in the autumn of 2016: the annual development talks. The aim of these talks is to expand the Group-wide feedback culture – in addition to promote staff qualifications. It is based on the Group-wide competence model. It comprises the competences "co-operating and working together", "developing personal impact", "entrepreneurial thinking and action", "driving change" as well as "living management", and a variety of modules for senior executives and employees.

In 2016, the new senior executive guideline "WIR gehen in Führung" which was initiated in 2015 contributed to additional transparency and internalisation of the management principles, tasks and responsibilities of senior executives. New senior executives in the freenet Group are also welcomed in an onboarding process and are actively supported in the process of orientation in their new function.

# Financial Management

Strategic corporate management is underpinned by focused financial management, with the capital structure and liquidity development as performance indicators. The strategy is implemented by means of a comprehensive treasury management system based on established controlling structures.

The capital structure is managed primarily through financial KPIs consisting of debt ratio, interest cover and the equity ratio.

The following overview shows the key indicators of financial management with their current figures compared with the previous year. For all periodic figures such as EBITDA and net interest income, the relevant period is the previous 12 months (i.e. January to December 2016 and January to December 2015).



Table 3: **Key figures of financial management**

| | 2015 | 2016 | Target |
|---|---|---|---|
| Debt ratio | 1.0 | 1.7 | 1.0 - 2.5 |
| Pro forma debt ratio | 1.0 | 3.2 | 1.0 - 2.5 |
| Interest Cover | 8.4 | 8.0 | > 5 |
| Equity ratio in % | 50.6 | 32.7 | > 50 |

The debt ratio indicates the relationship between financial debt (1,734.2 million euros) less liquid assets (318.2 million euros), less the Sunrise share of market value as of 31 December 2016 (11,051,578 shares multiplied by the closing price of 62.45 euros - source: Bloomberg) and the EBITDA generated within the past 12 months. It amounted to 1.7 as of 31 December 2016 and, as was also the case as of 31 December 2015, was within the strategic range of 1.0 to 2.5. With regard to the determination of the debt ratio, it must be borne in mind that the EBITDA of the last twelve months used for this purpose only included nine and a half months of the activities of the Media Broadcast Group (which featured a strong performance in terms of EBITDA). The debt primarily comprises borrowers' note loans with a total nominal value of 1,129.0 million euros which fall due upon final maturity between 2017 and 2026 as well as a syndicated bank loan (second tranche) with a nominal value of 610.0 million euros which was concluded in March 2016.

The pro-forma debt ratio (financial debt less liquid assets in relation to the EBITDA generated in the last 12 months) is stated as 3.2, and is accordingly higher than the strategic range of 1.0 and 2.5, due to the refinancing in the financial year 2016.

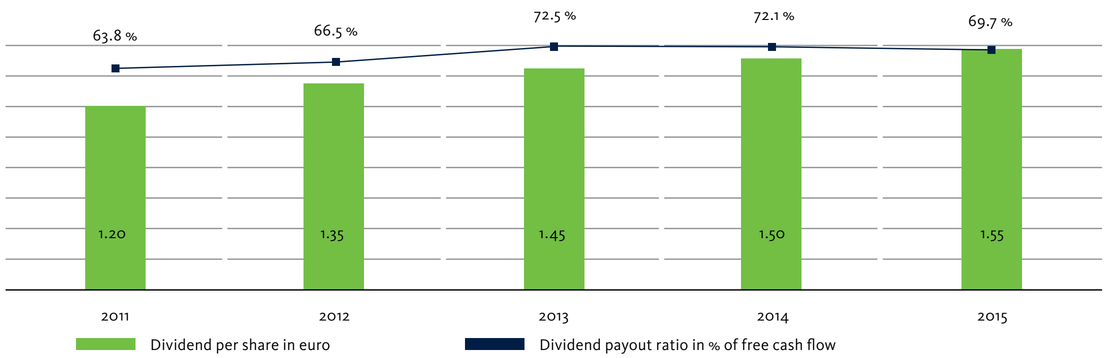
The interest cover (ratio between EBITDA and interest result) of 8.0 is lower compared with the corresponding prior-year figure (8.4), but is still higher than the target of 5.0. This development is mainly attributable to the increase in the interest expense in connection with the compounding of the liabilities relating to a framework rental agreement regarding the purchase price allocation of the Media Broadcast Group.

As of 31 December 2016, the equity ratio was below the target of 50 per cent; this is connected with the refinancing in 2016.

Despite the refinancing in relation to the acquisitions, the Executive Board has not made any changes to its financial strategy and thus continues to be committed to the target.

Concerning the derivation of the input value „Interest cover" we refer to section "Definition of alternative performance measures" in this chapter.

Figure 7: **Dividend policy KPIs**




Pursuant to the dividend policy, adopted by the Executive Board at the beginning of 2013 and endorsed by the Supervisory Board, annual dividend payments are supposed to be in the range of 50 to 75 per cent of free cash flow. By upping this range from the 2013 financial year onwards, the Executive Board is taking into account the interests of value-oriented shareholders who wish to participate to a reasonable extent in the company's free cash flow, while ensuring an optimum capital structure to safeguard the company's long-term value.

Due to the positive business development in 2016, the Executive Board and the Supervisory Board are going to propose to the Annual General Meeting on 1 June 2017 the distribution of a dividend in the amount of 1.60 euros per share from retained earnings for the financial year 2016. This corresponds to a payout ratio of around 60 per cent of free cash flow.



# Definition of alternative performance measures

In order to illustrate the financial position and results of operations of the freenet Group, we use the following alternative performance measures (APMs) which do not form part of the IRFS. Please note that these do not replace historical financial results, assets or liabilities of the company or other performance indicators defined by the company or IFRS parameters, and therefore should not be viewed in isolation and should therefore be considered to be additional information. Despite the fact that management and investors commonly use alternative performance measures for assessing the current operating performance and the company's debt situation, these are only meaningful to a limited extent when used as a sole analysis tool. In addition, despite the fact that they might use similar or even identical designations, the listed APMs are not necessarily equivalent to the APMs used by other companies because of different calculation methods which may be used.

The alternative performance measures used by freenet AG are as follows:

- EBITDA
- EBIT
- Gross profit and gross profit margin
- Net financial debt, pro-forma net financial debt and related debt ratios
- Interest cover
- Free cash flow
- Equity ratio.

Special factors which are used for establishing some alternative performance measures result from the process of integrating and subsequently recognising business which has been acquired.

## Definition and calculation of EBITDA

EBITDA is defined as earnings before interest and taxes, including the earnings elements of the companies included using the equity method (EBIT) excluding depreciation and deferred taxes resulting from the subsequent recognition of companies included using the equity method and including write-downs and impairments.

Since the acquisition of Sunrise, EBITDA has been concretised as follows: As has been the case in the past, only the percentages of results under the item "Results of companies accounted for using the equity method" have been used for the calculation. The amortisations resulting from the subsequent recognition of the shadow purchase price allocation do not affect EBITDA. This means that it was not necessary for the previous-year figures to be adjusted. In this connection, please also refer to note 17.1 of the notes to the consolidated financial statements.

Table 4: **Calculation of EBITDA**

| In EUR `000s | 1.1.2016-31.12.2016 | 1.1.2015-31.12.2015 |
|---|---|---|
| EBIT | 298,822 | 298,775 |
| Depreciation and impairment write-downs | 124,324 | 71,403 |
| Recognition from purchase price allocation | 15,678 | 0 |
| **EBITDA** | **438,824** | **370,178** |

EBITDA is a non-GAAP parameter which management uses for evaluating the business development and operational viability of the company.

Because the company is not able to influence the element of Sunrise results, the Executive Board manages EBITDA without including the elements of Sunrise results. Accordingly, the budget-actual comparison as well as the forecast of the financial performance indicator do not take account of the Sunrise results elements.

If the term "EBITDA" is used elsewhere, it is understood to include the Sunrise results elements.



## Definition and calculation of EBIT

EBIT is defined as the result before interest and taxes on income, including the profit shares of companies accounted for using the equity method.

Table 5: **Calculation of EBIT**

| In EUR `000s | 1.1.2016-31.12.2016 | 1.1.2015-31.12.2015 |
|---|---|---|
| Operating result | 277,803 | 298,604 |
| Share of results of associates accounted for using the equity method | 21,019 | 171 |
| **EBIT** | **298,822** | **298,775** |

## Definition and calculation of gross profit (incl. gross profit margin)

Gross profit is defined as the balance of revenue and cost of materials. The gross profit margin represents the ratio between revenue and cost of materials.

Table 6: **Calculation of gross profit**

| In EUR `000s / as indicated | 1.1.2016-31.12.2016 | 1.1.2015-31.12.2015 |
|---|---|---|
| Revenue | 3,362,407 | 3,117,892 |
| Cost of material | -2,463,670 | -2,327,475 |
| **Gross profit** | **898,737** | **790,417** |
| **Gross profit margin in %** | **26.7** | **25.4** |

## Definition and calculation of net financial debt, pro-forma net financial debt and related debt ratios

Net financial debt is defined as long-term and short-term financial debt, less liquid assets, less the interest of the freenet Group in the market value of Sunrise Communications Group AG as of the reference date. The market value of Sunrise Communications Group AG is calculated by multiplying the closing price of the shares of Sunrise Communications Group AG on the Swiss stock exchange by the number of shares in Sunrise Communications Group AG held by the freenet Group (11,051,578) as of the relevant reference date. The amount is converted from Swiss francs into euros on the basis of Bloomberg data using an official exchange rate at the balance sheet date.

Table 7: **Calculation of net financial debt**

| In EUR `000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Non-current borrowings | 1,673,871 | 218,382 |
| Current borrowings | 60,302 | 420,532 |
| Liquid funds | 318,186 | 269,761 |
| Market value of Sunrise Communications Group AG | 690,171 | 0 |
| **Net debt** | **725,816** | **369,153** |

Pro-forma net financial debt is defined as long-term and short-term financial debt less liquid assets.

Table 8: **Calculation of pro-forma net financial debt**

| In EUR `000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Non-current borrowings | 1,673,871 | 218,382 |
| Current borrowings | 60,302 | 420,532 |
| Liquid funds | 318,186 | 269,761 |
| **Pro forma net debt** | **1,415,987** | **369,153** |

In the previous year, the pro-forma net financial debt was described as “net financial debt”. Accordingly, this is an adjustment of the definition of the indicator “net financial debt” which was carried out as a result of the acquisition of shares in Sunrise (referred to in the following as “Sunrise acquisition”). The Sunrise acquisition was financed entirely by way of raising new financial debt. Accordingly, after the Sunrise acquisition, it would not have made much economic sense to detail the net financial debt without including the interest held in Sunrise. Because the Sunrise acquisition is a new acquisition in the financial year 2016, it was not necessary for any adjustment to be made to the previous-year comparison figure for “net financial debt”.

In general, net financial debt is a non-GAAP parameter which is used by management for managing the financing structure of the Group. It is thus an integral part of Group-wide capital risk management, and is included in the calculation of the debt ratio and pro-forma debt ratio.

The debt ratio is calculated as the ratio between net financial debt and EBITDA generated in the last 12 months. This is also applicable for the pro-forma debt ratio; however, in this case, pro-forma net financial debt is used as the basis for calculating the ratio. The development of the two parameters as well as the target range are detailed in the section “Financial management”.

## Definition and calculation of interest cover

Interest cover is the ratio between EBITDA and interest result in the last 12 months. Interest result is defined as the balance between “interest and similar income” and “interest and similar expenses” in the consolidated income statement.

Table 9: **Calculation of interest result**

| In EUR `000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Interest payable and similar expenses | 55,675 | 44,502 |
| Interest receivable and similar income | -809 | -418 |
| **Interest result** | **54,866** | **44,084** |

The development of this parameter as well as the target range are detailed in the section “Financial management”

## Definition and calculation of free cash flow

Free cash flow is defined as cash flow from operating activities, minus investments in property, plant and equipment and intangible assets, plus proceeds from the disposal of property, plant and equipment and intangible assets.

Table 10: **Calculation of free cash flow**

| In EUR `000s | 1.1.2016-31.12.2016 | 1.1.2015-31.12.2015 |
|---|---|---|
| Cash flow from operating activities | 389,649 | 314,938 |
| Investments in property, plant and equipment and intangible assets | -62,792 | -31,384 |
| Proceeds from the disposal of property, plant and equipment and intangible assets | 14,681 | 981 |
| **Free cash flow** | **341,538** | **284,535** |

Free cash flow is a financial performance indicator of the freenet Group. In addition to the presentation of EBITDA, this parameter is used as an indicator for showing the ability of the Group to generate cash in the long term.

Because the company is not able to influence the amount of the dividend of Sunrise, the executive board determines the free cash flow without including the Sunrise dividend. Accordingly, the budget-actual comparisons as well as the forecast of the financial performance indicator do not take account of the Sunrise results elements.

If the term “free cash flow” is used elsewhere, it is understood to be inclusive of the Sunrise dividend which has been received.

## Definition and calculation of the equity ratio

The equity ratio defines the ratio between equity and the balance sheet total, and is used as an additional measurement for an efficient modulation of corporate financing.

Table 11: **Calculation of the equity ratio**

| In EUR `000s / as indicated | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Shareholders` equity | 1,402,267 | 1,379,035 |
| Balance sheet total | 4,284,759 | 2,724,020 |
| **Equity ratio in %** | **32.7** | **50.6** |

# ECONOMIC REPORT

## Macroeconomic conditions

In the course of 2016, the economic climate deteriorated further as a result of numerous international crises and political uncertainties. In its economic outlook published in October 2016, the International Monetary Fund ("IMF") downgraded its expectations for global economic growth in the whole of 2016 by 0.1 percentage points compared with its April forecast, namely to 3.1 per cent. In its economic outlook published in November, and following a five-year phase of weak global growth, the Organisation for Economic Cooperation and Development ("OECD") continues to predict growth of 2.9 per cent for global growth domestic product for the whole of 2016 (unchanged compared with its September forecast). Both organisations were moderate in their expectations particularly with regard to the expected growth of the advanced economies in view of the fact that it is still impossible to estimate the impact of the British referendum for exiting the European Union held in June 2016 and also in view of the fact that economic growth in the United States of America failed to meet expectations. As a result of these developments, the IMF expects that monetary policy will continue to be expansionary and that the global level of interest rates will continue to be under pressure.

Following a long phase of weakening, the organisations are again predicting slight economic growth in the emerging countries and developing countries in 2016, on the basis of interest rates in the industrialised nations continuing to be low and also on the assumption that commodity prices will strengthen. Particularly with regard to the short-term growth prospects in China, sentiment on the financial markets has recently picked up some in view of the announced political measures designed to encourage growth.

For the euro zone, the IMF and OECD are anticipating economic growth of 1.7 per cent in 2016, a slight increase of 0.1 percentage points compared with the last IMF outlook of July 2016 and 0.2 percentage points compared with the last OECD forecast from September 2016. According to a survey carried out by the financial information service IHS Markit in 19 euro countries, the growth reported for the economic activities in the euro zone at the end of 2016 was stronger than at any time since May 2011. Accordingly, a purchasing manager's index, which is considered to be a comprehensive measure for the economy in the production and service sectors, increased strongly in December 2016 compared with the previous month. The weak euro in particular is considered to have permitted industry and the service sector in Europe to achieve growth. According to the survey, the strongest economic growth has been reported for Spain, closely followed by Germany, whose gross domestic product ("GDP") increased by 1.8 per cent in 2016 compared with the previous year (on a price- and calendar-adjusted basis) according to initial calculations of the Federal Office of Statistics.

Overall, according to information released by the Federal Office of Statistics, the economy in Germany in 2016 was again characterised by sound and constant economic growth. This was due to the increase in private and government consumer spending compared with the previous year and also the increase in construction spending and spending on machinery and equipment. The vigorous domestic demand was benefitting particularly from the rising private household incomes as well as the favourable state of the labour market. On average for 2016, economic output in Germany was driven by a working population of 43.5 million persons whose work is based in Germany; according to the Federal Office of Statistics, this is the highest figure seen since 1991. The positive assessment of the economic situation in Germany is also shared by the Deutsche Bundesbank, which also predicted a sound upswing with GDP growth of 1.8 per cent for the whole of 2016 in its monthly report published in December.

# Telecommunications market 2016

The increasing digitising process is having an impact on the business models of the established telecommunications companies, who are feeling pressure mainly as a result of the changes in user needs. The sector is also facing further challenges in view of the fact that the core market is saturated, with falling growth rates, rising competition and consolidation pressure as well as a rising regulatory intensity. In order to significantly strengthen competitiveness, the focus is on strengthening core business and particularly on establishing positions in alternative growth markets in order to open up new revenue sources. Developments relating to the Internet of things, the general trend towards flatrate tariffs, demand for higher bandwidths as well as the increasing smartphone and mobile data use are playing a role in this respect.

In 2016, the German telecommunications market will probably achieve only slight growth. This is indicated by the "18th Telecommunication Market Analysis Germany 2016" published jointly in October 2016 by the Verband der Anbieter von Telekommunikations- und Mehrwertdiensten (VATM) as well as the consultancy company Dialog Consult. According to this analysis, the total revenue generated by telecommunication services in Germany in 2016 will increase only slightly by 0.8 per cent compared with the previous year, namely to 60.5 billion euros. This development is considered to be due mainly to the revenue generated by landline activities, which in 2016 are estimated to increase by 1.8 per cent compared with the previous year, to 34.1 billion euros. Of this figure, 28.7 billion euros will be attributable to the telecommunication landline operators, representing growth of 1.4 per cent compared with the previous year, and a total of 5.4 billion euros will be attributable to the cable network operators, representing a gain of 3.8 per cent compared with the previous year.

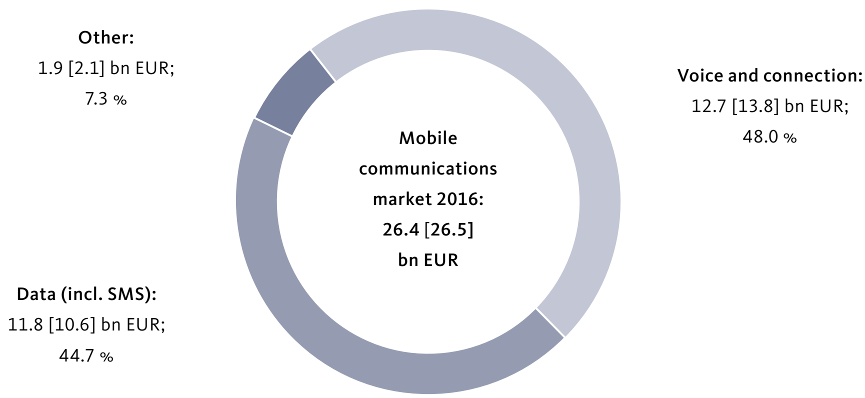
According to VATM and Dialog Consult, the mobile communications submarket declined by 0.1 billion euros compared with 2015 (to 26.4 billion euros) due to various factors, including price reductions, tariff optimisation of customers, declines in roaming revenue and declines in termination charges. Including the mobile providers without own network, the mobile revenue continues to be spread over a total of six market players. Deutsche Telekom is again the market leader with a market share of 30.3 per cent (previous year: 32.7 per cent), followed by Vodafone with a market share of 26.1 per cent (previous year: 27.8 per cent). Telefónica Deutschland occupies third place with a market share of 25.0 per cent (previous year: 22.6 per cent).

With a revenue-related market share of approximately 19 per cent, the network independent providers in 2016 will probably increase their mobile revenue slightly compared with the previous year. freenet AG is the dominant player among the providers without own network, with a market share of 12.1 per cent (unchanged compared with the previous year). It is followed by United Internet and Drillisch with market shares of 3.8 per cent and 2.7 per cent respectively.

According to the Federal Office of Statistics, prices for telecommunication services in Germany continue to decline; however, the trend since 2011 has been weakening. Between 2011 and 2015, there were signs of a slight recovery particularly for the mobile prices. According to the investment house Kepler Cheuvreux, price competition in the German mobile market, which comprises the premium and discount sectors, again weakened in the course of 2016, mainly as a result of price increases of various market players at the bottom end of the price range. At the same time, according to Kepler Cheuvreux, the network operators are maintaining the strategy of monetarising the increasing data use.

According to VATM and Dialog Consult, revenue generated with mobile data services in 2016 will account for approximately 44.7 per cent of the total revenue generated by the mobile network operators in Germany; compared with the previous year, this represents a probable increase of almost five percentage points to 11.8 billion euros. With regard to the development in volumes, data traffic from German mobile networks in 2016 will increase by almost one third to 774 million gigabytes compared with the previous year (previous year: 591 million gigabytes). The average mobile data volume per SIM card an month will probably increase by 22.9 per cent to 510 megabytes. On the other hand, according to VATM and Dialog Consult, voice service activities will continue to decline in significance in 2016.

Figure 8: **Mobile revenues according to groups of services 2016 (estimate)***




** Information in square brackets indicate the corresponding absolute previous year's revenues.*
*Source: Dialog Consult/VATM - 18. TK-Marktanalyse Deutschland 2016.*



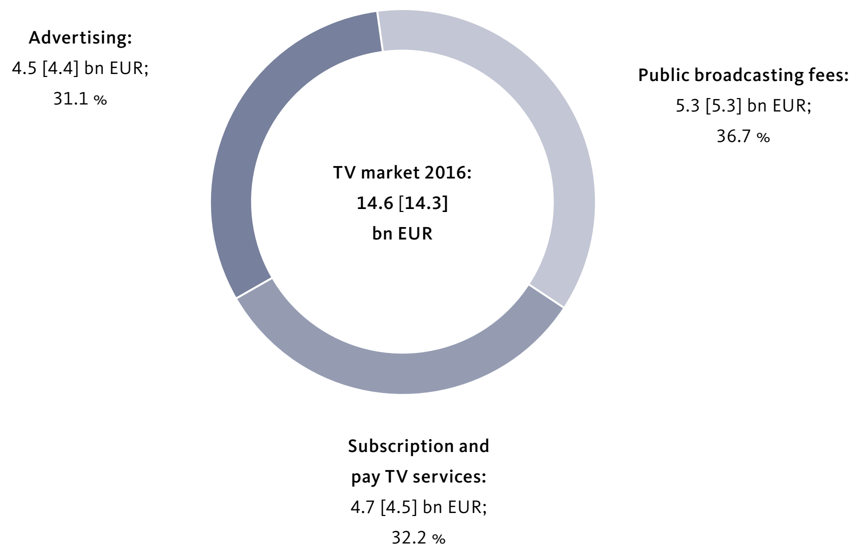
The increase in mobile Internet use is closely related to the increasing significance of the smartphone, which already acts as a multi-function device in daily life and which is increasingly becoming the key control element of the "Internet of things". Survey results of TNS Infratest show that, in 2016, more than three quarters of all 14- to 69-year olds in Germany use the Internet with a smartphone – and this trend is rising. The smartphone can already replace daily tools such as address books, watches and alarm clocks, landline telephones, cameras and video cameras, satnavs, MP3 players and games consoles and TVs. Whereas traditional standard applications such as telephony and text messages are becoming less and less significant, the use of digital lifestyle applications with the smartphone is increasing. The smartphone combines with other every-day devices (usually via an app), such as audio devices, games consoles, wearables and smart TVs.

At the end of 2015, the number of world-wide mobile communication connections amounted to approximately 7.3 billion; at the end of the first quarter of 2016, this figure had risen to approximately 7.4 billion. This is shown by the Ericsson Mobility Report, published in June 2016. According to the Swedish network equipment corporation, annual average growth of approximately five per cent means that this figure will rise further to 9 billion by the year 2021. Between 2015 and 2021, the number of smartphone users world-wide will increase by 3.1 billion to 6.3 billion. For Germany, VATM and Dialog Consult in October were still anticipating 128.1 million issued SIM cards and thus a probable increase of 3.4 million compared with the previous year. According to the Bundesnetzagentur (Federal Network Agency), the number of mobile telecommunication connections amounted to 128.6 million in the third quarter of 2016. Of this figure, according to the Bundesverband Informationswirtschaft, Telekommunikation und neue Medien e.V. ("Bitkom"), a total of 51 million Germans use a smartphone on average for 82 minutes per day in 2016. According to Bitkom, the number of smartphones and phablets sold in Germany will rise by 6.4 per cent from 26.2 million devices in 2015 to 27.9 million devices.

# TV market 2016

The continuous growth of the German TV market will continue in the financial year 2016. According to the auditing and consultancy company Pricewaterhouse-Coopers ("PwC"), the total revenue of the TV sector, comprising advertising revenues, revenues from subscription and pay-TV services as well as revenues from radio charges, will rise from 14.3 billion euros in 2015 to approximately 14.6 billion euros in 2016. Whereas the revenues from radio charges will remain unchanged, the main growth will probably again be achieved in activities with subscription and pay-TV services (+3.5 per cent), followed by a stable increase in advertising revenues (+2.3 per cent).

Figure 9: **Market volume German TV market 2016 (estimate)***




** Information in square brackets indicate the corresponding absolute previous year's revenues.*
*Source: PWC, German Entertainment and Media Outlook 2016-2020.*

The German TV market is increasingly merging with adjacent communication and Internet markets. This development is also reflected in the move away from traditional linear TV to the process of downloading motion picture content from the Internet. The research results of a survey carried out by TNS Infratest, which were published in October 2016 in the digitising report of the media institutions, demonstrate that the traditional linear TV still accounts for most of the motion picture use of all TV viewers in Germany. However, the popularity of video-on-demand ("VOD") services and live-streams, in which media content is offered in real time via streaming, is becoming increasingly popular, particularly among the younger generation.

According to the digitising report, more than 38 million households in Germany had at least one TV device in 2016; this corresponds to approximately 97 per cent of all German households. In addition, the trend towards two or more TV devices per household is continuing: approximately 38 per cent of German TV households currently have two or more TVs. In 2016, this was equivalent to an average of 1.5 TVs per TV household. For 37 per cent of persons who are at least 14 years old, the TV is the most important screen device, followed by smartphone (approximately 28 per cent) and PC or desk top (12 per cent).

With regard to the broadcasting channels for TV which, according to the digitising report, are about to be fully digitised, the market in 2016 was again dominated by satellite (47 per cent of TV households) and cable (46 per cent of TV households). Whereas cable TV has declined by approximately 6 percentage points since 2006, satellite TV has increased by 4.5

percentage points. Digital terrestrial TV ("DVB-T") has remained stable, at 9 per cent of TV households in Germany; it has declined only slightly by 0.2 percentage points during the past 10 years. DVB-T is thus again the third most important broadcasting channel for digital TV in Germany in 2016. There is also the use of DVB-T on desktop PCs and the increasing use of mobile devices for the reception of DVB-T TV, e.g. laptops, smartphones and tablets, which represents a unique selling point of digital terrestrial TV compared with alternative methods of dissemination. In total, approximately 19 per cent of all TV households in Germany used the digital antenna TV DVB-T as the broadcasting solution in 2016; this is equivalent in absolute terms to more than 7.4 million households.

As a result of the change-over to the DVB-T2 HD standard, DVB-T broadcasting will end in all major cities in Germany on 29 March 2017. The main reasons behind the change-over to the successor standard are the reduction of the previous broadcasting frequencies as well as the increasing wish of viewers for high-definition ("HD") content. The new TV broadcasting technology DVB-T2 HD offers high-definition image quality "full-HD" and also has a wider range of programmes, with approximately 40 stations in the major German cities. The DVB-T radio frequencies which are freed up are to be used in future for mobile Internet and thus accelerate the process of expanding broadband in rural areas. In the first phase of DVB-T2 HD, it has been possible for six programmes to be received in selected major German cities since 31 May 2016. Further regions in which the entire range of programmes will be available are to be added in the course of 2017 and 2018. The public sector radio service also plans to convert additional regions to DVB-T2 HD by mid-2019. With the new broadcasting standard, a fee will be payable for receiving private stations via digital antenna TV, probably from the summer of 2017 onwards.

Overall, the reception of high-definition TV images across all broadcasting channels continues to rise in Germany. According to the digitising report, more than half of German TV households in 2016 received programmes in HD, whereby the households which have IPTV report the highest HDTV reception percentage (more than 70 per cent). According to the digitising report, IPTV, with which the Internet connection transports the TV signal, reported the strongest growth of TV broadcasting channels during the past ten years, namely from 0.0 per cent to 6.2 per cent of all German TV households in 2016. The rising trend towards IPTV is also reflected in the number of German households equipped with TVs which are connected to the Internet either directly or via another device ("connected TVs"). In 2016, at least 45 per cent of German TV households had connected at least one TV device to the Internet; this is equivalent to approximately 17.2 million TVs in Germany. This means that the possibility of reception via a connected TV in Germany is roughly in line with the possibility of TV reception via satellite or cable. In particular, smart TVs, which have additional interfaces such as USB, network, WiFi and memory cards as well as HbbTV functionality, are becoming more wide-spread; they are now to be found in more than every fourth German household.

Although traditional linear TV is still the most frequent form of using the TV, use forms such as online motion picture offerings are becoming increasingly important. Particularly in the younger target groups of the 14- to 19-year olds and the 20- to 29-year olds, less than half of motion picture consumption is attributable to the traditional TV. On the contrary, VOD use of 41 per cent and 34 per cent respectively is already roughly in line with the corresponding figures for linear TV use. According to the digitising report, almost 27 million persons who are at least 14 years old used live-stream and video content from the Internet at least once a month in 2016 in Germany; this represents an increase of 10.5 per cent compared with the previous year. According to PwC analyses, the total revenue generated by the digital distribution of video content in Germany will rise from 181 million euros in 2015 to 410 million euros in 2019. According to PwC, the factors of success of the young growth sector are the provision of attractive content with high image quality, high user comfort as well as adequate bandwidth, also for mobile downloading of videos.

# Business performance

The Group can draw a positive conclusion from the financial year 2016: We have succeeded in meeting or exceeding all of the objectives which we set ourselves at the beginning of the financial year 2016 with regard to the main management parameters.

Consolidated EBITDA achieved in 2016 amounted to 438.8 million euros. It has increased by 18.5 per cent compared with the previous year (370.2 million euros). Excluding the pro-rata results of our holding in Sunrise, we generated a Group EBITDA of 402.3 million euros – which means that we have met our original target (slightly above 400.0 million euros). A significant contribution to this was made by the 13.7 per cent increase in gross profit to 898.7 million euros.

The other earnings parameters have declined slightly compared with the previous year: after deduction of depreciation and amortisation, for example, EBIT is reported at 298.8 million euros (previous year: 298.8 million euros). At 244.0 million euros, earnings before taxes on income (EBT) declined by 4.2 per cent compared with the previous year (254.7 million euros). The Group result for the financial year 2016 is reported at 216.4 million euros, a decline of 2.3 per cent compared with the previous year.

The free cash flow, one of the most important management-relevant performance indicators in the Group, amounted to 341.5 million euros in the reporting period (previous year: 284.5 million euros). Even when the dividend of 30.1 million euros received from Sunrise is excluded, the forecast figure of 300.0 million euros has been exceeded. Net financial debt increased from 369.2 million euros at the end of the financial year 2015 to the current figure of 725.8 million euros.

The customer base in the key contract customer sector (postpaid) increased by around 203,000 from 6.31 million customers to 6.51 million customers compared with the end of 2015. In conjunction with the increase in the no-frills customer portfolio (3.02 million at the end of 2016), this has led to a customer ownership of 9.53 million as at the end of 2016, corresponding to an increase of 232,000 customers compared with the previous year. As a result, the target of a slight increase in customer ownership was reached. In the year under review, the monthly postpaid-ARPU amounted to 21.4 euros, and was exactly in line with the corresponding previous year figure, thus meeting our original expectation.

In connection with the acquisitions and equity participations which have been concluded and also the higher level of customer ownership, consolidated revenue increased by 7.8 per cent compared with the previous year, namely from 3,117.9 million euros to 3,362.4 million euros. We have thus attained our objective of reporting moderately higher revenue.

Table 12: **Key performance indicators in 2016**

| In EUR million / as indicated | 2015 | Forecast 2016 | 2016 |
|---|---|---|---|
| Group revenue | 3,117.9 | moderate increase | 3,362.4 |
| Group EBITDA | 370.2 | slightly above 400 | 402.3[2] |
| Free cash flow[1] | 284.5 | around 300 | 311.4[3] |
| Customer Ownership in million | 9.30 | slight increase | 9.53 |
| Postpaid ARPU in EUR | 21.4 | stable | 21.4 |

These results confirm the company's strategic alignment as a digital lifestyle provider covering the mobile communications and mobile internet as well as the TV and Media sector and constitute a sound basis for continuing freenet AG's successful course over the coming months and years.

1 For a definition of free cash flow, see section „Financial performance indicators".
2 Excl. the share of freenet AG in the results of Sunrise Communications Group AG (36.5 million euros) in the financial year 2016.
3 Excl. the dividend payment of 30.1 million euros received by freenet AG in the financial year 2016 from the investment in Sunrise Communications Group AG.

# Key drivers of the business development

## Customer base development in the Mobile Communications Segment

Table 13: **Development of Mobile Communications customers**

| In EUR `000s / as indicated | 31.12.2016 | 31.12.2015 | Change in % |
|---|---|---|---|
| **Customer Ownership** | **9.53** | **9.30** | **2.5** |
| Thereof Postpaid | 6.51 | 6.31 | 3.2 |
| Thereof No-frills | 3.02 | 2.99 | 1.0 |
| Prepaid | 2.53 | 2.94 | -13.9 |
| Mobile Communications customers/cards | 12.06 | 12.24 | -1.4 |

In our core business of mobile communications, the financial year 2016 saw the successful continuation of our strategy, which we had adopted in previous years, of focussing on sustainable customer relations for the purpose of signing up new customers and managing existing customers and also of consistently focussing on digital lifestyle activities. We accordingly again succeeded in considerably increasing the number of postpaid customers last year. The number of customers with 24-month contracts in this strategically most important group rose to 6.51 million by the end of the reporting year (previous year: 6.31 million). This is equivalent to an increase of approximately 3.2 per cent or 203,000 users. This development was underpinned by a targeted approach to customers through all sales channels in high-street retailing and on the mobilcom-debitel website, as well as through further improvement of the freenet Group's customer management.

All mobile communication tariffs with shorter durations distributed via the Group's discount brands are pooled in the no-frills sector. Despite the focus on postpaid contract customers, the number of customers in this sector also increased in the year under review, by approximately 29,000 customers. As at the end of 2016, the customer portfolio in this customer group amounted to 3.02 million (previous year: 2.99 million).

The result of the strategy described above can be seen in a further increase in the non-financial performance indicator which is significant for the company, namely customer ownership, which represents the number of contract and no-frills customer groups. Compared with the figures for the previous year, the numbers have increased by approximately 232,000 customers from 9.30 million to 9.53 million. This is equivalent to growth of approximately 2.5 per cent.

The number of prepaid cards issued in the financial year ended, on the other hand, again decreased and amounted to 2.53 million as at the end of the year (previous year: 2.94 million). This decline is attributable to the network operators deactivating SIM-cards which have not been used (technical churn) and due to the decreasing activation of new customers.

Accordingly, the total number of mobile communication customers declined by approximately 175,000 customers, namely from 12.24 million in the previous year to 12.06 million at the end of December 2016.

## Monthly average revenue per user in the mobile communications segment (ARPU)

The development of the average monthly revenue per postpaid user ("postpaid-ARPU") also demonstrates the success of our strategy of focussing on valuable customers and digital lifestyle activities for the purpose of signing up new customers and managing existing customers. In the financial year 2016, we again succeeded in stabilising postpaid-ARPU at the level of the two previous years (21.4 euros).

No-frills ARPU decreased slightly by 0.1 euros to 2.4 euros compared with the previous year. This development demonstrates the fact that price pressure is still high in the discount market in which the freenet Group mainly operates via a range of online distribution channels. Nevertheless, there are also signs of stabilisation in this customer group following considerable declines in ARPU in certain cases in previous years.

The average monthly revenue per prepaid customer (prepaid-ARPU) in the financial year 2016 (3.1 euros) was slightly above the previous year's level (namely 3.0 euros).

Table 14: **Monthly average revenue per user in the Mobile Communications segment (ARPU)**

| In EUR | 2016 | 2015 |
|---|---|---|
| Postpaid | 21.4 | 21.4 |
| No-frills | 2.4 | 2.5 |
| Prepaid | 3.1 | 3.0 |

## Digital lifestyle

In addition to optimising its core business of mobile communications the freenet Group has increasingly been concentrating on the young growth sector of internet-based mobile applications for private customers since 2013. For the freenet Group, digital lifestyle business, as part of the Mobile Communications segment, encompasses telecommunications, internet and energy plus all the services, applications and devices that are connected to the internet by way of a mobile device or can be controlled through such a device.

The existing digital lifestyle strategy is focused on the enhancement and broadening of the current product and service portfolio to include the overall field of digital lifestyle while making systematic use of existing strengths and areas of expertise.

The freenet Group is positioning itself in this growth market by means of partnerships; it does not carry out however any development works of its own. At the same time, the Group is enlarging and optimising its digital lifestyle sales territory, in particular via its own stores in premium locations which are operated under the premium brand GRAVIS and through the company freenet digital GmbH, which markets modern, digital entertainment formats and services.



# Assets, earnings and financial position

## Revenue and earnings position

Table 15: **The Group's key performance indicators**

| In EUR `000s | 2016 | 2015 | Change |
|---|---|---|---|
| Revenue | 3,362,407 | 3,117,892 | 244,515 |
| Gross profit | 898,737 | 790,417 | 108,320 |
| EBITDA | 438,824 | 370,178 | 68,646 |
| EBITDA exclusive Sunrise | 402,331 | 370,178 | 32,153 |
| EBIT | 298,822 | 298,775 | 47 |
| EBT | 243,956 | 254,691 | -10,735 |
| **Group result** | **216,420** | **221,460** | **-5,040** |

**GROUP REVENUE** increased by 7.8 per cent compared with the previous year from 3,117.9 million euros to 3,362.4 million euros. This was achieved primarily as a result of the revenue generated in the TV and Media segment (218.9 million euros) as well as the higher customer ownership (31 December 2016: 9.53 million customers – previous year: 9.30 million customers) in conjunction with a stable postpaid-ARPU (21.4 euros in 2016 and also the previous year) as well as higher hardware revenue.

The **GROSS PROFIT** improved by 1.4 percentage points to 26.7 per cent. At 898.7 million euros, the gross profit has increased by 108.3 million euros compared with the figure reported for the previous year. Both developments are primarily connected with the new segment TV and Media contributing 110.8 million euros to the gross profit of the group.

**OTHER OPERATING INCOME** increased compared with the previous year period by 9.3 million euros to 60.5 million euros. This development is mainly due to the one-off income generated by the disposal of "mds Repair/Service" assets (3.3 million euros), the increase in income from reminder charges and returned debit charges as well as the initial integration of the segment TV and Media (other operating income of 3.3 million euros).

The **other capitalised own work** is attributable to internally generated software, and increased by 7.3 million euros to 18.7 million euros – mainly due to the segment TV and Media with a contribution of 6.4 million euros.

**personnel expenses** increased by 25.2 million euros from 195.2 million euros in the previous year to 220.4 million euros, primarily as a result of the increased number of employees in connection with the new segment TV and Media, accounting for personnel expenses of in total 48.2 million euros. In contrast, the number of employees and accordingly also personnel expenses were reduced in the segments Mobile Communications and Other/Holding.

The **other operating expenses** increased by 67.5 million euros compared with the previous year, to 355.4 million euros, mainly due to the of the inclusion of the segment TV and Media (contribution of 44.3 million euros) as well as higher expenses incurred for impairments recognised in relation to receivables. The other operating expenses in both years comprised marketing costs, administration costs (e.g. rents and incidental costs of the shops and administration building), costs of impairments and bad debts, legal/consultancy fees, costs of billing as well as outsourcing.

The **result of associates accounted for using the equity method** of 21.0 million euros (previous year: 0.2 million euros) is almost exclusively attributable to the acquisition of the shares in Sunrise Communications Group AG, Zurich, Switzerland (referred to in the following as "Sunrise"). A figure of 13.5 million euros is disclosed as of 31 December 2016 for the result attributable to Sunrise; of this figure, 36.5 million euros relates to shares in the group earnings of Sunrise after tax, and -15.7 million euros is attributable to the subsequent accounting of the shadow purchase price allocation.

As has been the case in the past, only the profit share from the item "Result of associates accounted for using the equity method" have been used for calculating our key financial performance indicator EBITDA. The depreciation resulting from the subsequent recognition of the shadow purchase price allocation does not have a negative impact on Group EBITDA.

As a result of the effects referred to above, **group ebitda** totalled 438.8 million euros, 68.6 million euros more than its previous year's level of 370.2 million euros.

Compared with the previous year, **depreciation and impairment write-downs** have increased by 52.9 million euros to 124.3 million euros, namely as a result of the increase in property, plant and equipment and intangible assets resulting from the acquisition of the Media Broadcast Group as well as the purchase price allocation carried out in this connection.

The **interest result**, i.e. the difference between interest income and interest expenses, is disclosed as -54.9 million euros in the reporting period (previous year: -44.1 million euros). The increase of 11.2 million euros in interest expenses is mainly attributable to the compounding of the liabilities resulting from the framework rental agreement, recognised as finance leasing, with regard to the purchase price allocation of the Media Broadcast Group. In this context, please refer to note 36, Company acquisitions, in the notes to the consolidated financial statements.

This has resulted in **earnings before tax** of 244.0 million euros in 2016 – representing a decline of 10.7 million euros compared with the previous year (254.7 million euros).

**income tax expenses** decreased by 5.7 million euros compared with 2015 to 27.5 million euros. The current tax expenses have declined by 2.7 million euros compared with the previous year, to 32.5 million euros. Income of 5.0 million euros from deferred taxes has also been netted in this position (previous year: 2.0 million euros). The increase in income from deferred taxes is mainly attributable to temporary differences relating to the additional write-downs in connection with the purchase price allocation for the acquisition of the Media Broadcast Group.

In consequence, **group earnings** after tax declined by 5.0 million euros, from 221.5 million euros in 2015 to 216.4 million euros in 2016.

## Assets and financial position

Table 16: **Selected Group balance sheet figures**

Assets

| In EUR million | 31.12.2016 |
|---|---|
| Non-current assets | 3,421.0 |
| Current assets | 863.8 |
| **Total assets** | **4,284.8** |

| In EUR million | 31.12.2015 |
|---|---|
| Non-current assets | 1,916.7 |
| Current assets | 807.3 |
| **Total assets** | **2,724.0** |

Shareholders' equity and liabilities

| In EUR million | 31.12.2016 |
|---|---|
| Shareholders' equity | 1,402.3 |
| Non-current and current liabilities | 2,882.5 |
| **Total equity and liabilities** | **4,284.8** |

| In EUR million | 31.12.2015 |
|---|---|
| Shareholders' equity | 1,379.0 |
| Non-current and current liabilities | 1,345.0 |
| **Total equity and liabilities** | **2,724.0** |

The **BALANCE SHEET TOTAL** as of 31 December 2016 amounted to 4,284.8 million euros, and has increased by 1,560.7 million euros (plus 57.3 per cent) compared with the previous year (2,724.0 million euros) following the acquisition of the shares in the Media Broadcast Group and Sunrise.

On the **ASSETS SIDE** of the balance sheet, **NON-CURRENT ASSETS** increased by 1,504.3 million euros to 3,421.0 million euros. This is due to various factors, including the acquisition of 24.56 per cent of shares in Sunrise. As an associated company, the holding in Sunrise is disclosed under the item „Investments in associates accounted for using the equity method" with a carrying amount of 743.1 million euros. At this point, please refer to note 17.1, Associated companies, in the notes to the consolidated financial statements. The considerable increase in the intangible assets, goodwill and property, plant and equipment is primarily due to the acquisition of 100 per cent of the shares in the Media Broadcast Group in March 2016. Please refer to our comments in note 36, Company acquisitions, in the notes to the consolidated financial statements.

Within **CURRENT ASSETS**, liquid assets increased by 48.4 million euros to 318.2 million euros. Whereas the Group reported an inflow of 389.6 million euros for cash flow from operating activities in 2016, it reported outflows of 862.4 million euros for cash flow from investing activities and inflows of 521.2 million euros for cash flow from financing activities.

On the **LIABILITIES' SIDE** of the balance sheet, there has again been an increase in **EQUITY**. As of 31 December 2016, equity is stated as 1,402.3 million euros (31 December 2015: 1,379.0 million euros). The increase of 23.2 million euros resulted in the amount of 216.4 million euros from the Group's net income for the financial year 2016 and in the amount of -198.4 million euros from the dividend payment for the financial year 2015 paid out in 2016.

The equity ratio accordingly declined to 32.7 per cent as of 31 December 2016, compared with 50.6 per cent as of the corresponding previous-year date.

Total **NON-CURRENT AND CURRENT LIABILITIES** increased by 1,537.5 million euros to 2,882.5 million euros.

As of 31 December 2016, **FINANCIAL DEBT** was again the major item within non-current and current liabilities, and increased from 638.9 million euros in the previous year to 1,734.2 million euros in 2016. The increase of 1,455.5 million euros in non-current financial debt, to 1,673.9 million euros, is mainly attributable to the placing of two borrower's note loans in February and October 2016 for a total volume of nominal 910.0 million euros (carrying amount as of 31 December 2016: 905.2 million euros) as well as the second tranche of the syndicated bank loan of nominal 610.0 million euros (carrying amount as of 31 December 2016: 604.6 million euros). The decline of 360.2 million euros in current financial debt, to 60.3 million euros, is mainly attributable to the scheduled repayment of the corporate bond in April 2016 for a nominal volume of 400.0 million euros.

**NET FINANCIAL DEBT** increased to 725.8 million euros as of 31 December 2016 (31 December 2015: 369.2 million euros). For this parameter, financial debt is reduced by the liquid assets and the stake in the market value of Sunrise as of 31 December 2016 (11,051,578 shares multiplied by the closing price of 62.45 euros – source: Bloomberg). Accordingly, the debt ratio, which is expressed as the ratio between net debt and EBITDA, increased considerably from

1.0 in 2015 to 1.7 in 2016. In this context, please refer to the statements in the chapter „Financial management" in this Group management report.

The considerable increase in various other items within the non-current and current liabilities, such as the 254.6 million euros increase in the other liabilities and deferred items, the 72.0 million euros (including liabilities arising from the frame lease agreement, which was registered as finance lease), increase in trade accounts payable, the 59.8 million euros increase in other provisions and the increase of 41.4 million euros in pension provisions are mainly attributable to the initial integration of the Media Broadcast Group. For more information, please refer to note 36, Company acquisitions, in the notes to the consolidated financial statements.

# Cash flow

Table 17: **The Group's key cash flow indicators**

| In EUR million | 2016 | 2015 | Change |
|---|---|---|---|
| Cash flow from operating activities | 389.6 | 314.9 | 74.7 |
| Cash flow from investing activities | -862.4 | -28.5 | -834.0 |
| Cash flow from financing activities | 521.2 | -128.7 | 649.9 |
| **Change in cash and cash equivalents** | **48.4** | **157.8** | **-109.4** |
| | | | |
| **Free cash flow[1]** | **341.5** | **284.5** | **57.0** |

Compared with the corresponding period last year, **CASH FLOW FROM OPERATING ACTIVITIES** increased by 74.7 million euros to 389.6 million euros. Excluding the non-cash-effective earnings of 36.5 million euros relating to the associated company Sunrise, EBITDA increased by 32.2 million euros compared with the previous year. In the financial year 2016, freenet AG received a dividend payment of 30.1 million euros as a result of the dividend payment of 3.00 CHF per share adopted in the annual general meeting of Sunrise on 15 April 2016. Net working capital increased in 2016 by 3.8 million euros, compared with an increase of 10.3 million euros in the previous year. The increase of 3.8 million euros in net working capital in 2016 can be attributed mainly to the scheduled reduction of 25.0 million euros in liabilities and accruals vis-à-vis distribution partners arising from distribution rights impacting cash flows. This has been opposed mainly by the volume of factoring of mobile option receivables, which increased by 22.8 million euros compared with 31 December 2015 – please refer in this respect to note 34.6, Transfer of financial assets, of the notes to the consolidated financial statements.

In addition, there were net cash outflows in the financial year 2016 amounting to 40.0 million euros (previous year: 44.3 million euros) that resulted from income tax payments and refunds.

In 2016, the **CASH INFLOW FROM INVESTING ACTIVITIES** developed from -28.5 million euros in the previous year to -862.4 million euros. This was due primarily to the outflow of 738.9 million euros for the acquisition of 24.56 per cent of shares in Sunrise, which are disclosed under the outflows for the acquisition of companies accounted for using the equity method.

The outflows for the acquisition of subsidiaries relate to the acquisition of 100 per cent of the shares in the Media Broadcast Group – a total of 101.7 million euros was paid for this purpose in the financial year 2016, whereas the Group received liquid assets of 25.1 million euros via the initial consolidation of the Media Broadcast Group as of 18 March 2016 – resulting in outflows of 76.6 million euros for the acquisition of subsidiaries.

The cash outflows for investments in intangible fixed assets and in property, plant and equipment, netted out against the cash inflows from such assets, increased in 2016 by 17.7 million euros over the previous year from 30.4 million euros to 48.1 million euros. The cash-effective investments were financed entirely out of the company's own resources, and mainly related to property, plant and equipment of the Media Broadcast Group. The inflows from the disposal of assets were mainly due to sale-and-lease-back transactions of the Media Broadcast Group (12.7 million euros).

1 For a definition of free cash flow see section „Definition of alternative performance measures".

**CASH FLOW FROM FINANCING ACTIVITIES** improved to 521.2 million euros compared with -128.7 million euros in the previous year.

For financing the transactions which were carried out and also for refinancing the corporate bond which fell due upon final maturity in 2016, the Group received funds of 1,853.6 million euros in 2016 by raising two borrower's note loans and a syndicated bank loan. In this context, please refer to note 29, Financial debt, in the notes to the consolidated financial statements.

The outflows for repaying financial debt of 1,047.3 million euros mainly comprise the repayment of the corporate bond with a volume of 400.0 million euros, the repayment of parts of the syndicated bank loan (350.0 million euros) as well as the repayment of shareholder and bank loans of the Media Broadcast Group (297.2 million euros).

The dividend payments had a negative impact of 198.4 million euros on the cash flow from financing activities in the financial year 2016 (previous year: 192.0 million euros).

In 2016, interest payments, mainly as a result of the refinancing, amounted to 68.1 million euros, representing an increase of 33.3 million euros compared with the previous year.

There were also payments of 18.6 million euros relating to the framework rental agreement of the Media Broadcast Group classified as a financing lease in the course of the purchase price allocation. Please refer at this point to note 27, Trade accounts payable, other liabilities and accruals, in the notes to the consolidated financial statements.

**FREE CASH FLOW** amounted to 341.5 million euros in the financial year 2016. It increased by 57.0 million euros compared with 2015.



# SIGNIFICANT EVENTS AFTER THE REPORTING DATE

No events of major significance for the freenet Group have occurred after the balance sheet date. In this connection, please also refer to note 38 of the notes to the consolidated financial statements.

# OPPORTUNITIES AND RISK REPORT

## Opportunities

In order to manage and monitor its ongoing business activities, the Executive Board has established an extensive monthly reporting system that covers both the financial and non-financial performance indicators in the freenet Group. In regular meetings with all of the relevant business areas and units, the Executive Board ensures that all members are informed in a timely manner about operational developments. At these meetings, not only current themes, but also future internal and external developments, measures and potential opportunities are discussed. The identification, analysis and communication of the opportunities, as well as their exploitation, is a commercial (management) task that is performed by the Executive Board, the responsible managers in the individual business areas and units, and the relevant decision-makers in a process of permanent communication.

freenet AG sets itself the objective of performing a pioneering role in all areas of digital lifestyle and of successfully defending this role. For this reason, freenet AG and its subsidiaries continued the strategy of focusing on mobile voice and data services and the marketing of digital lifestyle products with a careful and consistent approach. In the marketing of smartphones and flat-rate tariffs, the focus of commercial activity was mainly on customer quality and the stabilisation of the contract customer base.

The existing digital lifestyle product and service portfolio has been continuously expanded.

The relevant activities in this respect comprise products in the field of e-health, data security as well as app-based applications. Examples of such products are the SmartCare products "Withings aura" and "Gymondo" as well as "Norton Security Online" in the field of security.

In the field of digital lifestyle, the positioning of freenet AG is now more broadly based than has ever been the case in the past. As the largest network-independent mobile communications provider, freenet AG is going to expand along this successful path in digital lifestyle business and make use of opportunities against the backdrop of a strict orientation towards stakeholder value.

freenet AG sees external opportunities particularly in the following market trends:

- Increasing readiness of customers to pay for mobile communication devices
- Continuation of the trend towards mobile Internet and data use via smartphone, tablet and PC
- Trend towards higher-priced devices (smartphones) and concomitant increased use of flat-rate products
- Trend towards the interconnection of products ("Internet of Things", "integrated product landscapes")

Furthermore, the effects of the increased mobile internet and data usage and the associated trend towards higher-priced flatrate products could lead to a stronger increase in customer ownership than expected, although overall, the latter tends to be regarded as rather improbable.

With the acquisition of the Media Broadcast Group and the equity participation in EXARING AG, freenet AG has also completed the process of breaking into the new TV and Media field of business. The entry into the new field of terrestrial and internet-based TV is providing the company with the opportunity of achieving further diversification in the digital lifestyle field and of developing new growth potential and sources of revenue. The company considers that this is an opportunity to establish a further relevant mainstay in addition to its core business of Mobile Communications.

All these aspects might have a positive impact on the anticipated development of revenue, EBITDA and free cash flow.

Internal opportunities for freenet AG could emerge in particular from:

- the assessment and implementation of strategic options in the field of mobile communications, digital lifestyle and TV,
- the continuous intensification of business relationships with suppliers for the stabilisation of existing and the development of new condition models,
- the consolidation and consistent further development of IT systems to achieve a further improvement in customer satisfaction,
- the enhancement of our selling power through the expansion of existing sales channels (multichannel approach) and the use of existing and new sales collaborations and partnerships,
- a further improvement in shop performance, also by marketing additional products,
- the implementation and marketing of new products in the digital lifestyle and TV sector,
- the intensified establishment of the brands klarmobil, freenetmobile, callmobile and debitel light in the steadily growing discount market, with the aim of participating even more actively in their growth, and,
- the continuous improvement of processes and quality for a lasting reduction in cost structures.

The assessment and implementation of strategic options in the mobile communications and the digital lifestyle areas, the implementation and marketing of new, innovative products and the enhancement of our own selling power could have a positive effect on the development of the underlying financial performance indicators and hence exceed our expectations. A stronger selling power and customer satisfaction could, as it were, lead to a more positive trend in customer ownership than had been forecast. The likelihood of this happening, however, is regarded as rather low.

In addition to the established main brand mobilcom-debitel, the no-frills brands klarmobil, freenetmobile, callmobile and debitel light in particular, as well as others, could establish themselves more firmly on the market, possibly leading to a higher rate of market penetration.

At the beginning of June 2016, klarmobil restructured a number of tariff offers. Formerly temporary special actions had been converted into a fixed allnet tariff group. This provides the customer with more extensive services for the same monthly charge – in particular a higher data volume and a higher surfing speed. If the brands perform stronger than expected on the steadily growing discount market, this could lead to higher revenue and to improved results and higher free cash flow than had been forecast.

The strategic collaboration of mobile communications services and digital lifestyle applications was accelerated further. This Group-level orientation of business activities will be pursued consistently in the future as well, as the trend towards the continuing digitalisation and interconnection of products and services will carry on into the future. In this connection, we continue to see growth opportunities, potential synergy and opportunities for new strategic partnerships with regard to rendering digital lifestyle services. In the future, this could lead to more positive contributions to the underlying financial performance indicators than had hitherto been expected. The significance of the strategic transformation from a mobile communications specialist pure and simple to a digital lifestyle provider will increase against this background.

If the measures and efficiency improvements for a lasting reduction in cost structures that are resulting from the continuous improvement of processes and quality turn out to be more positive than expected, this might have a more positive impact in the years to come on the level of material overheads and personnel expenses, and hence on EBITDA and free cash flow, than has so far been budgeted for.

# Overall evaluation of the opportunities situation

Thanks to the regular monitoring of the internal and external opportunities by the monthly reporting system and to the communication in the scheduled meetings, the management is in a position to perform the corporate (management) task that is incumbent upon it, and therefore to make a positive contribution to the operating and strategic safeguarding of the company, by taking advantage of opportunities.

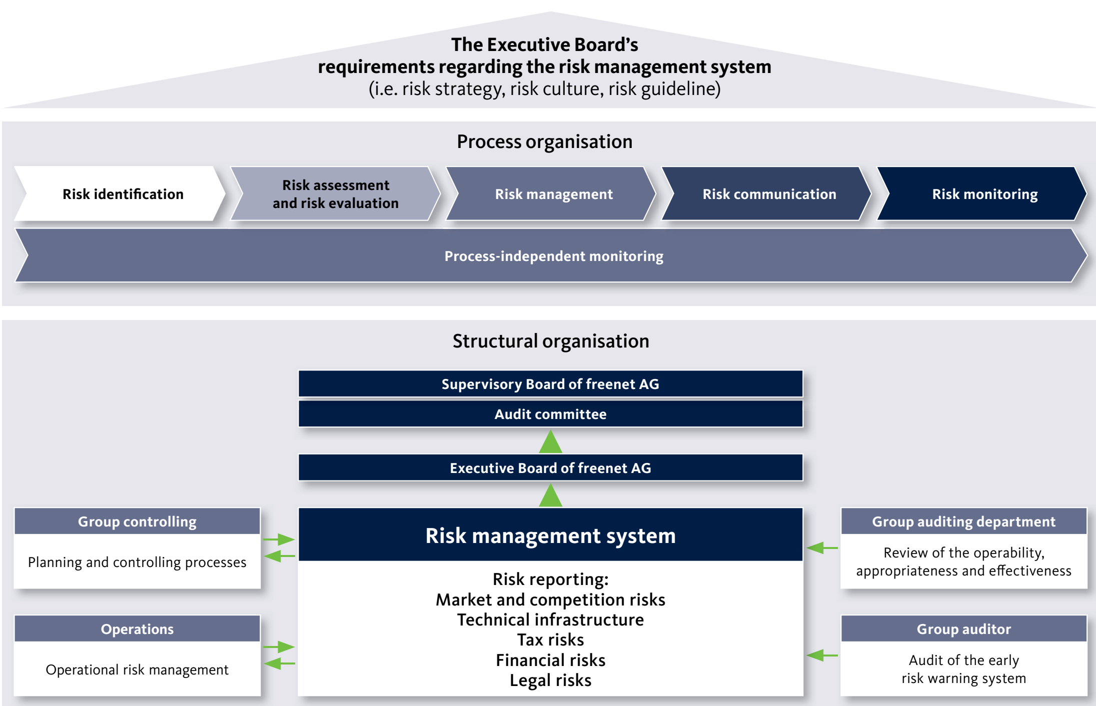
Both external and internal opportunities that had basically remained the same since the previous year were identified. The significance of the opportunities shown and the resulting positive effects on the forecast financial and non-financial performance indicators, and therefore on the development of freenet AG as a whole, are collectively rated as low. The management is therefore expecting the positive trend in business performance that was forecast in the outlook.

# Risk management system

An effective risk management system is essential for safeguarding the continued existence of freenet AG in the long term. freenet AG's risk management system is applied solely to risks, not opportunities. This should ensure that any risks to the company's future development are identified at an early stage by all executives of the Group and communicated in a systematic, transparent manner to the responsible decision-makers in the company. The timely communication of risks to the responsible decision-makers is designed to ensure that appropriate steps are taken to deal with the identified risks, thereby averting damage to our company, our employees and our customers.

To this end, the freenet AG Executive Board has set up an efficient early warning, monitoring and management system within the Group that also integrates the subsidiaries. As part of the statutory audit assignment for the annual and consolidated financial statements, the system is examined by the auditor to determine whether it is suitable to identify at an early stage any developments that endanger the company's continued existence. The early warning system for risks conforms with statutory requirements. The systems and methods of the risk management system are an integral part of the overall organisation of freenet AG's structure and processes.

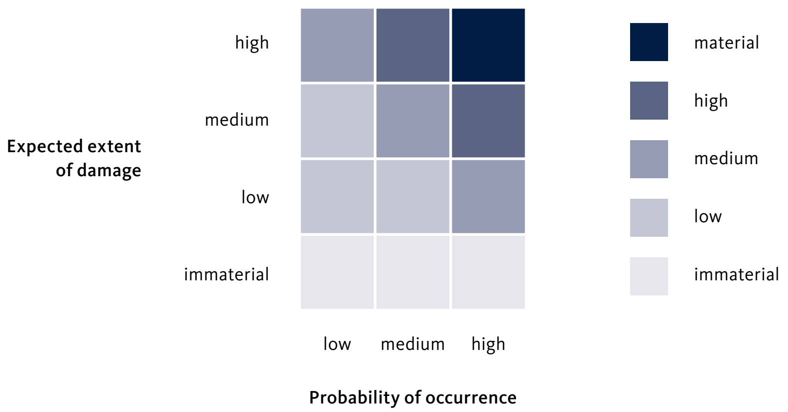
Figure 10: **Process and structural organisation of freenet AG's risk management system**



At least every six months, freenet AG's individual departments and subsidiaries identify or update existing and new risks that exceed a defined materiality threshold in formalised risk reports (risk identification). The risk reports describe the specific risks and consider the probability of their occurrence, as well as their implications for the company, on the basis of standardised criteria (risk analysis and assessment).

The risks within freenet AG are assessed in accordance with the net principle, by which the risk is observed in conjunction with the mitigating influence of any countermeasures that were implemented. The criteria "probability of occurrence" and "anticipated extent of damage" are used to assess the risks. In the process, risks with a low (<50 per cent), medium (50 to 75 per cent), and high (>75 per cent) probability of occurrence are systematically categorised and differentiated from each other. With regard to the extent of the anticipated damage arising from a risk, distinctions are drawn between immaterial (<1.0 million euros), low (1.0 to 2.5 million euros), medium (2.5 to 10.0 million euros) and high (>10.0 million euros) anticipated damages. The combination of the probability of occurrence and the extent of the anticipated damage results in the classification of the risks' significance as "immaterial", "low", "medium", "high" and "material". These risk categories are shown in the following illustration.

Figure 11: **Risk matrix at freenet AG**




Based on the results of the risk analysis and assessment that were communicated, various alternatives for action are carried out as part of the company's general management, in order to be able to react appropriately to the identified risks (risk control and risk monitoring). The individual risk reports are consolidated into a Group risk report and forwarded to the Executive Board. Between the standard reporting times, too, risks are recorded, analysed, evaluated and controlled immediately after their identification and, if they are of sufficient magnitude, reported immediately to the Executive Board and the Supervisory Board (risk communication).

In its guidelines, which are continuously being extended and improved, the Executive Board has defined the significant risk categories for the Group, elaborated a strategy for dealing with these risk categories, and documented the allocation of tasks and areas of responsibility within the risk management system in the Group. These guidelines are familiar to all employees and enhance their risk awareness in a targeted fashion (part of risk communication).

The methods and systems of risk management are continuously being examined, enhanced and adjusted. In the process, freenet AG's internal auditing department plays a supporting role, with the regular audits of the risk reports being the main focus. The Supervisory Board, in particular freenet AG's audit committee, monitors the effectiveness of the risk management system from the standpoint of German stock corporation law. The Supervisory Board is integrated by means of regular reporting and, if necessary, an up-to-date report by the Executive Board (process-independent risk monitoring).

In addition to the risk management system, the Executive Board has established an extensive monthly reporting system that covers both the financial and non-financial performance indicators in the Group for the purpose of managing and monitoring its ongoing business activities. In regular meetings with all of the relevant business areas and units, the Executive Board ensures that all members are informed in a timely manner about operational developments. Current topics and future measures are also discussed at these scheduled meetings (part of risk communication).

# Risk report

This section presents the risks that could influence freenet AG's net assets, financial position or results of operations. The risks are categorised as market risks, IT risks, tax risks and financial risks. The individual risks are specified in accordance with their ranking in the respective categories.

The Mobile Communications segment is by far the most significant segment in the freenet Group in terms of both revenue and earnings. This is also the source of the main market risks in this particular field; they are therefore detailed in the following primarily in relation to this segment. The estimation of risk for the other categories basically applies for all segments. Material differences between the segments in relation to the estimation of risk are specified as such separately.

## Market risks

### Highly competitive markets

The telecommunications markets continue to be characterised by intense competition. This can lead to shortfalls in revenue, loss of market shares and pressure on margins in the respective business areas and/or can make it more difficult to gain market shares.

Vigorous competition can also lead to higher costs for new customer acquisitions, accompanied by falling revenue and a significant propensity of customers to switch. As a result, the forecast revenue-based key performance indicators, earnings indicators and free cash flow could develop in a slightly more negative fashion than had previously been expected. In order to prevail against its competitors, freenet AG must continue to design its products and services attractively, market them successfully and carry out customer retention activities. In addition, freenet AG must respond flexibly to the development of the competition's business and anticipate new customer requirements. This involves a medium risk for the achievement of the company's goals.

### Network operators

Bonus payments and commissions of the network operators form part of the revenue of freenet AG. A reduction of these network operator payments can lead to a higher capital commitment and marketing risk. This aspect constitutes a medium risk for freenet AG. freenet AG is trying to minimise the risk by negotiating flexible purchasing terms and by continuously monitoring goal attainment for premium payments and renegotiating as and when necessary.

The margins in mobile service provider business are very much determined by the network operators and their defined tariff models. This imposes certain restrictions within the tariff models, for instance by way of restrictions faced by users wishing to change tariffs. Nevertheless, the company constantly monitors the implementation of further volume-based purchasing models – in the postpaid and also in the prepaid fields. The risk has been classified as low by freenet AG.

The network operators are increasingly marketing their products themselves and forcing the mobile communications service providers out of the market ("shift to direct"). Also, due to their business structure, the network operators are sometimes able to offer better rates than the mobile communications service providers. This, in turn, can lead to a loss of distribution channels and customers. This aspect represents a minor risk for freenet AG.

As a countermeasure, freenet AG concludes long-term contracts with its main distribution partners and offers them attractive incentive systems (e.g. Airtime models). An additional possibility of maintaining and expanding existing distribution channels is to be seen in the acquisition of further franchise partners.

The merger between the two network operators O2 and E-Plus might result in a reduced amount of competition between the remaining mobile network operators (“MNOs”) and an associated weakening of the service provider model. This might be reflected in various ways, including a reduction of the margin. There is also the risk of coordinated behaviour of the three network operators remaining after the merger to the detriment of all service providers. Any coordinated action of these three network operators might mean that they would be less willing to negotiate and that freenet AG would find it more difficult to achieve positive negotiation results. The network capacity provided by Telefónica Deutschland to another market player without its own mobile network will probably be marketed quite aggressively. On the positive side of the equation, existing contracts were extended until 2025, which provides freenet AG with a certain amount of protection. If conditions were to be reduced across the market, the conditions for the distribution partners would be adjusted. freenet AG considers that this risk is of a minor nature.

The network operator risks, either individually or in combinations, could affect the forecast earnings indicators and free cash flow more negatively than has so far been anticipated.

## Acquisition of companies

freenet AG has acquired companies in the past. In connection with this, there is a medium risk that the operating activities of these new investments will not develop as expected and that consequently, among other things, growth in digital lifestyle will remain below expectations and therefore below the forecast results and free cash flows. The management report contains regular monitoring of the investment development with the aim of initiating countermeasures immediately if there are any deviations from the original plan.

## Acquisition of the Media Broadcast Group

The acquisition which was completed in the first quarter 2016 has resulted in various risks for the company. As of 31 December 2016, freenet AG considered that there was a medium risk in the form of the current VHF regulation of the Bundesnetzagentur (Federal Network Agency). This regulation might have intensified and encouraged competition, which means that the company might have suffered losses in terms of market share, revenue and earnings in this particular field. However, the VHF regulation for the charge period until 03/2019 is virtually concluded by now. There have been no major changes regarding the planning assumptions. The planning process has adequately taken account of the possibility of further customer loss. A further aspect is that customer demand for the product freenet TV might be less significant than originally anticipated. This constitutes a medium risk for freenet.

## Termination charges

If the Federal Network Agency lowers the “termination charges” any further, this could reduce revenue per customer on the market more sharply than expected. Based on past reductions of these charges, however, this risk is low. freenet AG monitors the regulatory environment on a permanent basis.

## Laws and regulation

Legislative changes, interventions by regulators or even landmark judicial decisions may have repercussions for the tariff structure and for the possibility of collecting receivables from customers. This might have a negative impact on the forecast revenue and on the amount of free cash flow. The effects of individual decisions or legislative changes might not be significant in themselves, with the result that the associated risk can be classified as low overall. freenet AG counters this risk by regularly monitoring regulatory developments and following the outcomes of legal judgements.

## Regulation EU-Roaming

The implementation of the new EU Roaming Directive (“Roam like at Home”) will result in the risk that the network operators will charge wholesale costs for the roaming service despite lower end user revenues. To combat this risk, negotiations are held with the network operators for ensuring cost-neutral implementation of the roaming regulations. The risk has been classified by freenet AG as low.

## IT-Risks

### Data theft and hacker attack

The operational availability and efficiency of the technical infrastructure, including the company's data centres and billing systems, are of major importance for the company's successful operation and continued existence. There is a low risk that network failures or service problems caused by system malfunctions or breakdowns might lead to a loss of customers. Apart from the decline in revenue that results from a loss of customers, a system breakdown means that freenet AG might not be able to provide any services and is therefore unable to generate any revenue or make any positive contribution to the anticipated earnings or free cash flow. Technical early warning systems are used to prevent such breakdown and failure risks. Continuous maintenance and updates keep the security precautions up to date at all times. To prevent the loss of sensitive data, a backup is generated every 24 hours and is stored at a different location when saved.

A hacker attack on the freenet TV database might result in harmful data manipulation which, under extreme circumstances, might result in failure of the TV boxes. The risk has been classified as low by freenet.

## Tax risks

### Loss carryforwards

If, within five years, over 25 per cent of the shares or voting rights in the company came to be held directly or indirectly by a single shareholder or by several shareholders with parallel interests (harmful acquisition of shares), any negative income (corporation and trade tax loss carry-forwards) of the company not settled or deducted by the time of the harmful acquisition could be lost in whole or in part, in accordance with section 8c of the German Corporation Tax Act (KStG). Shares are considered to be united in a single shareholder if they are transferred to a buyer, to persons close to the buyer, or to a group of buyers with parallel interests.

The company has no influence on the occurrence of this risk, as the (perhaps partial) elimination of any negative income (corporation and trade tax loss carry-forwards) not settled or deducted by the time of the harmful acquisition is brought about by measures and transactions at shareholder level. Against this backdrop, it cannot be ruled out that as a result of a sale or additional purchase of shares by the company's shareholders; more than 25 per cent of the shares could be united under a single shareholder. The same medium risk exists if more than 25 per cent of the shares or voting rights are first united through other measures under a single shareholder or several shareholders with parallel interests. The legal consequences described above apply mutatis mutandis.

### VAT risk on „remuneration from third party“

In a letter from the Federal Ministry of Finance dated 4 December 2014 and a simultaneous addendum to the VAT application decree, the fiscal authority issued the following rule: If the intermediary in a mobile communications contract supplies the customer in the intermediary's own name with a mobile communications device or some other electronic article, and if the mobile communications company grants the intermediary a commission dependent on the supply of the mobile communications device or other electronic articles on the basis of a contractual agreement, or part of a commission dependent on the above, such a commission or part of a commission shall not be regarded as remuneration for an intermediary brokering role vis-à-vis the mobile communications company, but rather as remuneration from a third party as defined by section 10 (1) sentence 3 of the German VAT Act (UStG) for the supply of the mobile communications device or the other electronic article. This applies irrespective of the amount of any additional payment to be made by the customer. The application of this rule as from 1 January 2015 will not involve any reportable risks for the company. As for the revenue reported before 1 January 2015, the company regards it as very likely indeed that the rule specified above will have no significant negative effects for freenet AG under VAT law. However, a low risk remains for the revenue reported before 1 January 2015 for assessment periods that have not been audited conclusively, as a result of which freenet AG would have to refund some of its input tax to the tax authorities.

### Other tax risks

In the case of assessment periods that have not been audited conclusively, there might in principle be changes that result in subsequent tax payments or changes in the loss carry-forwards if the tax authorities, within the framework of external tax audits, come to different interpretations of tax regulations or different assessments of the respective underlying circumstances. The same applies for types of official charges which in part have yet to be audited, in particular because they are usually not subject to external tax audits.

The risk of different interpretations and assessments of circumstances applies in particular to corporate restructuring processes under company law. It cannot therefore be ruled out entirely that as a result of contributions of assets, other conversion procedures, new capital injections and changes in the shareholding structure, the corporate income and trade tax carry-forwards declared by the corporations of freenet AG and hitherto ascertained separately by the tax authorities might be reduced or discontinued. All in all, this is regarded as a low risk.

## Financial Risks

The objective of financial risk management is to limit risks by means of the company's ongoing operating and financing activities. In this area the company is essentially subject to the risks described below in respect of its financial instruments, financial assets and financial liabilities.

### Bad debt losses

A risk of bad debt losses is the unexpected loss of funds or revenue as a result of the partial or complete default on receivables owed. There is a medium default risk with regard to the trade account receivables reported in the balance sheet and other assets.

The assessment of the risk of default on trade accounts receivable in the freenet Group is focused primarily on trade accounts receivable owed by end customers. Here, particular attention is devoted to the credit standing of customers and sales partners in our Group's large-scale business activities. For important contract customer sectors, credit assessments are carried out for the customers before the contract is signed. In the ongoing contractual relationship, the implementation of a swift and regular reminder and debt collection process involving a number of debt collection companies in the benchmarking area, together with long-term debt collection monitoring and high-spender monitoring, are essential measures for the minimisation of the default risk in our Group. An ongoing reminder and debt collection process is likewise used for receivables owed by retailers and franchise partners. In a similar vein, credit limits are established and monitored. Commercial credit insurance, moreover, safeguards us against significant default risks vis-a-vis major customers (traders and distributors in the Mobile Communications segment). The risks associated with uninsured traders and distributors are restricted by an internal limit system — generally, customers with a poor credit standing must pay cash in advance or the commercial relationship will not come into being. Finally, the appropriate formation of valuation allowances takes the risks of default on receivables into account.

There are regularly trade accounts receivable due from the mobile network operators in the Mobile Communications segment, and there are regularly trade accounts receivable in the TV and Media segment due from public and private providers of TV and radio programmes. The concept of collecting these receivables is also constantly monitored; however, past experience has shown that the risk of bad-debt losses in this respect is extremely low.

There is a factoring agreement between the Group and a bank on the sale of receivables from mobile options. The relevant risks (in particular the risk of default) and opportunities are transferred to the bank under this arrangement. Although of minor significance, the late payment risk shall be completely retained by the freenet Group.

### Impairment of the assets

In freenet AG's consolidated balance sheet, both goodwill and intangible assets such as customer relationships, trademark rights and usage rights are reported in their intrinsic amounts. There is a medium risk that impairment tests in the subsequent periods might lead to substantial diminutions in value.

freenet AG's assets are checked both regularly and on an ad-hoc basis otherwise as and when appropriate if there are potential indicators of lasting impairment. Such an indicator may be changes in the economic or regulatory environment. Any resultant impairment is not cash-effective, and therefore does not have any impact on the free cash flow. The revenue and EBITDA are also not affected (no impact on the financial performance indicators).

## Liquidity

The Group's general liquidity risk, which is classified as a medium risk, resides in the possibility that the company might potentially be unable to meet its financial obligations, for example the repayment of financial debts, the payment of purchasing obligations and the obligations from lease agreements.

Extensive financial planning instruments are used throughout the Group to monitor and control liquidity. The Group also controls its liquidity risk by holding appropriate bank balances and credit lines at banks, and by monitoring continuously the forecast and actual cash flows. The need for and investment of liquid funds in the Group is controlled centrally on the basis of several existing internal Group cash pooling agreements in which the significant companies in the freenet Group participate.

The Group uses a variety of financial instruments to reduce the general liquidity risk. The liabilities due to banks shown under borrowings relate to the borrowers' note loan concluded in December 2012, May 2015, February 2016 and October 2016 (disclosed as 1,129.5 million euros, including interest accruals, as of 31 December 2016) as well as the two loan tranches in the syndicated facility agreement of March 2016 for a total of max. 1,040.0 million euros (shown as 604.6 million euros, including interest accruals, as of 31 December 2016). The third tranche in the facility agreement for 100.0 million euros (in the form of a revolving credit line) had not been drawn as of 31 December 2016.

The credit agreements that were concluded bring about another low liquidity risk because the restrictions agreed therein ("undertakings" and "covenants") restrict freenet AG's financial and operational leeway. These impose restrictions on the company, for example regarding changes in the Group's business operations, the implementation of internal Group measures to change its structure under company law, the provision of collateral, and any acquisitions or disposals of assets, especially shareholdings. There are stringent restrictions on the company raising loans outside of these credit agreements, e.g. in order to finance future strategic investments. In view of the aforementioned liquidity reserves, however, the covenants represent only a minor restriction for freenet AG.

## Capital risk management

The Group's capital risk management is related to the shareholders' equity as shown in the consolidated balance sheet and to ratios derived therefrom. The primary objective of the Group's capital risk management is to guarantee compliance with the financial covenants contained within the credit agreements. The main financial covenants are defined in relation to the Group's equity (equity ratio) and the debt (ratio of Group net debt to Group EBITDA). If the macroeconomic conditions were to deteriorate, this might under certain circumstances lead to a situation where the freenet Group can no longer deliver on its agreements with the financing banks. There is a medium risk of the financing banks being entitled to declare the loans due and payable. freenet AG minimises the risk by monitoring the financial ratios continuously.

## Interest rate risk

As regards variable-interest financial debt, our company is subject to interest rate risks related largely to the EURIBOR. The company counters these medium risks by having a mix of fixed- and variable-interest financial debt. Although the interest rate risks are not explicitly secured, the cash holdings, which are invested mainly at variable interest rates based on EONIA or EURIBOR, serve as a natural hedge and accordingly mitigate interest rate risks arising from the variable-interest financial debts.

Funds are usually invested as call money or time deposits at commercial banks with high credit ratings.

The company continuously monitors the various opportunities available for investing the liquid assets on the basis of the day-to-day liquidity planning at its disposal as well as the various options available for scheduling the debt. Changes in market interest rates could have an impact on the net interest income from originally variable-interest financial instruments and are included in the calculation process for results-related sensitivities.

### Other financial risks

Other financial risks might occur in the form of foreign exchange and share price risks. The company is only exposed to foreign currency risks to a limited extent; this is the reason why the management report does not detail these risks separately. With regard to share price risks, it must be borne in mind that the company holds a stake of 24.56 per cent in the share capital of Sunrise. Sunrise prepares its consolidated financial statements in the reporting currency Swiss francs (CHF). The exchange rate between the euro and Swiss franc has an impact on the calculation of both elements of the item of our consolidated income statement “Results of associates accounted for using the equity method”, namely the interest in the current result of Sunrise and also the depreciation relating to the shadow purchase price allocation for Sunrise. Accordingly, this exchange rate has an impact on the results of operations of the freenet Group; however, as far as can be seen at present, this impact is considered to be minor.

## Strategic risks

### Stake in Sunrise Communications Group AG

In the first half of 2016, freenet AG acquired a stake of 24.56 per cent in Sunrise Communications Group AG. The business performance of Sunrise AG might turn out to be less positive than originally anticipated, which in turn might have a negative impact on the earnings and business development of freenet. The risk has been classified as low by freenet.

### EXARING AG

Since the end of 2015, freenet AG has owned a 24.99 per cent stake in EXARING AG. This might result in risks that the number of users at the time of the product launch might be lower than originally anticipated and that the costs, particularly costs of content (TV stations) and acquisition (sales partners/marketing partners), might be higher than originally anticipated. In addition, limited functionalities in the product portfolio might have a negative impact. freenet has classified these risks as medium.

# Overall assessment of the risk position

The risks for freenet AG that are outlined above are summarised in the overview below.

| Risks | Probability of occurence | Expected extent of damage | Risk | Tendency |
|---|---|---|---|---|
| **Market risks** | | | | |
| Highly competitive markets | medium | medium | medium | |
| Network operator | | | | |
| Bonuses and margins | medium | medium | medium | |
| Shift to direct | medium | low | low | |
| $O_2$ and E-Plus | low | immaterial | immaterial | |
| Acquisition of companies | medium | medium | medium | |
| Customer volume freenet TV | low | high | medium | |
| Termination charges | low | medium | low | |
| Laws and regulation | low | low | low | |
| Regulation EU-Roaming | low | immaterial | immaterial | |
| **IT risks** | low | medium | low | |
| Data theft and hacker attack | low | low | low | |
| **Tax risks** | | | | |
| Loss carryforwards | low | high | medium | |
| VAT risk on renumeration of a third party | low | medium | low | |
| Other tax risks | low | medium | low | |
| **Financial risks** | | | | |
| Bad debt losses | high | low | medium | |
| Impairment of the assets | low | high | medium | |
| Liquidity | | | | |
| General liquidity risk | low | high | medium | |
| Constraint of financial leeway | low | medium | low | |
| Capital risk management | low | high | medium | |
| Interest rate risk | medium | medium | medium | |
| Other financial risk | low | medium | low | |
| **Strategic risks** | | | | |
| Impact of earnings Sunrise | low | medium | low | |
| Customer development EXARING | medium | medium | medium | |
| Cost development EXARING | medium | medium | medium | |

Classification in higher risk class compared to previous report
Classification in same risk class compared to previous report or newly registered risk
Classification in same risk class compared to previous report or newly registered risk

Thanks to the risk management process that has been implemented and the monthly reporting system, the Executive Board has a good overall view of the risk situation presented here. Individual risks have changed only slightly compared with the previous year as far as their probability of occurrence or their impact are concerned. All in all, it can be assumed that the risks have no impact on the continued existence of freenet AG. The Executive Board is convinced that if the risk management approach used to date is continued, freenet AG will again be in a position to identify relevant risks in a timely manner and initiate suitable countermeasures to tackle them in the coming financial year.

Market, IT, tax as well as financial risks were identified as of 31 December 2016. Their potential effects on the general future development of freenet AG and its financial and non-financial performance indicators are classified by the management in overall terms as low. The management is therefore expecting that the positive trend forecast will not be compromised significantly as a result of the aforementioned risks.

## Key features of the internal control and risk management system in relation to the Group accounting process (section 315 (2) no. 5 HGB))

### Definition and elements of the freenet Group's internal control system

freenet AG's internal control system follows the internationally recognised COSO ("Committee of Sponsoring Organisations of the Treadway Commission") framework. It comprises all processes and measures to secure effective, cost-effective and proper accounting, in particular to ensure compliance with the pertinent legal provisions.

freenet AG's Executive Board has instructed all areas of the Group to manage their monitoring and control processes in accordance with standardised principles.

The departments analyse their processes continuously, also with regard to new legal requirements and other standards to be observed, develop internal standards based on the above and train the responsible employees.

The key elements of freenet AG's internal control system are based on automated IT control processes with alarm thresholds on the one hand, and on manual process controls to check the plausibility of the automatically aggregated results on the other. The risk management system is linked to the internal control system and covers not only operational risk management, but also the systematic early identification, control and monitoring of risks throughout the Group. For further explanatory notes about the risk management system, please refer to the "Risk management system" section of the risk report.

### Structure of the Group accounting process

The accounting processes for the individual financial statements of freenet AG's subsidiaries are basically recorded by local accounting systems manufactured by SAP. freenet AG uses SAP's "EC-CS" ("SAP EC-CS") module as its consolidation system at the ultimate Group level. For the preparation of the consolidated balance sheet, the consolidated income statement, the consolidated statement of cash flows, and the consolidation of the capital, debt, and expenses and income, etc., the data reported by the subsidiaries is entered into the consolidation system in a variety of ways — mostly automatically using the SAP module "FI" ("SAP-FI"), and in isolated cases also manually by entering the reported data. The individual disclosures in the Group management report and the notes to the consolidated financial statements are each generated from standardised reporting packages and institutionalised coordination processes as part of the internal control system; these processes are handled using Microsoft Excel ("MS Excel") among others. The aforementioned information for the notes, too, is consolidated using MS Excel.

freenet AG's Group internal auditing department reviews the accuracy and access authorisations of the SAP EC-CS consolidation system at regular intervals. freenet AG's Group auditor regularly inspects the interface between SAP-FI and the consolidation system SAP EC-CS, as well as the reconciliation from the subsidiaries' standardised reporting packages and freenet AG's consolidated financial statements.

### Key regulatory and controlling activities to ensure proper and reliable Group accounting

The internal control activities aimed at achieving proper and reliable Group accounting ensure that business transactions are recorded fully, in good time and in accordance with the statutory provisions and the articles of association.

The regular elements in the Group's internal control system are aimed at achieving the extensive automation of the formation and cross-checking of all relevant data, from raw accounting data and customer invoicing to valuation allowances, accruals, depreciation and amortisation. These automated controls are supplemented by manual plausibility checks of all relevant interim results and random checks of the underlying detailed data. This ensures proper inventory management and the accurate recognition, measurement and disclosure of assets and liabilities in the consolidated financial statements. In addition to this, there are extraordinary control elements including process independent reviews by freenet

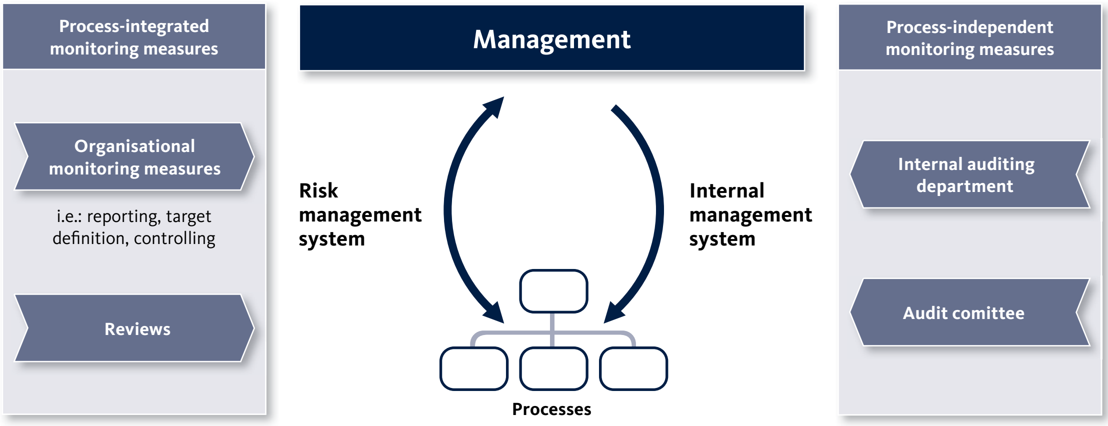
AG's internal Group audit department on behalf of the Supervisory Board, in particular under the supervision of freenet AG's Supervisory Board audit committee.

The Group internal audit department's annual review of the internal control system in 2016 showed that potential improvements ascertained in the departments audited in previous years have been implemented. On the one hand, the department has intensified its proven controlling activities continuously and increased the frequency of internal audits, and on the other hand, it has increased the level of automation within the controlling activities. The results are used to systematically derive measures and monitor their success.

The Group auditor and other review bodies are likewise involved in freenet AG's control environment with process-independent review activities.

The audit of consolidated financial statements by the Group auditor and the audit of the individual financial statements from Group companies included in the consolidated financial statements, in particular, constitute the final non-process-related monitoring measure with regard to Group accounting.

Figure 12: **Key features of the internal control system at freenet AG**



# CORPORATE GOVERNANCE

In this section, the Executive Board and Supervisory Board report on the Corporate Governance in the freenet Group in accordance with clause 3.10 of the German Corporate Governance Code. The chapter also contains the statement concerning corporate management in accordance with Sections 289a, 315 (5) HGB as well as the information relating to takeover law in accordance with Sections 289 (4), 315 (4) HGB.

freenet AG and its management and supervisory bodies are committed to the principles of good and responsible corporate management; they identify with the objectives of the German Corporate Governance Code and with the principles of transparent, responsible and value-appreciation-oriented management and supervision for the company. The Executive Board and the Supervisory Board, together with all managers and employees in the freenet Group, are obliged to pursue these objectives.

In its meeting on 8 December 2016, the Supervisory Board considered the regulations of the German Corporate Governance Code and, together with Executive Board, issued the annual statement of compliance with regard to the German Corporate Governance Code. The Code Commission did not revise the contents of the code in 2016, but announced an update for 2017. The Supervisory Board and Executive Board continued the stated differences and the related reasons from the previous years. The declaration of compliance from 8 December 2016 is included in the following corporate management statement and has been made permanently accessible on the company's website.

## Corporate management statement

In the corporate management statement in accordance with sections 289a, 315 (5) HGB, freenet AG displays its current declaration of compliance in accordance with section 161 of the German Stock Corporation Act (AktG) and explains the relevant disclosures about corporate management practices that are applied over and above the statutory provisions. In addition, the working methods of the Executive and Supervisory Boards are described and the composition and working methods of the Supervisory Board's committees are disclosed. Also to be found in the following are the information regarding the percentage of women in the Executive Board and in the two management tiers below the level of the Executive Board, as well as information regarding compliance with minimum percentages of women on the Supervisory Board.

freenet AG made the following corporate management statement in accordance with sections 289a, 315 (5) HGB which is simultaneously a part of its management report for the financial year 2016.

### Declaration in accordance with section 161 AktG

Since submitting the last declaration of compliance on 8 December 2016, freenet AG has complied with the recommendations of the German Corporate Governance Code ("Code") in the version of 5 May 2015 (subject to the following differences), and will continue to comply with the recommendations of the Code in the version of 5 May 2015, unless otherwise stated by the company in the following.

1. The company has taken out D&O insurance for its board members. No retention agreement has been signed with Supervisory Board members because it is not evident that this would represent an advantage for the company. It is taken for granted that all Supervisory Board members carry out their duties responsibly. In order to treat all the Supervisory Board members equally, moreover, any retention would have to be set at a uniform level, even though the members' personal financial backgrounds vary. A standard retention would therefore constitute different burdens for the individual Supervisory Board members. As their responsibilities are the same, this does not seem appropriate. (Code clause 3.8 (3))
2. The company has a strong commitment to transparent reporting. This also applies to the remuneration of the Executive Board members, the separate components of which are disclosed and discussed individually in the remuneration report. Nonetheless, the Executive Board and Supervisory Board have decided not to use the model tables in the remuneration report to depict the Executive Board's remuneration. Although the service contracts with the Executive Board members provide for caps, there is a risk that the disclosure of maximum amounts for share-based remuneration components creates an impression which is inconsistent with the actual assumptions for the performance of the share price. (Code clause 4.2.5 sentence 5 and 6)
3. The Supervisory Board considers the current Executive Board to be a success and is therefore striving for continuity on the Executive Board. In the opinion of the Supervisory Board, selection in accordance with the criteria for the composition of the Executive Board specified in Code point 5.1.2 (1) is of subordinate significance. (Code clause 5.1.2 (1))
4. No age limit has been set for members of the Executive Board and the Supervisory Board. It is not evident why qualified individuals with relevant professional and other experience should not be considered as candidates solely on the grounds of their age. (Code clause 5.1.2 sentence 8 and 5.4.1 sentence 2)
5. The Supervisory Board does not specify any concrete targets for its composition, as defined in clause 5.4.1 (2) and 5.4.2 sentence 1. It can therefore not follow the recommendations made in clause 5.4.1 (3). When proposing new members for election, the Supervisory Board has so far been guided solely by their suitability. The Supervisory Board is convinced that this has proven to be effective. It therefore sees no need to change the procedure. (Code clauses 5.4.1 (2), (3) and 5.4.2 sentence 1)
6. Clause 5.4.6 (2) of the Code recommends aligning performance-related pay for Supervisory Board members with the sustained performance of the company. The Supervisory Board's variable remuneration is set according to the dividend for the past financial year, in line with section 11 (5) of the company's articles of association. This form of variable remuneration has proven its worth in the past. Furthermore, the company's dividend policy as communicated to financial markets, which is based on free cash flow, is aligned with the company's sustained performance. Linking variable remuneration to this dividend strategy therefore also serves the company's sustained performance. For this reason, there is no intention of changing the Supervisory Board's variable remuneration. (Code clause 5.4.6 (2))

## Relevant disclosures on corporate management practices

freenet AG has a uniform compliance system that is continuously expanded and enhanced. The freenet Group's chief compliance officer ("CCO") reports directly to the Executive Board. He helps the Executive Board to highlight the legal requirements that are relevant for freenet AG and to implement them accordingly within the freenet Group, as well as to adapt the compliance system to changing requirements. The CCO also reports regularly to the Supervisory Board's audit committee. The CCO informs the Supervisory Board whenever risks arise which endanger the continued existence of the freenet Group.

The freenet Group is wholeheartedly committed to upholding the prevailing laws and statutes. For the freenet Group, compliance means that statutory provisions are adhered to, the Group's own rules and in-house guidelines are observed and criminal acts are prevented. The company does everything it can to ensure that violations of compliance, such as fraud, corruption and anti-competitive practices, do not arise in the first place. As soon as misconduct and infringements of compliance become evident, these are brought to light and tackled decisively.

The freenet Group's managers set a good example in upholding compliance and ensure that any significant steps taken within their own fields of responsibility are in accordance with the respective statutory provisions and our own values and rules.

The compliance organisation can be approached by any contact person for advice on individual issues.

The Compliance department has developed a whistle-blower tool and implemented it within the freenet Group. It enables whistle-blowers to give tip-offs anonymously whenever infringements of compliance come to their attention.

All tip-offs are investigated promptly as part of a transparent and accountable process in which the interests of the whistle-blower, the persons affected and the company are taken into account.

The aim is to enable the company to take systematic and appropriate action immediately when compliance is violated and thereby to avert damage to the freenet Group. In order to ensure the proper, swift handling of tip-offs in accordance with the whistle-blower process, the freenet Group has set up a whistle-blower committee. Permanent members of the whistle-blower committee are the CCO as well as the responsible head of internal auditing and the head of fraud management. The whistle-blower committee is responsible for the operational implementation of the whistle-blower process.

A centralised fraud management unit has also been set up. In addition to its coordinating function for the individual specialist fraud departments in the freenet Group, this unit is responsible in particular for the introduction and improvement of effective preventive measures and processes for preventing damage to the freenet Group caused by fraud.

The significance of data protection has increased continuously in recent years. The freenet Group is aware of its special responsibility with regard to the handling of the personal data of our customers, suppliers, contractual partners and employees. We therefore consider that it is important for these data to be protected against unauthorised access. For this reason, we use modern security technologies and regularly draw the attention of our employees to this subject in order to continuously improve the overall security level and to meet the challenges posed by the increasing threats.

## Working methods of the Executive Board and Supervisory Board

freenet AG's Executive Board and Supervisory Board work together in a close and trusting manner in their management and supervision of the company.

The Executive Board, as the parent company's management body, is obliged to serve the interests of the company and currently consists of three members. The Executive Board's work is governed by its rules of procedure. The members of the Executive Board are jointly responsible for corporate management as a whole. In other respects, each Executive Board member is responsible for his own sphere of business. The Executive Board members work together in a spirit of cooperation and inform one another in an ongoing fashion about facts and developments in their respective spheres of business at regular Executive Board meetings. In addition, the Executive Board members attend regular meetings of the specialist departments. As part of a distribution-of-business plan, the Supervisory Board determines the individual Executive Board members' areas of responsibility.

The Supervisory Board is convened at least twice in each calendar half-year. It generally makes its decisions at meetings requiring personal attendance, but also by way of telephone conferences or by written communications. The Supervisory Board regularly advises the Executive Board when the latter is making its decisions about the company's management and also supervises its management activities. The Executive Board includes the Supervisory Board in all decisions of a fundamental nature relating to the company's management and reports regularly about the business performance, the corporate planning, the strategic development and the situation of the company. The Supervisory Board conducts a detailed examination of all deviations of business performance from the plans and targets and discusses these with the Executive Board. It also conducts detailed checks on commercial transactions of significance for the company on the basis of Executive Board reports, takes counsel on such matters and makes decisions as and when required. Outside of the meetings, too, the Supervisory Board members were informed by the Executive Board about current business developments.

## Composition and working methods of committees

The Executive Board has not constituted any committees.

The Supervisory Board has constituted a steering committee and four other committees. These committees prepare the topics and resolutions of the Supervisory Board which are due to be discussed in the plenum and in some individual areas are authorised to make decisions in place of the plenum. The committees carry out their work in meetings requiring personal attendance. In exceptional cases, however, the meetings can also be conducted by telephone. The committees discuss the items on their agendas and make decisions concerning these if required. The committee chairpersons report on the subject matter of the committee meetings to the Supervisory Board's plenum. With the exception of the Nomination Committee, all committees comprise equal numbers of shareholders' representatives and employees' representatives.

### Steering committee

The steering committee discusses central themes and prepares Supervisory Board resolutions. It can take the place of the Supervisory Board, with the required approval of the Executive Board in accordance with the latter's rules of procedure, in deciding on measures and transactions of the Executive Board, insofar as the matter in question cannot be deferred and it is not possible for the Supervisory Board to make an appropriate decision within the time available.

Members: Dr Hartmut Schenk (Chairman), Prof Dr Helmut Thoma, Birgit Geffke, Knut Mackeprang

### Personnel committee

The personnel committee prepares the Supervisory Board's personnel decisions. It submits to the Supervisory Board proposals for decisions on the Executive Board's remuneration, the remuneration system and regular scrutiny of that system. The committee makes decisions in place of the Supervisory Board – but subject to mandatory responsibilities of the Supervisory Board – on Executive Board members' business that is relevant for personnel.

Members: Dr Hartmut Schenk (Chairman), Thorsten Kraemer, Claudia Anderleit, Birgit Geffke

### Audit committee

The audit committee concerns itself with the monitoring of the accounting process, the effectiveness of the internal control system, the risk management system and the internal auditing system, and financial statements auditing, in the latter case especially with regard to the auditor's independence and the additional services rendered by the auditor. It also concerns itself with compliance-related issues.

Members: Robert Weidinger (Chairman), Marc Tüngler, Ronny Minak, Michael Stephan

### Mediation committee

The mediation committee is constituted in accordance with section 27 (3) of the German Co-determination Act (MitbestG) so that it can perform the task described in section 31 (3) sentence 1 MitbestG.

Members: Dr Hartmut Schenk (Chairman), Thorsten Kraemer, Knut Mackeprang, Gesine Thomas

### Nomination committee

The nomination committee has the task of suggesting suitable candidates to the Supervisory Board for proposal to the Annual General Meeting in the run-up to new elections.

Members: Dr Hartmut Schenk (Chairman), Marc Tüngler, Sabine Christiansen

# Defined targets for the percentage of women in the Executive Board and in the two management tiers below the Executive Board; information on compliance with minimum percentages of women on the Supervisory Board

The Supervisory Board and Executive Board have each defined targets for the percentage of women in the Executive Board and in the two management tiers below the Executive Board:

| | Target |
|---|---|
| Executive Board | 0 per cent |
| Management tier 1 (direct reports) | 25 per cent |
| Management tier 2 (heads of department) | 27.5 per cent |

The deadline for attaining all specified targets was defined as 30 June 2017.

In the period under review, the percentages of men and women on the Supervisory Board complied with the legal requirements regarding the minimum percentages.



# Information required under takeover law according to sections 289 (4), 315 (4) HGB

## Composition of the subscribed capital

The subscribed capital (capital stock) of freenet AG amounts to 128,061,016 euros. It is divided up into the same number of no-par-value registered shares. Each share entitles its owner to one vote at the Annual General Meeting.

## Restriction on share transfer or voting rights

The Executive Board is not aware of any restrictions affecting the voting rights or the transferring of shares.

## Equity participations exceeding 10 per cent of the voting rights

As of 31 December 2016, on the basis of the existing notifications of voting rights in accordance with Sections 21 et seqq. WpHG, there were no capital holdings in freenet AG which exceeded 10 per cent of the overall voting rights.

## Shares with special rights and controlling powers

There are no shares with special rights that confer controlling powers.

## Type of voting rights control when employees hold an interest in share capital

If employees have an interest in the company's capital as shareholders, they cannot derive any special rights from this.

## Appointment and dismissal of the members of the Executive Board, changes in the articles of association

The appointment and dismissal of the members of freenet AG's Executive Board shall be governed by sections 84 and 85 AktG and section 31 MitbestG in conjunction with section 5 (1) of the articles of association. The relevant provisions governing changes to the articles of association are sections 133 and 179 AktG and section 16 of freenet AG's articles of association.

## Powers of the Executive Board to issue shares

The Executive Board, with the approval of the Supervisory Board, is authorised by a resolution of the Annual General Meeting of 23 May 2013 to increase the capital stock by issuing new shares against contributions in cash or kind up to a maximum sum of 12,800,000.00 euros until 5 June 2018 (authorised capital 2013).

The Executive Board, with the approval of the Supervisory Board, is also authorised by a resolution of the Annual General Meeting of 12 May 2016 to increase the capital stock by issuing new shares against contributions in cash or kind up to a maximum sum of 12,800,000.00 euros until 1 June 2021 (authorised capital 2016).

In addition, on 12 May 2016, the annual general meeting adopted a resolution regarding a conditional capital increase involving up to a total of 12,800,000.00 euros, consisting of 12,800,000 new no-par registered ordinary shares (conditional capital 2016). The purpose of the conditional capital increase is to enable no-par-value bearer shares to be granted to the holders or creditors of convertible and/or option bonds which are issued on the basis of the authorisation as adopted by the Annual General Meeting of 12 May 2016 under agenda item 10, letter A) and which provides a conversion or option right in relation to the no-par-value registered shares of the company or which establishes a conversion or option obligation in relation to these shares. The Executive Board is authorised to stipulate all further details pertaining to the implementation of a conditional capital increase.

## Powers of the Executive Board to repurchase shares

Pursuant to the resolution of the annual general meeting of 12 May 2016, the Executive Board was authorised, until 11 May 2021, to acquire treasury shares equivalent to up to 10 per cent of the current share capital or – if lower – 10 per cent of the share capital existing at the point at which the authorisation is exercised. This authorisation can be exercised by the company, by its subsidiaries, or by third parties for the account of the company or for the account of its subsidiaries. Acquisition of such stock shall be carried out at the discretion of the Executive Board through the stock market, by way of a public offer of purchase, through a public invitation to submit offers for sale, by issuing tender rights to the shareholders or by using equity derivatives (put or call options or a combination of the two). There is also the possibility of purchasing treasury shares in accordance with sections 71 et seq. AktG.

## Change of control

A change of control might have an impact on the repayment claims resulting from the syndicated loan agreement between the freenet Group and a syndicate of banks as well as the borrower's note loan issued by freenet AG. In such a case, these loans might be called in either in part or in their entirety without freenet being able to influence such a move. Such a change of control, irrespective of whether it precedes the take-over offer, might exist in the event of the acquisition of more than 50 per cent of the voting rights in freenet AG or if one or more jointly acting persons have the right to determine the majority of members of the Supervisory Board of freenet AG. In such a case, freenet would be exposed to the risk that subsequent financing for settling the repayment claims might not be agreed or might only be agreed subject to less favourable conditions.

## Compensation agreements of the company

There exist no remuneration agreements of the company between members of the Executive Board and employees to cover the case of a take-over bid.

## Declaration in accordance with section 289 a HGB

The declaration in accordance with section 289a HGB is published on the company's website at www.freenet-group.de/en in the Investor Relations/Corporate Governance section.

# Compensation report for the Executive Board and Supervisory Board

## Executive Board compensation in accordance with HGB

The remuneration paid to the members of the Executive Board consists of annual fixed remuneration, annual variable remuneration, and variable remuneration with a long-term incentive effect. There are also pension commitments. The annual variable remuneration amounts each result from an annual agreement on objectives in which regularly determined figures indicating the freenet Group's significant financial and non-financial performance indicators are defined as individual objectives. In the financial year 2011, a remuneration programme with a long-term incentive effect, known as the "LTIP programme" ("LTIP programme 1") was set up for the members of the Executive Board. The LTIP programme 1 was terminated on 31 December 2015 as a result of payment. On 26 February 2014, agreements were concluded with the members of the Executive Board regarding the service agreements which grant new LTIP ("LTIP programme 2").

In LTIP programme 2, an LTIP account is maintained for each member of the Executive Board; in each financial year, depending on the extent to which defined objectives for the financial year in question have been attained, credit or debit entries are made in the accounts in the form of virtual shares. Then, within a predetermined period of time, cash payouts less taxes and charges can be made for each financial year, depending on the balance in the respective LTIP account. The magnitude of these payments is dependent on various factors, including the relevant share price at the time of the payout.

The remuneration for the members of the company's Executive Board was broken down as follows in the reporting year and the preceding year; the tables used show the Executive Board remuneration as defined in section 314 (1) no. 6a HGB in conjunction with DRS 17. These figures include the remuneration paid in the course of the financial year. In accordance with section 314 (1) no. 6a HGB, changes in the value of the LTIP programmes that were not caused by a change in the exercise conditions are not disclosed.



Table 18: **Executive Board Compensation for financial year 2016 according to HGB**

| In EUR '000s | Fixed compensation | Variable cash compensation | Total cash compensation | Granted compensation with long-term incentive effect | Total compensation in accordance with HGB[1] |
|---|---|---|---|---|---|
| Christoph Vilanek | 765 | 613 | 1,378 | 0 | 1,378 |
| Joachim Preisig | 544 | 491 | 1,035 | 0 | 1,035 |
| Stephan Esch | 492 | 245 | 737 | 0 | 737 |
| **Total** | **1,801** | **1,349** | **3,150** | **0** | **3,150** |

Table 19: **Executive Board Compensation for financial year 2015 according to HGB**

| In EUR '000s | Fixed compensation | Variable cash compensation | Total cash compensation | Granted compensation with long-term incentive effect | Total compensation in accordance with HGB[1] |
|---|---|---|---|---|---|
| Christoph Vilanek | 765 | 639 | 1,404 | 0 | 1,404 |
| Joachm Preisig | 544 | 512 | 1,056 | 0 | 1,056 |
| Stephan Esch | 492 | 256 | 748 | 0 | 748 |
| **Total** | **1,801** | **1,407** | **3,208** | **0** | **3,208** |

In the financial year 2016, the Executive Board remuneration in accordance with section 314 (1) no. 6a HGB amounted to 3,150 thousand euros (previous year: 3,208 thousand euros). The totals for 2015 and 2016 contain no remuneration with long-term incentive effect; as such components had already been disclosed in the financial years in which the remuneration instruments had been granted.

1 The total amount of compensation in the above table does not include the benefit costs of 669 thousand euros (previous year: 662 thousand euros). Please refer to the following explanations.

In the financial year 2016, there were no cash payments resulting from the LTIP programme 2. In the financial year 2015, the LTIP programmes had resulted in cash payments totalling 2,324 thousand euros, namely 0 euros to Mr. Vilanek, 1,603 thousand euros to Mr. Preisig and 721 thousand euros to Mr. Esch. In the previous year, the cash payments to Mr. Preisig and Mr. Esch completely terminated their LTIP programme 1 (target attainment years 2011 to 2014). As of the balance sheet date 31 December 2016, all three members of the Executive Board were included in LTIP programme 2 – with the target attainment years 2014 to 2018 for Mr Vilanek and 2015 to 2019 for Mr Preisig and Mr Esch.

As of 31 December 2016, the value of the provision under HGB for LTIP programme 2 for Mr. Vilanek was 3,473 thousand euros (previous year: 2,347 thousand euros); the value for Mr. Preisig was 1,159 thousand euros (previous year: 571 thousand euros), and the value for Mr. Esch was 773 thousand euros (previous year: 381 thousand euros).

In November 2004, Mr Esch was granted an indirect pension commitment. In the financial year 2009, Mr Vilanek was granted an indirect pension commitment on the occasion of his appointment as chairman of the Executive Board as at 1 May 2009. freenet AG had taken on the pension commitment granted to Mr Preisig from the former debitel AG as at 1 September 2008. In February 2014, adjustments were made to all three Executive Board members' pension commitments. For further details, see the section "Remuneration rules in the event of a cessation of employment".

As at 31 December 2016, the defined benefit obligation (DBO) relating to commercial law for Mr Vilanek amounted to 2,201 thousand euros (previous year: 1,909 thousand euros), the DBO for Mr Preisig totalled 2,681 thousand euros (previous year: 2,424 thousand euros) and Mr Esch's DBO came to 2,045 thousand euros (previous year: 1,874 thousand euros). The obligation amount for Messrs Spoerr, Krieger and Berger, as former Executive Board members, totalled 5,429 thousand euros as at 31 December 2016 (previous year: 5,384 thousand euros).

Current service time expenses of 669 thousand euros (previous year: 662 thousand euros) were recognised in total in personnel expenses for the members of the Executive Board as a result of the pension commitments. Of these, 284 thousand euros for 2016 (previous year: 282 thousand euros) were accounted for by Mr Vilanek, 222 thousand euros (previous year: 219 thousand euros) by Mr Preisig and 163 thousand euros (previous year: 161 thousand euros) by Mr Esch.

As was the case in the previous year, in 2016, the personnel expenses for the members of the Executive Board related to the pension commitments did not include any past service costs.

No loans were extended to any of the Executive Board members and no guarantees or other warranties were provided for the Executive Board members.

## Executive Board compensation in accordance with DCGK

Within the meaning of clause 4.2.5 of the German Corporate Governance Code (DCGK), we hereby make the following disclosures about the remuneration awarded to the members of the Executive Board for the financial year 2016 and the previous year, and about the remuneration from actual payments to the members of the Executive Board in the financial year 2016 and the previous year.

Table 20: **Compensation awarded to the Executive Board for the financial year 2016 in accordance with DCGK**

| In EUR`000s | Christoph Vilanek | Joachim Preisig | Stephan Esch | Total |
|---|---|---|---|---|
| Fixed compensation | 750 | 530 | 480 | 1,760 |
| Fringe benefits | 15 | 14 | 12 | 41 |
| **Total** | **765** | **544** | **492** | **1,801** |
| | | | | |
| Annual variable compensation | 500 | 400 | 200 | 1,100 |
| Perennial variable compensation | | | | |
| LTIP-programme 1 | 0 | 0 | 0 | 0 |
| LTIP-programme 2 | 1,169 | 559 | 373 | 2,101 |
| **Total** | **1,669** | **959** | **573** | **3,201** |
| | | | | |
| Pension expense | | | | |
| Current service cost | 391 | 285 | 227 | 903 |
| Past service cost | 0 | 0 | 0 | 0 |
| **Total** | **391** | **285** | **227** | **903** |
| | | | | |
| **Total compensation** | **2,825** | **1,788** | **1,292** | **5,905** |

Table 21: **Compensation awarded to the Executive Board for the financial year 2015 in accordance with DCGK**

| In EUR`000s | Christoph Vilanek | Joachim Preisig | Stephan Esch | Total |
|---|---|---|---|---|
| Fixed compensation | 750 | 530 | 480 | 1,760 |
| Fringe benefits | 15 | 14 | 12 | 41 |
| **Total** | **765** | **544** | **492** | **1,801** |
| | | | | |
| Annual variable compensation | 500 | 400 | 200 | 1,100 |
| Perennial variable compensation | | | | |
| LTIP-programme 1 | 0 | 52 | 23 | 75 |
| LTIP-programme 2 | 1,348 | 559 | 373 | 2,280 |
| **Total** | **1,848** | **1,011** | **596** | **3,455** |
| | | | | |
| Pension expense | | | | |
| Current service cost | 446 | 314 | 260 | 1,020 |
| Past service cost | 0 | 0 | 0 | 0 |
| **Total** | **446** | **314** | **260** | **1,020** |
| | | | | |
| **Total compensation** | **3,059** | **1,869** | **1,348** | **6,276** |

Table 22: **Compensation from actual payments to the Executive Board in the financial year 2016 in accordance with DCGK**

| In EUR`000s | Christoph Vilanek | Joachim Preisig | Stephan Esch | Total |
|---|---|---|---|---|
| Fixed compensation | 750 | 530 | 480 | 1,760 |
| Fringe benefits | 15 | 14 | 12 | 41 |
| **Total** | **765** | **544** | **492** | **1,801** |
| | | | | |
| Annual variable compensation | 613 | 491 | 245 | 1,349 |
| Perennial variable compensation | | | | |
| LTIP-programme 1 | 0 | 0 | 0 | 0 |
| LTIP-programme 2 | 0 | 0 | 0 | 0 |
| **Total** | **613** | **491** | **245** | **1,349** |
| | | | | |
| Pension expense | | | | |
| Current service cost | 391 | 285 | 227 | 903 |
| Past service cost | 0 | 0 | 0 | 0 |
| **Total** | **391** | **285** | **227** | **903** |
| | | | | |
| **Total compensation** | **1,769** | **1,320** | **964** | **4,053** |

Table 23: **Compensation from actual payments to the Executive Board in the financial year 2015 in accordance with DCGK**

| In EUR`000s | Christoph Vilanek | Joachim Preisig | Stephan Esch | Summe |
|---|---|---|---|---|
| Fixed compensation | 750 | 530 | 480 | 1,760 |
| Fringe benefits | 15 | 14 | 12 | 41 |
| **Total** | **765** | **544** | **492** | **1,801** |
| | | | | |
| Annual variable compensation | 639 | 512 | 256 | 1,407 |
| Perennial variable compensation | | | | |
| LTIP-programme 1 | 0 | 1,603 | 721 | 2,324 |
| LTIP-programme 2 | 0 | 0 | 0 | 0 |
| **Total** | **639** | **2,115** | **977** | **3,731** |
| | | | | |
| Pension expense | | | | |
| Current service cost | 446 | 314 | 260 | 1,020 |
| Past service cost | 0 | 0 | 0 | 0 |
| **Total** | **446** | **314** | **260** | **1,020** |
| | | | | |
| **Total compensation** | **1,850** | **2,973** | **1,729** | **6,552** |

## Compensation rules in the event of a cessation of employment

Compensation provisions in the event of premature termination of employment contracts and pension plans are as follows:

Arrangements for the former Executive Board members Eckhard Spoerr, Axel Krieger and Eric Berger:

- From their 60th birthday, the abovementioned members of the Executive Board shall receive a pension amounting to 2.5 per cent of final annual fixed salary for each year commenced on the Executive Board of the company or its legal predecessor freenet.de AG, to a maximum of one-third of final annual fixed salary (guaranteed pension).
- Surviving dependant pension for the spouse or life companion and orphan's pension for any children until the end of schooling or vocational training,

terminating at the latest when they reach the age of 27, to a maximum total amount of the guaranteed pension.

For the Chief Executive Officer Christoph Vilanek, the following rules apply from 1 January 2014:

- From his 60th birthday, Mr Vilanek shall receive a pension amounting to 2.7 per cent of final annual fixed salary for each contractual year commenced on the Executive Board of the company, to a maximum of one-third of final annual fixed salary (target pension).
- Surviving dependant pension for the spouse or life companion, and orphan's pension for any children until the end of their schooling or vocational training, terminating at the latest when they reach the age of 27, to a maximum total amount of the guaranteed pension or the value of pension entitlements Mr Vilanek would obtain if he were to die.
- A five-year target agreement was signed. If the service contract ends due to expiry of term, termination, cancellation or otherwise, or his appointment to the position is revoked, Mr Vilanek can claim for payout of the Long-Term Incentive Account at the time of termination, provided it shows a positive balance. Provided that the termination of the service contract on the part of the company is not for good cause pursuant to clause 626 BGB, or that the revocation of his appointment to the position does not form part of the termination of the service contract on the part of the company, for which there is good cause under clause 626 BGB, the number of virtual shares in the Long Term Incentive Account is added to the number of shares that result from the Group EBITDA for the current financial year.

The following rules have applied for Executive Board member Stephan Esch since 1 January 2015 (agreement dated 26 February 2014):

- From his 60th birthday, Mr Esch shall receive a pension amounting to 2.5 per cent of final annual fixed salary for each contractual year commenced on the Executive Board of the company or its legal predecessor freenet.de AG, to a maximum of 40 per cent of final annual fixed salary (guaranteed pension).
- Surviving dependant pension for the spouse or life companion and orphan's pension for any children until the end of schooling or vocational training, terminating at the latest when they reach the age of 27, to a maximum total amount of the guaranteed pension.
- A five-year target agreement was signed. If the service contract ends due to expiry of term, termination, cancellation or otherwise, or his appointment to the position is revoked, Mr Esch can claim for payout of the Long-Term Incentive Account at the time of termination, provided it shows a positive balance. Provided that the termination of the service contract on the part of the company is not for good cause pursuant to clause 626 BGB, or that the revocation of his appointment to the position does not form part of the termination of the service contract on the part of the company, for which there is good cause under clause 626 BGB, the number of virtual shares in the Long Term Incentive Account is added to the number of shares that result from the Group EBITDA for the current financial year.

The following rules have applied for Executive Board member Joachim Preisig since 1 January 2015 (agreement dated 26 February 2014):

- On reaching the age of 60, Mr Preisig shall receive a retirement pension in the amount of 2.5 per cent of his last annual fixed salary for each year of his Executive Board duties or part thereof for the company, and/or previously at former debitel AG, but no more than one-third of the last annual fixed salary (guaranteed pension).
- Surviving dependant pension for the spouse or life companion and orphan's pension for any children until the end of schooling or vocational training, terminating at the latest when they reach the age of 27, to a maximum total amount of the guaranteed pension.
- Upon his departure on reaching the age of 60, Mr Preisig shall receive a retirement pension amounting to 9,333.0 euros (monthly retirement pension commitment) from the debitel pension fund. If he leaves early, Mr Preisig shall receive a pension, after reaching the age of 60 and once the conditions prerequisite to non-forfeiture arise, which is calculated according to legal requirements; the guaranteed pension is calculated on a pro rata basis in line with the actual length of service. All claims of Mr Preisig, his spouse or a domestic partner with rights as beneficiary, and any surviving dependants from the debitel pension fund shall be offset against all aforementioned claims arising from the current contract of employment.
- A five-year target agreement was signed. If the service contract ends due to expiry of term, termination, cancellation or otherwise, or his

appointment to the position is revoked, Mr Preisig can claim for payout of the Long-Term Incentive Account at the time of termination, provided it shows a positive balance. Provided that the termination of the service contract on the part of the company is not for good cause pursuant to clause 626 BGB, or that the revocation of his appointment to the position does not form part of the termination of the service contract on the part of the company, for which there is good cause under clause 626 BGB, the number of virtual shares in the Long Term Incentive Account is added to the number of shares that result from the Group EBITDA for the current financial year.

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

## Compensation of the Supervisory Board

The Supervisory Board compensation is governed by the articles of association, and consists of three components:

- Basic compensation
- Attendance fees
- Performance-linked compensation.

The Supervisory Board's members receive from the company fixed basic compensation of 30,000 euros for each full financial year of their Supervisory Board membership.

The chairperson of the Supervisory Board receives double this amount, the vice chairperson one-and-a-half times this amount.

In addition, every Supervisory Board member receives an attendance fee of 1,000 euros for each Supervisory Board meeting that he/she attends. Supervisory Board members who belong to a Supervisory Board committee – with the exception of the committee constituted in accordance with section 27 (3) of the German Co-determination Act (Mitbestimmungsgesetz) – receive in addition an attendance fee of 1,000 euros for each meeting of the respective committee that they attend. The committee chairperson receives double this amount.

Within the framework of a voluntary restriction imposed on its own activities, the Supervisory Board has decided that no compensation shall be payable for participation in telephone meetings of the Supervisory Board or its committees or for participation by telephone in meetings requiring physical attendance.

After the end of each financial year, the Supervisory Board's members also receive variable, performance-linked compensation in the amount of 500 euros for each 0.01 euro dividend in excess of 0.10 euro per no-par-value share in the company which is distributed to shareholders for the financial year ended. The amount of the compensation is limited to that 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 activities during the financial year 2016, the members of the company's Supervisory Board received fixed compensation of 405 thousand euros plus attendance fees amounting to 60 thousand euros. In addition, profit-linked compensation of 405 thousand euros was also recorded as a cost. The extent to which this performance-based compensation will indeed be paid out depends on the profit appropriation resolution for the financial year 2016. The aggregate compensation paid for Supervisory Board activities thereby amounted to 870 thousand euros.

Furthermore, Supervisory Board members are reimbursed for expenses incurred in connection with the performance of their official duties, as well as for value added tax.

No loans were extended to any of the Supervisory Board members and no guarantees or other warranties were provided for the Supervisory Board members.

Individualised 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 sum totals; this is because the figures have been rounded to one position after the decimal point.

Table 24: **Compensation for financial year 2016**

| In EUR `000s | Basic compensation | Attendance fee | Performance-based compensation | Total |
|---|---|---|---|---|
| **Active members** | | | | |
| Dr Hartmut Schenk | 60.0 | 7.0 | 60.0 | 127.0 |
| Knut Mackeprang[1] | 45.0 | 3.0 | 45.0 | 93.0 |
| Claudia Anderleit[1] | 30.0 | 3.0 | 30.0 | 63.0 |
| Birgit Geffke[1] | 30.0 | 2.0 | 30.0 | 62.0 |
| Thorsten Kraemer | 30.0 | 4.0 | 30.0 | 64.0 |
| Ronny Minak[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Michael Stephan[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Prof Dr Helmut Thoma | 30.0 | 3.0 | 30.0 | 63.0 |
| Gesine Thomas[1] | 30.0 | 2.0 | 30.0 | 62.0 |
| Marc Tüngler | 30.0 | 8.0 | 30.0 | 68.0 |
| Robert Weidinger | 30.0 | 11.0 | 30.0 | 71.0 |
| Sabine Christiansen | 30.0 | 3.0 | 30.0 | 63.0 |
| **Total** | **405.0** | **60.0** | **405.0** | **870.0** |

Table 25: **Compensation for financial year 2015**

| In EUR `000s | Basic compensation | Attendance fee | Performance-based compensation | Total |
|---|---|---|---|---|
| **Active members** | | | | |
| Dr Hartmut Schenk | 60.0 | 14.0 | 60.0 | 134.0 |
| Knut Mackeprang[1] | 45.0 | 5.0 | 45.0 | 95.0 |
| Claudia Anderleit[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Birgit Geffke[1] | 30.0 | 9.0 | 30.0 | 69.0 |
| Thorsten Kraemer | 30.0 | 7.0 | 30.0 | 67.0 |
| Ronny Minak[1] | 30.0 | 8.0 | 30.0 | 68.0 |
| Michael Stephan[1] | 30.0 | 8.0 | 30.0 | 68.0 |
| Prof Dr Helmut Thoma | 30.0 | 5.0 | 30.0 | 65.0 |
| Gesine Thomas[1] | 30.0 | 4.0 | 30.0 | 64.0 |
| Marc Tüngler | 30.0 | 8.0 | 30.0 | 68.0 |
| Robert Weidinger | 30.0 | 12.0 | 30.0 | 72.0 |
| Sabine Christiansen | 25.5 | 3.0 | 25.6 | 54.1 |
| | **400.5** | **90.0** | **400.6** | **891.1** |
| **Former members** | | | | |
| Achim Weiss | 2.5 | 0.0 | 2.5 | 5.0 |
| **Total** | **403.0** | **90.0** | **403.1** | **896.1** |

1 Employee representative in accordance with section 7 (1) clause 1 no. 1 MitbestG of 4 May 1976.

# FORECAST

## The market in 2017

According to the IMF, the global economy will recover somewhat in 2017, and will achieve growth of approximately 3.4 per cent, following 3.1 per cent in 2016. In its world economic outlook, the OECD is somewhat more moderate, predicting growth of 3.3 per cent for global GDP for the year 2017. According to the IMF, the main drivers behind global economic growth in 2017 will be the improved economic prospects in China and the United States of America. For both economies, the IMF has now upgraded its expectations for growth compared with the October forecast. With regard to the USA, the IMF pointed to the expectations of the financial markets, which are hoping that the new political direction of President Donald J. Trump will have a range of positive effects, including tax cuts, higher infrastructure spending as well as higher payments into the defence budget. In this connection, the IMF is also somewhat more optimistic with regard to the growth prospects for the advanced economies; however, at the same time, it issued warnings with regard to growing protectionism and the possible impact of US policy on emerging markets and developing countries.

For the euro zone, the IMF and OECD are predicting growth of 1.6 per cent for economic output in the year 2017, compared with 1.7 per cent in the year 2016. For Germany, the IMF's prediction for growth in 2017 amounts to 1.5 per cent, which is slightly lower than the above level. The Deutsche Bundesbank is somewhat more optimistic with regard to the economic development 2017 in Germany. In its monthly report of December 2016, it forecasts growth of 1.8 per cent for German GDP in 2017. The main reason for this sound upswing in 2017 will again be the domestic economy, which is benefitting from various factors, including the favourable labour market situation and rising private household incomes.

Against the backdrop of a domestic economy which continues to be strong, the VATM and Dialog Consult expect to see total revenue in the telecommunications market increase by between 1.5 per cent and 3.0 per cent, with stable prices for landline and slightly lower prices for mobile communications. According to the British investment Bank HSBC, the German mobile communications market continues to be intact, and will continue to report growth in the course of the next few years, also as a result of the acceleration in mobile data use. According to HSBC, the increasing volume of data traffic as well as the further development of the technological mobile communications standard in the direction of 5G will however involve higher costs and an increased level of investment for the market players. With regard to the refinancing of imminent investments, particularly in network infrastructures, new tariff and price structures are becoming more significant. In January of last year, the consultant company Deloitte forecast a reversal of the trend in mobile communication prices for the year 2016, indicating initial price increases last year, particularly in the discount market. Deloitte arrived at this assessment as a result of the increasing willingness of consumers to pay for higher speed networks and larger data packages. A further catalyst for the turnaround in prices is considered to be the rising number of networked mobile devices as well as the increasing popularity of OTT and audio or video streaming services.

An essential requirement for high-quality broadcasting of individual content is a modern data infrastructure capable of meeting future challenges – both in terms of the mobile communications networks and also in the broadband field. In this connection, the German government has defined the clear objective of ensuring nation-wide broadband coverage throughout Germany with min. 50 Mbps by the year 2018. The German government is already subsidising the expansion of broadband with approximately 3.3 billion euros. This is accompanied by approximately 625 million euros of the federal states from the so-called digital dividend 2. According to information of the Federal Ministry for the Economy and Energy, this has meant that it has been possible for more than one million households so far to be connected to the high-speed Internet, representing a further important step in the direction of digitising the economy and society.

This digital change is also reflected in the harmonising of the submarkets landline, mobile communications and TV. On the consumer side, this is reflected in the increasing demand for products and applications relating to the Internet of Things or the digitally networked private home. The telecommunication providers are responding to these developments to a greater extent with the implementation of new business models in order to participate in the growth of these new market segments.

According to a Statista survey of August 2016, 84 per cent of the surveyed 18- to 29-year-olds consider that networked living and smart-home products are very interesting or interesting, and the corresponding figure for the 30- to 39-year-olds is 67 per cent. For the older generation of between 40- and 59-year-olds, this figure is only approximately 50 per cent. According to the Statista survey, 48 per cent of the users of such applications spent between 500 and 5,000 euros during the past 12 months for home networking products; these are mainly consumer electronic products. According to Deloitte analyses, the number of smart-home households in Germany is rising rapidly. According to these analyses, one million households are expected to feature smart networking in 2018, subject to optimum conditions. In an unfavourable climate, the one-million threshold would be exceeded in 2020. With regard to the devices, Deloitte is assuming that approximately 100 million corresponding networked devices will be used in Germany by 2020. These include wearables, network audio hardware, smart-home components and connected cars and in particular networked TV screens.

Overall, the TV screen is still the preferred device for the reception of film and video services. With the increasing distribution of networked TVs, there is also an increase in the consumption of IPTV and pay-TV services, in which motion pictures are transmitted via the Internet protocol onto the TV. According to PwC, the dynamic development in the pay-TV field is the main reason behind the strong growth in TV subscription services. The revenue from subscriptions for cable, satellite, IPTV and pay-TV services are accordingly expected to rise from 4.7 billion euros in 2016 to 5.3 billion euros in the year 2020. This is equivalent to an average growth rate of 3.3 per cent. Overall, in the opinion of PwC, the German TV market will continue to report a positive development, with an average growth rate of 1.8 per cent per annum. The total revenues in the TV market will accordingly rise from 14.6 billion euros in 2016 to 14.8 billion euros in 2017, and will amount to 15.6 billion euros in the year 2020.

In summary, the following assumptions in particular are seen as material for the derivation of forecasts for the freenet Group:

- Saturated mobile communications market in Germany, with a declining market volume in 2016, limited growth potential and mixed price development
- High growth rates in new market segments relating to digital lifestyle, the Internet of Things and in the German TV market, particularly in the field of subscription services
- Increased consumption and payment propensity of private households, particularly for products and applications in the field of the digital home.

# freenet Group

As an independent provider of mobile communication services in Germany, the freenet Group is operating in a saturated market. The cumulative market volume which has been contracting slightly recently, the fierce level of competition as well as the continuing consolidation pressure on providers mean that the sector is increasingly having to face challenges.

The freenet Group continues to combat these challenges with its strategic focus on valuable customer relations with regard to signing up new customers and managing existing customers. The focus is on further enhancing the non-financial performance indicator Customer ownership, which comprises postpaid and no-frills customers, as well as stabilisation of the average monthly revenue per postpaid customer. In addition, the company also focusses on expanding and further developing customer service in the direction of customer excellence and digitising. In this connection, the freenet Group in November 2016 concluded an agreement with Capita Customer Services (Germany) GmbH regarding the transfer of business processes of mobilcom-debitel GmbH in customer service. The purpose of the strategic partnership (established for seven years) is to achieve customer-oriented digital expansion of the customer care processes of mobilcom-debitel GmbH.

The freenet Group works continuously on profitably expanding its digital lifestyle activities in order to develop further sources of revenue. The company already has a wide range of innovative digital applications and digital lifestyle products in the fields of entertainment, smart home, health and security, and thus addresses a dynamic market. At present, the revenue generated as a result of marketing digital lifestyle products and services makes only a marginal contribution to the overall business volume of the freenet Group, albeit with high growth rates. In the financial year 2016, digital lifestyle revenue increased to around 137 million euros, which is equivalent to growth of approximately 30 per cent compared with the previous year.

The declared aim of the freenet Group is to further strengthen its market position as a digital lifestyle provider and to achieve stronger growth than the overall market in the new digital lifestyle market sectors. Particular importance is attached to the development of new innovative areas of operation related to the core business. With the marketing start of the new TV products freenet TV and waipu.tv in the subscription model, the freenet Group completed the process of breaking into the new TV and media segment last year. In this way, the company is operating in the rapidly expanding market for TV subscription services, and is thus consistently continuing the process of diversifying its digital lifestyle business activities.

Since the launch of DVB-T2 HD in June 2016, it has been possible for the first time to receive high-definition digital TV via a terrestrial solution. The process of changing over to the new standard will take place in phases until 29 March 2017, when DVB-T broadcasting will be discontinued in many regions of Germany. The new broadcasting standard DVB-T2 HD will enhance the quality and also the range of programmes. Based on the advantages of the new standard, and after DVB-T has been shut down, the freenet Group plans to use the distribution of its new product freenet TV to develop inexpensive end customer business for the terrestrial reception of private stations. Last year, the freenet Group secured the corresponding infrastructure for the second generation of digital-terrestrial radio broadcasting with the acquisition of the Media Broadcast Group, the sole commercial provider of DVB-T2 and DAB+ in Germany. The freenet Group has been offering a further inexpensive possibility of TV entertainment since the end of September 2016, the launch of waipu.tv. The IPTV product combines maximum image quality with the user-friendliness of an app and the flexibility of the Internet. The IP entertainment offerings are transmitted via the closed 12,000 kilometre glass fibre network of EXARING AG, in which freenet AG owns a stake of approximately 25 per cent.

The successful business strategy of the freenet Group continues to be based on an efficient distribution network with cross-selling possibilities. For this purpose, the company with its multiple brand strategy uses high-street outlets as well as online channels for marketing its mobile and digital lifestyle portfolio. With a clear focus on customer service and its further development the company will in future continue to focus on the individual needs of its customers and participate in Germany in the growth of the digital lifestyle and TV market with customised products and services.

The business outlook of the freenet Group for the financial year 2016 that was forecasted with the help of the defined performance indicators in the Group management report 2015 has proved to be accurate. The targets forecasted by the Executive Board have been met or exceeded.

Table 26: **Development of the key performance indicators**[1]

| In EUR million/as indicated | Forecast of 2015 for financial year 2016 | 2016 | Change over previous year in % | Forecast for financial year 2017 |
|---|---|---|---|---|
| **Financial performance indicator** | | | | |
| Group revenue | moderate increase | 3,362.4 | 7.8 | slight increase |
| Group EBITDA[2] | slightly above 400 | 402.3 | 8.7 | slight increase |
| Free cash flow[2] | around 300 | 311.4 | 9.4 | slight increase |
| Postpaid-ARPU (in EUR) | stable | 21.4 | 0.0 | stable |
| **Non-financial performance indicator** | | | | |
| Customer Ownership (in million) | slight increase | 9.53 | 2.5 | slight increase |

For corporate management purposes, the freenet Group uses financial and non-financial performance indicators for measuring the short-, medium- and long-term success of its strategic alignment and the related operational implementation. The financial performance indicator free cash flow is not used for segment-related management, and instead is used exclusively at the Group level. The performance indicators postpaid ARPU and customer ownership are used exclusively for management purposes in the Mobile Communications segment.

Based on the positive results for the financial year 2016, the company aims to achieve slightly higher consolidated revenue and a slightly higher Group EBITDA for the financial year 2017. At the segment level, the executive board is predicting stable revenue and stable EBITDA in Mobile Communications compared with the previous year. For the TV and Media segment which was created last year, the company is predicting slightly higher revenue and also slightly higher EBITDA (both compared with the previous year), with due consideration being given to the fact that the Media Broadcast Group was consolidated for 9.5 months in the financial year 2016 and for 12 months in the current financial year. As was the case in the previous reporting periods, the EBITDA contribution from the holding of freenet AG in Sunrise Communications Group AG is not included in the forecast for the financial year 2017 because it is not an element which is relevant for management purposes.

For the financial year 2017, the company also aims to achieve group-wide free cash flow which is slightly higher than the corresponding previous-year figure. Any contribution to the group-wide free cash flow of freenet AG resulting from the holding of freenet AG in Sunrise Communications Group AG is also not included in the forecast for the financial year 2017 because it is not an element which is relevant for management purposes.

The targets for the development of the performance indicators postpaid ARPU and customer ownership in the financial year 2017 are unchanged: In the Mobile Communications segment, the company continues to expect that postpaid ARPU will stabilise at the corresponding previous-year level, and that there will be a slight increase in the number of customers in customer ownership compared with the previous year.

The freenet Group continues to face up to the challenges in the mobile communications market by means of a strategic focus on maintaining and gaining valuable customer relations. The company uses enhanced marketing of data tariffs and current devices, such as smartphones and tablets, to take account of the change in consumer patterns in the direction of increased mobile data use and higher data volumes. In addition, the company expects to increasingly develop new sources of revenue by means of marketing innovative products and services for mobile digital lifestyle applications. The new TV and media segment is also becoming more important with regard to generating additional contributions to revenue and results. Further comments concerning the future development of performance indicators which are not relevant for management purposes are detailed in the economic report.



1 For a definition of the indicators, please refer to the section “Definition of alternative performance measures” in this Group management report.

2 Group EBITDA and free cash flow are determined without recognising the interest of freenet AG in the results of Sunrise or the dividend payment of Sunrise.

# Overall guidance of the Group's expected development

The Executive Board expects that the overall development of the company will continue to be positive in the financial year 2017. The company's strategic focus on valuable customer relations in the fields of postpaid and no-frills (customer ownership) in the core mobile communications segment has again proved to be successful. For this reason, the freenet Group will continue to follow this fundamental focus in future in order to secure its established positioning in the mobile communications market.

By strategically focussing itself as a comprehensive digital lifestyle provider at an early stage, the freenet Group has also established a position in new and rapidly expanding market sectors related to mobile applications and the "Internet of Things". The company will continue to utilise this existing growth potential in future by way of marketing innovative digital lifestyle products and services. As a result of breaking into the new TV segment, the freenet Group has laid the foundation for an extensive and innovative TV experience and has simultaneously prepared the way for the next generation TV. In the new TV and media segment, the company has identified the opportunity of establishing a further relevant pillar in addition to its core mobile communications activities.

The assurance and expansion of sustainable profitability and cash flow strength form the basis of the strategic business focus of freenet AG. The company will continue in future to concentrate on expanding its product portfolio and to develop new segments by organic and external means subject to strict profitability and investment requirements.

Büdelsdorf, 6 March 2017
The Executive Board

Christoph Vilanek | Joachim Preisig | Stephan Esch

# CONSOLIDATED FINANCIAL STATEMENTS

# OVERVIEW

# CONSOLIDATED INCOME STATEMENT

## for the period from 1 January to 31 December 2016

| In EUR `000s /as indicated | Note | 1.1.2016 - 31.12.2016 | 1.1.2015 - 31.12.2015 |
|---|---|---|---|
| Revenue | 4 | 3,362,407 | 3,117,892 |
| Other operating income | 5 | 60,544 | 51,268 |
| Other own work capitalised | 6 | 18,731 | 11,470 |
| Cost of material | 7 | -2,463,670 | -2,327,475 |
| Personnel expenses | 8 | -220,437 | -195,235 |
| Depreciation and impairment write-downs | 9 | -124,324 | -71,403 |
| Other operating expenses | 10 | -355,448 | -287,913 |
| **Operating result** | | **277,803** | **298,604** |
| | | | |
| Share of results of associates accounted for using the equity method | 17 | 21,019 | 171 |
| Thereof profit share | | 36,697 | 171 |
| Thereof subsequent recognition from purchase price allocation | | -15,678 | 0 |
| Interest receivable and similar income | 11 | 809 | 418 |
| Interest payable and similar expenses | 12 | -55,675 | -44,502 |
| **Result before taxes on income** | | **243,956** | **254,691** |
| | | | |
| Taxes on income | 13 | -27,536 | -33,231 |
| | | | |
| **Group result** | | **216,420** | **221,460** |
| | | | |
| Group result attributable to shareholders of freenet AG | 25 | 228,422 | 220,969 |
| Group result attributable to non-controlling interest | 25 | -12,002 | 491 |
| | | | |
| **Earnings per share in EUR (undiluted)** | 14.1 | **1.78** | **1.73** |
| **Earnings per share in EUR (diluted)** | 14.2 | **1.78** | **1.73** |
| | | | |
| Weighted average of shares outstanding in thousand (undiluted) | 25 | 128,011 | 128,011 |
| Weighted average of shares outstanding in thousand (diluted) | 25 | 128,011 | 128,011 |

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

## for the period from 1 January to 31 December 2016

| In EUR `000s | Note | 1.1.2016 - 31.12.2016 | 1.1.2015 - 31.12.2015 |
|---|---|---|---|
| **Group result** | | **216,420** | **221,460** |
| | | | |
| Change in fair value of available-for-sale financial assets | | -37 | -57 |
| Reclassification adjustments from the change in fair value of available-for-sale financial assets | | 35 | 0 |
| Currency difference | | 94 | 168 |
| Currency difference from subsequent accounting of associates accounted for using the equity method | 17.1 | 3,673 | 0 |
| Income tax recognised in other comprehensive income | | 102 | -34 |
| **Other comprehensive income/to be reclassified to the income statement in the following periods** | | **3,867** | **77** |
| Recognition of actuarial gains and losses arising from the accounting for pension plans acc. IAS 19 (2011) | 30 | -10,281 | 8,376 |
| Profit shares of associates accounted for using the equity method | 17.1 | 8,689 | 0 |
| Income tax recognised in other comprehensive income | | 2,954 | -2,521 |
| **Other comprehensive income/to be reclassified to the income statement in the following periods** | | **1,362** | **5,855** |
| **Other comprehensive income** | | **5,229** | **5,932** |
| **Consolidated comprehensive income** | | **221,649** | **227,392** |
| | | | |
| Consolidated comprehensive income attributable to shareholders of freenet AG | | 233,651 | 226,901 |
| Consolidated comprehensive income attributable to non-controlling interest | | -12,002 | 491 |

# CONSOLIDATED BALANCE SHEET

as of 31 December 2016

## Assets

| In EUR '000s | Note | 31.12.2016 | 31.12.2015 |
|---|---|---|---|
| **Non-current assets** | | | |
| Intangible assets | 15, 16 | 526,234 | 458,089 |
| Goodwill | 15, 16 | 1,379,919 | 1,153,985 |
| Property, plant and equipment | 15, 16 | 493,132 | 32,542 |
| Investments in associates accounted for using the equity method | 17 | 745,066 | 1,760 |
| Other investments | 18 | 586 | 1,517 |
| Deferred income tax assets | 19 | 174,172 | 177,337 |
| Trade accounts receivable | 21 | 81,132 | 79,438 |
| Other receivables and other assets | 21 | 20,738 | 12,045 |
| | | **3,420,979** | **1,916,713** |
| **Current assets** | | | |
| Inventories | 20 | 74,906 | 79,468 |
| Current income tax assets | 23 | 5,169 | 3,058 |
| Trade accounts receivable | 21 | 438,764 | 436,009 |
| Other receivables and other assets | 21 | 26,558 | 18,910 |
| Cash and cash equivalents | 22 | 318,186 | 269,761 |
| Assets classified as held for sale | 24 | 197 | 101 |
| | | **863,780** | **807,307** |
| | | | |
| | | **4,284,759** | **2,724,020** |

# Shareholders' equity and liabilities

| In EUR `000s | Note | 31.12.2016 | 31.12.2015 |
|---|---|---|---|
| **Shareholders' equity** | | | |
| Share capital | 25.1 | 128,061 | 128,061 |
| Capital reserve | 25.2 | 737,536 | 737,536 |
| Cumulative other comprehensive income | | -10,134 | -15,363 |
| Retained earnings | 25.3 | 504,582 | 474,577 |
| **Capital and reserves attributable to shareholders of freenet AG** | | **1,360,045** | **1,324,811** |
| Capital and reserves attributable to non-controlling interest | 25.4 | 42,222 | 54,224 |
| | | **1,402,267** | **1,379,035** |
| **Non-current liabilities** | | | |
| Other payables | 27 | 294,608 | 42,452 |
| Borrowings | 29 | 1,673,871 | 218,382 |
| Deferred income tax liabilities | 19 | 0 | 6 |
| Pension provisions | 30 | 92,638 | 51,191 |
| Other provisions | 31 | 58,559 | 8,044 |
| | | **2,119,676** | **320,075** |
| **Current liabilities** | | | |
| Trade accounts payable | 27 | 515,696 | 443,718 |
| Other payables | 27 | 110,423 | 107,975 |
| Current income tax liabilities | 28 | 46,847 | 32,465 |
| Borrowings | 29 | 60,302 | 420,532 |
| Other provisions | 31 | 29,548 | 20,220 |
| | | **762,816** | **1,024,910** |
| | | | |
| | | **4,284,759** | **2,724,020** |

# SCHEDULE OF CHANGES IN EQUITY

## for the period from 1 January to 31 December 2016

| In EUR `000s | Share capital | Capital reserve | Cumulative other comprehensive income: Revaluation reserve | Cumulative other comprehensive income: Currency difference | Cumulative other comprehensive income: Valuation reserve in accordance with IAS 19 | Retained earnings | Capital and reserves attributable to shareholders of freenet AG | Capital and reserves attributable to non-controlling interest | Shareholders' equity |
|---|---|---|---|---|---|---|---|---|---|
| **As of 1.1.2015** | **128,061** | **737,536** | **-99** | **247** | **-21,443** | **445,625** | **1,289,927** | **3.693** | **1,293,620** |
| Initial consolidation of subsidiaries | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 50,040 | 50,040 |
| Dividend payment | 0 | 0 | 0 | 0 | 0 | -192,017 | -192,017 | 0 | -192,017 |
| Group result | 0 | 0 | 0 | 0 | 0 | 220,969 | 220,969 | 491 | 221,460 |
| Recognition of actuarial gains and losses acc. IAS 19 (2011)[1] | 0 | 0 | 0 | 0 | 5,855 | 0 | 5,855 | 0 | 5,855 |
| Change in fair value of available-for-sale financial instruments[1] | 0 | 0 | -40 | 0 | 0 | 0 | -40 | 0 | -40 |
| Foreign currency translation[1] | 0 | 0 | 0 | 117 | 0 | 0 | 117 | 0 | 117 |
| Sub-total: Consolidated comprehensive income | 0 | 0 | -40 | 117 | 5,855 | 220,969 | 226,901 | 491 | 227,392 |
| **As of 31.12.2015** | **128,061** | **737,536** | **-139** | **364** | **-15,588** | **474,577** | **1,324,811** | **54,224** | **1,379,035** |

1 Figures are balanced with income tax recognised in other comprehensive income.

| In EUR `000s | Share capital | Capital reserve | Cumulative other comprehensive income: Revaluation reserve | Currency difference | Currency difference from subsequent accounting of associates accounted for using the equity method | Valuation reserve in accordance with IAS 19 | Profit share of associates accounted for using the equity method | Retained earnings | Capital and reserves attributable to shareholders of freenet AG | Capital and reserves attributable to non-controlling interest | Shareholders' equity |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **As of 1.1.2016** | **128,061** | **737,536** | **-139** | **364** | **0** | **-15,588** | **0** | **474,577** | **1,324,811** | **54,224** | **1,379,035** |
| Dividend payment | 0 | 0 | 0 | 0 | 0 | 0 | 0 | -198,417 | -198,417 | 0 | -198,417 |
| Group result | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 228,422 | 228,422 | -12,002 | 216,420 |
| Profit share of associates accounted for using the equity method[1] | 0 | 0 | 0 | 0 | 0 | 0 | 8,559 | 0 | 8,559 | 0 | 8,559 |
| Recognition of actuarial gains and losses acc. IAS 19 (2011)[1] | 0 | 0 | 0 | 0 | 0 | -7,198 | 0 | 0 | -7,198 | 0 | -7,198 |
| Change in fair value of available-for-sale financial instruments[1] | 0 | 0 | -1 | 0 | 0 | 0 | 0 | 0 | -1 | 0 | -1 |
| Foreign currency translation[1] | 0 | 0 | 0 | 251 | 0 | 0 | 0 | 0 | 251 | 0 | 251 |
| Foreign currency translation from subsequent accounting of associates accounted for using the equity method[1] | 0 | 0 | 0 | 0 | 3,618 | 0 | 0 | 0 | 3,618 | 0 | 3,618 |
| Sub-total: Consolidated comprehensive income | 0 | 0 | -1 | 251 | 3,618 | -7,198 | 8,559 | 228,422 | 233,651 | -12,002 | 221,649 |
| **As of 31.12.2016** | **128,061** | **737,536** | **-140** | **615** | **3,618** | **-22,786** | **8,559** | **504,582** | **1,360,045** | **42,222** | **1,402,267** |

For further details, please refer to our explanations in note 25, Shareholders' equity.

1 Figures are balanced with income tax recognised in other comprehensive income.

# CONSOLIDATED STATEMENT OF CASH FLOWS

## for the period from 1 January to 31 December 2016

| EUR `000s | Note | 1.1.2016 –31.12.2016 | 1.1.2015 –31.12.2015 |
|---|---|---|---|
| **Result before interest and taxes (EBIT)** | | **298,822** | **298,775** |
| | | | |
| **Adjustments** | | | |
| Depreciation and impairment on items of fixed assets | 9 | 124,324 | 71,403 |
| Share of results of associates accounted for using the equity method | 17 | -21,019 | -171 |
| Dividends received from associates accounted for using the equity method | 17 | 30,124 | 0 |
| Gains on the sale of subsidiaries | | -285 | 0 |
| Losses/Gains on the disposal of fixed assets | | 1,419 | -413 |
| Increase in net working capital not attributable to investing or financing activities | 20, 21, 27, 30, 31, 33.1 | -3,750 | -10,316 |
| Tax payments | 13, 19 | -39,986 | -44,340 |
| **Cash flow from operating activities** | 33.1 | **389,649** | **314,938** |
| Investments in property, plant and equipment and intangible assets | | -62,792 | -31,384 |
| Proceeds from the disposal of property, plant and equipment and intangible assets | | 14,681 | 981 |
| Payments for the acquisition of subsidiaries | 36 | -76,618 | -2,775 |
| Proceeds from the sale of subsidiaries | | 440 | 100 |
| Proceeds from the sale of available-for-sale financial assets | 24 | 45 | 3,349 |
| Payments for the acquisition of associates, accounted for using the equity method | 17 | -738,938 | 0 |
| Payments in shareholders' equity, accounted for using the equity method | 17 | 0 | -70 |
| Interest received | | 753 | 1,345 |
| **Cash flow from investing activities** | 33.2 | **-862,429** | **-28,454** |
| Dividend payments to company owners and minority shareholders | | -198,417 | -192,017 |
| Proceeds from new borrowings | 29 | 1,853,580 | 99,400 |
| Cash repayments of borrowings | 29 | -1,047,268 | -1,256 |
| Cash repayments of borrowings from finance lease | 27 | -18,565 | 0 |
| Interest paid | | -68,125 | -34,794 |
| **Cash flow from financing activities** | 33.3 | **521,205** | **-128,667** |
| **Cash-effective change in cash and cash equivalents** | | **48,425** | **157,817** |
| | | | |
| **Cash and cash equivalents at the beginning of the period** | | **269,761** | **111,944** |
| **Cash and cash equivalents at the end of the period** | | **318,186** | **269,761** |

| **Composition of cash and cash equivalents** In EUR `000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Cash and cash equivalents | 318,186 | 269,761 |
| | **318,186** | **269,761** |

| **Composition of free cash flow**[1] In EUR `000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Cash flow from operating activities | 389,649 | 314,938 |
| Investments in property, plant and equipment and intangible assets | -62,792 | -31,384 |
| Proceeds from the disposal of property, plant and equipment and intangible assets | 14,681 | 981 |
| **Free cash flow (FCF)** | **341,538** | **284,535** |

1 Free cash flow is a non-GAAP parameter. In this context please refer to section „Definition of alternative performance measures“ in the group management report.

# NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS OF FREENET AG FOR THE FINANCIAL YEAR 2016

## 1. General information

### 1.1 Business activity and accounting standards

freenet AG ("the company"), the parent company of the Group ("freenet"), is headquartered in Büdelsdorf, Germany. The company was founded in 2005 and is registered with Kiel District Court under HRB 7306. The Group provides telecommunications, radio and multimedia services in Germany and focuses mainly on mobile communications/mobile internet and digital lifestyle.

The consolidated financial statements for the financial year 2016 were prepared in accordance with the IFRS accounting standards promulgated by the International Accounting Standards Board (IASB) and the interpretations of the International Financial Reporting Interpretations Committee (IFRIC) as applicable in the European Union as at 31 December 2016. The provisions of German commercial law to be applied in accordance with section 315a HGB were additionally taken into consideration.

The consolidated financial statements were prepared in euros, the company's functional currency. All amounts are stated in thousands of euros (EUR '000s) or millions of euros (EUR million), as applicable.

The consolidated financial statements were prepared on the basis of historical cost – subject to the limitation that certain financial assets are shown at fair value. The annual financial statements of the companies included in the consolidated financial statements are subject to uniform accounting and valuation principles. They have been prepared as at the same balance sheet date as the consolidated financial statements.

The consolidated financial statements are submitted to the electronical Federal Gazette.

The following table shows the new or modified standards (IAS/IFRS) and interpretations (IFRIC) whose application is mandatory from 1 January 2016 and their respective impact on the Group:

| Standard/interpretation | | Mandatory application | Adoption by EU Commission | Effects |
|---|---|---|---|---|
| Diverse | Annual Improvements Project 2012 to 2014 – Improvements of IFRS (IFRS 5, IFRS 7, IAS 19, IAS 34) | 01.01.2016 | 15.12.2015 | No material effects |
| IFRS 11 | Amendments to IFRS 11: Balancing an acquisition of shares in Joint Operations | 01.01.2016 | 24.11.2015 | Depending on the nature and type of future transactions |
| IAS 16 and IAS 38 | Amendments to IAS 16 and IAS 38: Clarification of Acceptable Methods of Depreciation and Amortisation | 01.01.2016 | 02.12.2015 | None |
| IAS 16 and IAS 41 | Amendments to IAS 16 and IAS 41: Bearer Plant | 01.01.2016 | 23.11.2015 | None |
| IFRS 10, IFRS 12 and IAS 28 | Amendments to IFRS 10, IFRS 12 and IAS 25: Investment Entities: Applying the Consolidation Exception | 01.01.2016 | 22.09.2016 | None |
| IAS 27 | Amendment to IAS 27: Equity method in separate financial statements | 01.01.2016 | 18.12.2015 | None |
| IAS 1 | Amendment to IAS 1: Disclosure-Initiative | 01.01.2016 | 18.12.2015 | No material effects |

The following table shows the new or modified standards (IAS/IFRS) and interpretations whose application was not yet mandatory in the 2016 financial year and their respective impact on the Group:

| **Standard/interpretation** | | **Mandatory application** | **Adoption by EU Commission** | **Effects** |
|---|---|---|---|---|
| IAS 12 | Amendment to IAS 12: Recognition of deferred tax assets from non-realised losses | 01.01.2017 | Pending | No material effects |
| IAS 7 | Amendment to IFRS 7: Disclosure-Initiative | 01.01.2017 | Pending | No material effects |
| IFRS 9 | Financial instruments | 01.01.2018 | 22.11.2016 | No material effects |
| IFRS 15 | Revenue from contracts with customers | 01.01.2018 | 22.9.2016 | Material effects; Subject to audit by management |
| IFRS 15 | Clarification to IFRS 15 (Revenue from contracts with customers) | 01.01.2018 | Pending | No material effects |
| IFRS 2 | Amendments to IFRS 2: Classification and Valuation of transactions with share-based compensation | 01.01.2018 | Pending | No material effects |
| IFRS 4 | Amendments to IFRS 4 (insurance contracts) by application of IFRS 9 (financial instruments) | 01.01.2018 | Pending | None |
| Diverse | Annual Improvements Project 2014 to 2016 – Improvements of IFRS (IFRS 1, IAS 28) | 01.01.2018 | Pending | No material effects |
| IFRIC 22 | Transactions in foreign currency and refund paid in advance | 01.01.2018 | Pending | None |
| IAS 40 | Amendments to IAS 40: Transfers of held property as financial investments | 01.01.2018 | Pending | None |
| IFRS 16 | Leases | 01.01.2019 | Pending | Material effects; Subject to audit by management |

The Group applied all of the accounting standards which have been mandatory since 1 January 2016. Their application had no material impact on these consolidated financial statements.

On 13 January 2016, the IASB published the standard IFRS 16 (Leases). The IFRS 16 replaces the previous standard regarding the recognition of leases (IAS 17) as well as the interpretations IFRIC 4 (Determining whether an Arrangement Contains a Lease), SIC-15 (Operating Leases – Incentives) and SIC-27 (Evaluating the Substance of Transactions Involving the Legal Form of a Lease). The standard will be the subject of mandatory adoption starting 1 January 2019.

The major innovations introduced by IFRS 16 relate to recognition at the lessee. Accordingly, for all leases, the value of assets for the acquired rights and liabilities for payment obligations which have been entered into must be recognised in the balance sheet of the lessee. No distinction is made between operating leases and finance leases. Exemptions are allowed for low-value leased assets and for short-term leases. The regulation regarding the recognition of assets in the balance sheet of the lessor remains virtually unchanged.

As a result of the introduction of IFRS 16, the disclosures in the notes to financial statements have been extended. The overriding objective is to enable the reader to assess the impact of existing leases on the company.

As a result of major operating lease obligations in the freenet Group, the adoption of IFRS 16 has a material impact on the consolidated financial statements as of 31 December 2019. Accordingly, a project for recognising leasing was included in the financial year 2016.

On 28 May 2014, the IASB published standard IFRS 15. IFRS 15 provides a standard body of rules for all questions arising from the reporting of revenue from contracts with customers. The requirements stipulated in IFRS 15 must be applied in a standardised manner for different transactions and across all sectors, thereby improving the global comparability of revenue-related disclosures made by companies. The only exceptions are contracts covered within the scope of IAS 17 (Leases), IFRS 4 (Insurance Contracts) and IFRS 9 (Financial Instruments). IFRS 15 replaces the previous standards and interpretations for the reporting of revenue, and therefore IAS 11

(Construction Contracts), IAS 18 (Revenue), IFRIC 13 (Customer Loyalty Programmes), IFRIC 15 (Agreements for the Construction of Real Estate), IFRIC 18 (Transfers of Assets from Customers) and SIC-31 (Revenue – Barter Transactions Involving Advertising Services).

The IASB published clarifications to IFRS 15 on 12 April 2016. It is a revision of proposals and examples of the areas of identifying performance obligations, principal versus agent consideration, license revenue as well as exemption regulations regarding initial adoption, and further examples were included. These clarifications did not result in any significant change to the specialist concept for our Group.

Initial adoption has to be carried out retrospectively, whereby Appendix C contains some simplifications for the transition to IFRS 15. freenet is planning full retrospective adoption, taking advantage of the exception that such retrospective adoption does not take account of those agreements in which freenet complied with all obligations at the beginning of the earliest detailed period, namely on 1 January 2018.

The new model provides for a five-stage scheme. According to this, the customer contract and the performance obligations contained therein must first be identified. The remuneration agreed for this purpose must then be ascertained and matched with the separate performance obligations. Finally, revenue must be recorded for each performance obligation as soon as the agreed performance has been rendered or the customer has been granted the power of disposal over it. In connection with this, a distinction is made between performances related to a particular point in time (e. g. delivery of mobile communications hardware) and performances related to a period of time (e. g. offer of mobile communications services over 24 months). With the new regulations on income recognition, the recognition of revenue in many cases – especially in the case of “multi-component” contracts with a number of different contractual performances – no longer corresponds to the invoice amount conveyed to the customer, with the result that among other things, changes regarding the amount and the time of the revenue recognition and revenue adjustments might occur because of contractual modifications.

Another significant consequence of IFRS 15 is the obligation to capitalise customer acquisition costs and customer retention costs and to amortise them thereafter.

On the basis of this new balance sheet accounting, enhanced disclosures in the notes will also be required. Among other things, comments concerning the times when the various types of performance obligations are fulfilled and concerning the contractually agreed payment plans will be required. Outstanding performance obligations must be explained with regard to the transaction price still to be allocated to them and the outstanding fulfilment period.

The IT introduction project associated with the IFRS 15 was started in the freenet Group at the end of 2012, and is at a very advanced stage as of 31 December 2016. The process of drawing up the various specialist concepts and also the IT conceptions has been completed. The processes of programming and commissioning the new IT systems which are required have also been essentially completed. Major parts of the project are currently in the production and plausibility phase. As a result of this introduction project, the IT system landscape of the freenet Group will be extended by new systems, which for instance are used for determining fair values of mobile telecommunications hardware and mobile tariffs, determining the various indicators for the planned application of the portfolio method within the IFRS 15, calculating the accounting records and also calculating the costs of acquiring customers.

At present, the main impact of IFRS 15 on our consolidated balance sheet and consolidated income statement is attributable to the Mobile Communications segment, and primarily for our postpaid end customers. In relation to the products and services offered on the balance sheet date 31 December 2016, we consider that the corresponding impact of IFRS 15 on our TV and Media as well as Other/Holding segments is comparatively minor.

With many of our postpaid end customers, the freenet Group generates service revenue from mobile and digital lifestyle services with the end customer, and also sells the corresponding device to the customer. In general, cross subsidy arrangements are used for pricing these two elements, i.e. the tariff and the device. Under the terms of the IFRS 15, a higher level of revenue will be reported with regard to the hardware revenue which is generated immediately upon the sale, whereas the revenue reported in relation to the monthly tariff revenue will be lower than is the case at present. In addition, the revenue recognised in relation to every customer contract throughout the entire duration of the contract will be the same as that which is already recognised. The only difference will be in relation to the time at which the revenue is realised: The application of the new standard means that the revenue for our postpaid activities will tend to be realised at an earlier stage than is the case at present. In the consolidated income statement, mainly as a result of the obligation to capitalise and write down the costs of acquiring customers, the gross profit and EBITDA will tend to rise; on the other hand, the write-downs will also tend to increase. In addition, we consider that there will be a trend towards lower revenue in the consolidated income statement.

## 1.2 Consolidated companies

The consolidated financial statements include as subsidiaries all companies which are controlled by the Group. For a complete list of all companies included in freenet AG's consolidated financial statements, please consult the disclosures made in accordance with section 315a HGB in note 37.

IFRS 11 stipulates that there are two forms of joint arrangements, depending on the form of the rights and obligations resulting from the joint arrangement in question: joint arrangements and joint ventures. freenet AG has reviewed its joint arrangements and identified them as joint ventures.

Associated companies are defined as companies over which the Group exerts a significant influence but which are not controlled by the Group; this usually involves a share of between 20 and 50 per cent in their voting rights.

The companies 01019 Telefondienste GmbH, 01024 Telefondienste GmbH, freenet.de GmbH, freenet Cityline GmbH, freenet Datenkommunikations GmbH, 01050.com GmbH, new directions GmbH, freenet Direkt GmbH, mobilcom-debitel GmbH, MobilCom Multimedia GmbH, mobilcom-debitel Shop GmbH, Stanniol GmbH für IT & PR, Gravis – Computervertriebsgesellschaft mbH („GRAVIS“), freenet Energy GmbH, freenet digital GmbH, iLove GmbH, Lorena Medienagentur GmbH, Quaid Media International GmbH, Motility GmbH, klarmobil GmbH, callmobile GmbH, Taunus Beteiligungs GmbH, Media Broadcast GmbH, Media Broadcast Services GmbH and Media Broadcast TV Services GmbH will make use of the exemption rules specified in section 264 (3) HGB for the annual financial statements for the period ending on 31 December 2016.

## 1.3 Consolidation principles

Companies are included for the first time in the consolidated financial statements (full consolidation) with effect from the date on which the possibility of control over the subsidiary is transferred to the Group. They are deconsolidated as of the time when such control has ceased to apply. The company is said to control another entity if it is able to exercise control over the entity in which it holds an equity interest, is exposed to fluctuating returns from that holding, and can influence the level of returns as a result of its control. Control is normally associated with a share of more than 50 per cent of the voting rights. In order to assess whether a situation of control exists, however, due consideration is also given to the existence and impact of potential voting rights, rights resulting from other contractual agreements, and, if applicable, any other facts and circumstances that indicate the possibility of control. The Group therefore also carries out an assessment to determine whether the prevailing situation constitutes control if the parent company holds fewer than 50 per cent of the voting rights but is able to direct the company's most important activities. A situation of control might also apply as a result of, for example, voting rights agreements or enhanced minority rights. freenet AG carries out a reassessment if there are indications that there have been changes to one or more of the criteria of control. Non-controlling interests are disclosed separately on the balance sheet.

The purchase method was applied to the capital consolidation.

The acquisition cost of a business combination is determined by the sum of the fair values of the assets assigned, the liabilities incurred and/or acquired and any equity instruments issued for acquisition purposes. In addition, the acquisition costs include the fair values of all recognised assets and liabilities that result from an agreement concerning a contingent consideration.

All of the acquired company's identifiable assets, liabilities and contingent liabilities that meet the recognition criteria stipulated by IFRS 3.37 are disclosed separately at their fair value, irrespective of the extent of any minority interests. For each corporate acquisition, the Group decides on an individual basis whether the non-controlling shares in the acquired company which are not controllable are recognised at fair value or on the basis of the percentage of net assets attributable to the acquired company.

Acquisition-related costs are recognised as expenses when they are incurred.

When options are granted to enable non-controlling shareholders to tender further shares in Group companies, how the options are recognised depends on how opportunities and risks arising from these shares are assigned. If the opportunities and risks are transferred to the freenet Group, this is reflected in a corresponding reduction in the share of the Group's equity which is attributable to the non-controlling shareholders. In such cases, only a financial liability in relation to the option obligation is recognised. If the opportunities and risks are retained by the non-controlling shareholder, the equity which is attributable to the non-controlling shareholders is recognised. In this case, the financial liability relating to the option obligation is recognised to the disadvantage of the equity attributable to the shareholders of freenet AG. The financial liability is initially valued at the present value of the estimated repurchase amount on the expected date of exercise and subsequently measured at amortised cost using the effective interest rate method and taking into account any possible changes in the repurchase amount.

Transactions with non-controlling interests without loss of control are treated as transactions with equity providers from the Group. If the acquisition of a non-controlling interest results in a difference between the amount that is paid and the corresponding share in the carrying amount of the subsidiary's net assets, such a difference is recognised in equity. Profits and losses which occur upon the disposal of non-controlling interests are also recognised in equity.

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 net fair value of the acquired company's identifiable assets, liabilities and contingent liabilities. Any excess in the share of the net fair value of the acquired company over the acquisition costs is recognised immediately as income.

Investments in associates as well as joint ventures are disclosed in the consolidated financial statements using the equity method, with the recognised values of the shareholdings being increased or reduced annually by the proportion of the changes in equity at the respective company which is attributable to the freenet Group. The Group's share of the profits and losses of associates and joint ventures is recognised in the income statement from the time when the associate is acquired. Goodwill arising from the acquisition of associates and joint ventures is not disclosed separately. If the Group's share of the losses of an associate or a joint venture is equal to or higher than the value of its shareholding in that company, the Group does not recognise any further proportional losses. After the amount recognised for the shareholding is reduced to zero, additional losses are recognised as a liability only to the extent that the company has entered into legal or constructive obligations or has made payments for the associate or joint venture.

If the Group loses control over a company, its remaining share is revalued at fair value and the resulting difference is recognised as profit or loss. In addition, all amounts shown under other comprehensive income in relation to that company are recognised as if the parent company had immediately disposed of the corresponding assets and liabilities. This means that a profit or loss that had previously been recognised in other comprehensive income is no longer recognised in equity, instead being shown under earnings.

Intra-Group profits and losses, revenue, expenses and income as well as trade accounts receivable and liabilities between the consolidated companies are eliminated. The elimination of intra-Group results is also applicable for joint ventures and associates.

# 2. Accounting and valuation methods

The following accounting and valuation methods were applied during the preparation of these consolidated financial statements. The accounting and valuation methods have basically been used continuously since last year. Regarding the changes, please refer to note 1.1, Business activity and accounting standards, of these notes.

## 2.1 Recognition of revenue and expenses

The Group largely provides services for a short period. Revenue is recognised when the services have been rendered in full, provided that the amount of revenue can be determined reliably and it is sufficiently probable that a future economic benefit will accrue to the company. Services rendered but not yet invoiced are accrued separately in the consolidated financial statements. Revenue is disclosed net of value added tax and cash discounts. Revenue comprises the fair value of the consideration that has been, or will be, received for the sale of products and services within the framework of normal business activity.

The bulk of the Group's revenue is generated from a large number of end customers, with the remaining revenue accounted for by corporate customers.

Supplementary notes on revenue recognition (for a breakdown of business sectors consult note 3, Segment reporting):

Revenue in the Mobile Communications segment is generated by the spectrum of mobile communications services on offer, one-off provision charges and the sale of mobile terminals and accessories. Mobile Communications revenue (voice communication as well as data transmission) consists of monthly charges, charges for special features and connection and roaming charges. The charges generated by mobile communications services are recognised as revenue over the period during which the services are provided. Revenue from the sale of mobile terminals and accessories is recognised when the products are delivered to the customer or the distributor.

Customer acquisition costs, which consist mainly of the costs incurred in acquiring the mobile devices and the dealer commissions, are usually recognised immediately as expenses when customers have signed up. In the case of particular agency services provided by dealers, for whom the amount of sales commission depends on the newly acquired customers remaining in the Group's customer base and also on the level of future Group revenue generated with the newly acquired customers, the purchased services are recognised partially as expenses in the income statement rather than being recognised in full at the point where the customers are acquired. The remaining costs are recognised over the life of each new customer's contract. The amount recognised immediately as expenditure in the income statement at the point when the customer is acquired depends on the extent of the service rendered by the dealer at the point at which the customer is acquired in relation to the dealer's entire service over the customer's contractual life.

Certain end user contracts in the Mobile Communications segment are multiple-component contracts within the meaning of IAS 18.13. The "relative fair value method" is used for revenue generated with multiple-component contracts. The Group applies the US-GAAP guideline ASC 605-25 (formerly EITF 00-21) in accordance with IAS 8.10 et seq. The price for the entire multiple-component business is broken down over the various valuation entities on the basis of the proportional fair values. The amount of revenue to be recognised in relation to the elements that have already been supplied is limited to the level of revenue that is not dependent on services to be provided in the future (known as "cash restriction").

The Group receives commission revenue from the operators of mobile communications networks in particular for newly acquired customers and for contract extensions. Commission revenue for new customers is recognised as soon as a new customer is provided with network access by a network provider. The commission claims are based on contractually defined qualitative and quantitative characteristics such as the number of new customers per quarter or the average revenue per customer. In addition, market development funds for individual advertising campaigns are also provided by the network operators and, if the granting of the funds is linked to the activation of new customers, these are recognised in revenue. Insofar as claims extend beyond the period in which the services were rendered, commission revenue is accrued accordingly.

The revenue in the TV and Media segment is generated by the rendering of services to end customers in the IP-TV and DVB-T2 fields and also by the operation and service of broadcast-related solutions for business users in the radio and media sector. Revenue is recognised at the point at which the service is rendered to the customer.

## 2.2 Intangible assets

Goodwill is tested for impairment at least once a year as well as with indications of impairment and is shown at original cost less cumulative impairment.

For this purpose, goodwill is allocated to cash-generating units. It is allocated to those cash-generating units or groups of cash-generating units which are expected to derive a benefit from the merger that gave rise to the goodwill. With regard to the specific breakdown, please refer to note 15, Intangible assets, property, plant and equipment and goodwill as well as note 16, Impairment test for non-monetary assets.

One trademark with a substantial residual carrying amount is an asset with an indefinite useful economic life, which is not depreciated but rather subject to an impairment test once a year or if there are any indications of impairment. An indefinite useful life has been chosen provided that no steady loss of value is discernible in relation to this asset and no time limit could be applied to its useful life.

The other trademarks, on the other hand, have definable lifespans. These trademarks are carried at their historical cost and are amortised on a scheduled straight-line basis over their anticipated useful economic lives of 36 to 180 months. On the balance sheet date 31 December 2016, the remaining useful life of these trademarks was between 13 and 170 months.

Licences, software and rights are shown at historical cost and are amortised on a scheduled straight-line basis over their expected useful economic life, which is generally three to four years for software and one to ten years for licences and rights.

Costs incurred in developing and/or maintaining software programs are generally recognised as expenses in the year in which they are incurred. If the costs are clearly attributable to a definable software product that can be used by the company, and if the product’s overall expected economic benefit is greater than the costs incurred, the costs are capitalised as intangible assets in the category “internally generated software”. The development costs are not capitalised until the point in time when the product's technical and economic feasibility can be proven. These costs include, for example, the personnel costs of the software development team and any expenses incurred for services and fees during the production of the asset. They also contain an appropriate portion of relevant overheads. Capitalised software development costs are subject to straight-line depreciation over the duration of their likely useful lives of three to seven years.

Customer relationships are amortised on a scheduled straight-line basis over a period of 36 to 262 months. On the balance sheet date 31 December 2016, the remaining useful life of the customer relationships recognised in the balance sheet was between 25 and 252 months.

Distribution rights are amortised on a scheduled straight-line basis over the expected duration of the underlying agreements (48 months). On the balance sheet date 31 December 2016, the remaining useful life of the distribution rights recognised in the balance sheet was 7 months.

## 2.3 Property, plant and equipment

Property, plant and equipment are valued at their acquisition or production cost less scheduled straight-line depreciation and, if applicable, impairments. The useful economic lives assumed for the depreciation of assets correspond to the assets' expected useful lives within the company. In the calculation of depreciation, any residual values were disregarded on grounds of immateriality.

The residual carrying amounts and useful economic lives are reviewed as at each balance sheet date and adjusted where applicable.

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

| Asset | Useful life |
|---|---|
| Buildings | 10 to 33 years |
| Technical equipment and machinery | 5 to 15 years |
| Motor vehicles | 3 to 6 years |
| IT equipment | 3 to 8 years |
| Telecommunications equipment and hardware | 2 to 5 years |
| Leasehold improvements | 3 to 10 years |

## 2.4 Impairment of non-monetary assets

Non-monetary 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 test must be carried out if events or changed circumstances (triggering events) indicate that the asset's value might be impaired. Goodwill and intangible assets with indefinite useful lives must be tested for impairment once a year in accordance with IAS 36.

If the reason for impairment no longer applies, the asset's value is written up to a figure not exceeding the amortised cost. This is not applicable for goodwill, as no write-up is permissible.

## 2.5 Leases

### 2.5.1 The Group as lessee

The Group decides on a case-by-case basis whether assets are to be leased or purchased. For non-current assets, specific rules apply to motor vehicles (operating leases) and to factory and office equipment (purchase), with the exception of IT hardware and telecommunications equipment.

Leases that 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 transferred. Payments made in connection with an operating lease (possibly net after taking account of incentive payments made by the lessor) are recognised as expenses in the income statement using the straight-line method over the duration of the lease.

In accordance with IAS 17, the leased assets which are attributable to the Group as the beneficial owner under finance leases are capitalised at the lower of fair value of the leased asset and the present value of the minimum lease payments, and are depreciated over the shorter of their normal useful life and the term of the lease. Accordingly, the liability arising from the lease is classified as a liability and reduced by the repayment portion of the lease instalments that have already been paid. The interest portion of the lease instalments is recognised under expenses.

As of the balance sheet date 31 December 2016, and in connection with the acquisition of the Media Broadcast Group, a framework rental agreement was classified as a finance lease with the part of the minimum rental obligation. Please refer to the comments in note 27, Trade accounts payable, other liabilities and accruals.

### 2.5.2 The Group as lessor in finance leases

When the beneficial ownership of an asset is transferred to the contractual partner or customer, the Group reports a receivable due from the lessee in accordance with IAS 17. The receivable is shown in the amount of the net investment value as of the time when the contract is concluded. Lease instalments which are received are split into an interest component, which is recognised in the income statement, and a redemption component. The interest components are recognised as financial income spread over the relevant periods. As at the closing date 31 December 2016, comparable to the closing date 2014, there are no contracts in which the Group is classified as the lessor in finance leases.

## 2.6 Investments in associates and joint ventures

Ongoing equity investments in associates and joint ventures are recognised through separate financial statements or consolidated financial statements prepared for the respective associates or joint ventures in accordance with IFRS and the Group's accounting and valuation methods. With regard to the principles of consolidation using the equity method, please refer to note 1.3, Consolidation principles.

## 2.7 Financial instruments

### 2.7.1 Definition and classification

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

How the financial assets and financial liabilities are classified depends on the individual purposes for which they were acquired. The management determines how the financial assets and financial liabilities are to be classified upon initial recognition.

### 2.7.2 Financial assets measured at fair value through profit or loss

This category comprises two subcategories: Financial assets which are classified as held-for-trading right from the start, 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 basically acquired with the intention of being sold in the near future or if the financial asset is designated accordingly by management. Derivatives are likewise included in this category.

As at the balance sheet date, there are no financial assets measured at fair value through profit or loss.

### 2.7.3 Loans and receivables

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 classified as current assets, with the exception of those which do not fall due until twelve 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, and cash and cash equivalents.

Liquid assets consist of cash and cash equivalents comprising cash, demand deposits and other current highly liquid financial assets with a maximum original term of three months.

Loans and receivables also include services which have been rendered but which have not yet been billed, although a contractual claim exists for them.

### 2.7.4 Held-to-maturity financial assets

Held-to-maturity financial assets are non-derivative financial assets with fixed or determinable payments and fixed terms on the basis of which the Group management intends, and is able to hold them until their maturity. Held-to-maturity financial assets – with the exception of those that fall due within twelve months of the balance sheet date and are correspondingly shown as current assets – must be shown under non-current assets.

At present, the Group does not classify any financial instruments as held-to-maturity.

### 2.7.5 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 have not been classified under any of the other categories shown. They are assigned to non-current assets provided that management does not have the intention of selling them within twelve months from the balance sheet date.

This category includes shares in affiliated companies, investments and securities. The available-for-sale financial assets that existed on the balance sheet date are shown under other financial assets and under other receivables and other assets.

### 2.7.6 Financial liabilities, measured at amortised costs

Financial liabilities are based on contractual agreements regarding the payment of liquid assets or the rendering of other financial assets to a third party. A financial liability is recognised when freenet becomes the contracting party.

The financial liabilities as of the balance sheet date are disclosed in the trade accounts payable, financial debt and the other liabilities and deferred items.

### 2.7.7 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 that do not belong to the "measured at fair value through profit or loss" category are initially shown at 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.

Financial assets measured at fair value through profit or loss are subsequently measured at fair value. Any profit or loss resulting from the subsequent measurement of financial assets held for trading is recognised in the income statement. After initial recognition, loans and receivables are shown at amortised cost using the effective interest rate method less valuation allowances for impairment. Profits and losses are recognised in the result for the period if the loans and receivables are derecognised, impaired or amortised.

After initial recognition, held-to-maturity investments are shown at fair value plus transaction costs. Profits and losses are recognised in the result for the period if the held-to-maturity investments are derecognised, impaired or amortised.

After initial recognition, available-for-sale financial assets are shown at their fair value, with unrealised profits or losses being recognised directly in other comprehensive income, under the revaluation reserve. Dividends due on available-for-sale equity instruments must be shown in the income statement as other income at the point at which the Group's legal claim for payment arises.

Shares in affiliated companies, investments and securities are generally shown at acquisition costs, unless it is possible to determine their fair values reliably. The shares are not listed and there is no active market for them; neither is there any intention to sell them at present. If there are indications that fair values are lower, these are used.

Upon initial recognition, financial liabilities measured at amortised cost are shown at the fair value of the consideration received less the transaction costs associated with borrowing. In the subsequent period, the financial liabilities are shown at amortised cost using the effective interest rate method. Profits and losses are recognised in the income statement when the liabilities are derecognised or amortised. Non-current liabilities are shown in the balance sheet at amortised cost. Any differences between historical cost and the repayment amount are recognised in accordance with the effective interest rate method. Current liabilities are shown in the amount due for repayment or fulfilment. Loan liabilities are classified as current liabilities provided that the Group does not have the unconditional right to postpone settlement of the liability to a point in time at least twelve months after the balance sheet date. Derivative financial instruments are measured on the basis of future cash flows. Accordingly, derivative financial instruments can also be shown as financial liabilities. Financial liabilities arising from finance leases are shown at the present value of the minimum lease payments.



### 2.7.8 Impairment of financial assets

As at every balance sheet date, a check is carried out to determine whether there are any objective indications of impairment affecting a financial asset or a group of financial assets. In the case of equity instruments that are classified as available-for-sale financial assets, a significant and permanent decline in their fair value to a level below the cost of these equity instruments is regarded as an indication that the equity instruments are impaired. If there is such an indication with regard to available-for sale assets, the cumulative loss – measured as the difference between the carrying amount and the present value of the estimated future cash flows – 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.

Unlisted shares which are classified as available-for-sale are an example of the equity instruments described in the previous paragraph. In the case of such shares, any significant or continuing reduction in the fair value of the securities to a level below the purchase price of the shares must be regarded as an objective indication of impairment. If no market prices are available, other methods, e.g. the DCF method, are used to determine any need for impairment.

An impairment of trade accounts receivable is recognised if there are objective indications that the due amounts are not fully recoverable. Considerable financial difficulties faced by a debtor, an increased probability that the debtor will become bankrupt or will have to go through some other restructuring process, as well as any breach of contract, e. g. default or late payment of interest or redemption payments, are regarded as indications of the existence of impairment.

With some categories of financial assets, for example trade accounts receivable, assets for which no impairment has been determined on an individual basis are tested for impairment on a portfolio basis. Examples of objective indications of impairment affecting a portfolio of receivables are the Group's experience with payment inflows in the past, an increase in the frequency of default on payment within the portfolio over the average duration of a loan, and evident changes in the national or local economic climate that are associated with defaults on 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.

### 2.7.9 Derecognition of financial assets

Financial assets and liabilities are netted and shown as a net amount in the balance sheet only if there is a legal entitlement to such treatment and if it is intended that the position will be settled on a net basis or that the associated liability will be settled simultaneously with the realisation of the asset. For details, please refer to the comments in note 34.6, Transfer of financial assets.

### 2.7.10 Netting of financial instruments

Financial assets and liabilities are netted and shown as a net amount in the balance sheet only if there is a legal entitlement to such treatment and if it is intended that the position will be settled on a net basis or that the associated liability will be settled simultaneously with the realisation of the asset.

## 2.8 Inventories

Inventories are shown at the lower of purchase and production 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 be incurred.

## 2.9 Foreign currency transactions

The items included in the annual financial statements of each Group company are valued on the basis of the currency corresponding to the currency of the primary economic environment in which the company operates (functional currency). The consolidated financial statements are prepared in euros, which constitute the reporting currency of freenet AG.

Foreign currency transactions are translated into the functional currency using the exchange rates applicable on the date of the transaction. Profits and losses that result from the fulfilment of such transactions, and also from the process of converting monetary assets and liabilities denominated in foreign currency as at the reference date, are recognised in the income statement. Minor volumes of foreign currency transactions were carried out in the financial year 2016.

Since 24 March 2016, Sunrise Communications Group AG, Zurich, Switzerland (referred to in the following as "Sunrise") has been included as an associated company in the consolidated financial statements of freenet AG. In this connection, the average exchange rate is used for currency translation in relation to the shares in the group net income of Sunrise as well as the subsequent write-down recognised in relation to the shadow purchase price allocation. The residual carrying amount established for the disclosed hidden reserves from the shadow purchase price allocation is translated using the rate applicable on the reference date; currency translation differences resulting from the recognition of companies accounted for using the equity method are shown in the consolidated statement of comprehensive income under the item currency translation differences from the subsequent recognition of companies accounted for using the equity method.

The earnings and balance sheet items of all Group companies that have a functional currency other than the euro are converted into euros using the modified reference date method. Any resulting currency translation differences are recognised in equity until the disposal of the subsidiary and reported as a separate component of equity.

## 2.10 Shareholders' equity

Ordinary shares, capital reserves, revaluation reserves, retained earnings and minority interests are shown as shareholders' equity. After the deduction of applicable current taxes, costs of capital increases are recognised directly in shareholders' equity under capital reserves.

## 2.11 Pension provisions

Pension provisions are recognised and measured in accordance with IAS 19. The pension provision shown in the balance sheet is equivalent to the actuarial present value of the defined benefit obligation on the balance sheet date less the fair value of the plan assets. 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 balance sheet date; it also includes anticipated future increases in pensions and salaries.

Actuarial gains and losses which are based on experience-related adjustments and changes to actuarial assumptions are shown in equity under other comprehensive income in the period in which they arise.

Differences between the theoretical and actual income from plan assets are recognised in equity under other result in the period in which they arise.

Pension commitments are subject to the regulations of the Betriebsrentengesetz (Company Pensions Act). If the pension plans provide for pension benefits, there is the biometric risk of longevity. There are further risks in terms of pension adjustment obligations due to the development of inflation as well as salary-linked commitments related to the development in salaries.

Past service cost is recognised immediately in the income statement. The service cost is shown under personnel expenses and the interest portion of the addition to provisions is shown in financial results.

Contributions to defined-contribution benefit plans are recognised in the income statement in the year in which they occur.

## 2.12 Provisions

Provisions are formed for legal or constructive obligations towards third parties of uncertain timing and/or amount which arise as a result of past events, where it is more likely than not that settlement of the obligation will lead to an outflow of assets and where a reliable estimate of the extent of the obligation can be made. The provisions are valued using the best possible estimate of the obligation as at the balance sheet date, taking the discounting of non-current obligations into account.

If there are several similar obligations, the probability of an asset charge based on this group of obligations is ascertained. A provision is classified as a liability even if there is only a minor probability of an asset charge in relation to individual obligations included in this group.

According to IAS 16, the purchase costs of transmission installations and leasehold improvements include costs expected for obligations to remove these fittings. In accordance with IAS 37, a provision is therefore created to cover the present value of these obligations if 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 book value of the transmission installations and leasehold improvements (upper limit: recoverable amount; lower limit: zero).

Restructuring provisions basically comprise severance payments to employees. Provisions for potential losses mainly relate to tariffs with negative margins and vacancy costs.

There are semi-retirement obligations in accordance with the Altersteilzeitgesetz (AltTZG – Semi-Retirement Act) of 23 July 1996 in line with the block model. The semi-retirement phase cannot begin before the employee's 55th birthday. During the semi-retirement phase, the employee's monthly semi-retirement net salary is normally topped up to 85 per cent (or 83 per cent for agreements concluded after 1 October 2012) of the theoretical monthly full-time salary which has been reduced by the statutory deductions. A discount rate of 0.49 per cent and a salary increase of 2.25 per cent p.a. have been used as the basis for measuring the semi-retirement obligations. No consideration has been given to any potential in this respect. The obligations have been netted with the fair values of the corresponding plan assets. If the fair value of the plan assets exceeds the obligations, the surplus assets are shown under the receivables and other assets.

The provisions for obligations relating to long-time work accounts are measured using the same assumptions as those applicable for the provisions for pension obligations. Long-time work accounts are set up to ensure that time accounts are balanced in the long term. The obligations are reduced by granting leave of absence at full pay. The obligations have been netted with the fair values of the corresponding plan assets. If the fair value of the plan assets is higher than the obligations, the surplus assets are shown under the receivables and other assets.



## 2.13 Employee participation programmes

There are (or were in 2016) two long-term incentive programmes ("LTIP programmes") as employee participation programmes in the Group.

The accounting and valuation methods of these employee participation programmes are described below:

On 26 February 2014, agreements concerning the contracts of employment that grant LTIPs (hereinafter referred to as "Programme 2") were concluded by freenet AG with the members of the Executive Board.

In January 2016, freenet AG and two other group companies granted LTIP to senior executives below the Executive Board level (referred to in the following as "Programme 3").

In LTIP programmes, an LTIP account is maintained for each beneficiary; in each financial year, depending on the extent to which defined objectives for the financial year in question have been attained, credit or debit entries are made in the accounts in the form of virtual shares. Then, within a predetermined period of time, cash payouts less taxes and charges can be made for each financial year, depending on the balance in the respective LTIP account. The magnitude of these payments is dependent on, among other things, the relevant share price at the time of the payout. The provision is measured at the fair value of the virtual shares that will probably become vested. For details, please refer to our explanations to note 26 "Employee participation programmes".

## 2.14 Deferred and current taxes on income

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 as well as tax loss carry-forwards. Deferred taxes are measured at the tax rates (and tax laws) that apply or have been substantively enacted on the balance sheet date and that are expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

Deferred tax assets in relation to allowable temporary differences are recognised to the extent that deferred tax liabilities are still in existence. If the amount of the deferred tax assets in relation to allowable temporary differences exceeds this figure, the deferred tax assets are only recognised to the extent that it is likely that the deferred tax assets will be used by future profits. Deferred tax assets in relation to any tax loss carry-forwards, too, are capitalised only to the extent that it is likely that they will be utilised by future profits. The profits expected for the future are based on the company's forecast for pre-tax earnings applicable as at the balance sheet date.

Deferred tax liabilities which result from temporary differences in connection with holdings in subsidiaries and associates are recognised, unless the time at which the temporary differences are reversed can be determined by the Group and it is likely that the temporary differences will not reverse in the foreseeable future as a result of this influence.

Current tax expenses are calculated in accordance with the German tax regulations which are applicable as at the balance sheet date or which will be applicable in the near future. The management regularly reviews tax declarations, particularly with regard to issues that are subject to interpretation, and, if appropriate, forms provisions based on the amounts that will probably have to be paid to the fiscal authorities.

## 2.15 Judgements, forward-looking assumptions and estimated uncertainties

The presentation of the net assets, financial position and results of operations in the consolidated financial statements depends on the recognition and valuation methods used and on forward-looking assumptions and estimates. The actual amounts may diverge from the estimates. The significant estimates and associated assumptions set out below, as well as any uncertainties with regard to the chosen accounting and valuation methods, are of crucial importance for a correct understanding of the underlying risks of financial reporting as well as the impact that these estimates, assumptions and uncertainties might have on the consolidated financial statements.

The valuation of property, plant and equipment and intangible assets involves estimates for determining the fair value at the time of acquisition if the assets were acquired as part of a business combination. The anticipated useful life of such assets must also be estimated.

With regard to the forward-looking assumptions made within the framework of the tests relating to potential goodwill impairments (book value as of 31 December 2016: 1,379.9 million euros; previous year: 1,154.0 million euros) as well as impairments of intangible assets with an indefinite useful economic life (book value as of 31

December 2016: 293.2 million euros, previous year: 293.2 million euros), please refer to note 16, Impairment test for non-monetary assets.

A sensitivity analysis regarding the impairment tests for the assets allocated to the cash-generating unit (CGU) "Mobile Communications" has established that the fair value less costs to sell would decline by approximately 262 million euros if the WACC were to be increased by 0.5 percentage points and would increase by approximately 315 million euros if the WACC were to decline by 0.5 percentage points, and that, if earnings before interest and taxes (EBIT) were to be reduced or increased by 10 per cent in the planning period, the fair value less costs to sell would decrease by approximately 623 million euros (if the WACC simultaneously were to be increased by 0.5 percentage points) or increase by 745 million euros (if the WACC simultaneously were to be reduced by 0.5 percentage points); this would not result in any impairment with regard to the assets allocated to this CGU.

A sensitivity analysis regarding the impairment tests for the assets allocated to the cash-generating unit "TV" has established that the fair value less costs to sell would decline by approximately 111 million euros if the WACC were to be increased by 0.5 percentage points and would increase by 131 million euros if the WACC were to decline by 0.5 percentage points, and that, if earnings before interest and taxes (EBIT) were to be reduced or increased by 10 per cent in the planning period, the fair value less costs to sell would decrease by approximately 252 million euros (if the WACC simultaneously were to be increased by 0.5 percentage points) or increase by 296 million euros (if the WACC simultaneously were to be reduced by 0.5 percentage points); this would not result in any impairment with regard to the assets allocated to this CGU.

A sensitivity analysis regarding the impairment tests for the assets allocated to the cash-generating unit "Online" has established that the fair value less costs to sell would decline by approximately 5 million euros if the WACC were to be increased by 0.5 percentage points and would increase by 6 million euros if the WACC were to decline by 0.5 percentage points, and that, if earnings before interest and taxes (EBIT) were to be reduced or increased by 10 per cent in the planning period, the fair value less costs to sell would decrease by approximately 12 million euros (if the WACC simultaneously were to be increased by 0.5 percentage points) or increase by 14 million euros (if the WACC simultaneously were to be reduced by 0.5 percentage points); this would not result in any impairment with regard to the assets allocated to this CGU.

An assessment of the value of the receivables and other assets was carried out in order to determine suitable valuation allowances for trade accounts receivable and other assets. These assessments were based largely on past experience, as well as on the age structure and status of receivables in the dunning and collection process.

With regard to the trade accounts receivable arising from multiple-component agreements in relation to the offer for end customers to select more valuable mobile devices in return for an additional monthly payment (mobile option), and in order to determine the fair value of those receivables, assumptions were made about the duration and risk-adjusted interest rate to determine the present value of the anticipated future payment flows arising from these agreements. This interest rate takes the maturities of these interest rates into account, as well as their default risk. A sensitivity analysis in relation to this interest rate has established that these receivables would have been 1.0 million euros lower if the interest rate had increased by 0.5 percentage points and would have been 1.0 million euros higher if the interest rate had decreased by 0.5 percentage points.

With regard to the accrual of purchased services from sales commissions for the various products offered by 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.

In the case of particular agency services provided by dealers, for whom the amount of sales commissions depends on the newly acquired customers remaining in the Group's customer base and also on the level of future Group revenue generated with the newly acquired customers, the purchased services are recognised partially as expenses in the income statement rather than being recognised in full at the point at which the customers are acquired. The remaining costs are recognised over the life of each new customer's contract. The amount recognised immediately as expenditure in the income statement at the point when the customer is acquired depends on the extent of the service rendered by the dealer at the point at which the customer is acquired in relation to the dealer's entire service over the customer's contractual life. The amount which is recognised in this way is essentially an assessment of the future average revenue of the Group generated with the end users acquired by this dealer and also based on cost estimates of the value of that part of the dealer's consideration that is generated during the contractual life of the customer whom the dealer acquired.

As of the balance sheet date 31 December 2016, and in connection with the acquisition of the Media Broadcast Group, a framework rental agreement was classified as a finance lease with the part of the minimum rental obligation. This is a framework rental agreement with an infrastructure provider relating to the use of radio infrastructures (such as towers and masts) and radio locations and other areas, due to run until 31 December 2027. The Media Broadcast Group has the right to demand that the agreement be extended by a further period of ten years until 31 December 2037. The probability of this extension option being exercised is assumed to be less than 50 per cent.

The recognition and calculation of provisions depend on estimates. In particular, provisions for legal disputes are formed on the basis of the assessment by the lawyers representing the Group companies.

Regarding the formation of the provision for contingent losses for any vacancy of rented shops and/or office buildings, assumptions were made in respect of the possibility of these premises being sublet in the future. With regard to the formation of provisions for contingent losses in relation to anticipated losses from negative-margin tariffs, assumptions were made largely in respect of how long customers will spend in these tariffs in the future.

With regard to the assumptions and estimates made in the valuation model used for determining the provision for the LTIP programme as at 31 December 2016, please refer to note 26, Employee participation programmes.

With regard to pension provisions and similar obligations, note 30 describes how forward-looking assumptions have been made for the valuation of the provisions for pensions and similar obligations. This involves the estimation of a discount rate, the pension trend, the assessment of the future development of the beneficiary's pensionable income and an assessment of the beneficiary's life expectancy. A sensitivity analysis came to the conclusion that if the discount rate were to increase by 1.0 percentage points, the present value of the funded and unfunded obligations would be reduced by 15,218 thousand euros, while a decrease of 1.0 percentage points in the discount rate would increase the present value of the funded and unfunded obligations by 19,870 thousand euros. With regard to further sensitivity analyses pertaining to the pension obligations, please refer to note 30, Pension provisions and similar obligations, of the notes to the consolidated financial statements.

There are commercial transactions for which it is not possible to determine the definitive taxation during the normal course of business. The Group determines the amount of the provisions for anticipated tax audits on the basis of estimates as to whether, and if so to what extent, additional taxes on income will become due. Insofar as the definitive taxation for these transactions differs from the figure originally assumed, this will have an impact on the current and deferred taxes on income in the period in which the taxation is definitively determined.

The deferred tax assets in relation to loss carry-forwards are based on corporate planning for the four subsequent financial years involving forward-looking assumptions about, for example, the macroeconomic trend and the development of the telecommunications market. With regard to the extent of the capitalised deferred taxes on losses carried forward and also the extent of the losses carried forward in relation to which no deferred tax assets have been recognised, please refer to note 19, Deferred tax assets and deferred tax liabilities. A sensitivity analysis carried out in relation to the deferred tax assets has established that the deferred tax assets would increase by approx. 20.6 million euros if the trade income or corporation tax income were to increase by 10 per cent in the relevant planning period, and that they would decline by approx. 20.6 million euros if the trade income or the corporation tax income were to decline by 10 per cent in the relevant planning period.

## 2.16 Assets classified as held for sale

Discontinued operations and held-for-sale non-current assets, which are classified under IFRS 5 as held-for-sale, are shown at the lower of carrying amount and fair value less costs to sell if it is generally more likely that their carrying amount can be realised by way of a sale than by further use. At the time of reclassification to the discontinued operations and held-for-sale non-current assets, there is no further scheduled depreciation of the assets in question.

The held-for-sale assets or the held-for-sale group of assets are reclassified as “Continued operations” when the criteria of IFRS 5 are no longer satisfied. The assets or the group of assets are shown at the lower of carrying amount less scheduled depreciation or revaluations which would have been carried out if the assets or group of assets had not been classified as discontinued operations, and the recoverable amount at the time of reclassification. The adjustments to the revaluation of the group of assets are shown in the income statement as part of continued operations.

## 2.17 Comparative figures

The consolidation group has changed compared with the previous year as a result of the acquisition of the Media Broadcast Group. We have described the assets and liabilities as of the reference date of initial consolidation (17 March 2016) at fair values under note 36, Company acquisitions.

At the same time, a total of 24.56 per cent in the share capital of Sunrise was acquired in 2016. Sunrise is included in the consolidated financial statements of freenet AG. We have described further details under note 17, Companies accounted for using the equity method.

Beyond that, comparability with the consolidated financial statements as at 31 December 2015 is not significantly impaired with regard to the net assets, financial position and results of operations.

# 3. Segment reporting



IFRS 8 stipulates that by means of internal management, operating segments must be distinguished from Group segments whose operating results are reviewed regularly by the company’s main decision-making body with regard to decisions affecting the allocation of resources to this segment and the measurement of its profitability.

As its main decision-making body, the Executive Board organises and manages the company on the basis of the differences between the individual products and services offered by the company. As the Group performs its business operations almost entirely in Germany, it has no organisation and management based on geographical regions. The Group was active in the following operating segments in the financial year 2016:

- Mobile Communications:
  - Activities as a mobile communications service provider – marketing of mobile communications services (voice and data services) from the mobile communications network operators T-Mobile, Vodafone and Telefónica Deutschland in Germany
  - Based on the network operator agreements concluded with these network operators, a range of the company’s own network-independent services and tariffs as well as a range of network operator tariffs
  - Sale/distribution of mobile communications devices as well as additional services for mobile data communications and digital lifestyle
  - Rendering of sales services
  - Activity of Sunrise (business areas of Sunrise: mobile communications, landline, Internet and digital TV)

- TV and Media:
  - Rendering of services, mainly to end users, in the field of IP-TV
  - Planning, project management, installation, operation, service and marketing of broadcast-related solutions for business clients in the radio and media sectors
  - Rendering of services to end users in the field of DVB-T2
- Other/Holding:
  - Rendering of portal services such as e-commerce/advertising services (these essentially comprise the offer of online shopping and the marketing of advertising space on websites), of payment services for end customers as well as various digital products and entertainment formats for downloading and displaying and use on mobile devices
  - Development of communication solutions, IT solutions and other services for corporate customers
  - Range of narrowband voice services (call-by-call, preselection) and data services
  - Rendering of sales services

With the acquisitions of EXARING AG (referred to in the following as "EXARING") as well as the Media Broadcast Group, the freenet Group operates in the new business unit “TV and Media”. Since Q2 2016, the main decision makers of the Group have been provided with an amended reporting structure, according to which EXARING as well as the Media Broadcast Group are reported separately as a business unit. Because the quantitative thresholds in accordance with IFRS 8.13 have also been exceeded, the Media Broadcast Group as well as EXARING have been allocated to the new segment “TV and Media” in these consolidated financial statements. Because the information in the amended reporting structure has been available from the time of initial consolidation, EXARING was allocated to the segment "TV and Media" with effect as of 1 January 2016, and the Media Broadcast Group was allocated to the segment “TV and Media” with effect as of 18 March 2016. In the corresponding period of 2015, the freenet Group was not yet operating in the segment “TV and Media”; this is the reason why it was not necessary for any adjustment to be made in segment reporting for the comparison figures of the previous year.

As from the second quarter 2016 the management reporting presented to the main decision makers of the Group was changed. The income statement of the individual segments is no longer shown down to segment EBIT level but ends at the segment EBITDA level as the EBIT is not defined as financial key performance indicator. This means that the EBIT figure is not used for corporate management purposes. A corresponding adjustment of the previous years’ disclosure has been carried out.

The “Other/Holding” segment includes other business activities in addition to operating activities. This mainly comprises the holding activities of freenet AG (with the rendering of services within the Group in central areas, such as legal, human resources and finance) as well as entries which cannot be clearly allocated to operating segments. The segment revenue of 76.9 million euros (previous year: 87.2 million euros) reported for the “Other/Holding” segment in 2016 is attributable to operating activities (75.4 million euros; previous year: 81.2 million euros) and other business activities (1.5 million euros; previous year: 6.0 million euros). Of the figure of 51.0 million euros (previous year: 54.6 million euros) reported for gross profit for the "Other/Holding" segment in 2016, 52.4 million euros (previous year: 55.5 million euros) is attributable to the operating activities and -1.4 million euros (previous year: -0.9 million euros) is attributable to the other business activities. The EBITDA of -9.6 million euros reported for the “Other/Holding” segment in 2016 (previous year: -12.6 million euros) was accounted for by operating activities to the extent of 14.8 million euros (previous year: 11.2 million euros) and by other business activities (-24.4 million euros; previous year: -23.8 million euros).

The segments provide, or used to provide, services to the other segment. If there are equivalent external market prices for internally offered services, these market prices are used as internal transfer prices. The costs which are incurred (plus an overhead mark-up) are used as the basis for the transfer prices for services which cannot be valued on an arm’s-length basis.

Income and expenses are allocated to the segments on the basis of selected criteria and commercial relevance. For purposes of segment reporting, the values and measurements shown for the assigned expenses and income do not differ from the values and measurements shown in the consolidated balance sheet and the consolidated income statement, as was the case last year.

A breakdown by individual products or services of revenue earned with third parties is shown in note 4, Revenue. A more extensive breakdown based on individual products or services is not available.

The freenet Group engages in mass-market business that focuses primarily on private customers. Accordingly, the Group is not dependent on individual customers.

### Segment report for the period from 1 January to 31 December 2016

| In EUR'000s | Mobile Communications | TV and Media | Other/Holding | Elimination of intersegment revenue and costs | Total |
|---|---|---|---|---|---|
| **Third-party revenue** | **3,084,091** | **218,869** | **59,447** | **0** | **3,362,407** |
| Intersegment revenue | 41,879 | 6 | 17,419 | -59,304 | 0 |
| Total revenue | 3,125,970 | 218,875 | 76,866 | -59,304 | 3,362,407 |
| | | | | | |
| **Cost of materials, third party** | **-2,370,400** | **-73,432** | **-19,838** | **0** | **-2,463,670** |
| Intersegment cost of materials | -11,435 | -34,600 | -6,069 | 52,104 | 0 |
| Total cost of materials | -2,381,835 | -108,032 | -25,907 | 52,104 | -2,463,670 |
| | | | | | |
| **Segment gross profit** | **744,135** | **110,843** | **50,959** | **-7,200** | **898,737** |
| Other operating income | 54,993 | 3,313 | 6,782 | -4,544 | 60,544 |
| Other own work capitalised | 10,305 | 6,361 | 2,065 | 0 | 18,731 |
| Personnel expenses | -139,042 | -48,190 | -33,205 | 0 | -220,437 |
| Other operating expenses | -286,505 | -44,312 | -36,375 | 11,744 | -355,448 |
| Profit share of results of associates accounted for using the equity method | 36,493 | 0 | 204 | 0 | 36,697 |
| **Segment EBITDA** | **420,379** | **28,015** | **-9,570** | **0** | **438,824** |
| Depreciation and impairment write-downs | | | | | -124,324 |
| Subsequent accounting for associates accounted for using the equity method | | | | | -15,678 |
| **EBIT** | | | | | **298,822** |
| Group financial result | | | | | -54,866 |
| Taxes on income | | | | | -27,536 |
| **Group result** | | | | | **216,420** |
| Group result attributable to shareholders of freenet AG | | | | | 228,422 |
| Group result attributable to non-controlling interest | | | | | -12,002 |
| | | | | | |
| **Cash-effective net investments** | **18,692** | **25,777** | **3,642** | **0** | **48,111** |

### Segment report for the period from 1 January to 31 December 2015 adjusted[1]

| In EUR'000s | Mobile Communications | Other/Holding | Elimination of intersegment revenue and costs | Total |
|---|---|---|---|---|
| **Third-party revenue** | **3,051,499** | **66,393** | **0** | **3,117,892** |
| Intersegment revenue | 9,695 | 20,768 | -30,463 | 0 |
| Total revenue | 3,061,194 | 87,161 | -30,463 | 3,117,892 |
| | | | | |
| **Cost of materials, third party** | **-2,303,816** | **-23,659** | **0** | **-2,327,475** |
| Intersegment cost of materials | -14,535 | -8,942 | 23,477 | 0 |
| Total cost of materials | -2,318,351 | -32,601 | 23,477 | -2,327,475 |
| | | | | |
| **Segment gross profit** | **742,843** | **54,560** | **-6,986** | **790,417** |
| Other operating income | 50,800 | 6,452 | -5,984 | 51,268 |
| Other own work capitalised | 9,180 | 2,290 | 0 | 11,470 |
| Personnel expenses | -154,951 | -40,284 | 0 | -195,235 |
| Other operating expenses | -265,111 | -35,772 | 12,970 | -287,913 |
| Profit share of results of associates accounted for using the equity method | 0 | 171 | 0 | 171 |
| **Segment EBITDA** | **382,761** | **-12,583** | **0** | **370,178** |
| Depreciation and impairment write-downs | | | | -71,403 |
| Subsequent accounting for associates accounted for using the equity method | | | | 0 |
| **EBIT** | | | | **298,775** |
| Group financial result | | | | -44,084 |
| Taxes on income | | | | -33,231 |
| **Group result** | | | | **221,460** |
| Group result attributable to shareholders of freenet AG | | | | 220,969 |
| Group result attributable to non-controlling interest | | | | 491 |
| | | | | |
| **Cash-effective net investments** | **26,215** | **4,188** | **0** | **30,403** |

# 4. Revenue

A breakdown of revenue of 3,362 million euros (previous year: 3,118 million euros) over the segments is set out under note 3, Segment reporting.

Of the external revenue generated in the Mobile Communications segment, 1,753 million euros (previous year: 1,752 million euros) was related to service revenue and fees, 609 million euros (previous year: 616 million euros) fees for premiums and commissions and 682 million euros (previous year: 634 million euros) revenue from the sale of mobile communications devices, computers/IT products and accessories.

# 5. Other operating income

Other operating income consists mainly of income from dunning charges and charges for reversing direct debits, income from the charging-on of expenses, market development funds (insofar as not linked to new customer activation) and income from charging employees fees for the use of company cars.

1 The management reporting presented to the main decision makers of the Group was changed in the second quarter of 2016. The income statement of the individual segments is no longer reported up to segment EBIT, and instead ends with the segment EBITDA, because EBIT is not a financial performance indicator and is thus not used for management purposes. A corresponding adjustment has been made to the previous year period.

# 6. Other own work capitalised

The other own work capitalised mainly relates to the development of mobile communications software, due almost exclusively to strategic projects as well as the company's own assembly services in connection with the process of establishing radio infrastructure.

The capitalised costs comprise the directly attributable individual costs, which are largely consulting fees and personnel expenses, and the directly attributable overheads.

# 7. Cost of materials

The cost of materials is broken down as follows:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| Costs of purchased goods | 668,512 | 659,937 |
| Costs of purchased services | 1,795,158 | 1.667,538 |
| **Total** | **2,463,670** | **2,327,475** |

The cost of purchased goods largely consists of the cost prices for sold mobile communications devices, computers/ IT products and bundles from prepaid operations.

The cost of purchased services mainly comprises mobile communications charges, commissions and premiums for sales partners.

# 8. Personnel expenses

Personnel expenses are broken down as follows:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| Wages and salaries | 185,311 | 165,860 |
| Social contributions and expenses for retirement pensions | 35,126 | 29,375 |
| **Total** | **220,437** | **195,235** |

An average of 4,921 persons were employed in the Group in the financial year 2016 (previous year: 4,560). At the end of the financial year, the Group employed 4,886 persons (previous year: 4,367). Of this figure, 48 (previous year: 27) were senior executives and 354 (previous year: 306) were apprentices or students of the vocational academy as of 31 December 2016.

The Group's employee participation programmes resulted in personnel expenses as per IFRS 2 amounting to 2,880 thousand euros (previous year: 2,157 thousand euros).

With regard to an explanation of the employee participation programme, please refer to our comments to notes 2.13 and 26, Employee participation programmes.

Personnel expenses also comprise an expense of 1,749 thousand euros for defined benefit plans (previous year: 1,122 thousand euros), see also note 30, Pension provisions and similar obligations.

Personnel expenses include a figure of 14,405 thousand euros as the employer's social insurance contribution as costs of defined contribution benefit plans (previous year: 13,514 thousand euros).

# 9. Depreciation and amortisation

The following table sets out the composition of depreciation and amortisation:

| In EUR `000s | 2016 | 2015 |
|---|---|---|
| Amortisation on intangible assets | 64,238 | 60,480 |
| Impairment write-downs on intangible assets | 14 | 0 |
| Depreciation on property, plant and equipment | 60,072 | 10,743 |
| Impairment on property, plant and equipment | 0 | 180 |
| **Total** | **124,324** | **71,403** |

The increase in the depreciation on property, plant and equipment is primarily attributable to depreciation recognised in relation to technical equipment, plant and machinery within the Media Broadcast Group which was acquired in 2016.

The impairments of intangible assets concern a license that is no longer used.

The depreciation recognised in the previous year in relation to property, plant and equipment related to tenant fittings in stores which are no longer used.

# 10. Other operating expenses

Other operating expenses consist mainly of marketing costs (120,507 thousand euros in 2016 compared with 96,671 thousand euros in 2015), legal and consulting fees, administration costs (e. g. rents and ancillary costs at the shops and administrative buildings), impairment costs and default on receivables, as well as costs of billing, outsourcing and postage.

In the financial year, costs of valuation allowances and the write-off of receivables totalling 57,163 thousand euros (previous year: 44,396 thousand euros) were incurred. These expenses were attributable almost exclusively to trade accounts receivable.

A total of 37,204 thousand euros was recognised in the income statement in connection with rental agreements and leases (previous year: 33,324 thousand euros).

# 11. Interest and similar income

Interest and similar income consists of the following items:

| In EUR `000s | 2016 | 2015 |
|---|---|---|
| Interest receivable from banks, debt collection and similar income | 731 | 393 |
| Interest of tax fund | 78 | 25 |
| **Total** | **809** | **418** |

# 12. Interest and similar expenses

Interest and similar expenses are broken down as follows:

| In EUR `000s | 2016 | 2015 |
|---|---|---|
| Interest payable and similar costs | 40,436 | 35,063 |
| Interest from finance lease | 10,665 | 3 |
| Interest on pension obligations | 1,639 | 1,106 |
| Compounding of liabilities | 937 | 6,790 |
| Interest expense of additional tax payments and similar expenses | 111 | 719 |
| Other | 1,887 | 821 |
| **Total** | **55,675** | **44,502** |

As was the case in the previous year, the interest expense for 2016 relating to the compounding of liabilities (937 thousand euros compared with 6,790 thousand euros in 2015) is mainly attributable to the compounding of trade accounts payable, other liabilities and current income tax liabilities.

# 13. Taxes on income

Taxes on income comprise paid and outstanding taxes on income, plus deferred taxes.

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| Current tax expenses for the financial year | -33,495 | -35,173 |
| Tax income for previous years | 1,009 | 8 |
| Deferred tax income due to the write-up of deferred tax assets | 5,438 | 3,840 |
| Deferred tax income (previous year: tax expenses) due to temporary differences | 959 | -2,270 |
| Deferred tax income attributable to rate changes | -1,447 | 364 |
| **Total** | **-27,536** | **-33,231** |

For further disclosures concerning deferred taxes, please refer to note 19, Deferred tax assets and liabilities.

Applying the average tax rate of the consolidated companies to the Group result before taxes on income would result in anticipated tax expenses of 73.2 million euros (previous year: 76.7 million euros). The difference between this amount and the actual tax expense of 27.5 million euros (previous year: 33.2 million euros) is shown in the following reconciliation:

| In EUR '000s/as indicated | 2016[1] | 2015 |
|---|---|---|
| Earnings before taxes | 243,956 | 254,691 |
| Expected tax expenses applying a tax rate of 30.00% (previous year: 30.10%) | -73,187 | -76,662 |
| Change in the allowance for deferred tax assets and non-recognised deferred tax assets in relation to losses carried forward | 49,708 | 54,960 |
| Tax effect on tax-free income | -7,129 | -4,203 |
| Tax effect on non-deductible expenses due to trade tax additions | 0 | -5.268 |
| Tax effect on non-deductible expenses and tax-free income | -1,553 | -3,423 |
| Tax effect from reduction of capital reserves | 5,062 | 993 |
| Effects due to changes in tax rate | -1,446 | 364 |
| Tax income for previous years | 1.009 | 8 |
| **Actual tax expense** | **-27,536** | **-33,231** |
| Effective tax rate in % | 11.63 | 13.05 |

1 The structure of the table is more detailed than the corresponding structure of the table published in the previous year.

For the Group companies, a corporation tax rate of 15.0 per cent (previous year: 15.0 per cent) was used in the financial year 2016 for calculating the current and deferred taxes on income. A solidarity surcharge of 5.5 per cent in relation to the corporation tax as well as an average trade tax assessment rate of 404.10 per cent (previous year: 407.48 per cent) were also used. The deferred taxes in the financial year 2016 were calculated using an average rate of 30.00 per cent (previous year: 30.10 per cent). This reduction of 0.10 percentage points in the average tax rate is attributable to the above-mentioned reduction in the average trade tax assessment rate, due mainly to the acquisition of the Media Broadcast Group.

# 14. Earnings per share

## 14.1 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. In the future, it is possible that the undiluted earnings per share may decrease as a result of the possible utilisation of conditional capital. For information purposes, please refer to our comments under note 25.6, Contingent capital.

| | 2016 | 2015 |
|---|---|---|
| Group result attributable to shareholders of freenet AG in EUR '000s | 228,422 | 220,969 |
| Weighted average of shares outstanding | 128,011,016 | 128,011,016 |
| **Earnings per share in EUR (undiluted)** | **1.78** | **1.73** |

## 14.2 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.

As at 31 December 2016, there are neither actual nor potential dilution effects.

| | 2016 | 2015 |
|---|---|---|
| Group result attributable to shareholders of freenet AG in '000s | 228,422 | 220,969 |
| Weighted average of shares outstanding | 128,011,016 | 128,011,016 |
| Weighted average of shares outstanding plus number of diluting shares | 128,011,016 | 128,011,016 |
| **Earnings per share in EUR (diluted)** | **1.78** | **1.73** |

# 15. Intangible assets, property, plant and equipment and goodwill

Movements in property, plant and equipment and intangible assets are shown in the statement of changes in fixed assets, note 39.

The most significant carrying amount in the intangible assets is for trademark rights arising from the purchase price allocation on the occasion of the acquisition of the debitel Group in the financial year 2008.

The following table sets out the carrying amounts of these intangible assets from purchase price allocations:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Trademarks | 304,520 | 296,641 |
| User charges | 101,073 | 8,219 |
| Customer relations | 65,046 | 72,296 |
| Software | 3,729 | 5,555 |
| **Total** | **474,368** | **382,711** |

In addition to the intangible assets from various purchase price allocations, further intangible assets of 51.8 million euros are shown as of 31 December 2016 (31 December 2015: 75.4 million euros), including distribution rights of 14.5 million euros (previous year: 46.3 million euros).

The recapitalisation and its prolongation agreed in 2015 of the exclusive distribution right with Media Saturn Deutschland GmbH, which became effective in 2013, had resulted in a carrying amount of 14.5 million euros as at 31 December 2016 (previous year: 38.6 million euros).

No impaired intangible assets were in existence as at 31 December 2016.

The goodwill in the balance sheet apportioned to CGUs is shown below:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Mobile Communications | 1,119,396 | 1,119,396 |
| Online | 29,750 | 29,750 |
| TV | 226,621 | 687 |
| Other | 4,152 | 4,152 |
| **Total** | **1,379,919** | **1,153,985** |

The purchase price allocation on the occasion of the acquisition of the Media Broadcast Group resulted in goodwill of 225,934 thousand euros, which is shown under the CGU "TV". In connection with this, please refer also to the statements in note 36, Company acquisitions, of these notes.

Since 2016, the CGU “TV” has been attributed to the “TV and Media” segment, and the CGU “Other” has been attributed to the “Other/Holding” segment.

In the financial year and in the previous year, the income statement was not affected significantly by research and development costs.



# 16. Impairment test for non-monetary assets

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

Goodwill of 1,119,396 thousand euros (previous year: 1,119,396 thousand euros) was allocated to the CGU “Mobile Communications”, which belongs to the Mobile Communications segment, and a trademark right as an intangible asset with an undefined useful economic life in the amount of 293,204 thousand euros (previous year: 293,204 thousand euros).

The fair value less costs to sell has been used as the recoverable amount of the “Mobile Communications” CGU. Planning that covers the period up to and including 2020 and was approved by management was used to calculate the fair value. The detailed planning phase was extrapolated in perpetuity. This is equivalent to level 3 of the fair value hierarchy in accordance with IFRS 13.

Planning is based on detailed assumptions derived from previous experience and future expectations in relation to the main result and value drivers. In principle, the gross profit of the “Mobile Communications” CGU can be broken down into two earnings flows: the contribution made to earnings by new customers, and customer retention. These are opposed by the costs for purchased services, particularly with regard to the mobile network operators. The costs of acquiring and retaining customers dominate the contribution to earnings made by new customers and customer loyalty. On the other side are costs for procuring hardware and for dealer commissions to be paid to sales partners as a result of the acquisition or loyalty programmes. In the planning period, the freenet Group is expecting to see stable customer acquisition costs as well as stable customer loyalty costs. In addition, the Group is expecting to see a slight increase in the customer ownership base (postpaid and no-frills) and stable postpaid ARPU in 2017. In the planning period, the freenet Group expects that, within the “Mobile Communications” CGU, customer ownership will continue to report further slight growth, with a stable performance in revenue, postpaid ARPU and EBITDA. freenet expects that, within the "Mobile Telecommunications" CGU, there will be an increase in the contributions made to revenue and earnings by the digital lifestyle products in the planning period.

The WACC after tax derived in relation to the specific risk structure of the “Mobile Communications” CGU on the basis of market data and used in the course of determining the fair value is 6.02 per cent (previous year: 6.23 per cent). With regard to the capitalisation rate in the subsequent phase (as from 2021), a discount of 0.5 per cent has been assumed as a result of growth assumptions (previous year: 0.5 per cent); this is also the growth rate which has been used for extrapolating the cash flow forecasts.

The impairment test carried out in 2016 in relation to the “Mobile Communications” CGU confirmed that no impairment has to be recognised in relation to the goodwill allocated or to the trademark right with an undefined useful life.

Goodwill of 29,750 thousand euros has been attributed to the “Online” CGU (previous year: 29,750 thousand euros). The "Online" CGU is part of the “Other/Holding” segment. The fair value less costs to sell has been used as the recoverable amount of the "Online" CGU. Planning that covers the period up to and including 2020 and was approved by management was used to calculate the fair value. The detailed planning phase was extrapolated in perpetuity. This is equivalent to level 3 of the fair value hierarchy in accordance with IFRS 13.

Planning for the "Online" CGU is based on detailed assumptions derived from previous experience and future expectations in relation to the main result and value drivers. These are essentially the revenue and gross profits generated by the individual end products, differentiated in accordance with the respective sales markets. The freenet Group is assuming that the "Online" CGU will generate declining revenue, declining gross profits and constant contributions to EBITDA in the planning period.

The WACC after tax derived in relation to the specific risk structure of the “Online” CGU on the basis of market data and used in the course of determining the fair value is 6.75 per cent (previous year: 7.72 per cent). With regard to the capitalisation rate in the subsequent phase (starting 2021), the company has not assumed any growth (for the extrapolation of the cash flow forecast) and has also not assumed any reduction (previous year: reduction of 0.5 per cent) as a result of growth assumptions.

The impairment test carried out in 2016 in relation to the "Online" CGU confirmed that no impairment is required for the goodwill allocated.

As of 31 December 2016, goodwill of 226,621 thousand euros was allocated to the new “TV and Media” CGU which was created in the financial year 2016 and which is identical to the “TV and Media” segment. The fair value less costs to sell has been used as the recoverable amount of the "TV and Media" CGU. Planning that covers the period up to and including 2020 and was approved by management was used to calculate the fair value. The detailed planning phase was extrapolated in perpetuity. This is equivalent to level 3 of the fair value hierarchy in accordance with IFRS 13.

Planning for the "TV and Media" CGU is based on detailed assumptions derived from previous experience and future expectations in relation to the main result and value drivers. These are essentially the revenue and gross profits generated by the individual end products, differentiated in accordance with the respective sales markets. The freenet Group is assuming that the "TV and Media" CGU will generate slightly increasing revenue, gross profits and contributions to EBITDA in the planning period.

The WACC after tax derived in relation to the specific risk structure of the "TV and Media" CGU on the basis of market data and used in the course of determining the fair value is 7.37 per cent. With regard to the capitalisation rate in the subsequent phase (as from 2021), a discount of 1.0 per cent has been assumed as a result of growth assumptions; this is also the growth rate used for extrapolating the cash flow forecasts.

The impairment test carried out in 2016 in relation to the "TV and Media" CGU confirmed that no impairment is required for the goodwill allocated.

The consolidated financial statements as at 31 December 2016 include other goodwill for various CGUs in the amount of 4,152 thousand euros (previous year: 4,839 thousand euros), all of which is allocated to the “Other/ Holding” segment.

All in all, the impairment of non-monetary assets in the Group in the financial year 2016 amounted to 14 thousand euros (previous year: 0.2 million euros). This relates to licences which are no longer used (previous year: tenant fittings in stores which were no longer used).

In accordance with IAS 36 in conjunction with IAS 28.40 et seqq., a separate impairment test had to be carried out in relation to the total carrying amount of the shares in the associated company Sunrise as of 31 December 2016 in the amount of 743.1 million euros. This is an ad-hoc impairment test as the market capitalisation of Sunrise was lower than the proportionate carrying amount recognised in the balance sheet. The recoverability was estimated on the basis of information available in the public domain. The main sources in this respect were analyst estimates and also the application of EBITDA multiples which are usual in the telecommunications sector. On the basis of this information, it was possible to confirm the recoverability of the share in the associated company Sunrise. There was no impairment requirement.



# 17. Companies included using the equity method

| In EUR '000s | Note | 31.12.2016 | 31.12.2015 |
|---|---|---|---|
| Shares in associated companies | 17.1. | 743,102 | 0 |
| Shares in Joint Ventures | 17.2. | 1,964 | 1,760 |
| **As of 31 December** | | **745,066** | **1,760** |

## 17.1 Associated companies

With the agreement of 17 March 2016, freenet acquired a 23.83 per cent stake in the share capital of Sunrise Communications Group AG, Zurich, Switzerland. This transaction was completed on 23 March 2016. The shares were acquired for a price of 72.95 CHF. Overall, purchasing costs including incidental purchasing costs amounted to 718.0 million euros.

Since 24 March 2016, Sunrise has been included in the consolidated financial statements of freenet AG. By way of two seats on the Administrative Board of Sunrise and with more than 20 per cent of voting rights, freenet AG is able to exert a significant influence.

With the completion of the transaction on 14 April 2016, freenet acquired a further stake of 0.73 per cent in the share capital of Sunrise. The shares were also acquired for a price of 72.95 CHF. This additional acquisition resulted in purchase costs of 22.1 million euros.

Overall, freenet AG now holds a stake of 24.56 per cent in the share capital of Sunrise.

Sunrise is the largest private telecommunications provider in Switzerland and accounts for more than 3 million customers in the fields of mobile communications, landline, internet and digital TV.

The most recent financial information published by Sunrise relates to the consolidated financial statements as of 31 December 2016. A brief overview is provided in the following.

### Summarised Information for Sunrise as of 31 December 2016

| **Balance sheet**[1]<br>In CHF `000s | **31.12.2016** |
|---|---|
| Non-current assets | 3,289,538 |
| Thereof intangible assets | 2,348,900 |
| Current assets | 644,688 |
| Thereof cash and cash equivalents | 214,175 |
| **Total assets** | **3,934,226** |
| | |
| Non-current liabilities | 2,269,352 |
| Thereof non-current borrowings | 1,828,327 |
| Current liabilities | 528,586 |
| Thereof trade accounts payable and other payables | 476,271 |
| **Total liabilities** | **2,797,938** |

| **Income statement**[2]<br>In CHF `000s | **1.1.2016 - 31.12.2016** |
|---|---|
| Revenue | 1,896,673 |
| Gross profit | 1,192,699 |
| EBITDA | 598,688 |
| Depreciation and Amortisation | -459,568 |
| Interest payable and similar expenses | -58,708 |
| Taxes on income | 3,236 |
| **Group result after taxes** | **87,093** |

| **Other comprehensive income**<br>In CHF `000s | **1.1.2016 - 31.12.2016** |
|---|---|
| **Group result after taxes** | **87,093** |
| Recognition of actuarial gains and losses arising from the accounting for pension plans acc. IAS 19 (2011) | 18,891 |
| Taxes on income | -4,494 |
| **Other comprehensive income / not to be reclassified to the income statement in the following periods** | **14,397** |
| **Other comprehensive income** | **101,490** |

| **Reconciliation to carrying amount**<br>In EUR million | **2016** |
|---|---|
| Purchase price for 23.83% (17 March 2016) | **718.0** |
| Purchase price for 0.73% (14 April 2016) | **22.1** |
| **Total purchase price (24.56%)** | **740.1** |
| Current profit share | 36.5 |
| Subsequent recognition from purchase price allocation | -15.7 |
| Other comprehensive income | 12.3 |
| Dividend paid to freenet | -30.1 |
| **Carrying amount as of 31 December 2016** | **743.1** |

1 Closing date as of 31.12.2016 amounted to 0.9346 CHF/EUR.
2 The average exchange rate for financial year 2016 amounted to 0.9179 CHF/EUR.

A shadow purchase price allocation was created in accordance with IAS 28. The term “shadow purchase price allocation” is used because the purchase price allocation for an associated company is not directly reflected in the consolidated balance sheet of freenet AG, and instead is reflected only via subsequent depreciation. The shadow purchase price allocation identified goodwill of 755.5 million CHF which is applicable to the freenet share but which is not subject to ongoing depreciation, as well as assets totalling 237.8 million CHF which are attributable to the freenet share and which are subject to ongoing depreciation (thereof customer relations 169.9 million CHF, thereof brand rights 67.9 million CHF).

For the period between 24 March 2016 and 31 December 2016, the income statement shows a figure of 20,815 thousand euros for the share of results of associates accounted for using the equity method which is attributable to Sunrise; of this figure, shares in the consolidated net income of Sunrise after tax (after adjustment for write-downs in relation to assets revalued within the framework of the shadow PPA) account for 36,493 thousand euros, and the subsequent depreciation of the shadow purchase price allocation accounts for -15,679 thousand euros. With regard to the shares in the consolidated net income of Sunrise after tax, it has to be borne in mind that freenet initially adjusts the Group result after tax disclosed by Sunrise by the amount which Sunrise has included in this Group result as depreciation as well as deferred tax effects in relation to purchase price allocation. This ensures that this depreciation and these deferred tax effects are not recognised twice, because freenet shows these effects in the “Results of associates accounted for using the equity method, thereof from subsequent recognition from purchase price allocation”.

Other comprehensive income of 3,673 thousand euros resulting from currency difference in subsequent recognition and also other comprehensive income of 8,689 thousand euros resulting from profit share in relation to Sunrise as an element of the other comprehensive income of the consolidated statement of comprehensive income.

On 21 April 2016,, freenet AG received a dividend payment of 30.1 million euros as a result of the dividend payment of 3.00 CHF per share adopted in the annual general meeting of Sunrise on 15 April 2016. This inflow boosted the cash flow from operating activities.

As of 31 December 2016, the carrying amount of the Group’s holding in Sunrise amounted to 743.1 million euros. At the balance sheet date the share price of Sunrise amounted to 62.45 euros (source: Bloomberg).

In segment reporting of the freenet Group, Sunrise is allocated to the segment "Mobile Communications".

The acquisition of shares in Sunrise has resulted in a new situation for the freenet Group with regard to the presentation of the income statement item “Result of associates accounted for using the equity method”: Whereas in the past at the freenet Group, the subsequent recognition of an associated company was achieved only by way of writing up or writing down the carrying amount of the investment to take account of the current earnings elements and also by way of writing down the carrying amount as a result of impairments, the shadow purchase price allocation relating to the acquisition has resulted in intangible assets which have to be written down, and have thus resulted in a further element of the result of associates accounted for using the equity method.

In order to achieve better transparency of the results of associates accounted for using the equity method, we have therefore included lines for the corresponding "Thereof" details for this item starting with the consolidated interim financial statements for the period ending 31 March 2016.

As has been the case in the past, only the result elements from the item "Results of companies accounted for using the equity method" have been used for calculating our key financial performance indicator EBITDA. The depreciation resulting from the subsequent recognition of the shadow purchase price allocation does not have a negative impact on Group EBITDA.

### 17.2 Joint Ventures

In the consolidated financial statements as at 31 December 2016, FunDorado GmbH, Hamburg ("FunDorado"), including its subsidiaries and investments, is included as a joint venture. The freenet Group holds 50 per cent of the shares in FunDorado (previous year: 50 per cent). FunDorado operates a fee-based internet portal.

In 2016, FunDorado, including its subsidiaries and investments, generated earnings of 204 thousand euros (previous year: 171 thousand euros).

The carrying amount of the Group's investment in FunDorado, including its subsidiaries and investments, was 1,964 thousand euros as at 31 December 2016 (previous year: 1,760 thousand euros).

## 18. Other financial assets

The other financial assets shown as of the balance sheet date mainly relate to a dormant holding with an unchanged carrying amount of 500 thousand euros which has been measured at its acquisition cost in light of an absent market.

The fixed-income bonds which served as rent collateral for shops were sold at their carrying amounts in 2016.

The other financial assets are broken down as follows:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Dormant holding | 500 | 500 |
| Other holding | 3 | 3 |
| Other | 83 | 0 |
| **Other financial assets, measured at cost of purchase** | **586** | **503** |
| Fixed-income bonds | 0 | 1,014 |
| **Other financial assets, in equity measured at fair value** | **0** | **1,014** |
| **Total** | **586** | **1,517** |

## 19. Deferred tax assets and liabilities

The deferred tax assets and liabilities, taking account of the temporary differences in accordance with the liability method, were taxed at an overall rate of 30.00 per cent (previous year: 30.10 per cent).

The following amounts are shown in the consolidated balance sheet:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Deferred tax assets | 174,172 | 177,337 |
| Deferred tax liabilities | 0 | -6 |
| **Total** | **174,172** | **177,331** |

The overhang of deferred tax assets for the corporation tax and trade tax group of freenet AG which are recognised (174.2 million euros; previous year: 177.3 million euros) is classified as short-term (43.6 million euros; previous year: 47.5 million euros) and long-term (130.7 million euros; previous year: 129.8 million euros) as a result of the anticipated use of tax loss carry-forwards.

Changes in the deferred income tax assets and liabilities in the financial year 2016 are shown in the following table:

| In EUR '000s | 1.1.2016 | Change in group of consolidated companies | Shown directly in other result | Expenses and income from taxes on income | 31.12.2016 |
|---|---|---|---|---|---|
| Property, plant and equipment | 380 | 615 | 0 | 820 | 1,815 |
| Intangible assets | -140,929 | -17,067 | 0 | -779 | -158,775 |
| Financial assets | -14 | 0 | 0 | 443 | 429 |
| Loss carry-forwards | 290,039 | 0 | 0 | 4.384 | 294,423 |
| Pension provisions | 7,710 | 2,502 | 3,085 | -2,053 | 11,244 |
| Other provisions | 1,803 | 2,024 | 0 | 887 | 4,714 |
| Other liabilities | -99 | 0 | 0 | 75 | -24 |
| Borrowings | 413 | 0 | 0 | 554 | 967 |
| Other assets and liabilities | 18,028 | 761 | -29 | 619 | 19,379 |
| **Total** | **177,331** | **-11,165** | **3,056** | **4,950** | **174,172** |

The expenses and income from income tax amounting to a net amount of 4,950 thousand euros (previous year: 1,934 thousand euros) are shown in the consolidated income statement as deferred income taxes under "Taxes on income". They basically correspond to the sum of the deferred taxes on income attributable to continued and discontinued operations. As in the previous year, income tax expenses and income in 2016 were attributable solely to continued operations.

The deferred tax assets and deferred liabilities developed as follows in the financial year 2015:

| In EUR '000s | 1.1.2015 | Change in group of consolidated companies | Shown directly in other result | Correction | Expenses and income from taxes on income | 31.12.2015 |
|---|---|---|---|---|---|---|
| Property, plant and equipment | 1,925 | 0 | 0 | 0 | -1,545 | 380 |
| Intangible assets | -119,268 | -21,761 | 0 | -154 | 254 | -140,929 |
| Financial assets | -11 | 0 | 0 | 0 | -3 | -14 |
| Loss carry-forwards | 285,713 | 0 | 0 | 0 | 4,326 | 290,039 |
| Pension provisions | 10,111 | 0 | -2,521 | 154 | -34 | 7,710 |
| Other provisions | 4,048 | 0 | 0 | 0 | -2,245 | 1,803 |
| Other liabilities | -507 | 0 | 0 | 0 | 408 | -99 |
| Borrowings | 337 | 0 | 0 | 0 | 76 | 413 |
| Other assets and liabilities | 17,382 | 0 | -51 | 0 | 697 | 18,028 |
| **Total** | **199,730** | **-21,761** | **-2,572** | **0** | **1,934** | **177,331** |

The summarised net development of deferred taxes is shown below:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| As of 1. 1. | 177,331 | 199,730 |
| Change in group of consolidated companies | -11,165 | -21,761 |
| Shown directly in other result | 3,056 | -2,572 |
| Tax income | 4,950 | 1,934 |
| **As of 31. 12.** | **174,172** | **177,331** |

The existing tax loss carry-forwards that can be carried forward without any restrictions exceed the sum of the forecast cumulative results for the next four financial years. Accordingly, a deferred tax asset was only recognised in the consolidated balance sheet to the extent that it is regarded as probable that this asset will indeed be realised. The expected results are based on the company's forecast for pre-tax earnings applicable as at the balance sheet date. As at 31 December 2016, deferred tax assets amounting to 174.2 thousand euros had been created in relation to loss carry-forwards (previous year: 290,039 thousand euros). Of this figure, 145,093 thousand euros (previous year: 151,430 thousand euros) is attributable to corporation tax loss carry-forwards and 149,330 thousand euros (previous year: 138,609 thousand euros) is attributable to trade tax loss carry-forwards. Of the figure shown for other loss carry-forwards, for which no deferred tax assets had been created in the consolidated balance sheet, 1.1 billion euros relate to corporation tax and 0.4 billion euros relate to trade tax (previous year: 1.2 billion euros corporation tax and 0.7 billion euros trade tax). As was the case on the previous year's balance sheet date, there were no unreported interest carry-forwards as per section 4h (1) sentence 2 of the German Income Tax Act (EStG).

As at 31 December 2016, there are temporary outside basis differences (net shareholders' equity in accordance with IFRS is higher than the corresponding carrying amounts of investments shown for tax purposes) of approximately 7.5 million euros (previous year: approximately 1.1 million euros). No deferred taxes have been recorded in connection with these differences because they are not expected to reverse in the fiscal planning period.

# 20. Inventories

The inventories are broken down as follows:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Mobile phones/accessories | 43,550 | 48,984 |
| Computers/IT products | 17,604 | 18,980 |
| SIM cards | 6,748 | 7,117 |
| Bundles and vouchers | 109 | 63 |
| Other | 6,895 | 4,324 |
| **Total** | **74,906** | **79,468** |

Impairment of 3,480 thousand euros (previous year: 4,465 thousand euros) has been recognised in relation to the year-end inventories.

# 21. Receivables and other assets

Receivables and other assets are broken down as follows:

| | 31.12.2016 | | |
|---|---|---|---|
| In EUR '000s | Total | Non-current | current |
| Trade accounts receivable | 519,896 | 81,132 | 438,764 |
| Other non-derivative financial assets | 34,419 | 17,964 | 16,455 |
| | **554,315** | **99,096** | **455,219** |
| Available-for-sale financial assets | 2,774 | 2,774 | 0 |
| **Financial assets** | **557,089** | **101,870** | **455,219** |
| Other assets | 0 | 0 | 0 |
| Advance payments | 10,103 | 0 | 10,103 |
| **Non-financial assets** | **10,103** | **0** | **10,103** |
| **Total trade accounts receivable and other assets** | **567,192** | **101,870** | **465,322** |

| | 31.12.2015 | | |
|---|---|---|---|
| In EUR '000s | Total | Non-current | current |
| Trade accounts receivable | 515,447 | 79,438 | 436,009 |
| Other non-derivative financial assets | 18,403 | 4,525 | 13,878 |
| | **533,850** | **83,963** | **449,887** |
| Available-for-sale financial assets | 2,802 | 2,802 | 0 |
| **Financial assets** | **536,652** | **86,765** | **449,887** |
| Other assets | 5,280 | 4,718 | 562 |
| Advance payments | 4,470 | 0 | 4,470 |
| **Non-financial assets** | **9,750** | **4,718** | **5,032** |
| **Total trade accounts receivable and other assets** | **546,402** | **91,483** | **454,919** |

Trade accounts receivable are due from third parties and consist mainly of receivables arising from charges, equipment sales, and landline and internet services.

The sum total of trade accounts receivable and other non-derivative financial assets, less valuation allowances that had been recognised, amounted to 554,315 thousand euros as at 31 December 2016 (previous year: 533,850 thousand euros). For more information, please refer to the statements in note 34, Information concerning financial instruments. In the freenet Group, trade accounts receivable are the most significant item in this category. These are due mainly from end customers and to a lesser extent from corporate customers, dealers and sales partners. Other assets and advance payments of 12,877 thousand euros (previous year: 12,552 thousand euros) consist of available-for-sale financial assets and non-financial assets as at 31 December 2016.

Invoices in the Mobile Communications segment are issued by the Group itself. In the segment Other/Holding some invoices are partially issued by the Group itself; for narrowband services, the collection services of Deutsche Telekom AG (DTAG) are utilised.

When invoices are issued to end customers by the Group itself, they are mostly due immediately upon receipt. The invoicing carried out by DTAG has a payment term of 30 days.

In the previous year, no renegotiations concerning existing receivables were held in the case of trade accounts receivable that were not impaired and not overdue.

As at 31 December 2016, trade accounts receivable and other non-derivative financial assets in the amount of 469,648 thousand euros (previous year: 445,309 thousand euros) were neither impaired nor overdue.

Trade accounts receivable and other non-derivative financial assets in the amount of 13,513 thousand euros (previous year: 21,420 thousand euros) are overdue but not impaired. These receivables are due from various customers who have not defaulted in the past.

The other receivables and other assets shown in the balance sheet result from other non-derivative financial assets, available-for-sale financial assets, other assets and advanced payments.

The maximum default risk of the trade accounts receivable as at the balance sheet date amounts to 494.5 million euros due to existing commercial credit insurances.

The following information concerns the age structure of this category of trade accounts receivable and non-derivative financial assets:

| In EUR '000s | Carrying amount 31.12.2016 | Thereof: on closing date neither impaired nor overdue | Thereof: On closing date not impaired and in following periods overdue | | |
|---|---|---|---|---|---|
| | | | less than 90 days | between 91 and 180 days | more than 180 days |
| Trade accounts receivable | 519,896 | 436,636 | 7,166 | 3,825 | 1,318 |
| Other non-derivative financial assets | 34,419 | 33,012 | 378 | 10 | 816 |
| **Total** | **554,315** | **469,648** | **7,544** | **3,835** | **2,134** |

| In EUR '000s | Carrying amount 31.12.2015 | Thereof: on closing date neither impaired nor overdue | Thereof: on closing date neither impaired nor overdue | | |
|---|---|---|---|---|---|
| | | | less than 90 days | between 91 and 180 days | more than 180 days |
| Trade accounts receivable | 515,447 | 428,137 | 15,241 | 600 | 4,348 |
| Other non-derivative financial assets | 18,403 | 17,172 | 704 | 6 | 521 |
| **Total** | **533,850** | **445,309** | **15,945** | **606** | **4,869** |

The following information concerns the trend in impairments for the category of trade accounts receivable and non-derivative financial assets:

| In EUR ’000s | |
|---|---|
| Allowances recorded as of 31 December 2015 | 109,416 |
| Allowances recorded as of 31 December 2016 | 128,720 |
| **Net reductions to impairments** | **19,304** |

| In EUR ’000s | |
|---|---|
| Allowances recorded as of 31 December 2014 | 99,061 |
| Allowances recorded as of 31 December 2015 | 109,416 |
| **Net reductions to impairments** | **10,355** |

The valuation allowances formed at the balance sheet date were attributable to the following categories of receivables:

| In TEUR | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Global individual allowances according to time buckets | | |
| Thereof for receivables not past due | 1,636 | 1,734 |
| Thereof for receivables overdue for < 90 days | 6,769 | 6,877 |
| Thereof for receivables overdue between 90 and 180 days | 8,593 | 9,008 |
| Thereof for receivables overdue for > 180 days | 105,183 | 86,069 |
| | **122,181** | **103,688** |
| **Individual allowances** | **6,539** | **5,728** |
| **Total allowances** | **128,720** | **109,416** |

As at the two reference dates, the global individual allowances concerned receivables due from end customers, whereas most of the individual allowances were formed in connection with receivables due from corporate customers, mainly distribution partners.

The following overview shows the development in individual allowances.

| In EUR ’000s | 2016 | 2015 |
|---|---|---|
| **Development in individual allowances relating to trade accounts receivable** | | |
| As of 1. 1. | 4,990 | 5,273 |
| Additions, initial consolidation | 1,621 | 0 |
| Allocation | 1,792 | 476 |
| Utilisation | 1,572 | 357 |
| Reversal | 1,086 | 402 |
| **As of 31. 12.** | **5,745** | **4,990** |
| | | |
| **Development in individual allowances relating to other non-derivative assets** | | |
| As of 1. 1. | 738 | 717 |
| Additions, initial consolidation | 0 | 0 |
| Allocation | 794 | 365 |
| Utilisation | 738 | 0 |
| Reversal | 0 | 344 |
| **As of 31. 12.** | **794** | **738** |
| | | |
| **Total individual allowances** | **6,539** | **5,728** |

# 22. Liquid funds

Liquid funds are broken down as follows:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Cash in hand and cash at banks | 318,186 | 269,761 |
| **Total** | **318,186** | **269,761** |

# 23. Current income tax assets

The current income tax assets mainly relate to receivables from reversal factors regarding tax audits for previous years (corporation tax and trade tax) as well as receivables due from former shareholders in connection with tax clauses from acquisitions.

# 24. Assets classified as held for sale

On 21 November 2016, the freenet Group and Capita Customer Services (Germany) GmbH, Berlin ("Capita") concluded an agreement for acquiring the business processes of mobilcom-debitel GmbH in customer service.

The purpose of the strategic partnership which has been set up for seven years is to drive ahead the process of digitising the customer care processes of mobilcom-debitel GmbH in a customer-oriented manner. Starting 1 March 2017, Capita will assume responsibility for the entire customer service of mobilcom-debitel GmbH, incl. the associated IT infrastructure, and will take on approximately 650 in-house employees in customer support as well as the location in Erfurt.

As part of this process, mobilcom-debitel GmbH sold assets (essentially office and business equipment) to Capita at residual carrying amounts of 242 thousand euros. The held-for-sale assets were shown with their residual carrying amount of 197 thousand euros as of 31 December 2016 in the balance sheet under the item "Assets classified as held for sale".

In the freenet Group, the process of outsourcing the business processes to Capita will result in a reduction in personnel expenses and a simultaneous increase in the other operating expenses.



# 25. Shareholders' equity

In regard to the following notes we also refer to the schedule of changes in equity.

## 25.1 Share capital

Unchanged to the previous year the company's issued share capital amounts to 128,061 thousand euros. The share capital consists of 128,061,016 registered no-par-value shares, each with a notional nominal value of 1.00 euro. The entire share capital is fully paid in. As in 2015 all shares have been issued with equal rights. As in the previous year 50,000 thousand of these shares are held by mobilcom-debitel Logistik GmbH, Schleswig, which in turn is wholly owned by the company, unchanged to the prior year. The treasury shares were deducted unchanged to the previous year from the capital reserve at their acquisition cost of 50 thousand euros.

Pursuant to section 71 (1) no. 8 of the German Stock Corporation Act (AktG), the Executive Board is authorised by the Annual General Meeting of 12 May 2016 to purchase treasury shares amounting to a total of 10 per cent of the share capital existing at the time of the resolution on 12 May 2016 with the approval of the Supervisory Board or – if this amount is lower – the share capital existing at the time this authorisation is exercised accordingly, for any permissible purpose within the legal restrictions. The authorisation is valid until 11 May 2021. In financial year 2016 the Executive Board made no use of this authorisation.

In addition to the authorisation pursuant to section 71 (1) no. 8 AktG, the Executive Board may additionally use equity derivatives to acquire treasury shares. This does not result in an increase in the maximum volume of shares which is permitted to be purchased; it only provides another alternative to acquire treasury shares.

The full wording of these authorisation resolutions was published under agenda items 8 and 9 of the invitation to the 2016 Annual General Meeting in the Federal Gazette.

## 25.2 Capital reserve

Major components of the capital reserve reported as at 31 December 2016 originate unchanged to the previous year from the capital increase in 2008 due to the acquisition of the debitel Group (349.8 million euros) as well as the merger between mobilcom AG and freenet.de AG to form freenet AG, which became effective in 2007, and the related acquisition of the minority shares in the former freenet.de AG (134.7 million euros).

## 25.3 Retained earnings

The Group's retained earnings for the financial year 2016 comprise the cumulative Group results attributable to the freenet AG shareholders, less the dividend payments. In 2016, a dividend of 1.55 euros per no-par-value share, making a total of 198.4 million euros, was paid out for the financial year 2015.

## 25.4 Minority shares

The non-controlling interests in equity are mainly (38,991 thousand euros; previous year: 50,040 thousand euros) attributable to the 75.01 per cent of shares which are held by non-controlling shareholders in EXARING. We have provided the following information regarding the assets and liabilities of EXARING as of 31 December 2016, before the consolidation of debt, income and expenses and also including the effects of the subsequent recognition of the purchase price allocation:

| EXARING AG<br>In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Non-current assets | 74,770 | 74,925 |
| Current assets | 7,261 | 22,822 |
| **Total assets** | **82,031** | **97,747** |
| Non-current liabilities | 19,514 | 21,761 |
| Current liabilities | 2,253 | 946 |
| **Total liabilities** | **21,767** | **22,707** |
| **Net assets** | **60,264** | **75,040** |
| **Thereof: Capital and reserves attributable to shareholders of freenet AG** | **38,991** | **50,040** |

## 25.5 Authorised Capital

New authorised capital was created at the ordinary Annual General Meeting held on 23 May 2013 (Authorised Capital 2013). According to these arrangements, the Executive Board is authorised, with the approval of the Supervisory Board, to increase the share capital up to 6 June 2018 by issuing new shares in return for payment in cash or kind on one or more occasions, but by no more than 12.8 million euros in all. The full wording of the Executive Board's authorisation was published in the Federal Gazette under agenda item 6 of the invitation to the 2013 Annual General Meeting.

New authorised capital was created at the ordinary Annual General Meeting held on 12 May 2016 (Authorised Capital 2016). According to these arrangements, the Executive Board is authorised, with the approval of the Supervisory Board, to increase the share capital up to 1 June 2021 by issuing new shares in return for payment in cash or kind on one or more occasions, but by no more than 12.8 million euros in all. The full wording of the Executive Board's authorisation was published in the Federal Gazette under agenda item 7 of the invitation to the 2016 Annual General Meeting. In financial year 2016 the Executive Board made no use of this authorisation.

## 25.6 Conditional Capital

In accordance with the resolution by the Annual General Meeting held on 12 May 2016, the company's share capital is subject to a conditional capital increase of up to 12.8 million euros by issuing up to 12,800,000 new no-par value registered shares, with each individual no-par-value share accounting for 1.00 euro of the share capital (conditional capital 2016). The purpose of the conditional capital increase is to enable registered no-par-value shares to be granted to the holders or creditors of convertible and/or option bonds which are issued on the basis of the authorisation as adopted by the Annual General Meeting of 12 May 2016 under agenda item 10, letter A) and which provides a conversion or option right or the right to delivery of shares in relation to the registered no-par-value shares of the company or which establishes a conversion or option obligation in relation to these shares.

The issue amount for the new no-par value registered shares is subject to regulations set out in section 4 (7) of the articles of incorporation. The conditional capital increase is to be carried out only to the extent to which conversion or option rights or a right to delivery of shares are utilised or to which holders or creditors with a conversion or option obligation meet their conversion or option obligation and if treasury shares are not used for settlement or if the company does not provide a cash settlement. The new registered no-par-value shares participate in the profits from the beginning of the financial year in which they are created. The Executive Board is authorised to fix the further details for carrying out the conditional capital increase. In financial year 2016 the Executive Board made no use of this authorisation.



# 26. Employee participation programmes

## 26.1 freenet AG LTIP programmes – Programme 1

In the financial year 2011, agreements granting long-term variable salary components (so-called LTIPs) had been concluded in relation to the employment agreements with the members of the Executive Board. The programme thus granted in 2011 is hereinafter referred to as "Programme 1".

This programme was terminated for Mr Vilanek in 2014 as a result of payment; it also terminated in 2015 for Mr Preisig and Mr Esch when all the virtual shares were paid out.

## 26.2 freenet AG LTIP programmes – Programme 2

On 26 February 2014, agreements concerning the contracts of employment that grant new LTIPs (hereinafter referred to as "Programme 2") were concluded with the members of the Executive Board.

Again in addition to the annual target agreement, a five-year target agreement was concluded in which EBITDA in the financial years 2014 to 2018 (for Mr Vilanek) and EBITDA in the financial years 2015 to 2019 (for Mr Preisig and Mr Esch) was designated as the target parameter. In the event of acquisitions which are financed by the issuing of new shares, the earnings targets are adjusted proportionately to the effective net dilution effect on the date on which new shares are issued. A basic amount has been defined in each beneficiary's employment contract for this component of compensation; as described below, and in accordance with the target attainment in each financial year, this basic amount is recorded as a positive or negative amount in a virtual account belonging to the respective Executive Board member and is paid out in annual instalments depending on the future development in its value, assuming that a credit balance is shown. Basic amounts totalling 1,050 thousand euros in each case have been defined for each financial year for the beneficiaries.

If the Group EBITDA target is attained in a financial year, 100 per cent of the basic amount is credited to the virtual account. If the Group EBITDA defined for 120 per cent target attainment is achieved, 200 per cent of the basic amount is credited to the virtual account. If the 120 per cent target is exceeded, only 200 per cent of the basic amount is credited to the virtual account. When the respective target attainment is being determined, the Supervisory Board is entitled to reward exceptional performance and success by setting a notional Group EBITDA amount. If such a step results in the target attainment of 120 per cent being exceeded in arithmetical terms, the Supervisory Board may also set a higher level for target attainment, bearing in mind that a maximum of 300 per cent of the basic amount may be credited to the virtual account. If the target attainment for the defined Group EBITDA is between the fixed 90 per cent target and 100 per cent, a percentage of the basic amount which is reduced on a linear basis is credited to the virtual account; if only 90 per cent of the target is attained, nothing is credited to the virtual account for the financial year in question. If Group EBITDA fails to meet the 90 per cent target, a negative amount of up to max. 200 per cent of the basic amount (if Group EBITDA is 80 per cent of the target or less) is debited to the virtual account. For the purpose of posting the (positive or negative) number of virtual shares in the virtual account, sub-accounts are maintained in the LTIP account bearing the designation of the financial year for which the number posted was ascertained.

The amount shown on the virtual account (known as the "allotment amount" as the product of the basic amount and the basic amount multiplier) is converted into virtual shares. This calculation is based on the reference value used for the share price, i.e. the average Xetra closing price on the 20 stock exchange trading days after the day on which the consolidated financial statements for the relevant financial year are published. In 2016, the Supervisory Board adopted a resolution (only for 2016) whereby the relevant share price is calculated on the basis of the average of Xetra closing prices of the 20 stock exchange trading days starting with 1 February 2016.

Starting from the end of the second financial year to benefit from the programme (for Mr Vilanek therefore starting from the financial year 2016, for Messrs Preisig and Esch starting from the financial year 2017), and in each case after the crediting to the virtual account of a (positive or negative) amount for the financial year ended, the respective beneficiary is entitled to have 25 per cent of the account balance paid out annually within a time frame of three months from the day which is 20 stock market trading days after the day on which the consolidated financial statements were published, provided that the account shows a credit balance. For this purpose, the respective balance of virtual shares is, in turn, converted into cash on the basis of the average Xetra closing price on the 20 stock exchange trading days after the day on which the consolidated financial statements for the relevant financial year are published. The increase in the share price is recognised only up to a price of 50.00 euros (cap). Irrespective of that, the gross payout amount is restricted additionally in each financial year as follows: the maximum gross amount to be paid out per financial year corresponds to 25 per cent of 500 per cent of the number of virtual shares in the respective sub-account, multiplied by the applicable share price on which the calculation of the allotment amount when the respective post was made in the sub-account was based.

For the purpose of conversion into virtual shares, dividend payments, as well as circumstances for which dilution protection stipulations are applicable in the case of marketable financial instruments dependent on the share value, must be included in the calculations. If the virtual account shows a negative balance at the point at which a payment is due to be made, the Executive Board member in question will receive a (further) payment only when the negative amount has been cancelled out by success in attaining the relevant target parameters for the subsequent year or years.

The obligation arising from the LTIP programme was determined at fair value in accordance with IFRS 2 with the help of a recognised valuation model. The main parameters in this valuation model are the share price of freenet AG as of the balance sheet date, the volatility of share prices in line with the remaining life of the LTIP programme, the estimate of target attainment for the respective financial year as well as the estimate of the discount rate. The graded vesting method is used; according to this method, the personnel expenses for all board members come into being as from the time when the programme is granted, i.e. in this case as from 26 February 2014.

The development of the holdings in the virtual accounts for each Executive Board member for Programme 2 is shown in the following table:

| Programme 2 | Number of virtual shares 31.12.2015 | Additions | Disposal of pay-out | Number of virtual shares 31. 12. 2016 | Provisions 31.12.2016 in EUR '000s |
|---|---|---|---|---|---|
| Christoph Vilanek | 41,214 | 40,411 | 0 | 81,625 | 3,437 |
| Joachim Preisig | 0 | 22,043 | 0 | 22,043 | 1,679 |
| Stephan Esch | 0 | 14,695 | 0 | 14,695 | 1,119 |
| **Total** | **41,214** | **77,149** | **0** | **118,363** | **6,235** |

The actual target attainment defined for 2015 is 120 per cent. Accordingly, 200 per cent of the basic amount is used for paying the following amounts into the virtual account: 1,100 thousand euros for Mr Vilanek, 600 thousand euros for Mr Preisig and 400 thousand euros for Mr Esch. After the consolidated financial statements for 2015 had been approved, this amount was converted into virtual shares for the financial year 2015 based on an average share price of 27.22 euros, with the result that a total of 77,149 virtual shares was credited to the virtual accounts of the board members. Target attainment for the financial year ended 2016 will be 120 per cent.

The Programme 2 resulted in personnel expenses of 2,092 thousand euros in the financial year 2016; the provision has been increased by 2,092 thousand euros from 4,143 thousand euros (as of 31 December 2015) to 6,235 thousand euros as of 31 December 2016.

## 26.3 LTIP Programme for senior executives – Programme 3

In January 2016, freenet AG and two other group companies granted long-term variable salary elements to senior executives below the Executive Board level (referred to in the following as "Programme 3").

The Programme 3 is based on the Group EBITDA for the financial years 2016 to 2020.

An LTIP account is maintained for each vested employee. LTIP amounts totalling 2,700 thousand euros have been defined. On 31 December 2015, the LTIP value was converted on one occasion to a number of LTIP shares by division by the relevant share price. The relevant share price was defined as the average Xetra closing price of all stock exchange trading days of December 2015, namely 30.69 euros. Overall, this resulted in an LTIP number of 87,976 virtual shares across all vested employees.

It is possible for payments to be made out of the non-interest-bearing LTIP accounts depending on the attainment of defined targets. The target for a specific financial year (2016 to 2020) is deemed to have been attained when the amount of Group EBITDA for the relevant financial year equals or exceeds the guidance. The guidance is the forecast for Group EBITDA communicated to the capital market by the Executive Board for the respective financial year. If this forecast fails to meet the target for a specific financial year, any surplus amount relating to the target applicable for a subsequent financial year can be used to retroactively compensate for this failure. However, the maximum target attainment is defined as 100 per cent in each case. The respective target attainment is determined immediately after approval of the audited consolidated financial statements by the Supervisory Board of freenet AG.

In each financial year, starting in 2017 for the financial year 2016, the vested employees are able to receive the payment from the LTIP account in a corridor of three months. If the target has been attained in the respective financial year, and if the beneficiary wishes to receive payment, the number of LTIP shares is multiplied with the payment element specified for the financial year and the payment factor. The payment elements have been defined as follows: 15 per cent for the financial year 2016, 15 per cent for the financial year 2017, 20 per cent for the financial year 2018 and 25 per cent for the financial years 2019 and 2020. The payment factor is the average Xetra closing price of the 20 stock exchange trading days starting with the first stock exchange trading day after the day on which the consolidated financial statements for the relevant financial year are published. Any dividend payments have to be taken into consideration for determining the payment factor and determining the number of virtual shares, and the standard dilution protection regulations are applicable.

If a vested employee does not request a payment in the annual three-month exercise corridor, this request can only be subsequently exercised in the same period of the respective following year. In the event of payment, the share price performance is only taken into consideration up to a share price of 50.00 euros (cap).

The obligation arising from Programme 3 was determined at fair value in accordance with IFRS 2 with the help of a recognised valuation model. The main parameters in this valuation model are the share price of freenet AG as of the balance sheet date, the volatility of share prices in line with the remaining life of the LTIP programme, the estimate of target attainment for the respective financial year as well as the estimate of the discount rate. The graded vesting method is used; according to this method, personnel expenses for all vested employees come into being as from the time when the programme is granted, i.e. in this case as from January 2016.

No payments out of the programme were possible as of the balance sheet date 31 December 2016. All vested employees are still in the company, so that the number of LTIP shares is still 87,976 virtual shares. The target for the financial year 2016 will be attained.

In the financial year 2016, the Programme 3 resulted in personnel expenses of 788 thousand euros; due to the increase in the payment into the provision from 0 (as of 31 December 2015) to 788 thousand euros.

# 27. Trade accounts payable, other liabilities and accruals

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

| | 31.12.2016 | | |
|---|---|---|---|
| In EUR '000s | Total | non-current | current |
| Trade accounts payable | 515,696 | 0 | 515,696 |
| Other non-derivative financial liabilities | 343,601 | 294,608 | 48,993 |
| **Financial liabilities** | **859,297** | **294,608** | **564,689** |
| Other liabilities and accruals | 5,923 | 0 | 5,923 |
| Advance payments received | 55,507 | 0 | 55,507 |
| **Non-financial liabilities** | **61,430** | **0** | **61,430** |
| **Total trade accounts payable and other liabilities and accruals** | **920,727** | **294,608** | **626,119** |

| | 31.12.2015 | | |
|---|---|---|---|
| In EUR '000s | Total | non-current | current |
| Trade accounts payable | 443,718 | 0 | 443,718 |
| Other non-derivative financial liabilities | 93,748 | 42,452 | 51,296 |
| **Financial liabilities** | **537,466** | **42,452** | **495,014** |
| Other liabilities and accruals | 2,285 | 0 | 2,285 |
| Advance payments received | 54,394 | 0 | 54,394 |
| **Non-financial liabilities** | **56,679** | **0** | **56,679** |
| **Total trade accounts payable and other liabilities and accruals** | **594,145** | **42,452** | **551,693** |

For the purposes of the above table, the balance sheet item "Sundry liabilities and accruals" has been broken down into advance payments received and other liabilities and accruals as well as other non-derivative financial liabilities. As was the case in the previous year, as at 31 December 2016, there are no liabilities vis-a-vis related parties; please refer to note 35, Transactions with related parties.

Of the figure shown for liabilities, 626,119 thousand euros (previous year: 551,693 thousand euros) are due within the next twelve months. Liabilities amounting to 94,903 thousand euros (previous year: 29,582 thousand euros) have a maturity of between one year and five years; liabilities of 199,705 thousand euros (previous year: 12,870 thousand euros) are due in more than five years.

For long-term other liabilities and accruals, the market value is approximately equivalent to the recognised book value due to the discounting.

Of the figure shown for the liabilities, which is combined under the financial liabilities, 564,689 thousand euros (previous year: 495,041 thousand euros) fall due within one year, 94,903 thousand euros (previous year: 29,582 thousand euros) fall due between one and five years and 199,705 thousand euros (previous year: 12,870 thousand euros) fall due after more than five years after the balance sheet date.

The finance lease liabilities shown as of the balance sheet date are a framework rental agreement with an infrastructure provider regarding the use of radio infrastructures (such as towers and masts) at radio locations and other areas, due to run until 31 December 2027. The Media Broadcast Group has the right to demand that the agreement be extended by ten years until 31 December 2037. The probability of this extension option being exercised has been assumed to be less than 50 per cent.

The carrying amounts of the finance lease assets were stated as 303,191 thousand euros for technical equipment, plant and machinery as of 31 December 2016.

| In EUR `000s | 31.12.2016 |
|---|---|
| Within one year | 37,000 |
| Within one and five years | 135,737 |
| Greater than five years | 215,234 |
| **Total** | **387,971** |
| **Interest share of future leasing rates** | |
| Within one year | -12,620 |
| Within one and five years | -40,874 |
| Greater than five years | -28,142 |
| **Present value of total liabilities from finance lease** | **306,335** |

The maturities of the overall finance lease liabilities are shown below:

| In EUR '000s | 31.12.2016 |
|---|---|
| Within one year | 24,380 |
| Within one and five years | 94,863 |
| Greater than five years | 187,092 |
| **Total** | **306,335** |

For the Media Broadcast Group finance lease did not exist in the previous year.

The figure disclosed in the balance sheet corresponds to the present value of the contractual minimum leasing payments. The interest rate used as the basis for recognising the resultant financing liabilities is 4.12 per cent.

# 28. Current income tax liabilities

Current income tax liabilities consist mainly of anticipated additional corporation tax and trade tax payments for previous financial years.

# 29. Financial debt

Financial debt is structured as follows:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| **Non-Current** | | |
| Liabilities from promissory notes | 1,069,318 | 218,276 |
| Liabilities due to banks | 604,553 | 106 |
| **Total** | **1,673,871** | **218,382** |
| | | |
| **Current** | | |
| Liabilities from corporate bonds | 0 | 419,479 |
| Liabilities from promissory notes | 60,146 | 919 |
| Liabilities due to banks | 156 | 134 |
| **Total** | **60,302** | **420,532** |

In April 2011, freenet AG placed a five-year corporate bond with a volume of 400.0 million euros and an annual coupon of 7.125 per cent on the capital market as some of the instruments for repaying private equity financing. The bond was repaid in full, including interest, on time on 20 April 2016.

In addition, freenet AG had concluded a credit facility for up to 300.0 million euros in December 2013. This facility was not utilised in 2016; it was terminated by the company in March 2016, and was replaced by a more extensive syndicated bank loan.

At the beginning of the reporting period, freenet AG took advantage of the favourable interest rate climate and raised debt totalling up to 1.7 billion euros. For financing the transactions carried out in the first quarter of 2016 and for refinancing the corporate bond which fell due upon final maturity in April 2016, the company raised a borrower's note loan and a syndicated bank loan.

The borrower's note loan in the amount of 560.0 million euros was successfully placed at the end of February 2016 with domestic and international institutional investors – in a total of five tranches with maturities of between five and ten years and with an average rate over these maturities of 1.12 per cent per annum.

The syndicated bank loan has a total volume of 1.14 billion euros and permits the company to draw funds in three different tranches for possible acquisitions and current operations. The first two tranches were used as bridging loans for the two acquisitions and equity participations carried out at the end of 2015 or in the first quarter of 2016, and were also used for refinancing the corporate bond which expired in April 2016.

The first tranche with a volume of 240.0 million euros had a maturity of 12 plus 6 months; interest is applied at a variable rate, with an initial margin of 0.8 per cent. This tranche was completely repaid with the issue of a second borrower's note loan in the autumn of 2016.

The second tranche has a maturity of three years; interest is applied at a variable rate, with an initial margin of 2.1 per cent. The second tranche, which provides for max. 800.0 million euros, has been utilised to the extent of 720.0 million euros (nominal) for the acquisition of Sunrise Communications Group AG. The remaining line of 80.0 million euros has not been drawn down. After the issue of a second borrower's note loan in the autumn of 2016, a total of 110.0 million euros was repaid; accordingly, this tranche comprised a volume of 610.0 million euros at the end of 2016.

The third tranche has a volume of 100.0 million euros; interest is also applied at a variable rate, with an initial margin of 1.8 per cent. It is designed specifically as a revolving credit facility. Accordingly, the funds can be drawn down and repaid at any time during the five-year maturity. As at the end of 2016, this tranche was completely unused.

For funding the syndicated bank loan, freenet AG at the end of October 2016 successfully placed a borrower's note loan due upon final maturity with five tranches for a total of 350.0 million euros. The transaction which was carried out on an arm's-length basis was supported by Bayerische Landesbank, Landesbank Baden-Württemberg, Norddeutsche Landesbank and ING Bank. The transaction was taken up over the entire volume at the bottom end of the respective marketing range with an initial average rate of 1.11 per cent per annum and maturities of between four and eight years. The borrower's note loan comprises two four-year tranches with a fixed coupon and one variable coupon of 1.00 per cent per annum, one six-year tranche with a fixed coupon of 1.28 per cent per annum, a six-year tranche with a variable coupon of 1.20 per cent per annum as well as an eight-year tranche with a fixed coupon of 1.68 per cent per annum. With this transaction, freenet was able to confirm its investment grade rating.

The revolving credit line for a maximum of 100.0 million euros had, as in the previous year, not been utilised as at the balance sheet date.

The borrower's note loans from the years 2012 and 2015 with a total nominal amount of 219.0 million euros as well as the borrower's note loans placed in February and October 2016 with a total nominal volume of 910.0 million euros are shown, after charges, with an amount of 1,129.3 million euros in the liabilities of borrower's note loans (thereof non-current: 1,069.3 million euros, thereof current: 60.1 million euros).

The second tranche of the syndicated bank loan with a nominal amount of 610.0 million euros is shown, less charges, in an amount of 604.6 million euros under the liabilities due to banks (thereof non-current: 604.5 million euros).

As of 31 December 2016, the net financial debt amounted to 725.8 million euros (previous year: 369.2 million euros). For this parameter, the financial debt (31 December 2016: 1,734.2 million euros, previous year: 638.9 million euros) is reduced by the liquid assets (31 December 2016: 318.2 million euros, previous year: 269.8 million euros) and the interest in the market value of Sunrise as of 31 December 2016 (11,051,578 shares multiplied by the closing price of 62.45 euros (source: Bloomberg).

# 30. Pension provisions and similar obligations

The pension obligations are based on defined benefit and contribution plans. The pension benefit provided in each case is the payment of a lifetime retirement pension upon reaching the age of 60 or 65 and the payment of benefits to surviving dependants. The pension benefits are partly financed by a reinsured benevolent fund. All pension commitments are always determined by the salary amount and the length of service at the company.

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

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Present value of funded obligations | 21,026 | 16,162 |
| Present value of unfunded obligations | 79,541 | 41,604 |
| **Sub-total present value of obligation** | **100,567** | **57,766** |
| Fair value of plan assets | -7,929 | -6,575 |
| **Provision shown in balance sheet** | **92,638** | **51,191** |

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

The increase in the pension provisions in the financial year 2016 is mainly attributable to the initial inclusion of obligations of the Media Broadcast Group.

The following table sets out the development in the present value of the funded and non-funded obligations:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| **As of 1.1.** | **57,766** | **64,990** |
| Change in group of consolidated companies as of 18 March 2016 (Media Broadcast Group) | 30,349 | 0 |
| Current service costs | 1,858 | 1,122 |
| Past service costs | -109 | 0 |
| Interest expense | 1,843 | 1,232 |
| Employees' contributions | 29 | 28 |
| Actuarial losses (+)/gains (-) | | |
| Thereof due to experience adjustments | 45 | 284 |
| Thereof due to changes in financial assumptions | 10,124 | -8,902 |
| **Sub-total actuarial losses** | **10,169** | **-8,618** |
| Benefit payments | -1,338 | -988 |
| **As of 31.12.** | **100,567** | **57,766** |

The weighted average remaining term of the obligations as of 31 December 2016 amounted to 27.2 years for the freenet programme (previous year: 27.3 years), 18.2 years for the debitel programmes (previous year: 17.8 years) and 10.0 years for the programmes of the Media Broadcast Group.

The following amounts have been shown for the defined benefit plans for the current reporting period and the previous reporting periods:

| In EUR '000s | 2016 | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Present value of funded obligations | 21,026 | 16,162 | 17,461 | 9,920 | 9,777 |
| Present value of unfunded obligations | 79,541 | 41,604 | 47,529 | 38,751 | 39,103 |
| Fair value of plan assets | -7,929 | -6,575 | -5,644 | -4,302 | -3,894 |
| **Net deficit of defined benefit plans** | **92,638** | **51,191** | **59,346** | **44,369** | **44,986** |
| Experience-based adjustments of the liabilities of the plan | 45 | 284 | 45 | 95 | 35 |
| Experience-based adjustments of the assets of the plan | -112 | -226 | 512 | -383 | 51 |

The plan assets consist of several reinsurance policies concluded by the benefit fund set up for this purpose with an aggregate fair value of 7,929 thousand euros (previous year: 6,575 thousand euros). The reinsurance policies put the plan assets in equity funds or shares, which are quoted in an active market. There is no active market for the reinsurance policies.

The development of fair value is set out in the table below:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| **As of 1.1.** | **6,575** | **5,644** |
| Expected income from plan assets (with actuarial interest rate) | 183 | 121 |
| Difference between calculated and actual income from plan assets (recognised in other comprehensive income) | -112 | -226 |
| Employer's contribution to plan assets | 1,283 | 1,036 |
| **As of 31.12.** | **7,929** | **6,575** |

The actual income from the plan assets amounts to 71 thousand euros (previous year: -105 thousand euros), and is calculated as the sum of the calculated income from the plan assets and the actuarial profits or losses.

For the financial year 2017, freenet is expecting payments of 1,282 thousand euros into the plan assets and payments of 2,182 thousand euros out of the plan assets for pensions. In the previous year 2015, freenet had expected for the financial year 2016 payments of 1,036 thousand euros into the plan assets and payments of 954 thousand euros out of the plan assets for pensions.

The amounts recognised as provisions in the balance sheet developed as follows:

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| **As of 1.1.** | **51,191** | **59,346** |
| Consolidation-related changes as of 18 March 2016 (Media Broadcast Group) | 30,349 | 0 |
| Current service costs | 1,858 | 1,122 |
| Past service costs | -109 | 0 |
| Interest expense | 1,659 | 1,111 |
| **Sub-total consolidated comprehensive expense** | **3,408** | **2,233** |
| Remeasurements | | |
| Experience-based profits (-)/losses (+) | 45 | 284 |
| Profits(-)/losses(-) due to changes in financial parameters | 10,124 | -8,902 |
| Income(-)/Expense(+) from plan assets not contained in interest result | 112 | 226 |
| **Sub-total remeasurements recognised in other comprehensive income** | **10,281** | **-8,392** |
| Benefit payments | -1,338 | -988 |
| Employer's contribution to plan assets | -1,282 | -1,036 |
| Employees' contributions | 29 | 28 |
| **As of 31.12.** | **92,638** | **51,191** |

The main actuarial assumptions were as follows:

| In % | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Discount rate (programme freenet, debitel) | 1.90 | 2.60 |
| Discount rate (programme Media Broadcast Group) | 1.41 | 1.39 |
| Future salary increases (programme debitel) | 1.50 | 1.50 |
| Future salary increases (programme freenet) | 0.00 | 0.00 |
| Future salary increases (programme Media Broadcast Group) | 2.25 | 2.25 |
| Future pension increases (programme debitel) | 1.25 | 1.25 |
| Future pension increases (programme freenet) | 1.75 | 1.75 |
| Future pension increases (programme Media Broadcast Group) | 1.70 | 1.70 |

The RT 2005G mortality tables devised by Dr Klaus Heubeck have been used as the biometric basis.

The sensitivities of the present value of the funded and unfunded obligations have been calculated on the basis of the actuarial report. We have made the following comments in this respect.

| **As of 31.12.2016**<br>In EUR '000s | **Change in present value** | |
|---|---|---|
| | **Increase** | **Decrease** |
| Increase of 1.0 percentage points in discount rate | | 15,218 |
| Reduction of 1.0 percentage points in discount rate | 19,870 | |
| Increase of 0.5 percentage points in future salary increases | 543 | |
| Reduction of 0.5 percentage points in future salary increases | | 22 |
| Increase of 0.25 percentage points in future pension increases | 1,514 | |
| Reduction of 0.25 percentage points in future pension increases | | 1,433 |
| Life expectancy: Age shift +2 years | 4,406 | |

| **As of 31.12.2015**<br>In EUR '000s | **Change in present value** | |
|---|---|---|
| | **Increase** | **Decrease** |
| Increase of 1.0 percentage points in discount rate | | 10,032 |
| Reduction of 1.0 percentage points in discount rate | 13,316 | |
| Increase of 0.5 percentage points in future salary increases | 420 | |
| Reduction of 0.5 percentage points in future salary increases | | 1 |
| Increase of 0.25 percentage points in future pension increases | 1,198 | |
| Reduction of 0.25 percentage points in future pension increases | | 1,139 |
| Life expectancy: Age shift +2 years | 2,769 | |

The sensitivities were calculated on the basis of the same holdings and using the same valuation method as that used for determining the extent of the obligation as of 31 December 2016. For this purpose, one parameter was varied and the other parameters were left unchanged. Any interdependencies between individual parameters which occur in practise are disregarded.

# 31. Other provisions

The following overview gives a breakdown of the development of the provisions` carrying amounts:

| In EUR '000s | **1.1.2016** | **Addition initial consolidation** | **Consumption** | **Reversal** | **Compounding/Discounting** | **Allocation** | **Reclassification** | **31.12.2016** |
|---|---|---|---|---|---|---|---|---|
| Contingent losses | 2,644 | 0 | 727 | 33 | 11 | 4,757 | 0 | 6,652 |
| Litigation risks | 5,431 | 7,861 | 755 | 2,758 | 0 | 328 | 0 | 10,107 |
| Dismantling obligations | 3,956 | 50,613 | 227 | 5,567 | -361 | 219 | 653 | 49,286 |
| Employee incentive programmes | 4,144 | 0 | 0 | 0 | 0 | 2,880 | 0 | 7,024 |
| Service anniversaries | 858 | 277 | 298 | 3 | 0 | 394 | 0 | 1,228 |
| Restructuring | 3,466 | 4,014 | 4,273 | 0 | 32 | 211 | 0 | 3,450 |
| Warranty/guarantee | 1,547 | 0 | 780 | 181 | 0 | 11 | 0 | 597 |
| Storage costs | 308 | 196 | 0 | 12 | 47 | 0 | 0 | 539 |
| License costs | 5,145 | 0 | 104 | 1,080 | 0 | 274 | 0 | 4,235 |
| Other | 765 | 2,832 | 813 | 60 | 14 | 2,251 | 0 | 4,989 |
| **Total** | **28,264** | **65,793** | **7,977** | **9,694** | **-257** | **11,325** | **653** | **88,107** |
| thereof non-current | 8,044 | | | | | | | 58,559 |
| thereof current | 20,220 | | | | | | | 29,548 |

As a result of the acquisition of the Media Broadcast Group, the company also acquired obligations for semi-retirement and long-time work accounts. These obligations are netted with the fair values of the corresponding plan assets as of each balance sheet date. As of 31 December 2016, the provisions before netting for long-time work accounts amounted to 6,259 thousand euros, and the corresponding provisions for semi-retirement amounted to 4,450 thousand euros.

| In EUR `000s | 2016 |
|---|---|
| **Long-term work accounts** | |
| Obligation at the time of initial consolidation | 5,817 |
| Proceeds from long-term accounts | -118 |
| Personnel expense | 477 |
| Interest expense | 83 |
| **Obligation as of 31.12. before netting** | **6,259** |
| | |
| Fair value of plan assets at the time of initial consolidation | 7,808 |
| Proceeds from plan assets | -1,473 |
| Income from plan assets | 234 |
| **Plan assets as of 31.12.** | **6,569** |

| In EUR `000s | 2016 |
|---|---|
| **Partial retirement** | |
| Obligation at the time of initial consolidation | 4,340 |
| Personnel expense | 98 |
| Interest expense | 12 |
| **Obligation as of 31.12. before netting** | **4,450** |
| | |
| Fair value of plan assets at the time of initial consolidation | 3,161 |
| Proceeds from plan assets | 0 |
| Income from plan assets | 113 |
| **Plan assets as of 31.12.** | **3,274** |

The remaining provision of 1,176 thousand euros has been shown in the schedule of provisions under “Other”.

The provisions for contingent losses relate to pending services in connection with the Group’s landline activities amounting to 413 thousand euros, with the outflow of assets being expected to take place in the amount of 270 thousand euros in 2017 and in the amount of 143 thousand euros in 2018.

Provisions for contingent losses have also been created for vacancy costs incurred with rented shops and office buildings (867 thousand euros); the outflow of assets is expected to be seen in full in 2017. Finally, the provisions for contingent losses include a sum of 5,372 thousand euros for losses expected from negative-margin tariffs, for which the likely outflow of assets is expected in 2017.

The provision for reinstatement obligations resulting from the acquisition of the Media Broadcast Group mainly comprises obligations for the reinstatement of radio infrastructure at numerous locations. Following the probable expiry of the underlying rental agreements, the outflow of funds is expected to be 4,578 thousand euros in 2017 and 40,787 thousand euros in the years from 2025 to 2030. There are further obligations for the reinstatement of tenant fittings at various technology and administration locations of the Group. Following the probable expiry of the underlying rental agreements, the outflow of funds is expected to be 2,314 thousand euros in 2016 and 1,607 thousand euros in the years from 2018 to 2026.

Provisions for service anniversaries have been formed; the outflow of assets for 2017 is expected to be 168 thousand euros and the outflow of assets for the years 2018 to 2036 is expected to be 1,060 thousand euros. A discount rate of 1.2 per cent and an average period of eight years between the balance sheet date and the actual payment have been assumed as the basis for calculation.

The provisions for litigation mainly relate to the initial consolidation of the Media Broadcast Group. A figure of 7,500 thousand euros has also been set aside to cover a litigation risk within the framework of the purchase price allocation. Further amounts continue to relate to the probable costs of various legal actions against group companies as well as other as yet unresolved disputes with third parties. Most of these provisions related to litigation with former trade partners and customers as well as issues of competition law. The Group is anticipating an asset outflow of 2,607 thousand euros in 2017 as well as 7,500 thousand euros in 2018 or later. To avoid disclosing prematurely, and therefore endangering, the legal and negotiation position, we shall refrain from giving further information at this juncture.

Further details concerning the creation of provisions for employee participation programmes are documented under note 26, Employee participation programmes.

The provisions for restructuring mainly comprise personnel expenses for severance payments. The outflow of assets for these provisions is expected for 2017.

# 32. Other financial obligations, contingencies and collateral for loans

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

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| **Rent and leasing obligations** | | |
| Due within one year | 59,909 | 36,071 |
| Due within one and five years | 85,678 | 65,507 |
| Due term greater than five years | 11,386 | 12,853 |
| | 156,973 | 114,431 |
| Thereof already recognised as provision for contingent losses | 729 | 1,689 |
| | **156,244** | **112,742** |
| **Maintenance, support and other obligations** | | |
| Due within one year | 9,967 | 12,661 |
| Due within one and five years | 769 | 122 |
| Due term greater than five years | 0 | 0 |
| | **10,736** | **12,783** |
| **Order commitments** | | |
| Regarding intangible assets | 0 | 21 |
| Regarding property, plant and equipment | 11,457 | 419 |
| Regarding inventories, expenses and services | 148,986 | 5,627 |
| | **160,443** | **6,067** |
| **Total** | **327,423** | **131,592** |

The obligations from rental and lease agreements are derived mainly from the rental of office buildings, shops and hardware leasing as well as rental obligations resulting from the shared use of locations with public-sector broadcasting stations. On the other hand, the revenue expected from subletting arrangements amounts to 5,928 thousand euros (previous year: 8,501 thousand euros). 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 currently valid conditions in the agreements.

In the financial year 2016, and within the framework of a sale-and-leaseback agreement, broadcasting technology of the Media Broadcast Group was sold and leased back for a period of five years without an extension option. With regard to the resultant inflows, please refer to note 33.2 of the notes to the consolidated financial statements. The profit resulting from the transaction was received immediately. The above table contains the minimum lease payments for the operating lease resulting from the sale-and-leaseback agreement.

The obligations arising from maintenance, support and other agreements relate predominantly to agreements for the maintenance of IT hardware and databases, building services engineering and the network infrastructure.

The order commitments as at the end of the financial year amounted to 160,443 thousand euros (previous year: 6,067 thousand euros). Of this sum, 11,457 thousand euros (previous year: 440 thousand euros) is attributable to the procurement of fixed assets. There are other acceptance obligations amounting to 148,986 thousand euros (previous year: 5,627 thousand euros). The tremendous increase is again due to the acquisition of the Media Broadcast Group, and primarily relates to obligations arising from the sourcing of electricity for production at the various rental locations as well as broadband connections within the framework of media networks (audio and video broadcasts).

There are further contingencies resulting from letters of comfort and rental guarantees; they amounted to 23,257 thousand euros as of the balance sheet date (previous year: 16,570 thousand euros). It is not expected that any claims will be submitted under the terms of the letters of comfort and rent guarantees because it is expected that the corresponding invoices will be paid in line with the contractual agreements and that the corresponding rental agreements will be paid regularly.

The following contingent liability exists as at 31 December 2016: In a letter from the Federal Ministry of Finance dated 4 December 2014 and a simultaneous addendum to the VAT application decree, the fiscal authority issued the following rule: If the intermediary in a mobile communications contract supplies the customer in the intermediary's own name with a mobile communications device or some other electronic article, and if the mobile communications company grants the intermediary a commission dependent on the supply of the mobile communications device or other electronic articles on the basis of a contractual agreement, or part of a commission dependent on the above, such a commission or part of a commission shall not be regarded as remuneration for an intermediary brokering role vis-à-vis the mobile communications company, but rather as remuneration from a third party as defined by section 10 (1) sentence 3 of the German VAT Act (UStG) for the supply of the mobile communications device or the other electronic article. This applies irrespective of the amount of any additional payment to be made by the customer. The application of this rule as from 1 January 2015 will not involve any reportable risks for the company. As for the revenue reported before 1 January 2015, the company regards it as very likely indeed that the rule specified above will have no significant negative effects for freenet AG under VAT law. However, a low risk remains for the revenue reported before 1 January 2015 for assessment periods that have not been audited conclusively; if this risk materialises, freenet AG would have to refund some of its input tax to the tax authorities.



# 33. Notes to the consolidated cash flow statement

In the consolidated cash flow statement, the figures are reported for the Group as a whole (continued and discontinued operations). In the financial year 2016, as in the previous year, the cash flows were attributable solely to continued operations.

Cash and cash equivalents consist of cash at banks, cash in hand, cheques, short-term money market instruments that can be liquidated at any time and current financial liabilities, each with an original term of up to three months. As in the previous year, cash and cash equivalents do not include any liquid funds from discontinued operations.

The payment flows are broken down into operating activities, investing activities and financing activities. The indirect presentation method has been used to present cash flow from operating activities.

The item “Increase in net working capital, if not attributable to investing or financing activities” contains the change in the balance sheet items “Trade accounts receivable”, “Other receivables and other assets”, “Inventories”, “Trade accounts payable”, “Sundry liabilities and accruals”, “Other provisions”, and the change in other assets and liabilities if not attributable to investing or financing activities.

## 33.1 Cash flow from operating activities

Compared with the corresponding period last year, cash flow from operating activities increased by 74.7 million euros to 389.6 million euros. Excluding the non-cash-effective earnings elements from the associated company Sunrise (36.5 million euros), EBITDA has increased by 32.2 million euros compared with the previous year. In the financial year 2016, freenet AG received a dividend payment of 30.1 million euros as a result of the dividend payment of 3.00 CHF per share adopted in the annual general meeting of Sunrise on 15 April 2016. Net working capital increased in 2016 by 3.8 million euros, compared with an increase of 10.3 million euros in the previous year. The increase of 3.8 million euros in net working capital in 2016 can be attributed mainly to the scheduled reduction of 25.0 million euros in liabilities and accruals vis-à-vis distribution partners arising from distribution rights impacting cash flows. This has been opposed mainly by the volume of factoring of mobile option receivables, which increased by 22.8 million euros compared with 31 December 2015 – please refer in this respect to note 34.6, Transfer of financial assets.

In addition, there were net cash outflows in the financial year 2016 amounting to 40.0 million euros (previous year: 44.3 million euros) that resulted from income tax payments and refunds.

## 33.2 Cash flow from investing activities

In 2016, the cash inflow from investing activities developed from -28.5 million euros in the previous year to -862.4 million euros. This was due primarily to the outflow of 738.9 million euros for the acquisition of 24.56 per cent of the shares in Sunrise, which are shown under the outflows for the acquisition of companies accounted for using the equity method.

The outflows for the acquisition of subsidiaries relate to the acquisition of 100 per cent of the shares in the Media Broadcast Group – a total of 101.7 million euros was paid for this purpose in the financial year 2016, whereas the Group received liquid assets of 25.1 million euros via the initial consolidation of the Media Broadcast Group as of 18 March 2016 – resulting in outflows of 76.6 million euros for the acquisition of subsidiaries.

The cash outflows for investments in intangible fixed assets and in property, plant and equipment, netted out against the cash inflows from such assets, increased in 2016 by 17.7 million euros over the previous year from 30.4 million euros to 48.1 million euros. The cash-effective investments were financed entirely out of the company’s own resources, and mainly related to property, plant and equipment of the Media Broadcast Group. The inflows from the disposal of assets are mainly attributable to sale-and-leaseback transactions of the Media Broadcast Group (12.7 million euros).

## 33.3 Cash flow from financing activities

In the reporting quarter, cash flow from financing activities improved to 521.2 million euros compared with -128.7 million euros in the previous year.

For financing the transactions which had been carried out and for refinancing the corporate bond which fell due upon final maturity in 2016, the Group received proceeds of 1,853.6 million euros in the financial year 2016 due to the raising of two borrower's note loans and a syndicated bank loan. In this context, please refer to note 29, Financial debt.

The outflows relating to the repayment of financial debt of 1,047.3 million euros essentially comprise the repayment of the corporate bond with a volume of 400.0 million euros, the repayment of parts of the syndicated bank loan of 350.0 million euros as well as the repayment of shareholder and bank loans of the Media Broadcast Group in the amount of 297.2 million euros.

Dividend payments had a negative impact on the cash flow from financing activities in the financial year ended in the amount of 198.4 million euros (previous year: 192.0 million euros).

In 2016, interest payments of 68.1 million euros were disclosed (mainly as a result of the refinancing); this represents an increase of 33.3 million euros compared with the previous year.

There were also payments of 18.6 million euros relating to the framework rental agreement of the Media Broadcast Group classified as a finance lease in the course of the purchase price allocation. Please refer to note 27, Trade accounts payable, other liabilities and accruals.

### 33.4 Calculating the underlying figure for the consolidated cash flow statement

The underlying figure for the cash flow statement is the earnings generated by ongoing and discontinued operations before interest and income taxes (EBIT). The following shows the way in which this EBIT figure is derived from the consolidated income statement.

| In EUR '000s | 1.1.2016-31.12.2016 | 1.1.2015-31.12.2015 |
|---|---|---|
| Earnings before taxes | 243,956 | 254,691 |
| Interest payable and similar expenses | 55,675 | 44,502 |
| Interest receivable and similar income | -809 | -418 |
| **Earnings before interest and taxes (EBIT)** | **298,822** | **298,775** |



# 34. Additional information concerning financial instruments

### 34.1 Disclosures in accordance with IFRS 7

This section provides an overview of the significance of financial instruments for the Group, while also providing additional information on balance sheet items which contain financial instruments.

We are setting out the following information for the purpose of presenting the financial instruments in the Group as at 31 December 2016 and 31 December 2015, their allocation to categories and the reconciliation with the corresponding valuation categories under IAS 39 (see tables on the opposite and following page):

## Financial instruments according to classes as of 31 December 2016

| December 2016 In EUR '000s | Valuation category according to IAS 39 | Carrying amount balance sheet 31.12.2016 | Value approach: Amortised cost | Value approach: Cost | Value approach: Fair value recognised in profit or loss | Value approach: Fair value recognised in equity | Non-financial assets/ liabilities | Fair value financial assets 31.12.2016 |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and cash equivalents | LR | 318,186 | 318,186 | | | | | -* |
| Other financial assets | AFS | 586 | | | | | | |
| Other financial assets (measured at cost) | AFS | 586 | | 586 | | | | -* |
| Trade accounts receivable | LR | 519,896 | 519,896 | | | | | -* |
| Other receivables and other assets | | 47,296 | | | | | 10,103 | |
| Other non-derivative financial assets | LR | 34,419 | 34,419 | | | | | -* |
| Available-for-sale financial assets | AFS | 2,774 | | | | 2,774 | | 2,774 |
| | | | | | | | | |
| **Liabilities** | | | | | | | | |
| Trade accounts payable | FLAC | 515,696 | 515,696 | | | | | -* |
| Borrowings | FLAC | 1,734,173 | 1,734,173 | | | | | 1,133,391 |
| Other liabilities and deferrals | | 405,031 | | | | | 61,430 | |
| Other non-derivative financial liabilities | FV | 343,601 | 343,601 | | | | | -* |
| | | | | | | | | |
| **Thereof aggregated by valuation categories acc. to IAS 39** | | | | | | | | |
| Available-for-sale financial instruments | AFS | 3,360 | | 586 | | 2,774 | | 2,774 |
| Loans and receivables | LR | 872,501 | 872,501 | | | | | 0* |
| Financial liabilities (measured at amortised cost) | FLAC | 2,593,470 | 2,593,470 | | | | | 1,133,391* |

* No fair value has been established for the positions; however, the carrying amount is a reasonable approximation of the fair value. This means that the aggregate fair value for the valuation categories LR and FLAC are considerably lower than the corresponding aggregate carrying amounts in the balance sheet.

## Financial instruments according to classes as of 31 December 2015 adjusted

| In EUR '000s | Valuation category according to IAS 39 | Carrying amount balance sheet 31.12.2015 | Value approach: Amortised cost | Value approach: Cost | Value approach: Fair value recognised in profit or loss | Value approach: Fair value recognised in equity | Non-financial assets/ liabilities | Fair value financial assets 31.12.2015 |
|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | |
| Cash and cash equivalents | LR | 269,761 | 269,761 | | | | | -* |
| Other financial assets | AFS | 1,517 | | | | | | |
| Other financial assets (measured at cost) | AFS | 503 | | 503 | | | | -* |
| Other financial assets (measured at fair value) | AFS | 1,014 | | | | 1,014 | | 1,014 |
| Trade accounts receivable | LR | 515,447 | 515,447 | | | | | -* |
| Other receivables and other assets | | 30,955 | | | | | 9,750 | |
| Other non-derivative financial assets | LR | 18,403 | 18,403 | | | | | -* |
| Available-for-sale financial assets | AFS | 2,802 | | | | 2,802 | | 2,802 |
| | | | | | | | | |
| **Liabilities** | | | | | | | | |
| Trade accounts payable | FLAC | 443,718 | 443,718 | | | | | -* |
| Borrowings | FLAC | 638,914 | 638,914 | | | | | 632,142 |
| Other liabilities and deferrals | | 150,427 | | | | | 56,679 | |
| Other non-derivative financial liabilities | FLAC | 93,748 | 93,748 | | | | | -* |
| | | | | | | | | |
| **Thereof aggregated by valuation categories acc. to IAS 39** | | | | | | | | |
| Available-for-sale financial instruments | AFS | 4,319 | | 503 | | 3.816 | | 3,816 |
| Loans and receivables | LR | 803,611 | 803,611 | | | | | 0* |
| Financial liabilities (measured at amortised cost) | FLAC | 1,176,380 | 1,176,380 | | | | | 632,142* |



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 carrying amount of the financial liability resulting from the put option in conjunction with the acquisition of MOTION TM corresponds to the fair value as of 31 December 2016.

The non-financial liabilities constitute that part of the balance sheet item "Sundry liabilities and accruals" which is not covered by the scope of IFRS 7.

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

The fair values of the long-term trade accounts receivables and other financial assets with remaining terms of more than one year correspond to the present values of the payments associated with the assets, with due consideration being given to the relevant interest parameters. Thanks to discounting using the effective interest rate method and based on the current interest rate level, there are only minor differences between the carrying amounts of these financial instruments and the fair values.

* No fair value has been established for the positions; however, the carrying amount is a reasonable approximation of the fair value. This means that the aggregate fair value for the valuation categories LR and FLAC are considerably lower than the corresponding aggregate carrying amounts in the balance sheet.

Other financial assets are measured at fair value. If it is not possible for the fair value to be reliably determined, the other financial assets are measured at cost of purchase. The shares are not listed publicly and there is no active market for them. Furthermore, a sale is not currently planned. If there are indications that fair values are lower, these are used.

For the other available-for-sale financial assets, the Group defines the fair value as the price in an active market.

Because of the maturity involved, the fair value of the current financial debt corresponds to the carrying amount. The fair value of the non-current financial liabilities exceeds their carrying amount by 9,630 thousand euros as at 31 December 2016 (previous year: 14,244 thousand euros). This difference results from the valuation of the borrower's note loan at fair value; this was ascertained as at the valuation date using up-to-date estimates of the company's own credit risk and the interest rate level.

The fair value of the derivative financial instruments that are not traded on an exchange is determined by the Group on the basis of recognised actuarial methods (discounted cash flow method or option price models). The expected future cash flows from the financial instrument are calculated on the basis of the relevant interest rate structure and forward curves and are then discounted to the closing date. The market value confirmations obtained from the external partners are periodically compared with the market values that have been calculated internally. The Group had no derivative financial instruments as at 31 December 2016.

The following overview shows the major parameters on which the assessment of the fair value of financial instruments, and the assessment of the financial instruments reported at fair value in accordance with IFRS 7 are based. The individual levels are defined in accordance with IFRS 13 as follows:

- Level 1:
  Unchanged use of prices from active markets for identical financial assets or financial liabilities (Deutsche Börse AG, Frankfurt stock exchange).
- Level 2:
  Use of input factors which are not the listed prices recognised in Level 1, but which are directly (i.e. in the form of a price) or indirectly (i.e. derived from prices) observable for the financial asset or the financial liability.
- Level 3:
  Use of input factors which are not based on observable market data for measuring the financial asset or the financial liability (input factors not based on observable market data). In financial year 2016 no transfer has occurred between the individual levels.

### Fair value hierarchy as of 31 December 2016

| In EUR'000s | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| **Assets** | | | | |
| Available-for-sale financial assets | 2,774 | 2,774 | 0 | 0 |
| **Liabilities** | | | | |
| Borrowings | 1,133,391 | 0 | 0 | 1,133,391 |

### Fair value hierarchy as of 31 December 2015 adjusted

| In EUR'000s | Total | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|
| **Assets** | | | | |
| Available-for-sale financial assets | 2,802 | 2,802 | 0 | 0 |
| Other financial assets | 1,014 | 1,014 | 0 | 0 |
| **Liabilities** | | | | |
| Borrowings | 632,142 | 408,116 | 0 | 224,026 |

For the individual categories of financial instruments in accordance with IAS 39, the following net results were shown in the financial year 2016 and in the previous year:

### Net result by valuation categories 2016

| In EUR '000s | From interest | From subsequent measurement: At fair value through other comprehensive income | From subsequent measurement: Impairment/receivables losses | From disposals | Net result |
|---|---|---|---|---|---|
| Available-for-sale financial instruments (AFS) | 0 | -2 | 0 | 0 | -2 |
| Loans and receivables (LR) | 58 | 0 | -56,394 | -769 | -57,105 |
| Financial liabilities measured at amortised cost (FLAC) | -51,101 | 0 | 0 | 0 | -51,101 |
| **Total** | **-51,043** | **-2** | **-56,394** | **-769** | **-108,208** |

### Net result by valuation categories 2015

| In EUR '000s | From interest | From subsequent measurement: At fair value through other comprehensive income | From subsequent measurement: Impairment/receivables losses | From disposals | Net result |
|---|---|---|---|---|---|
| Available-for-sale financial instruments (AFS) | 0 | -57 | 0 | 0 | -57 |
| Loans and receivables (LR) | -251 | 0 | -44,309 | -87 | -44,647 |
| Financial liabilities measured at amortised cost (FLAC) | -39,436 | 0 | 0 | 0 | -39,436 |
| **Total** | **-39,687** | **-57** | **-44,309** | **-87** | **-84,140** |

Net gains and losses from loans and receivables include changes in the allowances, gains and losses from derecognition as well as inflows and recoveries in the value of previously written-off loans and receivables.

Net gains or losses attributable to the category of financial liabilities measured at amortised cost include the income and expenses from the measurement of the financial liability from the put option in connection with the acquisition of MOTION TM (carrying amount of the liabilities as of 31 December 2016: 12,614 thousand euros; previous year: 12,870 thousand euros). A sensitivity calculation regarding the enterprise value has established that the figure stated for the financial liability would have been 1.2 million euros higher if the enterprise value increased by 10 per cent, and that it would have been 1.2 million euros lower if the enterprise value declined by 10 per cent.

Net gains and losses from the category of available-for-sale financial instruments include impairments.

Net gains and losses from financial liabilities measured at amortised cost of purchase consist of interest expenses.

Disclosures concerning interest income and interest expenses from the financial assets and financial liabilities not measured at fair value through profit or loss are based on the application of the effective interest rate method.

### Netting of financial assets and liabilities as of 31 December 2016

| In EUR '000s | Gross amount before balance | Balance amounts | Net amount in balance | Fair Value of financial securities | Total net amount |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Trade accounts receivable | 526,196 | 6,300 | 519,896 | 0 | 519,896 |
| Other receivables and other assets | 56,829 | 9,533 | 47,296 | 0 | 47,296 |
| **Total** | **583,025** | **15,833** | **567,192** | **0** | **567,192** |
| **Financial liabilities** | | | | | |
| Trade accounts payable | 521,996 | 6,300 | 515,696 | 4,000 | 511,696 |
| Other provisions | 97,640 | 9,533 | 88,107 | 0 | 88,107 |
| **Total** | **619,636** | **15,833** | **603,803** | **4,000** | **599,803** |

**Netting of financial assets and liabilities as of 31 December 2015**

| In EUR '000s | Gross amount before balance | Balance amounts | Net amount in balance | Fair Value of financial securities | Total net amount |
|---|---|---|---|---|---|
| **Financial assets** | | | | | |
| Trade accounts receivable | 521,447 | 6,000 | 515,447 | 0 | 515,447 |
| **Total** | **521,447** | **6,000** | **515,447** | **0** | **515,447** |
| **Financial liabilities** | | | | | |
| Trade accounts payable | 449,718 | 6,000 | 443,718 | 4,000 | 439,718 |
| **Total** | **449,718** | **6,000** | **443,718** | **4,000** | **439,718** |

Based on an agreement with a network operator to adjust the terms of payment, monthly advance payments are made for the mobile communications services rendered by the network operator in question. These are netted out on the balance sheet date and settled in the subsequent month. In addition to the netting amount of 6,300 thousand euros, there is also a long-term collateral payment of 4,000 thousand euros.

As a result of the acquisition of the Media Broadcast Group, the company has also taken on obligations for semi-retirement and long-time work accounts. These obligations are netted with the fair values of the corresponding plan assets as of every balance sheet date. As of the balance sheet date, the netted provisions for long-time work accounts amounted to 6,259 thousand euros, and the corresponding provisions for semi-retirement amounted to 3,274 thousand euros. We refer to our statements in note 31, Other provisions.

## 34.2 Principles and objectives of financial risk management and capital risk management

With regard to 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 with operational and finance-oriented activities.

The basic characteristics of financial policy, whose components are explained below, are determined by the Executive Board. In addition, certain financial transactions require the Executive Board's prior approval.

The Group Treasury department renders services to the business areas and coordinates access to the financial markets. It also monitors and manages the market and liquidity risks associated with the Group's business areas by way of regular internal risk reporting which analyses the risks in terms of their degree and scale. The overriding priority for the Group Treasury department is the principle of minimising risk; another important objective is to optimise net interest income. Prudent liquidity management controlled by the Group Treasury department involves holding an adequate reserve of cash and cash equivalents, the possibility of obtaining finance by way of adequate commitments from credit lines, and the possibility of closing open market positions. Liquidity risks are reduced by constantly monitoring the financial status and by maintaining adequate reserves in the form of credit lines.

The Group Treasury department is responsible for monitoring the default risks of major debtors (in particular distributors, dealers and other B2B partners) as well as regular internal reporting for these risks. Receivables due from end customers are monitored in the Receivables Management department. One of the department's primary objectives is to minimise the costs attributable to the default or impairment of receivables due from end customers and sales partners.

The Group's capital risk management is related to the shareholders' equity as shown in the consolidated balance sheet and to ratios derived there from.

The foremost objective of the Group's capital risk management is to monitor the financial covenants specified in the loan agreements, where failure to fulfil such financial covenants might lead to the loans being called in immediately. The main financial covenants are defined in relation to the equity ratio (32.5 per cent – previous year: 50.6 per cent) of the Group as well as the debt ratio. The debt ratio (1.7 – previous year: 1.0) indicates the relationship between net debt (1,734.2 million euros) less liquid assets (318.2 million euros), less the Sunrise share of market value as of 31 December 2016 (11,051,578 shares multiplied by the closing price of 62.45 euros - source: Bloomberg) and the EBITDA generated within the past 12 months.

All covenants are fulfilled as at the balance sheet date.

In order to actively manage the capital structure, the management is permitted to sell assets to reduce debt, as well as being entitled to implement measures such as issuing new shares.

The following information concerning the specific risks is based on information presented to the Executive Board.

## 34.3 Market risk

Our Group's activities are primarily exposed to financial risks resulting from changes in interest rates and currency exchange rates.

### 34.3.1 Interest rate risk

The liabilities shown under the financial debt relate to four borrower's note loans (disclosed as a total net amount of 1,129.5 million euros as of 31 December 2016 (previous year: 219.2 million euros) – including 457.1 million euros in relation to the variable-interest tranches) and a bank loan which is due upon final maturity and which features a variable interest rate (shown as a total net amount of 604.6 million euros as of 31 December 2016) (previous year: 0). The Group also has a revolving credit line amounting to 100.0 million euros (previous year: 300.0 million euros) that had again not been drawn on by the end of the year.

As at 31 December 2016, the Group reported variable-interest financial liabilities amounting to 1,061.7 million euros (previous year: 79.9 million euros). In this respect, the Group is exposed to interest rate risks. Although the interest rate risks are not explicitly secured, the cash holdings (which are invested mainly at variable interest rates based on EONIA or EURIBOR) serve as a natural hedge and accordingly mitigate interest rate risks arising from the variable-interest financial debt.

The Group Treasury department continuously monitors the various opportunities available for investing the liquid assets on the basis of the day-to-day liquidity planning at its disposal as well as the various options available for scheduling the debt. Changes in market interest rates could have an impact on the net interest income from originally variable-interest financial instruments and are included in the calculation process for results-related sensitivities.

In order to depict the market risks, the Group uses a sensitivity analysis that shows the effects of changes in interest rates on earnings and on shareholders' equity.

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

In the balance sheet, liabilities of 1,734.2 million euros are shown under short-term and long-term financial debt as at 31 December 2016 (previous year: 638.9 million euros), 1,061.7 million euros of which have variable interest rates. The variable-interest liabilities to banks as at the closing date were charged interest of 1.6 per cent. Of the aggregate amount shown for financial debt as at 31 December 2016, 60.3 million euros are shown as current debt. There is a mandatory repayment for 2016 for the repayment of the tranches of the borrower's note loan of 2012 for 54.5 million euros falling due in December 2017 as well as 5.8 million euros for expected payments of cumulative interest. As of 31 December 2016, interest was applied to the variable part of the loans in a corridor of 0.7 to 2.1 per cent. On the basis of market estimates, we are predicting a corridor of between 0.7 and 2.1 per cent for the variable part in 2017. This means that the cash outflows for the entire financial debt in 2017 would amount to 27.3 million euros. Based on the net position of variable-interest assets and liabilities measured at fair value, a parallel upward shift of 50 basis points in the interest rate curve would have an impact of -2.6 million euros on the result before tax (previous year: -157 thousand euros), while a downward shift of 50 basis points in the interest rate curve would have an impact of 1.8 million euros on the result before tax (previous year: 157 thousand euros).

Money market funds are subject to marginal interest rate fluctuations, so there is always a possibility of price losses. There is no significant risk, however, as the money has been invested in funds on a very short-term basis. There are no contractually defined maturity dates or interest adjustment dates, with returns coming from changes in the price of the instrument and any dividend payments. Based on the financial investments in money market funds and bonds shown in the balance sheet under other receivables and other assets and other financial assets, an upward shift of 5 per cent in the price of the acquired shares would have an impact of 139 thousand euros (previous year: 133 thousand euros) on shareholders' equity, while a downward shift of 5 per cent would have an impact of -139 thousand euros (previous year: -133 thousand euros) on shareholders' equity.

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

Changes in interest rates have an impact on fixed-income financial instruments only if they are recognised at fair value. The financial liabilities of freenet are therefore not exposed to an interest rate risk because they are recognised at amortised cost of purchase.

### 34.3.2 Foreign currency risk

Commercial transactions in foreign currencies are conducted to a limited extent in the Group. The foreign currency risk is generally hedged by concluding currency futures, or, if necessary, by way of cash holdings denominated in foreign currency.

All in all, the Group regards the foreign currency risk as negligible.

### 34.3.3 Exchange rate risk

With regard to the exchange rate risks, it must be borne in mind that the company holds an interest of 24.56 per cent in the share capital of Sunrise. Sunrise uses the Swiss franc (CHF) as the reporting currency for preparing its consolidated financial statements. The foreign currency risk between the euro and Swiss franc has an impact on determining both elements of the position of our consolidated income statement "Result of companies accounted for using the equity method", namely the interest in the current result of Sunrise and also the amortisation resulting from the shadow purchase price allocation regarding Sunrise. Accordingly, this exchange rate also has an influence on the results of operations of the freenet Group; however, this is considered to be minor at present.

## 34.4 Liquidity risk

The Group's general liquidity risk resides in the possibility that the company might possibly be unable to meet its financial obligations, for example the repayment of financial debt, the payment of purchasing obligations and the obligations from lease agreements.

Extensive financial planning instruments are used throughout the Group to monitor and control liquidity. Different planning horizons of up to one year are considered in connection with this. The short-term liquidity planning and control are carried out on a daily basis, each for the subsequent three months. This planning is updated daily by the Group Treasury department following liaison with the Accounting and Controlling departments on the basis of current data.

The Group also controls its liquidity risk by holding appropriate bank balances and credit lines at banks, and by monitoring continuously the forecast and actual cash flows. Reconciliations are also performed for the maturity profiles of the financial assets and liabilities. The Group uses a wide range of different financing instruments to reduce the liquidity risk.

The need for and investment of liquid funds in the Group is controlled centrally on the basis of several existing internal Group cash pooling agreements in which the significant companies in the freenet Group participate.

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

As at the balance sheet date, the Group had not utilised the revolving credit line of 100.0 million euros (previous year: 300.0 million euros) which had been provided. There are stringent restrictions on the company raising loans outside of these credit agreements, e. g. in order to finance future strategic investments.

Securities (money market funds and bonds in the securities deposit account) 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 might possibly be more difficult because there is no organised capital market for these shareholdings.

The Group's financial and operational scope is restricted by certain regulations in the loan agreements. These impose restrictions on the company, for example regarding changes in the Group's business operations, the implementation of internal Group measures to change its structure under company law, the provision of collateral, and any acquisitions or disposals of assets, especially shareholdings. The following tables show the contractually agreed undiscounted interest and redemption payments on the Group's original financial liabilities at the end of the financial years 2016 and 2015:

### Financial liabilities

| In EUR '000s | Carrying amount 31.12.2016 | Cash flows 2017 | | | Cash flows 2018 | | | Cash flows 2019 and later | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Interest (fixed) | Interest (variable) | Repayment | Interest (fixed) | Interest (variable) | Repayment | Interest (fixed) | Interest (variable) | Repayment |
| Trade accounts payable | 515,696 | | | 515,696 | | | | | | |
| Debt (liabilities due to banks) | 1,734,173 | 9,802 | 17,507 | 60,302 | 8,344 | 17,377 | 35 | 29,674 | 13,892 | 1,673,836 |
| Other non-derivative f inancial liabilities | 343,601 | 12,620 | | 48,993 | 11,616 | | 21,794 | 57,400 | | 272,814 |

### Financial liabilities

| In EUR '000s | Carrying amount 31.12.2015 | Cash flows 2016 | | | Cash flows 2017 | | | Cash flows 2018 and later | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | | Interest (fixed) | Interest (variable) | Repayment | Interest (fixed) | Interest (variable) | Repayment | Interest (fixed) | Interest (variable) | Repayment |
| Trade accounts payable | 443,718 | | | 443,718 | | | | | | |
| Debt (liabilities due to banks) | 638,914 | 31,994 | 1,056 | 420,532 | 3,492 | 1,077 | 54,464 | 7,091 | 1,948 | 163,918 |
| Other non-derivative financial liabilities | 93,748 | | | 51,296 | | | 29,582 | | | 12,870 |

## 34.5 Credit default risk

A credit default risk consists of the unexpected loss of cash and cash equivalents or revenue as a result of the partial or complete default on receivables owed. This risk materialises if contractual partners are unable to meet their obligations within the agreed period.

The assessment of the risk of default in the freenet Group is focused primarily on trade accounts receivable owed by end customers. For more information, please refer to the statements in note 21, Receivables and other assets. Here, particular attention is devoted to the credit standing of customers and sales partners in our Group's large-scale business activities. For important contract customer sectors, credit assessments are carried out for the customers before the contract is signed.

In the ongoing contractual relationship, the implementation of a swift and regular reminder and debt collection process involving a number of debt collection companies in the benchmarking area, together with long-term debt collection monitoring and high-spender monitoring, are essential measures for the minimisation of the default risk in our Group.

An ongoing reminder and debt collection process is likewise used for receivables owed by retailers and franchise partners. In a similar vein, credit limits are established and monitored. Where appropriate, a delivery block is imposed when the limit is reached.

Commercial credit insurance, moreover, safeguards us against significant credit default risks vis-a-vis major customers (traders and distributors in the Mobile Communications segment). In order to minimise the credit risk, the Group has insured a certain percentage of this revenue. Every month, the Group Treasury department notifies the insurer of the current revenue of each key account. The insurer uses this notification to calculate the revenue volume to be insured. The risks associated with uninsured customers are restricted by an internal limit system – generally, customers with a poor credit standing must pay cash in advance or the commercial relationship will not come into being. Default risks vis-a-vis end customers have not been hedged.

In order to determine the intrinsic value 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.

The appropriate formation of valuation allowances takes the risks of default into account. Receivables and other assets are derecognised if the Group regards the receivable as irrecoverable.

Securities and liquid assets are invested mainly at major German banks. The default risk has been limited significantly as a result of the risk being spread over various banks. The Group Treasury department constantly monitors the investments' current and expected future yields.

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

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

## 34.6 Transfer of financial assets

For some time now, the freenet Group has been offering its customers the opportunity to choose higher-value devices for an additional monthly fee with its mobile phone upgrade option. Contracts with this mobile phone upgrade option continue to be recognised as follows: freenet has an unconditional right to payment from the customer receiving the mobile phone as part of the mobile phone upgrade option. freenet records a receivable in the amount of the present value of the additional monthly amounts to be paid by the customer for the higher-value mobile phone over the term of the contract when the contract is signed and the mobile phone is handed over. As customers' willingness to pay more for higher-value smartphones has increased, the number of postpaid customers selecting this mobile phone upgrade option has risen steadily over the past few financial years. This also means that the figure for deferred receivables relating to the mobile phone upgrade option recognised under non-current and current trade accounts receivable has climbed continuously. For the freenet Group, this means that tied-up capital has been increasing for years: today's higher-value smartphones are more expensive to purchase than the mobile phones of the past, and while cash outflows to acquire these devices occur before or when a contract is signed with the end customer, cash inflows from the mobile phone upgrade option are spread over the 24 months of the contract with the end customer.

Since 2014, the Group concluded a factoring agreement with a bank against this background. The agreement is a master agreement with an indefinite term. The sale of mobile phone option receivables is possible on a quarterly basis. The bank purchases the receivables with a defined del credere discount and it also bills freenet for interest and fees. The relevant risks (such as the risk of default in particular) and opportunities are transferred to the bank, with the result that the receivables sold are derecognised in their entirety. The freenet Group continues to bear the risk of late payment, as well as being responsible for the collection and administration of the receivables sold (known as "servicing").

In the financial year, the sale of receivables resulted in costs of 769 thousand euros (previous year: costs of 87 thousand euros). All major opportunities and risks associated with ownership of these receivables were transferred to the purchaser.

Of the sales carried out on a quarterly basis in the reporting year (nominal volume 142.3 million euros, previous year: 119.8 million euros), a total of 2.9 million euros (previous year: 2.5 million euros) was posted to expenses. 2.2 million euros (previous year: 1.8 million euros) of this sum concerns the credit default risk taken on from the bank (del credere deduction and charges) and 0.8 million euros (previous year: 0.7 million euros) are accounted for by interest expenses from the late payment risk. As at the balance sheet date, receivables amounting to 81.3 million euros (previous year: 58.5 million euros) have been sold and derecognised but not yet paid for. The expenses of 10 thousand euros (previous year: 10 thousand euros) to be anticipated from the late payment risk and the servicing will be realised over the residual term of the receivables (6 months). The maximum loss risk for the Group is 0.8 million euros (previous year: 0.6 million euros).

The bank automatically assigns the newly defaulted receivables from the financial period ended to freenet at a fixed price each month. The buyback has no effect on either the apportionment of the risk of receivables default or the freenet Group's liquidity.

# 35. Related-party transactions

## 35.1 Overview

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

| In EUR '000s | 2016 | 2015 |
|---|---|---|
| **Sales and income attributable to services** | | |
| **Joint ventures** | | |
| FunDorado GmbH, Hamburg | 358 | 377 |
| **Total** | **358** | **377** |

The following major receivables due from and liabilities due to related parties existed as at 31 December 2016:

| In EUR '000s | 31.12.2016 | 31.12.2015 |
|---|---|---|
| **Receivables from regular transactions** | | |
| **Joint ventures** | | |
| FunDorado GmbH, Hamburg | 50 | 44 |
| **Total** | **50** | **44** |

Total emoluments of 402 thousand euros (previous year: 460 thousand euros) were granted to the employees' representatives of the Supervisory Board in the financial year 2016.

All transactions were at market rates. There are no securities.

## 35.2 Executive Board compensation

The compensation paid to the members of the Executive Board consists of annual fixed compensation, annual variable compensation, and variable compensation with a long-term incentive effect. There are also pension commitments. The annual variable compensation amounts each result from an annual agreement on objectives in which regularly determined figures indicating the freenet Group's significant financial and non-financial performance indicators are defined as individual objectives. With regard to the compensation with long-term incentive effect, we refer to the statements made in relation to the LTIP programmes in notes 26.1 and 26.2 of these notes.

The compensation for the members of the company`s Executive Board was as follows in the reporting year and in the previous year:

### Executive Board compensation 2016

| In EUR '000s | Fixed compensation | Variable compensation | Sub-total cash compensation | Variable compensation with longterm incentive effect[1] | Total compensation[2] |
|---|---|---|---|---|---|
| Christoph Vilanek | 765 | 613 | 1,378 | 949 | 2,327 |
| Joachm Preisig | 544 | 491 | 1,035 | 686 | 1,721 |
| Stephan Esch | 492 | 245 | 737 | 457 | 1,194 |
| **Total** | **1,801** | **1,349** | **3,150** | **2,092** | **5,242** |

1 This comprises variable compensation from the LTIP programme, including amounts which were non-cash-effective in the financial year and which were measured in accordance with IFRS 2.

2 The total amount of compensation in the above table does not include the benefit costs of 903 thousand euros (previous year: 1,020 thousand euros). Please refer to the following explanations.

### Executive Board compensation 2015

| In EUR '000s | Fixed compensation | Variable compensation | Sub-total cash compensation | Variable compensation with longterm incentive effect[1] | Total compensation[2] |
|---|---|---|---|---|---|
| Christoph Vilanek | 765 | 639 | 1,404 | 1,283 | 2,687 |
| Joachm Preisig | 544 | 512 | 1,056 | 531 | 1,587 |
| Stephan Esch | 492 | 256 | 748 | 343 | 1,091 |
| **Total** | **1,801** | **1,407** | **3,208** | **2,157** | **5,365** |

The composition of the variable compensation with long-term incentive effect was as follows:

### Variable compensation with long-term incentive effect 2016

| In EUR '000s | LTIP programme compensation from change in provision (non-cash-effective) | LTIP programme compensation from actual payments | Total variable compensation with long-term incentive effect |
|---|---|---|---|
| Christoph Vilanek | 949 | 0 | 949 |
| Joachim Preisig | 686 | 0 | 686 |
| Stephan Esch | 457 | 0 | 457 |
| **Total** | **2,092** | **0** | **2,092** |

### Variable compensation with long-term incentive effect 2015

| In EUR '000s | LTIP programme compensation from change in provision (non-cash-effective) | LTIP programme compensation from actual payments | Total variable compensation with long-term incentive effect |
|---|---|---|---|
| Christoph Vilanek | 1.283 | 0 | 1,283 |
| Joachim Preisig | -1,072 | 1,603 | 531 |
| Stephan Esch | -378 | 721 | 343 |
| **Total** | **-167** | **2,324** | **2,157** |

On 26 February 2014, agreements concerning the contracts of employment that grant new long-term variable compensation components (LTIPs) were concluded with the members of the Executive Board. For this LTIP programme which is also designated as "Programme 2", please refer to note 26.2 of these notes to the financial statements.

The members of the Executive Board were granted an LTIP programme for the first time in 2011; this programme was designated "Programme 1". This programme had been terminated as of 31 December 2015 as a result of complete payment. We refer to note 26.1 of these notes.

In the financial year 2016, there were no cash payments made out of the current LTIP programme (Programme 2). In the previous year, there were total cash payments of 2,324 thousand euros out of the LTIP programmes: 1,603 thousand euros to Mr Preisig and 721 thousand euros to Mr Esch. As of the balance sheet date 31 December 2016, all three members of the Executive Board were included in Programme 2 – with the target attainment years 2014 to 2018 for Mr Vilanek and 2015 to 2019 for Mr Preisig and Mr Esch.

As of 31 December 2016, the value of the provision for the LTIP programme for Mr Vilanek was 3,437 thousand euros (previous year: 2,488 thousand euros); the value for Mr Preisig was 1,679 thousand euros (previous year: 993 thousand euros), and the value for Mr Esch was 1,119 thousand euros (previous year: 662 thousand euros).

All in all, the Executive Board compensation in 2016 as defined by section 314 (1) no. 6a HGB/German Accounting Standard No. 17 (DRS 17) amounted to 3,150 thousand euros (previous year: 3,208 thousand euros). As was the case in 2015, the total for 2016 contains no compensation with long-term incentive effect; as such com-

1 This comprises variable compensation from the LTIP programme, including amounts which were non-cash-effective in the financial year and which were measured in accordance with IFRS 2.
2 The total amount of compensation in the above table does not include the benefit costs of 903 thousand euros (previous year: 1,020 thousand euros). Please refer to the following explanations.

ponents had already been disclosed in the financial years in which the compensation instruments under HGB had been granted.

In November 2004, Mr Esch was granted an indirect pension commitment. In the financial year 2009, Mr Vilanek was granted an indirect pension commitment on the occasion of his appointment as chairman of the Executive Board as at 1 May 2009. freenet AG had taken on the pension commitment granted to Mr Preisig from the former debitel AG as at 1 September 2008. In February 2014, adjustments were made to all three Executive Board members' pension commitments. For further details, see the section "Compensation rules in the event of a cessation of employment" in the Executive Board remuneration report within the Group management report.

As at 31 December 2016, the defined benefit obligation (DBO) for Mr Vilanek amounted to 3,804 thousand euros (previous year: 2,686 thousand euros), with Mr Preisig receiving 4,129 thousand euros (previous year: 3,180 thousand euros) and Mr Esch receiving 3,610 thousand euros (previous year: 2,671 thousand euros). The DBOs for Messrs Spoerr, Krieger and Berger, as former Executive Board members, totalled 9,483 thousand euros as at 31 December 2016 (previous year: 7,625 thousand euros).

Current service time expenses of 903 thousand euros (previous year: 1,020 thousand euros) were recognised in total in personnel expenses for the members of the Executive Board as a result of the pension commitments. Of these, 391 thousand euros for 2016 (previous year: 446 thousand euros) were accounted for by Mr Vilanek, 285 thousand euros (previous year: 314 thousand euros) by Mr Preisig and 227 thousand euros (previous year: 260 thousand euros) by Mr Esch.

As was the case in the previous year, in 2016, the personnel expenses for the members of the Executive Board related to the pension commitments did not include any past service costs.

No loans were extended to any of the Executive Board members and no guarantees or other warranties were provided for the Executive Board members.

## 35.3 Compensation for the Supervisory Board

The Supervisory Board's compensation is governed by the articles of association and consists of three components:

- Basic compensation
- Attendance fees
- Performance-linked compensation.

The Supervisory Board's members receive from the company fixed basic compensation of 30,000 euros for each full financial year of their Supervisory Board membership.

The chairperson of the Supervisory Board receives double this amount, the vice chairperson one-and-a-half times this amount.

In addition, every Supervisory Board member receives an attendance fee of 1,000 euros for each Supervisory Board meeting that he/she attends. Supervisory Board members who belong to a Supervisory Board committee – with the exception of the committee constituted in accordance with section 27 (3) of the German Co-determination Act (Mitbestimmungsgesetz) – receive in addition an attendance fee of 1,000 euros for each meeting of the respective committee that they attend. The committee chairperson receives double this amount.

Within the framework of a voluntary restriction imposed on its own activities, the Supervisory Board has decided that no compensation shall be payable for participation in telephone meetings of the Supervisory Board or its committees or for participation by telephone in meetings requiring physical attendance.

After the end of each financial year, the Supervisory Board's members also receive variable, performance-linked compensation in the amount of 500 euros for each 0.01 euro dividend in excess of 0.10 euro per no-par-value share in the company which is distributed to shareholders for the financial year ended. The amount of the compensation is limited to that 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 activities during the financial year 2016, the members of the company's Supervisory Board received fixed compensation of 405 thousand euros plus attendance fees amounting to 60 thousand euros. In addition, performance-linked compensation of 405 thousand euros was recorded as an expense. The extent to which this performance-based compensation will indeed be paid out depends on the profit appropriation resolution for the financial year 2016. The aggregate compensation paid for Supervisory Board activities thereby amounted to 870 thousand euros.

Furthermore, Supervisory Board members are reimbursed for expenses incurred in connection with the performance of their official duties, as well as for value added tax.

No loans were extended to any of the Supervisory Board members and no guarantees or other warranties were provided for the Supervisory Board members.

Individualised 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 sum totals; this is because the figures have been rounded to one position after the decimal point.

## Compensation for the financial year 2016

| In EUR '000s | Basic compensation | Attendance fee | Performance-based compensation | Total |
|---|---|---|---|---|
| **Active members** | | | | |
| Dr Hartmut Schenk | 60.0 | 7.0 | 60.0 | 127.0 |
| Knut Mackeprang[1] | 45.0 | 3.0 | 45.0 | 93.0 |
| Claudia Anderleit[1] | 30.0 | 3.0 | 30.0 | 63.0 |
| Birgit Geffke[1] | 30.0 | 2.0 | 30.0 | 62.0 |
| Thorsten Kraemer | 30.0 | 4.0 | 30.0 | 64.0 |
| Ronny Minak[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Michael Stephan[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Prof Dr Helmut Thoma | 30.0 | 3.0 | 30.0 | 63.0 |
| Gesine Thomas[1] | 30.0 | 2.0 | 30.0 | 62.0 |
| Marc Tüngler | 30.0 | 8.0 | 30.0 | 68.0 |
| Robert Weidinger | 30.0 | 11.0 | 30.0 | 71.0 |
| Sabine Christiansen | 30.0 | 3.0 | 30.0 | 63.0 |
| **Total** | **405.0** | **60.0** | **405.0** | **870.0** |



1 Employee representative in accordance with section 7 (1) clause 1 no. 1 MitbestG of 4 May 1976.

**Compensation for the financial year 2015**

| In EUR '000s | Basic compensation | Attendance fee | Performance-based compensation | Total |
|---|---|---|---|---|
| **Active members** | | | | |
| Dr Hartmut Schenk | 60.0 | 14.0 | 60.0 | 134.0 |
| Knut Mackeprang[1] | 45.0 | 5.0 | 45.0 | 95.0 |
| Claudia Anderleit[1] | 30.0 | 7.0 | 30.0 | 67.0 |
| Birgit Geffke[1] | 30.0 | 9.0 | 30.0 | 69.0 |
| Thorsten Kraemer | 30.0 | 7.0 | 30.0 | 67.0 |
| Ronny Minak[1] | 30.0 | 8.0 | 30.0 | 68.0 |
| Michael Stephan[1] | 30.0 | 8.0 | 30.0 | 68.0 |
| Prof Dr Helmut Thoma | 30.0 | 5.0 | 30.0 | 65.0 |
| Gesine Thomas[1] | 30.0 | 4.0 | 30.0 | 64.0 |
| Marc Tüngler | 30.0 | 8.0 | 30.0 | 68.0 |
| Robert Weidinger | 30.0 | 12.0 | 30.0 | 72.0 |
| Sabine Christiansen | 25.5 | 3.0 | 25.6 | 54.1 |
| | **400.5** | **90.0** | **400.6** | **891.1** |
| **Former members** | | | | |
| Achim Weiss | 2.5 | 0.0 | 2.5 | 5.0 |
| **Total** | **403.0** | **90.0** | **403.1** | **896.1** |

# 36. Company acquisitions

## 36.1 Acquisition of the Media Broadcast Group

mobilcom-debitel GmbH, a wholly-owned subsidiary of freenet AG, signed a purchase agreement dated 3 March 2016 with Tyrol Acquisition 1 & Cie S.C.A., Luxembourg (the vendor) for the acquisition of 100 per cent of the shares in the Media Broadcast Group. The Media Broadcast Group consists of a holding company (formerly two holding companies, one of which has since been merged with the other) as well as the main operating company Media Broadcast GmbH, Cologne, as well as further subsidiaries and equity participations. The satellite activities of the Media Broadcast Group (Media Broadcast Satellite GmbH and Media Broadcast Satellite Services GmbH) are not covered by the acquisition. The Media Broadcast Group employs more than 700 employees.

Following the approval of the cartel authorities, the acquisition was completed as of 17 March 2016, which enabled the Group to acquire control over this subsidiary. Since 18 March 2016 (reference date of initial consolidation), the Media Broadcast Group has been included in the consolidated financial statements of freenet AG.

The purchase price for the acquisition of the shares, which is not subject to any adjustments, is stated as 113.0 million euros. Of this figure, the Group has reported a cash outflow of 101.7 million euros. The Group acquired net liabilities for the difference of 11.4 million euros (other receivables of 13.5 million euros as well as other liabilities of 24.9 million euros). Costs of 2.7 million euros were incurred within the framework of the transaction; these have been recognised as other operating expenses.

For the acquisition of the Media Broadcast Group, there were outflows of 76.6 million euros stated in the cash flow statement – the figure of 101.7 million euros which was paid less the liquid assets of 25.1 million euros which existed in the Media Broadcast Group as of the reference date of initial consolidation.

In addition, the Group paid an amount of 195.0 million euros to the vendor for acquiring a loan receivable due from the Media Broadcast Group, and redeemed bank liabilities of the Media Broadcast Group in the amount of 102.2 million euros.

1 Employee representative in accordance with section 7 (1) clause 1 no. 1 MitbestG of 4 May 1976.

The Media Broadcast Group is the sole commercial provider of DVB-T2 and DAB+ in Germany. The acquisition of the Media Broadcast Group, in conjunction with the holding in EXARING AG acquired previously, represents an important addition to the strategic development of freenet AG towards becoming the leading digital lifestyle provider in Germany. The entry into the new field of linear and internet-based TV is providing the company with the opportunity of achieving further diversification in the digital lifestyle field and of developing new growth potential and sources of revenue.

The purchase price allocation under IFRS 3 carried out within the framework of the present consolidated financial statements for the acquisition of the Media Broadcast Group is of a final nature.

The following overview provides information concerning the assets and liabilities of the Media Broadcast Group acquired at fair values at the time of initial consolidation:

**Assets and liabilities of Media Broadcast Group measured at fair value as of 17 March 2016**

| **Assets**<br>In EUR `000s | 17.03.2016 | **Shareholders' equity and liabilities**<br>In EUR `000s | 17.03.2016 |
|---|---|---|---|
| **Non-current assets** | | **Non-current liabilities** | |
| Intangible assets | 112,052 | Trade accounts payable | 301,265 |
| Goodwill | 225,934 | Borrowings | 297,193 |
| Property, plant and equipment | 497,671 | Deferred income tax liabilities | 17,067 |
| Other investments | 64 | Pension provisions | 30,349 |
| Deferred income tax liabilities | 5,903 | Other provisions | 56,688 |
| Trade accounts receivable | 469 | | |
| | **842,093** | | **702,562** |
| **Current assets** | | **Current liabilities** | |
| Current liabilities | 17,632 | Trade accounts payable | 53,306 |
| Other receivables and other assets | 33,408 | Other payables | 13,185 |
| Cash and cash equivalents | 25,050 | Current income tax liabilities | 26,989 |
| | | Other provisions | 9,105 |
| | **76,090** | | **102,585** |
| | **918,183** | | **805,147** |

The purchase price is reflected by the difference between the assets and liabilities of 113.0 million euros for the acquired shares. Additional intangible assets of 109.8 million euros as well as goodwill of 225.9 million euros were disclosed in the final purchase price allocation. Of the figure shown for intangible assets, 99.7 million euros relates to customer relations with a useful life of 22 years, and 10.1 million euros relates to brand rights with a useful life of 15 years. The subsequent amortisation of customer relations and brand rights will result in amortisation of 1.3 million euros per quarter. In addition, a framework rental agreement has been classified as a finance lease with the part of the minimum rental obligation. An asset of 324.9 million euros shown under property, plant and equipment as well as a corresponding liability of the same amount have been disclosed in connection with this financing leasing agreement. The current element (23.7 million euros) of this liability of 324.9 million euros has been shown under the trade accounts payable, and the non-current element (301.2 million euros) has been shown under the other liabilities and accruals. Contingent liabilities of 24.8 million euros have been shown within the framework of the final purchase price allocation; of this figure, 17.3 million euros are shown for risks of a tax audit under the current income tax liabilities, and 7.5 million euros from a litigation risk are shown under the other non-current provisions. As of 31 December 2016, these positions existed in the same amount, without any utilisation, reversal or addition having taken place. For both contingent liabilities, there is uncertainty regarding the amount and also the actual dates of the outflows. If an outflow occurs, it is likely to take place in the financial year 2018. The fair value of the acquired receivables (incl. the other receivables and other assets) is 51.5 million euros. Impairments of 1.6 million euros were created as of the acquisition date in relation to gross trade account receivables as well as other receivables and other assets. We have not identified any transactions which have to be shown separately from the acquisition of the assets and liabilities. A budgeting plan based on the DCF procedure and with valuation relevance was made available for the final purchase price allocation. This covered a detailed period of five years. Capital-value-oriented methods have been used for determining the fair value of the intangible assets shown as part of the final purchase price allocation; these have been applied in the form of the residual value method for the customer relations and in the form of the licence price analogy method for the brand rights. In accordance with IFRS 13, a discounted cash flow method was used for calculating the fair values of the brand and the customer relations with the aid of stage 3 input factors (non-observable parameters). This valuation method is based on a cash flow forecast which would be assumed by a theoretical market player.

In the segment reporting of the freenet Group, the Media Broadcast Group has been allocated to the “TV and Media” segment.

The goodwill is allowable for tax purposes in relation to the time of initial consolidation in the amount of 199.7 million euros, and results primarily from the establishing of the new B2C business unit, and has been allocated to the cash-generating unit “TV and Media”.

After the time of its initial consolidation (18 March to 31 December 2016), the Media Broadcast Group contributed a total of 218.7 million euros to Group revenue with third parties. If this transaction had taken place as of 1 January 2016, the contribution to the Group revenue would have been 277.3 million euros. The EBITDA contribution of the Group for the period between 18 March 2016 and 31 December 2016 amounted to 45.1 million euros. If this transaction had taken place as of 1 January 2016, the contribution to the EBITDA of the Group would have been 55.7 million euros.

### 36.2 Finalisation of the purchase price allocation of EXARING AG

In the previous year, the Group acquired a stake of 24.99 per cent of the shares and voting rights in EXARING AG, Munich, in several stages. The Group acquired control over this subsidiary on 15 December 2015. Despite the lack of a voting right majority, this control was acquired as a result of substantial contractual rights in accordance with IFRS 10. These contractual rights provide the Group with the possibility of acquiring control and of influencing the returns of EXARING via a majority of members of the executive bodies of EXARING. The provisional purchase price allocation detailed under note 36 of the notes to the consolidated financial statements for the previous year is identical to the final purchase price allocation - accordingly, all disclosures set out in the notes to the consolidated financial statements as of 31 December 2015 are valid without any changes.

## 37. Declaration in accordance with section 315a HGB

The average number of employees in the Group (section 314 (1) no. 4 HGB) has been shown in note 8, Personnel expenses, in these notes.

With regard to the disclosures concerning compensation of the executive bodies of the Company (section 314 (1) no. 6 HGB), please refer to note 35, Transactions with related parties.

The acquisition and the initial consolidation of the Media Broadcast Group (section 313 (2) No. 1 HGB) is specified in note 36.1, Acquisition of the Media Broadcast Group, of these notes to the financial statements, whereas full consolidation and control of EXARING AG are described in note 36.2, Finalisation of the purchase price allocation of EXARING AG.

The acquisition and further details in connection with Sunrise Communications Group AG are specified in note 17.1, Associated companies, of these notes to the financial statements.

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 company's Executive Board and Supervisory Board on 8 December 2016. It has been made permanently available to shareholders in the Internet at the following address:

http://www.freenet-group.de/investor/corporate-governance

A total of 1,675 thousand euros in fees was paid to the auditor in accordance with section 314 (1) no. 9 HGB during the financial year 2016 Of this figure, 1,443 thousand euros is attributable to auditing services (thereof 1,061 thousand euros for the current audit for 2016 as well as 382 thousand euros for project-related audits within the framework of the introduction of IFRS 15), 8 thousand euros is attributable to other services, 211 thousand euros is attributable to other certification services and 13 thousand euros is attributable to tax consultancy services.

In accordance with section 313 (2) to (3) HGB, we provide the following overview of the companies included in the consolidated financial statements (see table on the following page):

| | Holding |
|---|---|
| **Fully consolidated companies** | |
| freenet Cityline GmbH, Kiel | 100.00% |
| freenet.de GmbH, Hamburg | 100.00% |
| 01019 Telefondienste GmbH, Hamburg | 100.00% |
| 01024 Telefondienste GmbH, Kiel | 100.00% |
| 01050.com GmbH, Hamburg | 100.00% |
| freenet Datenkommunikations GmbH, Hamburg | 100.00% |
| mobilcom-debitel GmbH, Büdelsdorf | 100.00% |
| mobilcom-debitel Logistik GmbH, Schleswig | 100.00% |
| MobilCom Multimedia GmbH, Schleswig | 100.00% |
| klarmobil GmbH, Hamburg | 100.00% |
| new directions GmbH, Hamburg | 100.00% |
| freenet Direkt GmbH, Hamburg | 100.00% |
| freenet Energy GmbH, Berlin (previously MFE Energie GmbH) | 100.00% |
| Stanniol GmbH für IT & PR, Oberkrämer | 100.00% |
| mobilcom-debitel Shop GmbH, Oberkrämer | 100.00% |
| callmobile GmbH, Hamburg | 100.00% |
| Gravis- Computervertriebsgesellschaft mbH, Berlin | 100.00% |
| MOTION TM Vertriebs GmbH, Troisdorf | 51.00% |
| freenet digital GmbH, Berlin | 100.00% |
| Ilove GmbH, Berlin | 100.00% |
| Lorena Medienagentur GmbH, Berlin (previously Quaid Media GmbH) | 100.00% |
| Quaid Media International GmbH, Berlin | 100.00% |
| freenet digital Espana S.L., Barcelona (Spain) | 100.00% |
| freenet digital Entretentimendo do Brasil Ltda., Sao Paulo (Brasil) | 100.00% |
| Motility GmbH, Berlin | 100.00% |
| freenet digital Holdings Inc., Wilmington (USA) | 100.00% |
| freenet digital Entertainment Inc., Los Angeles (USA) | 100.00% |
| freenet digital LLC, Wilmington (USA) | 100.00% |
| freenet digital North America Inc., Wilmington (USA) | 100.00% |
| Seedline Studios, LLC, Wilmington (USA) (previously freenet digital Studios, LLC) | 100.00% |
| Aldine Productions LLC, Wilmington (USA) | 100.00% |
| Seedling Productions LLC, Los Angeles (USA) | 100.00% |
| freenet digital Group US Holdings Inc., Wilmington (USA) | 100.00% |
| RS Games, LLC, Los Angeles (USA) (previously freenet digital USA LLC) | 100.00% |
| Motility Ads LLC, Los Angeles (USA) | 100.00% |
| Quaid Media, LLC, Los Angeles (USA) | 100.00% |
| EXARING AG, Munich | 24.99% |
| Synergy Networks GmbH, Leipzig | 24.99% |
| Taunus Beteiligungs GmbH, Cologne | 100.00% |
| MEDIA BROADCAST GmbH, Cologne | 100.00% |
| MEDIA BROADCAST Services GmbH, Cologne | 100.00% |
| Media Broadcast TV Services GmbH, Cologne | 100.00% |
| | |
| **At Equity valued companies** | |
| FunDorado GmbH, Hamburg | 50.00% |
| Sunrise Communications Group AG, Zurich (Switzerland) | 24.56% |

# 38. Major events after the balance sheet date

There were no further significant events after the reference date.

# 39. Consolidated statement of movements in non-current assets as at 31 December 2016

### Consolidated statement of movements in non-current assets as at 31 December 2016

| | Cost of purchase or production | | | | | | |
|---|---|---|---|---|---|---|---|
| In EUR '000s | 1.1.2016 | Change in companies included in consolidation | Additions | Transfers | Disposals | Foreign currency | 31.12.2016 |
| **Intangible assets** | | | | | | | |
| Internally-generated software | 95,527 | -287 | 17,218 | 0 | 18,855 | 0 | 93,603 |
| Software, licenses and rights of use | 225,710 | 1,137 | 3,357 | 267 | 11,126 | 0 | 219,345 |
| Trademarks | 336,352 | 10,000 | 0 | 0 | 0 | 0 | 346,352 |
| Customer relationships | 21,347 | 99,700 | 0 | 0 | 7,527 | 0 | 113,520 |
| Goodwill | 1,153,985 | 225,934 | 0 | 0 | 0 | 0 | 1,379,919 |
| | **1,832,921** | **336,484** | **20,575** | **267** | **37,508** | **0** | **2,152,739** |
| **Property, plant and equipment** | | | | | | | |
| Land, facilities on land and buildings | 16,042 | 25,636 | 5 | 3,166 | 6,193 | 0 | 38,656 |
| Switches and networks | 4,465 | 0 | 0 | 0 | 3,536 | 0 | 929 |
| Technical equipment and machinery | 22,509 | 451,390 | 28,487 | 4,717 | 14,958 | 0 | 492,145 |
| Other office equipment | 108,377 | 9,159 | 11,687 | 327 | 11,292 | 0 | 118,258 |
| Payments on account and assets under construction | 41 | 11.486 | 3.431 | -8.477 | 7 | 0 | 6,474 |
| | **151,434** | **497,671** | **43,610** | **-267** | **35,986** | **0** | **656,462** |
| **Total** | **1,984,355** | **834,155** | **64,185** | **0** | **73,494** | **0** | **2,809,201** |

### Consolidated statement of movements in non-current assets as at 31 December 2015

| | Cost of purchase or production | | | | | | |
|---|---|---|---|---|---|---|---|
| In EUR '000s | 1.1.2015 | Change in companies included in consolidation | Additions | Transfers | Disposals | Foreign currency | 31.12.2015 |
| **Intangible assets** | | | | | | | |
| Internally-generated software | 85,996 | 703 | 11,074 | 0 | 2,270 | 24 | 95,527 |
| Software, licenses and rights of use | 136,034 | 72,310 | 44,450 | 0 | 27,084 | 0 | 225,710 |
| Trademarks | 336,352 | 0 | 0 | 0 | 0 | 0 | 336,352 |
| Customer relationships | 33,746 | 0 | 0 | 0 | 12,399 | 0 | 21,347 |
| Goodwill | 1,153,298 | 687 | 0 | 0 | 0 | 0 | 1,153,985 |
| | **1,745,426** | **73,700** | **55,524** | **0** | **41,753** | **24** | **1,832,921** |
| **Property, plant and equipment** | | | | | | | |
| Land, facilities on land and buildings | 16,028 | 0 | 20 | 0 | 6 | 0 | 16,042 |
| Switches and networks | 4,506 | 0 | 0 | 0 | 41 | 0 | 4,465 |
| Technical equipment and machinery | 21,188 | 0 | 1,324 | 0 | 3 | 0 | 22,509 |
| Other office equipment | 104,563 | 1,225 | 7,009 | 110 | 4,531 | 1 | 108,377 |
| Payments on account and assets under construction | 142 | 0 | 18 | -110 | 9 | 0 | 41 |
| | **146,427** | **1,225** | **8,371** | **0** | **4,590** | **1** | **151,434** |
| **Total** | **1,891,853** | **74,925** | **63,895** | **0** | **46,343** | **25** | **1,984,355** |

| Depreciation and impairment write-downs | | | | | | | | Net book amounts | |
|---|---|---|---|---|---|---|---|---|---|
| 1.1.2016 | Change in companies included in consolidation | Additions | Impairment write-downs | Transfers | Disposals | Foreign currency | 31.12.2016 | 31.12.2016 | 1.1.2016 |
| | | | | | | | | | |
| 71,138 | -282 | 10,441 | 0 | 0 | 18,815 | 0 | 62,482 | 31,121 | 24,389 |
| 96,910 | -754 | 44,723 | 14 | 0 | 11,068 | 0 | 129,825 | 89,520 | 128,800 |
| 39,672 | -67 | 2,227 | 0 | 0 | 0 | 0 | 41,832 | 304,520 | 296,680 |
| 13,127 | 0 | 6,847 | 0 | 0 | 7,527 | 0 | 12,447 | 101,073 | 8,220 |
| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,379,919 | 1,153,985 |
| **220,847** | **-1,103** | **64.238** | **14** | **0** | **37,410** | **0** | **246,586** | **1,906,153** | **1,612,074** |
| | | | | | | | | | |
| 9,411 | 0 | 1,749 | 0 | 0 | 11 | 0 | 11,149 | 27,507 | 6,631 |
| 4,338 | 0 | 52 | 0 | 0 | 3,536 | 0 | 854 | 75 | 127 |
| 18,243 | 0 | 47,147 | 0 | 0 | 1,322 | 0 | 64,068 | 428,077 | 4,266 |
| 86,900 | 0 | 11,124 | 0 | 0 | 10,765 | 0 | 87,259 | 30,999 | 21,477 |
| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 6,474 | 41 |
| **118,892** | **0** | **60,072** | **0** | **0** | **15,634** | **0** | **163,330** | **493,132** | **32,542** |
| **339,739** | **-1,103** | **124,310** | **14** | **0** | **53,044** | **0** | **409,916** | **2,399,285** | **1,644,616** |

| Depreciation and impairment write-downs | | | | | | | | Net book amounts | |
|---|---|---|---|---|---|---|---|---|---|
| 1.1.2015 | Change in companies included in consolidation | Additions | Impairment write-downs | Transfers | Disposals | Foreign currency | 31.12.2015 | 31.12.2015 | 1.1.2015 |
| | | | | | | | | | |
| 64,803 | 0 | 8,602 | 0 | 0 | 2,270 | 3 | 71,138 | 24,389 | 21,193 |
| 83,086 | 0 | 40,782 | 0 | 0 | 26,958 | 0 | 96,910 | 128,800 | 52,948 |
| 33,415 | 0 | 6,257 | 0 | 0 | 0 | 0 | 39,672 | 296,680 | 302,937 |
| 20,687 | 0 | 4,839 | 0 | 0 | 12,399 | 0 | 13,127 | 8,220 | 13,059 |
| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 1,153,985 | 1,153,298 |
| **201,991** | **0** | **60,480** | **0** | **0** | **41,627** | **3** | **220,847** | **1,612,074** | **1,543,435** |
| | | | | | | | | | |
| 8,786 | 0 | 626 | 0 | 0 | 1 | 0 | 9,411 | 6,631 | 7,242 |
| 4,327 | 0 | 52 | 0 | 0 | 41 | 0 | 4,338 | 127 | 179 |
| 16,751 | 0 | 1,495 | 0 | 0 | 3 | 0 | 18,243 | 4,266 | 4,437 |
| 82,256 | 0 | 8,570 | 180 | 0 | 4,106 | 0 | 86,900 | 21,477 | 22,307 |
| 0 | 0 | 0 | 0 | 0 | 0 | 0 | 0 | 41 | 142 |
| **112,120** | **0** | **10,743** | **180** | **0** | **4,151** | **0** | **118,892** | **32,542** | **34,307** |
| **314,111** | **0** | **71,223** | **180** | **0** | **45,778** | **3** | **339,739** | **1,644,616** | **1,577,742** |

Christoph Vilanek          Joachim Preisig          Stephan Esch

Büdelsdorf, 6 March 2017
freenet AG
The Executive Board

# AUDITOR'S REPORT

We have audited the consolidated financial statements prepared by the freenet AG, Büdelsdorf, comprising the statement of financial position, the income statement and statement of comprehensive income, 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 January 1 to December 31, 2016. 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) is 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 as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Hamburg, 7 March 2016

PricewaterhouseCoopers GmbH
Wirtschaftsprüfungsgesellschaft

| | |
|---|---|
| Signed: | Signed: |
| Dr Andreas Focke<br>Wirtschaftsprüfer<br>(German Public Auditor) | ppa. Stephan Dreckmann<br>Wirtschaftsprüfer<br>(German Public Auditor) |

# RESPONSIBILITY STATEMENT

To the best of our knowledge, and in accordance with the applicable reporting 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, 6 March 2017
freenet AG
The Executive Board

Christoph Vilanek | Joachim Preisig | Stephan Esch

# FURTHER INFORMATION

# FINANCIAL CALENDAR

| | |
|---|---|
| **10 January 2017** | 19th German Investment Seminar, Commerzbank, New York, USA |
| **16 January 2017** | 16th German Corporate Conference, UniCredit / Kepler, Frankfurt, Germany |
| **22 March 2017** | 17th European Telecoms Conference, Citi, London, Great Britain |
| **23 March 2017** | Publication of the consolidated financial statements / Annual Report 2016 |
| **30 March 2017[1]** | 32nd ESN European Conference, equinet Bank, Paris, France |
| **4 May 2017[1]** | Quarterly Statement as of 31 March 2017 – First quarter 2017 |
| **17 and 18 May 2017[1]** | Commerzbank Boston & New York Conference, USA |
| **1 June 2017** | Annual General Meeting of freenet AG (New location: Halle A4, Messeplatz 1, Hamburg, Germany) |
| **9 August 2017[1]** | Interim Report as of 30 June 2017 – Second quarter 2017 |
| **9. November 2017[1]** | Quarterly Statement as of 30 September 2017 – Third quarter 2017 |

1 All dates are subject to change.

# IMPRINT, CONTACT, PUBLICATION

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The annual report and our interim reports are also available for download at:
*www.freenet-group.de/investor/publications*

The English version of the annual report is a convenient translation of the German version of the annual report. The German version of this annual report is legally binding.

Current information regarding freenet AG and the freenet shares is available on our homepage at:
*www.freenet-group.de/en*

If you have installed a QR-Code recognition software on your smartphone, you will be directed to the freenet Group homepage by scanning this code.

# GLOSSARY

**AFS** Available-for-sale financial instruments.

**AktG** German: Aktiengesetz; English: German Stock Corporation Act.

**App** The short form of “application”.

**ARPU** Average revenue per user.

**B2B** Business with business customers (B2B = Business to Business).

**B2C** Business with consumers (B2C = Business to Consumer).

**CGU** Cash generating unit; a cash generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

**Consumer electronics** Originally a category that was intended for radio and television, the consumer electronics is now moving more and more into the digital domain and is holistic in its claim. This happens mainly due to the integration into the “Internet of Things”.

**COSO** Committee of Sponsoring Organisations of the Treadway Commission; a voluntary private-sector organisation in the US, dedicated to improving the quality of financial reporting on the basis of ethical behaviour, effective internal controls and good corporate governance.

**Customer ownership** Includes the postpaid and no-frills customers.

**D&O insurance** Directors’ and Officers’ Liability Insurance; insurance payable to the directors and officers of a company, or to the corporation itself, to cover damages or defense costs in the event they are sued for wrongful acts while they were with that company.

**DBO** Defined Benefit Obligation.

**Dialog Consult** Dialog Consult GmbH; management consultancy company with international project experience in the areas of corporate, competitive and market entry strategy; Industry focus on telecommunication among others.

**Digital lifestyle** Describes simplification of everyday life via technical equipment based on internet and/or smartphones.

**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 outstanding 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.

**Downstream** In a telecommunications network or computer network, downstream refers to data sent from a network service provider to a customer.

**DTAG** Deutsche Telekom AG.

**Earnings per share** This ratio specifies the portion of consolidated net profit or loss which is attributable to an individual share. It is calculated by dividing the consolidated net profit/net loss by the weighted average number of issued shares.

**EBIT** Earnings before interest and taxes.

**EBITDA** Earnings before interest, taxes, depreciation and amortisation.

**EBT** Earnings before taxes.

**E-book** (electronic book) is a book in digital form that can be read on electronic devices.

**Federal Network Agency** Federal Network Agency for Electricity, Gas, Telecommunication, Posts and Railways (German: Bundesnetzagentur für Elektrizität, Gas, Telekommunikation, Post und Eisenbahnen).

**Fitness tracker** Accessory that acts as a training partner and sports motivator – counts steps, calories burned and monitors personal activity patterns.

**FLAC** Financial liabilities measured at amortised cost.

**Free cash flow** Free cash flow is defined as cash flow from operating activities, minus investments in property, plant and equipment and intangible assets, plus proceeds from the disposal of property, plant and equipment and intangible assets.

**Gross profit** Revenue minus cost of materials.

**HGB** German: Handelsgesetzbuch; English: German Commercial Code.

**Home Automation** Home Automation summarises the networked, sensing, control and optimisation of devices together in a private home. Home automation is a part of "Smart Home" and comprises mainly the areas of security/alarm systems, heating, lighting and control of windows and shutters.

**IFRS** International Financial Reporting Standards; a collection of standards for the external reporting of companies.

**Internet of Things** (IoT) IoT describes the increasing network of physical objects that employ digital technology to communicate – increasing comfort, security and energy savings in the process.

**ISIN** International Securities Identification Number.

**KStG** German: Körperschaftsteuergesetz; English: German Corporation Tax Act.

**Long-Term Incentive Account** See also LTIP.

**LR** Loans and receivables.

**LTE** Long Term Evolution; a new mobile communications standard and future successor of UMTS providing significantly higher transfer speeds in mobile communications with up to 300 megabit per second.

**LTIP** ELong Term Incentive Programme; compensation programme with long-term incentive effect.

**Mbps** Mbps stands for millions of bits per second or megabits per second and is a measure of bandwidth (the total information flow over a given time) on a telecommunications medium.

**MitbestG** German: Mitbestimmungsgesetz; English: German Codetermination Act.

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

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

**No frills** Basic services and necessities without any additional features.

**Onboarding** Onboarding, also known as organizational socialization, refers to the mechanism through which new employees acquire the necessary knowledge, skills, and behaviours to become effective organizational members and insiders.

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

**Prime standard** Stock market segment of the Frankfurt stock exchange with particularly high transparency requirements.

**Roaming** A feature in wireless telecommunications, which ensures the extension of connectivity service in a location different from the home location. Roaming can also reach to similar networks of various network operators (national roaming) as well as to international network operators (international roaming).

**Routing** It refers to setting message flows in the communication; or the transmission of messages over communication networks.

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

**Social Media** Websites and other online means of communication that are used by large groups of people to share information and to develop social and professional contacts.

**Smart home** Automatisation and interconnection of inhouse electricity (light, shutters etc.), electric appliances (washing machines, fridges etc.) and entertainment electronics (TV, radio and audio system etc.).

**Smartphone** Mobile device with touch and/or qwertz keyboard and feature set for easy internet access and/or e-mail transfer (for example push e-mail).

**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 outstanding during the financial year.

**VATM German** Verband der Anbieter von Telekommunikations-und Mehrwertdiensten e. V.; English: The association of telecommunications and value added service provider. WACC Weighted average cost of capital; the rate that a company is expected to pay on average to all its security holders to finance its assets.

**Wearables** The term wearables contains – not least fashionable – accessories that complement the smartphone or tablet. The device has to be worn directly like a watch or a necklet/bracelet. Examples are smartwatches or fitness trackers, which transfer data to the smartphone or tablet device.

**Whistleblower** A whistleblower (also known as a whistle-blower or whistle blower) is a person who exposes any kind of information or activity that is deemed illegal, unethical, or not correct within an organization that is either private or public.

**WKN** German: Wertpapierkennnummer; English: securities identification number.

**WpHG** German: Wertpapierhandelsgesetz; English: German Securities Trading Act.