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Consolidated Financial Statements 2017

Consolidated Financial Statements

for Financial Year 2017

Consolidated Financial Statements
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Consolidated Statement of Financial Position

Assets (Euros in millions)	Notes	**As of 31 December 2017**	As of 31 December 2016
A) Non-current assets		**11,940**	**13,055**
Goodwill	[4.1]	1,960	1,932
Other intangible assets	[4.2]	5,485	6,215
Property, plant and equipment	[4.3]	4,041	4,217
Trade and other receivables	[4.4]	69	77
Other financial assets	[4.5]	94	60
Other non-financial assets	[4.6]	129	128
Deferred tax assets	[5.7]	162	427
B) Current assets		**2,160**	**2,246**
Inventories	[4.7]	105	85
Trade and other receivables	[4.4]	1,265	1,460
Other financial assets	[4.5]	17	25
Other non-financial assets	[4.6]	186	63
Cash and cash equivalents	[4.8]	587	613
Total assets (A+B)		**14,100**	**15,301**

Equity and Liabilities (Euros in millions)	Notes	**As of 31 December 2017**	As of 31 December 2016
A) Equity		**8,297**	**9,408**
Subscribed capital	[4.9]	2,975	2,975
Additional paid-in capital	[4.9]	4,800	4,800
Retained earnings		523	1,634
Total equity attributable to owners of the parent		8,297	9,408
B) Non-current liabilities		**2,141**	**2,637**
Interest-bearing debt	[4.10]	1,268	1,721
Trade and other payables	[4.11]	19	17
Provisions	[4.12]	599	561
Deferred income	[4.11]	255	338
Deferred tax liabilities		1	–
C) Current liabilities		**3,662**	**3,256**
Interest-bearing debt	[4.10]	637	37
Trade and other payables	[4.11]	2,224	2,286
Provisions	[4.12]	142	190
Other non-financial liabilities	[4.6]	132	79
Deferred income	[4.11]	527	664
Total equity and liabilities (A+B+C)		**14,100**	**15,301**

Consolidated Income Statement

(Euros in millions)	Notes	2017	2016
		1 January to 31 December	
Revenues	[5.1]	7,296	7,503
Other income	[5.2]	159	502
Supplies		(2,396)	(2,452)
Personnel expenses	[5.3]	(642)	(646)
Other expenses	[5.4]	(2,633)	(2,838)
Operating income before depreciation and amortisation (OIBDA)		**1,785**	**2,069**
Depreciation and amortisation	[5.5]	(1,869)	(2,118)
Operating income		**(84)**	**(50)**
Finance income		5	11
Exchange gains		1	1
Finance costs		(39)	(48)
Exchange losses		(1)	(1)
Financial result	[5.6]	**(34)**	**(36)**
Loss before tax		**(118)**	**(86)**
Income tax	[5.7]	(262)	(90)
Profit/(loss) for the period		**(381)**	**(176)**
Profit/(loss) for the period attributable to owners of the parent		**(381)**	**(176)**
Profit/(loss) for the period		**(381)**	**(176)**
Earnings per share	[8]		
Basic earnings per share in EUR		**(0.13)**	**(0.06)**
Diluted earnings per share in EUR		**(0.13)**	**(0.06)**

Consolidated Statement of Comprehensive Income

		1 January to 31 December	
(Euros in millions)	Notes	2017	2016
Profit/(loss) for the period		**(381)**	**(176)**
Other comprehensive income/(loss)			
Items that will not be reclassified to profit/(loss)		**5**	**(25)**
Remeasurement of benefits after termination of employment	[4.12]	8	(36)
Income tax impact	[5.7]	(3)	11
Other comprehensive income/(loss)		**5**	**(25)**
Total comprehensive income/(loss)		**(375)**	**(201)**
Total comprehensive income/(loss) attributable to owners of the parent		(375)	(201)
Total comprehensive income/(loss)		**(375)**	**(201)**

Consolidated Statement of Changes in Equity

(Euros in millions)	Notes	Subscribed capital	Additional paid-in capital	Retained earnings	Total equity attributable to owners of the parent	Equity
Financial position as of 1 January 2016		**2,975**	**4,800**	**2,546**	**10,321**	**10,321**
Profit/(loss) for the period		–	–	(176)	(176)	(176)
Other comprehensive income/(loss)		–	–	(25)	(25)	(25)
Total comprehensive income/(loss)		**–**	**–**	**(201)**	**(201)**	**(201)**
Dividends	[4.9]	–	–	(714)	(714)	(714)
Other movements		–	–	2	2	2
Financial position as of 31 December 2016		**2,975**	**4,800**	**1,634**	**9,408**	**9,408**
Financial position as of 1 January 2017		**2,975**	**4,800**	**1,634**	**9,408**	**9,408**
Profit/(loss) for the period		–	–	(381)	(381)	(381)
Other comprehensive income/(loss)		–	–	5	5	5
Total comprehensive income/(loss)		**–**	**–**	**(375)**	**(375)**	**(375)**
Dividends	[4.9]	–	–	(744)	(744)	(744)
Other movements		–	–	7	7	7
Financial position as of 31 December 2017		**2,975**	**4,800**	**523**	**8,297**	**8,297**

Consolidated Statement of Cash Flows

(Euros in millions)	Notes	2017	2016
		1 January to 31 December	
Cash flow from operating activities			
Profit/(loss) for the period		**(381)**	**(176)**
Adjustments to profit/(loss)			
Financial result	[5.6]	34	36
Gains on disposal of assets	[7]	(30)	(352)
Net income tax expense	[5.7]	262	90
Depreciation and amortisation	[5.5]	1,869	2,118
Change in working capital and others			
Other non-current assets	[4.4], [4.5], [4.6], [4.7]	7	111
Other current assets	[4.4], [4.5], [4.6], [4.7]	58	85
Other non-current liabilities and provisions	[4.11], [4.12]	(116)	(188)
Other current liabilities and provisions	[4.11], [4.12]	24	157
Others			
Taxes paid		–	(0)
Interest received		9	16
Interest paid		(36)	(39)
Cash flow from operating activities		**1,702**	**1,859**
Cash flow from investing activities			
Proceeds from disposals of property, plant and equipment and intangible assets	[7]	31	591
Payments on investments relating to mobile phone frequency auctions		–	(4)
Payments on investments in property, plant and equipment and intangible assets	[4.2], [4.3]	(1,037)	(1,030)
Acquisition of companies, net of cash acquired	[6]	(29)	–
Proceeds from financial assets		18	–
Payments for financial assets		(4)	(13)
Cash flow from investing activities		**(1,022)**	**(455)**
Cash flow from financing activities			
Payments on investments relating to frequency auctions		(111)	(111)
Proceeds from interest-bearing debt	[4.10]	1,975	850
Payments made for the repayment of interest-bearing debt[1]	[4.10]	(1,843)	(1,348)
Dividends paid		(744)	(714)
Other payments made relating to financing activities		16	–
Cash flow from financing activities		**(706)**	**(1,323)**
Net increase/(decrease) in cash and cash equivalents		**(26)**	**80**
Cash and cash equivalents at the beginning of the period	[4.8]	**613**	**533**
Cash and cash equivalents at the end of the period	[4.8]	**587**	**613**

[1] Payments made for the clearance of payments that include interest-bearing debt related to finance leases of EUR 17 million for the twelve months ended 31 December 2017 and EUR 180 million for the twelve months ended 31 December 2016.

Notes to the Consolidated Financial Statements

for Financial Year 2017

1. Reporting Entity

The Consolidated Financial Statements of Telefónica Deutschland Holding AG have been prepared as of and for the year ending 31 December 2017 and are comprised of Telefónica Deutschland Holding AG (also referred to as "Telefónica Deutschland") and its subsidiaries as well as joint operations (together referred to as the "Telefónica Deutschland Group" or the "Group").

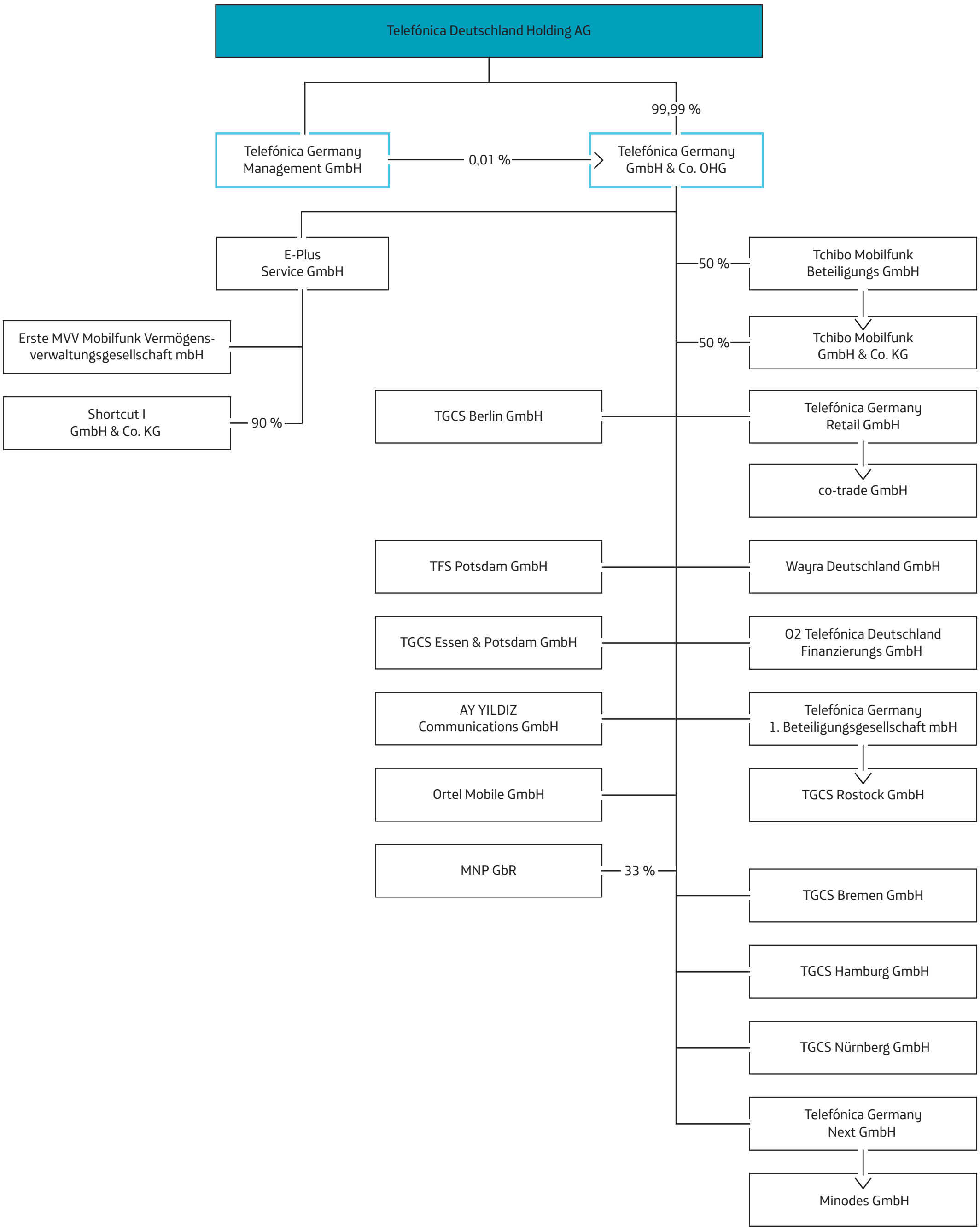
The Telefónica Deutschland Holding AG is a stock corporation (AG) incorporated under German law and is listed on the regulated market of the Frankfurt Stock Exchange.

The company's name is "Telefónica Deutschland Holding AG". The company's registered office is located in Munich, Germany. Telefónica Deutschland Holding AG is registered in the commercial register of the local court in Munich under registration number HRB 201055. The company's business address is Georg-Brauchle-Ring 23–25, 80992 Munich, Germany (telephone number: +49 (0)89 2442-0; **www.telefonica.de**). Telefónica Deutschland Holding AG was established for an indefinite period.

The financial year is the calendar year (1 January to 31 December).

Since the acquisition of the E-Plus Group, the Telefónica Deutschland Group has been one of the three leading integrated network operators in Germany. The Telefónica Deutschland Group offers private and business customers voice, data and value added services in mobile and fixed-line networks. In addition, the Telefónica Deutschland Group ranks among the leading wholesale providers in Germany. Wholesale partners are offered access to the Group's infrastructure and services. The Telefónica Deutschland Group is part of the Telefónica, S.A. Group, one of the biggest telecommunications corporations in the world.

As of 31 December 2017, the companies included in the Consolidated Financial Statements of the Telefónica Deutschland Group were organised as shown in the following organisation chart:



Unless stated otherwise, the ownership interests amount to 100 %.

2. Basis of Preparation

The Consolidated Financial Statements of Telefónica Deutschland Holding AG are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU).

In addition, the accounting policies are in line with the previous year's disclosures in the published Consolidated Financial Statements for the financial year ending 31 December 2016. Exceptions are the amendments to the IFRS and the measurement changes as presented in Note 3 (letter n) and p) Accounting Policies). Furthermore, the Group applied the additional requirements of German commercial law pursuant to section 315e (1) of the German Commercial Code (HGB).

The Consolidated Financial Statements of Telefónica Deutschland Holding AG were approved by the Supervisory Board on 19 February 2018.

Functional currency and presentation currency
These Consolidated Financial Statements are presented in euros, which is the functional currency of the Telefónica Deutschland Group and all the Telefónica Deutschland Group companies.

Unless stated otherwise, the figures in these Consolidated Financial Statements are presented in millions of euros (EUR million). The figures in the following have been rounded in accordance with established commercial practice. Figures or additions within a table may therefore result in different sums from those shown in the same table.

3. Accounting Policies

The principal accounting policies used in preparing the accompanying Consolidated Financial Statements are as follows:

a) Business combinations

Business combinations are accounted for in accordance with the purchase method. The costs of an acquisition are measured according to the fair values of the assets transferred and the liabilities incurred or assumed on the acquisition date.

Transaction costs are recognised in other expenses at the date they are incurred. Telefónica Deutschland initially recognises identifiable assets acquired in a business combination and the liabilities assumed, including contingent liabilities, at fair value at the acquisition date.

b) Goodwill

For business combinations, goodwill represents the excess of acquisition costs over the fair values of identifiable assets acquired and liabilities assumed at the acquisition date. Cost of acquisition is the sum of the fair value of consideration delivered and the value attributed to existing non-controlling interests. For each business combination, the Telefónica Deutschland Group determines the value of non-controlling interests at either their fair value or their proportional part of the net identifiable assets acquired.

For business combinations that occurred after 1 January 2004, goodwill represents the excess of the acquisition costs including transaction costs over the acquirer's interest, at acquisition date, in the fair values of the identifiable assets, liabilities and contingent liabilities of the acquired business.

After initial measurement, goodwill is carried less any accumulated impairment losses.

Goodwill is not amortised on a scheduled basis but subjected to an annual impairment test. In addition, an impairment test is carried out if events or circumstances indicate that the carrying amount is higher than the recoverable amount (see Note 4.1 Goodwill).

c) Other intangible assets

Other intangible assets are carried at acquisition or production cost, less any accumulated amortisation and any accumulated impairment losses. Subsequent expenditure is capitalised only for existing other intangible assets if it increases the future economic benefit embodied in the asset to which it relates. All other expenditures on internally generated goodwill and brands are recognised in the Consolidated Income Statement as incurred.

Borrowing costs within the scope of IAS 23 that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalised as a component of the cost of the respective asset.

The useful lives of other intangible assets either finite or indefinite are determined individually. The Telefónica Deutschland Group has not recognised other intangible assets with indefinite useful lives. Other intangible assets with finite useful lives are amortised on a scheduled basis over the economic useful life and are assessed for impairment if events or circumstances indicate that their carrying amount may not be recoverable. Other intangible assets that are not yet available for use are also tested for impairment annually. Residual values of assets, useful lives and amortisation methods are reviewed annually at year-end and, when appropriate, adjusted prospectively.

Licences
This category comprises, in the main, the acquisition costs for the agreements in which various authorities grant licences to provide telecommunication services. It also includes the values assigned to the licences held by particular companies at the time they were incorporated into the Telefónica Deutschland Group.

These licences will be amortised on a straight-line basis beginning with the period of commercial use throughout their terms (mostly between ten and 17 years).

Customer base
This primarily refers to the distribution of acquisition costs incurred as a result of the customers gained through mergers, as well as the acquisition value of these types of assets gained through acquisitions which led to a consideration for a third party. Amortisations take place on a straight-line basis for the estimated duration of the customer relationship (essentially nine and ten years).

Software
Software is classified as an acquisition and/or production cost and will be amortised on a straight-line basis over its period of use. The estimated period of use is generally between two and five years.

Brand names
This category is for brand names which were acquired through company transactions, and hence they were capitalised. Brand names will be amortised on a straight-line basis over the period of their expected useful lives (as a rule, between three and 20 years).

d) Property, plant and equipment

Property, plant and equipment are carried at cost less accumulated depreciation and any accumulated impairment losses. Land is not depreciated.

Cost includes external and internal costs comprising warehouse material used, direct labour used in installation work and the allocable portion of indirect costs required for the related investment. The latter two items are recorded as revenues in Other Income – Own Work Capitalised.

Cost includes in addition, when appropriate, the estimate of the costs at initial recognition for dismantling and removing the item and restoring the site on which it is located and the obligation which the entity incurs either when the item is acquired or as a consequence of having used it. Any corresponding valuation changes in subsequent years are allocated to the respective asset.

The costs of expansion, modernisation, or improvement leading to increased productivity, capacity and efficiency or to an extension of the useful lives of assets are capitalised when the recognition criteria are met.

Upkeep and maintenance costs are expensed as incurred.

If an asset within property, plant and equipment consists of multiple components with different useful lives, each part of the asset having a significant acquisition value is assessed and depreciated separately over the term of the useful life of the individual component (component approach).

The Telefónica Deutschland Group depreciates its property, plant and equipment once they are in full working condition using the straight-line method based on the following estimated useful lives of the assets. The useful lives are reviewed periodically and, where appropriate, updated based on technological advances and the rate of dismantling:

	Estimated useful life (in years)
Buildings	5 – 20
Plant and machinery (incl. telephone installations, networks and subscriber equipment)	5 – 20
Furniture, tools and other items	2 – 10

The estimated residual values of assets and depreciation methods are also regularly reviewed and, where appropriate, adjusted prospectively at each financial year-end.

e) Impairment of property, plant and equipment, goodwill and other intangible assets

Goodwill and intangible assets which have not yet been placed in service are tested for impairment annually at the reporting date or if there are any indications. Property, plant and equipment and intangible assets with a finite useful life are tested for impairment only if any indications of impairment exist at the reporting date. Assets are tested for impairment either individually or at the level of the cash-generating unit to which the asset belongs; goodwill is always tested at the level of a cash-generating unit to which it was allocated. As of 31 December 2017, the Telefónica Deutschland Group comprises one single cash-generating unit, the reportable segment Telecommunications. An impairment is required if the carrying amount of an asset or a cash-generating unit exceeds its recoverable amount.

As a matter of principle, the Telefónica Deutschland Group determines the recoverable amount of a cash-generating unit based on its fair value less costs to sell. The fair value is determined based on the market capitalisation of Telefónica Deutschland Holding AG as of the reporting date. Costs to sell contain costs such as legal and consulting fees that can be directly allocated to the sale of the cash-generating unit.

If the recoverable amount of a cash-generating unit to which goodwill is allocated is less than the carrying amount of the unit, an impairment loss shall be recognised corresponding to the difference. If the impairment loss exceeds the carrying amount of the goodwill, the remainder shall be allocated pro rata on the basis of the respective carrying amounts of the other assets.

If the carrying amount of an asset exceeds its recoverable amount, the carrying amount written down to its recoverable amount and the resulting loss is recognised in the Consolidated Income Statement. Future depreciation or amortisation charges are adjusted for the asset's new carrying amount over its remaining useful life.

If the requirements for impairments recorded in earlier periods no longer apply, the relevant assets (with the exception of goodwill) are written up through profit and loss.

f) Inventories

Inventories are stated at the lower of cost and net realisable value and are written down, if necessary. Cost is determined on the basis of weighted average cost and comprises direct materials and, where applicable, direct labour cost that has been incurred in bringing the inventory to its present location and condition. Estimates of the net realisable value are based on the most reliable evidence available and are based on the amount the inventories are expected to sell. These estimates take into consideration the fluctuations of sales prices or costs, as well as the purpose for which the inventory is held.

If the circumstances that previously caused inventories to be written down to an amount below cost no longer exist, the amount of the write-down is reversed, so that the new carrying amount is the lower of cost and revised net realisable value.

The Group's inventory mainly consists of merchandise intended for sale to end customers. At the time of the sale or transfer of the risk to the customer, inventory is expensed through cost of sales. The change in inventories is recorded in the item Cost of materials and purchased services.

g) Cash and cash equivalents

Cash and cash equivalents are defined as short-term, highly liquid financial investments with a maximum term of three months, which can be converted into cash at any time and are not materially impacted by the risk of a change in values.

h) Financial instruments

A financial instrument, according to IAS 39, is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity. Financial instruments are used as soon as Telefónica Deutschland Group becomes a contractual party to the financial instrument provisions. All purchases and sales of financial assets customary to the market are recognised on the trading day, i.e. the date on which the Telefónica Deutschland Group commits to purchase or sell the financial asset. Upon initial recognition, financial instruments are measured at fair value. Transaction costs directly attributable to the acquisition or issuance are considered in determining the carrying amount if the financial instruments are not measured at fair value through profit or loss.

For the purpose of subsequent measurement, financial instruments are allocated to the following categories:

- financial assets or financial liabilities at fair value through profit or loss
- held-to-maturity investments
- loans and receivables
- available-for-sale financial assets
- financial liabilities measured at amortised cost

The Telefónica Deutschland Group did not allocate any financial instruments to the category held-to-maturity during the reporting period.

The company classifies *derivative financial instruments* as held for trading unless they are designated as hedging instruments (hedge accounting) (see Note 4.10 Interest-bearing debt). The fair value is calculated using standard financial valuation models, such as discounted cash flow or option price models. Derivatives are presented as assets if their fair value is positive and as liabilities if their fair value is negative. Changes in the fair value of derivative financial instruments are recognised periodically in the Consolidated Income Statement. In the current financial year, the Telefónica Deutschland Group has two interest rate swaps (derivative financial instrument) to hedge interest-rate risks.

Hedging transactions: If the effectiveness of a hedging relationship can be demonstrated and documented accordingly, the Telefónica Deutschland Group designates a hedging relationship consisting of the underlying transaction and the corresponding hedging transaction.

If the company hedges a fair value (fair value hedges), the portion of profit or loss attributable to the hedged risk is allocated to the carrying amount of the hedged item. The carrying amount of the hedged item is increased or decreased by the profit or loss that is attributable to the hedged risk. For hedged items that are recorded at amortised cost, the increase or decrease of the carrying amount is completely released at maturity of the hedged item.

From the date the hedging instrument expires, or is sold, terminated, or exercised, the accounting of the hedging relationship also ends. The same applies if there is no longer a hedging transaction within the meaning of IAS 39 or the Telefónica Deutschland Group ends the designation.

Effective interest method : The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the interest rate that exactly discounts the estimated future cash receipts or payments through the expected life of the financial instrument or, where appropriate, a shorter period to the net carrying amount on initial recognition. The interest income or expense is recognised on an effective interest basis.

Financial assets
Financial assets mainly include trade and other receivables, other financial assets as well as cash and cash equivalents.

Financial assets measured at fair value through profit and loss
This category includes derivatives in the form of interest rate swaps that qualify for hedge accounting and have positive market values at the reporting date. Changes to the fair values recorded after the initial recognition are also recognised in profit or loss at the remeasurement date.

Telefónica Deutschland Group does not make use of the option of designating financial assets on first recognition at fair value through profit and loss ("fair value option").

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market (such as trade and other receivables). After the initial recognition, loans and receivables are subsequently carried at amortised cost using the effective interest method less any impairment losses. Gains and losses are recognised in the Consolidated Income Statement when the loans and receivables are written off or impaired. Interest effects from the application of the effective interest method are also recognised in profit or loss.

Available-for-sale financial assets
Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or that cannot be classified in any of the other categories. These include equity instruments (participations in start-ups). As there is no active market for these participations and their fair value cannot be reliably determined, they are measured at acquisition cost in accordance with IAS 39.46c.

Impairment of financial assets
At each reporting date, the carrying amounts of financial assets other than those measured at fair value through profit or loss are assessed to determine whether there is objective evidence of an impairment. Objective evidence may, for example, exist if a debtor faces serious financial difficulties or is unwilling to pay.

Loans and receivables
The amount of impairment loss on loans and receivables is measured as the difference between the carrying amount of the asset and the present value of the expected future cash flows (excluding expected future credit losses that have not been incurred), discounted at the original effective interest rate of the financial asset. The amount of the impairment is recognised in the Consolidated Income Statement. If, in a subsequent reporting period, the amount of impairment loss decreases and the decrease can be attributed objectively to an event occurring after the impairment was recognised, the impairment loss recorded in prior periods is corrected and recognised in the Consolidated Income Statement. The impairment losses of loans and receivables (e.g. trade receivables) are recorded using allowance accounts. When receivables are assessed as uncollectible, the impaired asset is derecognised.

Available-for-sale financial assets
If an available-for-sale financial asset is impaired, the difference between its cost and its fair value (less any impairment loss previously recognised in the Consolidated Income Statement) is

reclassified from other comprehensive income/loss to the Consolidated Income Statement.

For financial assets classified as available-for-sale, objective evidence of an impairment exists if there is a significant (> 20 %) or other than temporary decline (over a period of six months) in the fair value of the instrument.

Financial liabilities
Financial liabilities include primarily trade and other liabilities and interest-bearing debt (including bonds).

Financial liabilities at fair value through profit or loss
A financial liability is measured at fair value through profit or loss if it is held for trading or is designated as fair value through profit or loss on initial recognition. They are presented as current or non-current liabilities or debt depending on their maturity.

Financial instruments included in this category are recorded at fair value on initial recognition and on every subsequent reporting date. Any realised and unrealised gains or losses are recognised in the Consolidated Income Statement. Telefónica Deutschland Group does not make use of the option of designating financial liabilities on first recognition at fair value through profit and loss ("fair value option").

Financial liabilities at amortised costs
After initial recognition, financial liabilities are subsequently remeasured at amortised cost using the effective interest method.

Liabilities to members of partnerships with puttable shares are initially, and for the subsequent valuation, recognised at the present value of the buyout obligation.

Derecognition of financial assets and liabilities
Financial assets are derecognised when the rights to receive cash flows from the assets expire or the financial assets are transferred and the Telefónica Deutschland Group has transferred substantially all the risks and rewards of ownership of the financial assets.

On derecognition of a financial asset, the difference between the asset's carrying amount and the sum of consideration received including the cumulative gains or losses that had been recognised directly in equity, is recognised in the Consolidated Statements of Comprehensive Income. If the Telefónica Deutschland Group does not retain or transfer substantially all risks and rewards, and retains control, it continues to recognise the transferred asset to the extent of its continuing involvement.

Financial liabilities are derecognised when the underlying obligation is settled, cancelled, or expired. The difference between the carrying amount of the financial liability derecognised and the consideration paid is recognised in profit or loss.

i) Provisions

Pension obligations
The Telefónica Deutschland Group's obligations under defined benefit pension plans are determined using the projected unit credit method and are recognised as personnel expenses unless otherwise stated below.

The Telefónica Deutschland Group determines the net interest expense recognised in the financial result (net interest income) by multiplying the net defined benefit liability (asset) at the beginning of the period by the interest rate used to discount the defined benefit obligation at the beginning of the period.

The discount rate is determined using market yields at the end of the reporting period on fixed-interest high-quality corporate bonds.

The net defined benefit liability (asset) is determined at every reporting date on the basis of an actuary report based on assumptions that are explained as follows. If the plan assets less the defined benefit obligation results in a surplus, then the level of the reported net defined benefit asset is limited to the present value of economic benefits associated with the plan asset surplus in the form of refunds from the plan or on the basis of reduced future contributions. In addition, in the event of a surplus of the plan, the new valuation components include the change in the net defined benefit asset from the application of the asset ceiling, to the extent not taken into account in the net interest component.

Assets incurred by the Telefónica Deutschland Group to meet its pension obligations, which do not qualify as plan assets in accordance with IAS 19, are reported under other financial assets.

As part of the determination of the present value of economic benefits associated with the plan asset surplus, any existing minimum funding requirements are taken into account.

The remeasurement component includes on the one hand the actuarial gains and losses from the valuation of the defined benefit obligation and on the other hand the difference between the actual return on plan assets and the amounts contained in the net interest on net defined benefit liability (assets).

The company recognises all remeasurement effects in other comprehensive income, whereas the remaining components of the net pension expense (service cost and net interest) are recognised in the Consolidated Income Statement.

In the case of defined contribution plans, the relevant company pays contributions to special purpose pension institutions that are presented in personnel expenses.

Other provisions including termination benefits
Provisions are recognised when the Telefónica Deutschland Group has a present (legal or constructive) obligation, as a result of a past event that can be estimated reliably and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. If the effect of the time value of money is material, provisions are discounted and the corresponding increase in the provision due to the passage of time is recognised as interest expense. For the purpose of discounting, the group applies non-risk market interest rates before tax which are matched to the duration. This does not apply to other long-term employee benefits (partial retirement obligations), for which the discount rate is determined on the same basis as for pension obligations. Potential risks are fully taken into account in determining the settlement amount. When the Telefónica Deutschland Group expects some or all of a provision to be reimbursed, for example under an insurance contract, the reimbursement is recognised as a separate asset, but only when the reimbursement is virtually certain. The expense relating to any provision is presented, if applicable net of any reimbursement, in the Consolidated Income Statement.

Other provisions also include partial retirement obligations, to which the block model applies. Under this model, an outstanding settlement amount is incurred on the part of the employer during the employment phase that equates to the as yet uncompensated portion of work. After the end of the employment phase and during the reporting periods of the second block of the model (time-off phase), in which the employee receives part-time consideration without performing work, the liability is amortised accordingly.

Top-up amounts are accumulated in the amount of the present value of all future payments over a certain time period. The period over which the top-ups are earned extends to the end of the employment phase for all payments. The provision for partial retirement is allocated to other long-term employee benefits.

Provisions for death benefit obligations are recognised on the basis of actuarial reports based on the same parameters as those for pension obligations.

Provisions for restructuring including termination benefits are recognised if there is a detailed, formal plan that provides for the individual measures and has been adopted by the appropriate managing bodies. In addition, implementation is expected to begin as soon as possible and a valid expectation has been raised in those affected that the restructuring will be carried out.

The provisions for restructuring include only those expenses necessary and directly attributable to the respective measures.

Provisions for the costs of decommissioning or dismantling and retirement are recognised if the Telefónica Deutschland Group has a legal or constructive obligation to dismantle the relevant items after their utilisation. The estimated costs are recognised as an asset and a provision. Changes in the timing or estimation of the costs are reflected in the asset and in the provision, respectively.

Asset retirement obligation
The estimated costs of dismantling the network and interest rate movements are evaluated annually.

j) Revenues and expenses

Revenues and expenses are recognised in the Consolidated Income Statement in line with the accrual basis of accounting (i.e. when the goods are delivered or services are rendered) regardless of when actual payment or collection is made. Revenues are recognised if the amount can be measured reliably and the economic inflow of benefits from the transaction is classified as probable. Discounts, such as rebates, represent a reduction of revenues.

The revenues of the Telefónica Deutschland Group include all income attributable to the company's typical business activity.

The Telefónica Deutschland Group mainly realises revenues from the provision of the following telecommunication services: voice traffic, connection fees, regular (normally monthly) network usage fees, interconnection services, network and device leases, handset sales and value added services (e.g. text and data messages) and maintenance. Products and services may be sold separately or in promotional packages (bundled services).

Voice traffic, connection fees and network usage fees
Revenues from calls carried on the Telefónica Deutschland Group networks (voice traffic) include an initial connection fee plus a variable call rate, which is based on the length and distance of the call and type of service. Both fixed line and mobile voice traffic revenues are recognised at the time the service is rendered. For prepaid calls, the unused credit generates deferred revenues that are recognised in deferred income in the Consolidated Statement of Financial Position. Revenues from unused credits are recognised when the company is no longer obligated to provide a service or utilisation is no longer likely, whichever occurs first. Revenues from voice traffic sales and other services generated at a fixed rate over a specified period of time (flat rate) are recognised on a straight-line basis over the term that is covered by the customer's payment.

Initial connection fees are recognised in deferred income and are subsequently realised in profit or loss over the average estimated term of the customer relationship, which may vary depending on the type of service. All related costs, with the exception of expenses for the network expansion and general administration costs and overheads, are recognised in profit or loss for the period in which they were incurred.

Interconnection services
Interconnection revenues from fixed line to mobile calls and vice versa, as well as other customer services are recognised in the period in which the calls are made.

Handset sales
Revenues from handset and equipment sales are recognised once the sale is considered complete, i.e. generally at the time of delivery to the end customer. Revenues from instalment sales are recognised at the amount of the discounted future receipts. The amount is discounted based on an interest rate derived from market interest rates.

Network and equipment leasing
Leases are classified according to the principles described under l) Leases.

Leases from operating lease agreements with customers and income from the leasing of equipment and other services are recognised in profit or loss as the income is earned or the service is provided and therefore on a straight-line basis over the contract term.

Multiple element arrangements
The Group offers bundled packages which combine multiple elements from the fixed line, mobile and internet businesses. They are evaluated to identify the separate units of accounting and allocated the corresponding revenues to each element. Total package revenues are allocated to the individual identifiable elements based on their respective fair value (i.e. the fair value of each element in relation to the fair value of the package).

As connection fees or initial activation fees, or upfront non-refundable fees, are not separately identifiable elements in these types of packages, any revenues received from the customer for these items are allocated to the remaining elements. However, amounts contingent upon delivery of undelivered elements are not allocated to delivered elements.

The Group sells multiple element arrangements primarily through the sale or lease of handsets combined with a new mobile service contract. The purchase price is allocated based on the sales price of the items, if they were sold separately, and is recognised in the Consolidated Income Statement. Therefore, revenues for the handset are recognised upon delivery to the customer, while revenues for the mobile services are recognised pro rata over the contract term. However, if a subsidized handset is provided to the customer in connection with a bundled offer, the recognition of revenues related to the handset is limited. Additional payments which are dependent on further mobile services are not included herein.

All expenses related to bundled promotional packages are recognised in the Consolidated Income Statement as incurred.

Customer acquisition and retention costs
The Telefónica Deutschland Group pays commission to retailers and intermediaries for customer acquisition and retention. These payments are recognised into expense when the related services are rendered.

k) Income tax

Income taxes include both current and deferred taxes. Current and deferred tax are recognised in the Consolidated Income Statement unless they relate to business combinations or items directly recognised in equity or in other comprehensive income. To the extent that deferred taxes relate to items recognised directly in equity or in other comprehensive income, these are also recognised in equity or in other comprehensive income.

Current tax assets and liabilities for the current period and prior periods are measured at the amount expected to be recovered from, or paid to, the tax authorities. To calculate the amount, tax rates and tax laws applicable or enacted on the reporting date are used.

Deductible temporary differences and tax losses carried forward result in deferred tax assets in the Consolidated Statement of Financial Position. Taxable temporary differences give rise to deferred tax liabilities in the Consolidated Statement of Financial Position. Temporary differences arise due to the difference between the tax bases of the assets and liabilities and their respective carrying amounts.

The Telefónica Deutschland Group determines deferred tax assets and liabilities by applying the tax rates that will be effective when the corresponding asset is received or the liability is settled. Tax rates and tax laws that are enacted (or substantively enacted) at the reporting date are used.

Deferred tax assets and liabilities are not discounted to present value and are classified as non-current, irrespective of the date of their reversal.

The carrying amount of deferred tax assets is reviewed at each reporting date and recognised to the extent that it is probable that a sufficient taxable income will be available to utilise the deferred tax asset in the future. Unrecognised deferred tax assets are included in this review.

Deferred tax liabilities on investments in subsidiaries, branches, associates and joint operations are not recognised if the parent company is in a position to control the timing of the reversal and if the reversal is unlikely to take place in the foreseeable future. Cases in which no deferred tax liabilities were recognised for subsidiaries are of minor significance in terms of amount.

Deferred tax assets and liabilities arising from the initial recognition of the purchase price allocation of business combinations impact the amount of goodwill. However, subsequent changes in tax assets acquired in a business combination are recognised as an adjustment to profit or loss.

Deferred tax assets and liabilities are offset if a legally enforceable right exists to set off current tax assets against current tax liabilities and the deferred taxes relate to the same taxable entity and the same tax authority.

Uncertain income tax items are accounted at the estimated amount of corresponding tax payments.

l) Leases

The accounting of a lease is based on the substance of the agreement and requires an assessment of whether the fulfilment of the agreement is dependent on the use of a specific asset and whether the agreement grants the Telefónica Deutschland Group a right to use the asset.

Leases where the lessor does not transfer substantially all the risks and rewards of ownership of the asset are classified as operating leases. Operating lease payments are recognised as an expense or as income on a straight-line basis over the term of the lease in the Consolidated Income Statement.

Leases are classified as finance leases when the terms of the lease transfer substantially all risks and rewards incidental of ownership of the leased item to the Telefónica Deutschland Group or from the Telefónica Deutschland Group to the end customer. Leases are recorded at the inception of the lease, in accordance with their nature and the associated liability or receivable from financing leases, at the lower of the present value of the minimum lease payments or the fair value of the leased object. Lease payments are quantified at the principal and interest of the lease liability in order to apply a consistent effective interest rate over the outstanding balance over the term of the lease. Finance costs and income are recognised over the term of the lease in the financial result in the Consolidated Income Statement. Liabilities and receivables from financing leases are recalculated when estimates are changed.

If a lease includes a renewal option, the Group considers if these renewals are likely at the time of entering into the agreement. If the original estimate, as it relates to potential renewals, changes over the life of the lease, the Group will adjust the estimated future lease payments for operating leases accordingly.

In sale and leaseback transactions resulting in a finance lease, the asset sold is not derecognised and the funds received are considered financing for the asset during the term of the lease. Any excess of the sales proceeds over the carrying amount is accrued and distributed through profit and loss over the term of the lease. If the corresponding assets are leased on under a finance lease, the asset is immediately derecognised through profit and loss.

However, when the sale and leaseback transaction results in an operating lease, and it is clear that both the transaction and subsequent lease income are established at fair value, the asset is derecognised and any gain or loss generated on the transaction is recognised.

m) Use of estimates, assumptions and judgements

The key assumptions concerning the future and other relevant sources of uncertainty in estimates at the reporting date that could have a significant impact on the Consolidated Financial Statements within the next financial year are discussed below. The estimates and associated assumptions are based on historical experience as well as other factors considered to be relevant.

A significant change in the facts and circumstances on which these estimates and related judgements are based could have a material impact on the Telefónica Deutschland Group's net assets, financial position and results of operations.

Unforeseeable development outside management's control may cause actual amounts to differ from the original estimates. In this case the underlying assumptions and, if necessary, the carrying amounts of the pertinent assets and liabilities will be adjusted accordingly.

Changes in estimates are recognised in the period in which they occur, and also in subsequent periods if the changes affect both the reporting period and the subsequent periods.

Pensions / defined benefit plans
The determination of the present value of defined benefit obligations involves the application of actuarial assumptions.

To determine the interest rate for the defined benefit pension plans, the "bond universe" is first established on the basis of the AA corporate bonds available on the reporting date. On the basis of these bonds a yield curve is calculated. Then a uniform average interest rate is calculated with a cash flow that corresponds to the duration of the Telefónica Deutschland Group. This latter interest rate is the actuarial discount rate used.

The determination of the expected increase in pensions is aligned with the long-term inflation expectations in the euro area.

The assumption on the fluctuation of the respective employees is based on historical experience. The mortality rate underlying the calculation of the present value of the defined benefit obligation is based on official statistics and mortality tables.

Property, plant and equipment, intangible assets and goodwill

Accounting for investments in property, plant and equipment and intangible assets involves the use of estimates to determine the useful life for depreciation and amortisation purposes and to assess the fair value of assets acquired in a business combination at the acquisition date.

Determining the useful life requires making estimates in connection with future technological developments and alternative uses for assets. There is a significant element of judgement involved in making technological development assumptions, since the timing and scope of future technological advances are difficult to predict.

When an item of property, plant and equipment or an intangible asset is considered to be impaired, the impairment loss is recognised in the Consolidated Income Statement for the period. The decision to recognise an impairment loss involves estimates of the timing of the expected use and the amount of the impairment, as well as an analysis of the reasons for the potential loss. Furthermore, additional factors, such as technical obsolescence, the suspension of certain services and other circumstantial services are taken into account.

The Telefónica Deutschland Group evaluates the recoverable amount of its cash-generating unit regularly to identify potential goodwill impairment. Determining the recoverable amount of the cash-generating unit to which goodwill is allocated also entails the use of assumptions and estimates and requires a significant element of judgement. The fair value is determined based on the market capitalisation of Telefónica Deutschland Holding AG as of the reporting date.

Deferred income taxes

The Telefónica Deutschland Group assesses the recoverability of deferred tax assets based on estimates of future earnings. The ability to recover these taxes depends ultimately on the Telefónica Deutschland Group's ability to generate taxable income over the period for which the deferred tax assets remain deductible. This analysis is based on the estimated schedule for reversing deferred tax liabilities, as well as estimates of the taxable income, which are based on internal projections and updated to reflect the latest trends and estimates. In the past, time horizons of five to seven years have been used to measure loss carry forwards and temporary differences. The time horizons used have not changed since the previous year.

The recognition of tax assets and liabilities depends on a series of factors, including estimates with respect to timing and the realisation of deferred tax assets and the projected tax payment schedule. Actual income tax receipts and payments of the Telefónica Deutschland Group could differ from the estimates made by the Telefónica Deutschland Group as a result of changes in tax legislation or unforeseen transactions that could affect tax balance.

Provisions

Both the recognition and the valuation of provisions involve judgements to a high extent. The amount of the provision is determined based on the best estimate of the outflow of resources required to settle the obligation, bearing in mind all available information at the reporting date, including the opinions of independent experts such as legal counsel or consultants.

Given uncertainties inherent in the estimates used to determine the amount of provisions, the actual outflows of resources may differ from the amounts recognised originally on the basis of the estimates.

Termination benefits

If employees are offered voluntary severance, the benefits are measured on the basis of the number of employees expected to accept the offer. Benefits attributable to a period of more than twelve months after the reporting date are recognised at present value.

The amount for termination benefits is determined on the basis of various assumptions, which also require judgements and estimates and can therefore entail uncertainties. These primarily include the assumed salary, length of employment and gardening leave period until the date of departure.

Revenue recognition

Revenues from equipment leasing

The determination of minimum lease payments should in some cases account for future fair values determined by the Group on the basis of past and current transactions.

A change in the estimates of the fair value could affect the allocation of revenues among the elements and, as a result, the date at which the revenues are recognised.

Connection fees
Initial connection fees are deferred and recognised as revenues over the average estimated term of the customer relationship.

The estimate of the average customer relationship period is based on the recent history of customer churn. Potential changes in estimates could lead to changes in both the amount and timing of future recognition of revenues.

Bundled offers
Bundled offers that combine different elements are assessed to determine whether it is necessary to separate the different identifiable components and apply the corresponding revenue recognition policy to each element. The total package revenues are allocated among the identified elements based on their respective fair values.

Determining fair values for each identified elements requires estimates that vary from case to case.

A change in the estimates of the fair value could affect the allocation of revenues among the elements and, as a result, the date at which the revenues are recognised.

Joint operations
TCHIBO Mobilfunk Beteiligungs-GmbH and TCHIBO Mobilfunk GmbH & Co. KG were classified as joint operations under application of IFRS 11.17, taking into account the specific facts and circumstances. In particular, the fact that the contractual partners have rights to the entire production output generated by both companies supports our assessment that the arrangement constitutes joint operations.

Contingent Assets and Liabilities
Within the scope of determining the contingent assets and liabilities, (see Note 17 Contingent assets and liabilities), estimates, assumptions and discretionary decisions are also used.

These relate, inter alia, to risks from the assertion of patent infringements and participations in judicial and extra-judicial proceedings within the scope of ordinary business.

n) Significant changes of estimates, assumptions and judgements

Amended network planning
As the network consolidation progresses, original assumptions must be adjusted. These adjustments will lead to longer, as well as shorter, useful lives of certain network elements.

The useful lives of the non-current assets attributable to this part of the network were adjusted to reflect the new assumptions after the decision to amend the planned network.

Due to the offsetting effects, there were no significant impacts on the financial year under review or on future financial years.

Trade payables
Trade payables are reclassified to other financial liabilities when extended payment terms are agreed to which bear interest and which exceed standard industry terms. This reclassification reflects the changed nature of these liabilities.

o) Consolidation methods

The consolidation methods applied are as follows:

— Full consolidation method for companies where the Telefónica Deutschland Group has control. Control is assumed if the Telefónica Deutschland Group has power over an investee and is exposed to variable returns or has rights to these returns. In addition, the ability must exist to use its power over the investee to affect the returns.

— Proportionate consolidation of the attributable assets, liabilities, expenses and income for companies jointly controlled with third parties (joint operations), so that the corresponding share of total assets, liabilities, expenses, income and cash flows of these companies is integrated in the corresponding items in the Consolidated Financial Statements.

All material receivables and liabilities and transactions between the consolidated companies were eliminated in consolidation. The returns generated on transactions involving goods that may be capitalised or services by subsidiaries with other Telefónica Deutschland Group companies were also eliminated in consolidation.

The financial statements of the consolidated companies are prepared using the same accounting policies and have the same financial year-end as the parent company's individual financial statements. In the case of Group companies whose accounting and valuation methods differ from those of the Telefónica Deutschland Group, adjustments are made in consolidation in order to present the Consolidated Financial Statements on a consistent basis.

The Consolidated Income Statement and Consolidated Statement of Cash Flows include the revenues and expenses as well as the cash flows of companies that are no longer in the Telefónica

Deutschland Group up to the date on which the related investment was sold or the company was liquidated.

Revenues and expenses as well as the cash flows of new Group companies are included from the date on which the investment was acquired or the company was established until the end of the year.

p) Standards and IFRIC interpretations issued and effective as of 31 December 2017

The standards mandatory for application in the EU for the first time as of 1 January 2017 had no significant effects on the Consolidated Financial Statements.

Amendments to IAS 7: Disclosure Initiative
The IASB added an initiative to improve disclosure (disclosure initiative) to its work programme in 2013, which is made up of a number of smaller projects. The aim is to optimise and simplify the presentation and disclosure requirements in existing standards. As part of the project, the IASB issued amendments to IAS 7 Statement of Cash Flows on 29 January 2016. In the future, disclosures must be made regarding the development of borrowing costs during the reporting period, whereby payment transactions were reported or must be reported in the Statement of Cash Flows under cash flow from financing activities. The amendments have to be applied for financial years beginning on or after 1 January 2017.

q) New standards and IFRIC interpretations issued, but not yet effective as of 31 December 2017

At the time of publication of the Consolidated Financial Statements, the following standards and interpretations were published, but their application was not yet mandatory.

Standards, interpretations and amendments		Mandatory application for financial years beginning on or after
Annual Improvements to IFRSs 2014 – 2016 Cycle	Amendments to IFRS 12	1 January 2017[1]
Annual Improvements to IFRSs 2014 – 2016 Cycle	Amendments to IFRS 1 and IAS 28	1 January 2018[1]
Amendments to IAS 40	Transfers of Investment Property	1 January 2018[1]
IFRIC 22	Foreign Currency Transactions and Advance Consideration	1 January 2018[1]
Amendments to IFRS 2	Classification and Measurement of Share-based Payment Transactions	1 January 2018[1]
IFRS 15	Revenue from Contracts with Customers	1 January 2018
Clarifications to IFRS 15	Identifying Performance Obligations, Principal versus Agent Considerations, Licensing	1 January 2018
Amendments to IFRS 4	Application of IFRS 9 in the Context of IFRS 4 (Insurance Contracts)	1 January 2018
IFRS 16	Leases	1 January 2019
IFRIC 23	Uncertainty over Income Tax Treatments	1 January 2019[1]
Amendments to IFRS 9	Assessment Criteria for the Classification of Financial Assets	1 January 2019[1]
Amendments to IAS 28	Application of IFRS 9 in the Context of IAS 28	1 January 2019[1]
IFRS 17	Insurance Contracts	1 January 2021[1]
Amendments to IFRS 10 and IAS 28	Sale or Contribution of Assets between an Investor and its Associate or Joint Venture	[2]

[1] Endorsement by EU still outstanding, information for first-time adoption under IASB.

[2] First-time adoption postponed indefinitely in accordance with IASB resolution of 17 December 2015.

IFRS 15: Revenue from Contracts with Customers
On 28 May 2014, the IASB issued IFRS 15 – *Revenue from Contracts with Customers* with the aim of enshrining regulations from various standards and interpretations in a single standard for all industries. Consequently, IFRS 15 will replace, in particular, Standard IAS 18 – *Revenue* and Standard IAS 11 – *Construction contracts*. IFRS 15 provides for a comprehensive framework to determine whether revenue is reported, the amount of the revenue and the time said revenue is reported.

As a core principle IFRS 15 rules that revenue should be recognised for the amount which is the expected equivalent value of the performance obligation.

The new standard employs a five-step model framework for determining the amount and timing of revenue in order to implement this principle:

- Identify the contract(s) with the customer,
- Identify the performance obligations in the contract,

- Determine the transaction price,

- Allocate the transaction price to the performance obligations in the contract,

- Recognise revenue when (or as) the entity satisfies a performance obligation.

Furthermore, the standard contains some additional clarifications regarding detailed questions and no longer includes certain currently applied accounting rules. For example for the allocation of the transaction price it is no longer of importance whether the supply of goods or the provision of services take place in the future. Moreover, under certain conditions, IFRS 15 governs that customer acquisition costs directly attributable to a contract, such as commissions, are capitalised and allocated over the estimated customer retention period. Due to the customary fixed-term contracts, the first-time application starting from 1 January 2018 requires an analysis of the contracts concluded in previous financial years that were not yet completed as of the time of first application. The standard provides for two options of transition regulations of the entity applying the standard:

- full retrospective method taking into account certain practical relief measures,

- recognition of the effects from IFRS 15 through accumulated adjustments in equity at the beginning of the reporting period.

The Telefónica Deutschland Group will apply the modified retrospective method, according to which the cumulative adjustment amounts as of 1 January 2018 are recognised in the transition to IFRS 15, in its consolidated financial statements. Consequently, the Group will not apply the requirements of IFRS 15 to each comparative period presented.

As a rule, IFRS 15 requirements shall apply to every individual contract. This standard also makes it possible to apply the accounting standards to a portfolio comprising similarly structured contractual agreements provided that in doing so no material impact is expected as when compared with such application to an individual contract. Telefónica Deutschland Group has analysed its existing contracts and aggregated them to portfolios. The Group will apply IFRS 15 to these predefined portfolios.

It was necessary to adjust certain accounting processes with the introduction of IFRS 15. In particular, the requirements for the analysis of customer contracts during the product creation process had to be further specified to meet IFRS 15 requirements. An IT tool was also introduced to calculate the adjustments within the scope of IFRS 15.

As of 1 January 2018, the estimated impact on company equity as a result of applying IFRS 15 is based on current evaluations and is explained in the following paragraphs. The actual effects resulting from the application of this standard as of 1 January 2018 may deviate from the evaluations. The reasons for this are as follows:

- Telefónica Deutschland has not fully completed testing and evaluations of the security of its new IT systems and

- the new reporting and accounting methods may be subject to change when the first Consolidated Financial Statements are published in line with the initial application of the standard.

The total estimated adjustment of equity (before tax) in the Telefónica Deutschland Group's opening balance sheet of 1 January 2018 is between EUR 400 million and EUR 420 million. The largest impact of the estimated adjustments stems here from the capitalisation of customer acquisition costs, for which an amount will be capitalised as of 31 December 2017 that ranges from EUR 415 million to EUR 430 million. Counteracting effects will also arise from accounting changes for bundled mobile device and mobile service contracts when the relative individual sales prices of the contracts' contractual obligations are used.

In essence, the following topics were analysed and identified:

Revenue from Service Contracts and Multi-component Contracts
Telefónica Deutschland Group provides both mobile and fixed-line services which are performed over a specified period of time. According to IFRS 15, progress is measured using output-based methods. On the basis of such methods, sales are recorded based on the value of satisfied performance obligations towards the customer in relation to the remaining contractually agreed services to be performed. Unsteady discounts on services are recorded and amortised on a straight line basis throughout the term of the contract. As the straight line amortisation of these occasional discounts already occurred under IAS 18, Telefónica Deutschland Group does not anticipate a material impact on measuring progress.

In addition to uniquely service-based contracts, Telefónica Deutschland Group also offers its customers products through multi-component contracts. Specifically, they provide discounts on mobile services when the purchase of mobile services occurs in connection with the purchase of a mobile device. In application of IAS 18, a discount had already been provided for both components, i.e. part of the sale of the mobile device was recognised at a later accounting period. According to IFRS 15 discounts will continue to be allocated, whereby all contractual components that influence the transaction price of a contract will be taken into account when calculating the allocation factor. According to IAS 18, these additional contractual elements are not factored into such allocation; instead, they are accrued individually. As a result, both the allocation of sales revenue between mobile services and mobile devices and the time sales are recorded will change. No material effect on equity is expected when the standard is first applied.

In addition to shifts between types of sales revenue, changes to accrual periods will also have an impact. For example, according to IAS 18 connection fees are accrued individually throughout the average customer retention period and recognised as sales revenue, whereas IFRS 15 dictates that, within the scope of an overall assessment, they will be included in the allocation of contractual components and recorded accordingly as sales revenue for the duration of the underlying contract term. No material effect on equity is expected when the standard is first applied.

Significant financing components must be accounted for when determining the transaction price in accordance with IFRS 15. To align with the standard, Telefónica Deutschland Group does not take these financing components into account, as the analysis of the underlying contracts concluded that they are insignificant.

Deviating from industry practice, Telefónica Deutschland Group will not recognise any contract asset value owing to classification of part of the transaction price for mobile devices that were provided free of charge or at a significantly reduced price, as almost no subsidized devices were offered in the past.

Capitalisation of Customer Acquisition Costs

Expenses are recognised in profit or loss when the underlying service is performed. This also applies to customer acquisition costs, which are by their nature incurred in connection with contract conclusion. In contrast, IFRS 15 requires the capitalisation of customer acquisition costs that can be directly attributed to contracts with customers. Amortisation depends on how the performance obligations to which the costs relate are transferred to the customer under the relevant contract or over the estimated customer lifetime. In the future, capitalised customer acquisition costs will be recognised on a straight line basis in profit or loss under this system over the underlying amortisation period. However, assuming an even accurance of costs over time, a smoothing effect in the Income Statement is to be expected. Within the scope of this capitalisation, Telefónica Deutschland Group makes use of the practical expedients defined in the standard and only capitalises those contract acquisition costs whose underlying amortisation period is more than one year.

In addition to capitalisation of customer acquisition costs, the standard also regulates capitalisation of contractual fulfilment costs. The analysis of the underlying contracts concludes that there are no contractual fulfilment costs which Telefónica Deutschland Group has to capitalise.

Accounting for Contract Modifications

According to IFRS 15, there are more detailed and in some cases more complex requirements with regard to the recognition of contractual amendments compared to the existing regulations. In some cases, contractual amendments are prospectively listed as a separate contract on the balance sheet; in other cases the contractual amendment results in an adaption of the existing contract. As a result, accumulated income may be adjusted. Based on the analysis that was conducted, Telefónica Deutschland Group does not however anticipate any material impact.

Identification of the Principal and the Agent

According to IFRS 15, the judgement as to whether Telefónica Deutschland Group is the principal or the agent in the provision of service is based on whether the Group has control of particular goods before they are transferred to the end customer. According to IAS 18, however, it is Telefónica Deutschland Group's potential exposure to significant risks and opportunities in connection with the purchase of goods that is relevant. The analysis of essential services rendered by third parties concludes that no significant changes have occurred with regard to the assessment vis-a-vis IAS 18.

Licences

Telefónica Deutschland Group does not grant licences to customers who are to be considered within the scope of IFRS 15.

Consequently, based on Telefónica Deutschland Group's evaluation of these transactions, no material impact is expected on the Consolidated Financial Statements.

IFRS 9 and amendments to IFRS 7: Financial Instruments

On 24 July 2014, the IASB issued IFRS 9 on the accounting treatment of financial instruments. It replaces IAS 39. The new IFRS combines the three aspects of classification and measurement, impairment and hedging. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, but also permits early application. With the exception of hedge accounting, retrospective application is mandatory, but providing comparative information is not compulsory. The regulation applies to hedge accounting from the time of application, although with limited exceptions.

The Telefónica Deutschland Group plans to implement the standard as of the mandatory effective date and thereby waives to provide comparative information. In the past financial year, the Telefónica Deutschland Group carried out an extensive analysis of the effects of the three phases of IFRS 9. The analysis is based on all the available information and could therefore still be subject to subsequent adjustments. On the whole, the Group does not expect any significant effects on the Statement of Financial Position or on equity with the exception of the new requirements for determining impairments for contract assets newly introduced under IFRS 15, which are subject to the impairment regulations under IFRS 9. Furthermore, Telefónica Deutschland expects an adjustment to the risk provision as detailed below. The Telefónica Deutschland Group will also reclassify certain financial instruments.

Classification and Measurement
The Telefónica Deutschland Group does not currently expect a significant change to the Statement of Financial Position or to equity based on the introduction of IFRS 9. Rather, it is expected that the financial instruments accounted for at fair value will continue to be accounted for accordingly.

Available for sale financial assets which are currently measured at amortised cost due to the absence of other reliable measurement are, with the implementation of this standard, to be accounted at fair value through profit and loss.

Both loans issued and trade receivables are in general held in order to collect the contractual cash flows; these consist of interest and repayment of principal. Therefore the Group meets the criteria for measurement at amortised cost in accordance with IFRS 9; corresponding financial instruments therefore do not need to be reclassified.

Debt instruments in connection with factoring are measured at fair value and recognised directly in equity in accordance with IFRS 9, as it is expected that, in addition to collecting the contractual cash flows, the Telefónica Deutschland Group intends to sell the financial assets, and to do so on a regular basis.

Impairment
In accordance with IFRS 9, the Telefónica Deutschland Group in general has to determine all the expected credit losses from debt instruments either on a twelve-month basis or on a lifetime basis. For this purpose, the Telefónica Deutschland Group applies the simplified approach with respect to trade receivables and measures these business transactions on the basis of the lifetime. The Telefónica Deutschland Group does not expect any significant effects on the risk provision, with the exception of the new requirements for determining impairments for contract assets newly introduced under IFRS 15, which are subject to the impairment regulations under IFRS 9. Likewise, no significant effects result from any other financial assets.

Hedge Accounting
All existing hedge relationships currently designated in effective hedging relationships continue to qualify as such under IFRS 9. Furthermore, the regulations for the accounting treatment of hedges do not change under IFRS 9; there may possibly only be new options for presenting hedges as hedging relationships.

The effect on equity as of 31 December 2017 relating to the implementation of the standard is in the low six-digit range.

IFRS 16: Leases
On 13 January 2016, the IASB issued IFRS 16 – Leases, which will replace IAS 17 and other existing interpretations. Under IFRS 16, the lessee must account for all contracts identified as leases such that the associated right of use is recognised as an asset. The current distinction between finance leases and operating leases according to IAS 17 will cease to apply in the future. Accordingly, the present value of the lease liability must be recognised as a liability and a right of use in the same amount recognised as an asset. The lease liability and the right of use asset are subsequently reduced by lease payments and depreciation over the lease period. As a rule, the resulting interest effects lead to higher expenses at the commencement of the lease. Exceptions are possible for leased low value assets or short-term contracts. IFRS 16 requirements for lessors are similar to the current standard IAS 17.

In addition to the aforementioned systematic change, IFRS 16 includes further amendments and new requirements such as the definition of leases, accounting for sale and leaseback transactions and subleases, disclosure in the Statement of Financial Position and the scope of disclosures required in the notes.

Implementation of the standard is mandatory for financial years beginning on or after 1 January 2019, although early application is permitted.

The Group acts as a lessee on a very significant number of lease agreements over different assets, such as towers, cables, office buildings and stores and land where the towers are located, mainly. A significant portion of these contracts is accounted for as operating lease under the current lease standard, with lease payments being recognised generally on a straight-line basis over the contract term.

The Telefónica Deutschland Group is currently analysing the standard for its potential impact. The Telefónica Deutschland Group has set up a project to analyse and evaluate these and other potential effects in detail.

This analysis includes the estimation of the lease term, based on the non-cancellable period and the periods covered by options to extend the lease, when the exercise depends only on Telefónica and where such exercise is reasonably certain, considering the specific facts and circumstances by class of assets in the telecom industry (technology, regulation, competition, business model). In addition to this, the Group will make assumptions to calculate the discount rate, which will mainly be based on the incremental borrowing rate of interest for the estimated term. On the other hand, the Group is considering not to separately recognise non-lease components from lease components where non-lease components are not material with respect to the total value of the lease. In addition to the mentioned estimations, the standard allows for two transition methods for lessees: retrospectively for all periods presented, or using a modified retrospective approach where the cumulative effect of adoption is recognised at the date of initial application. The Group has tentatively decided to adopt the latter transition method; therefore the Group would recognise the cumulative effect of initial application as an adjustment to retained earnings in the year of initial application.

Also, certain practical expedients are available on first-time application in connection with the right of use asset measurement, discount rates, impairment, leases that finish within the twelve months subsequent to the date of first application, initial direct costs, and term of the lease. The Group is evaluating which of these practical expedients will be adopted. In this regard, the Group is considering opting for the practical expedient that allows not reassessing whether a contract is or contains a lease on the date of initial application of IFRS 16 but to directly apply the new requirements to all those contracts which under current accounting were identified as a lease.

On the basis of an initial, qualitative high-level assessment, the Group anticipates the following effects:

— In view of the number of available options, the complexity of required estimates as well as the high number of leasing agreements, the Group has not yet completed the implementation process and is currently unable to estimate the impact of the new requirements.

— Upon implementation of IFRS 16, payment obligations from contracts classified as operating leases must be recognised as right-of-use assets or liabilities. Accordingly, lease liabilities, non-current assets and net financial liabilities are expected to increase significantly. Future payments of all lease liabilities will be shown within cash flow from financing activities with a corresponding increase in cash flow from operating activities.

— Future depreciation and interest expense on right-of-use assets and liabilities will replace lease expense in the Income Statement. Accordingly, operating income before depreciation and amortisation (OIBDA) is expected to benefit to the detriment of depreciation and amortisation and the financial result.

As part of this project, all the requirements for timely implementation of IFRS 16 shall be met.

Additional disclosures
Telefónica Deutschland Group expects to adopt all required amendments. Except as disclosed otherwise, the Group does not expect the new and revised standards to have a material impact on the net assets, financial position and results of operations, as a result of the application of future standards, interpretations and amendments.

4. Selected Explanatory Notes to the Consolidated Statement of Financial Position

4.1. Goodwill

(Euros in millions)	2017	2016
Carrying amount of goodwill at 1 January	**1,932**	**1,955**
Additions due to acquisition	28	–
Disposal of Telxius Towers Germany GmbH	–	(23)
Carrying amount of goodwill at 31 December	**1,960**	**1,932**

The increase of EUR 28 million resulted from the acquisition of two companies. Further information can be found in Note 10 Group Companies of the Telefónica Deutschland Group.

The impairment test for goodwill, which was carried out at the level of the Telecommunications cash-generating unit, did not result in an impairment in fiscal year 2017 for goodwill because the recoverable amount of EUR 12,373 million (2016: EUR 12,028 million), which is based on the fair value less costs to sell, exceeded the carrying amount of the cash-generating unit. Furthermore, the Group did not recognise an impairment charge in financial year 2016.

The impairment test is described in Note 3 Accounting Policies.

4.2. Other intangible assets

(Euros in millions)	Service concession arrangements and licences	Customer base	Software	Thereof own work capitalised	Brand names	Others	Construction in progress/ prepayments on intangible assets	Other intangible assets
Cost								
As of 1 January 2016	**10,888**	**3,075**	**1,176**	**147**	**104**	**45**	**1,201**	**16,487**
Additions	0	–	348	30	–	0	17	366
Disposals	(175)	–	(391)	(29)	–	–	–	(566)
Reclassifications	10	–	2	–	–	–	(12)	(0)
As of 31 December 2016	**10,722**	**3,075**	**1,136**	**148**	**104**	**45**	**1,206**	**16,288**
As of 1 January 2017	**10,722**	**3,075**	**1,136**	**148**	**104**	**45**	**1,206**	**16,288**
Additions	–	1	279	28	–	0	(1)	278
Disposals	(6)	–	(40)	(2)	(2)	(1)	–	(50)
Reclassifications	858	–	5	(1)	–	–	(863)	–
As of 31 December 2017	**11,574**	**3,076**	**1,379**	**173**	**101**	**44**	**342**	**16,516**
Accumulated amortisation								
As of 1 January 2016	**(8,211)**	**(534)**	**(638)**	**(91)**	**(23)**	**(22)**	**–**	**(9,428)**
Additions	(437)	(328)	(423)	(38)	(18)	(4)	–	(1,210)
Disposals	175	–	391	29	–	–	–	566
Reclassifications	–	–	–	–	–	–	–	–
As of 31 December 2016	**(8,473)**	**(862)**	**(670)**	**(100)**	**(41)**	**(26)**	**–**	**(10,072)**
As of 1 January 2017	**(8,473)**	**(862)**	**(670)**	**(100)**	**(41)**	**(26)**	**–**	**(10,072)**
Additions	(412)	(328)	(245)	(23)	(15)	(8)	–	(1,008)
Disposals	6	–	40	2	2	1	–	50
Reclassifications	–	–	–	0	–	–	–	–
As of 31 December 2017	**(8,879)**	**(1,190)**	**(875)**	**(121)**	**(54)**	**(33)**	**–**	**(11,030)**
Net book value								
As of 31 December 2016	**2,249**	**2,213**	**466**	**48**	**62**	**19**	**1,206**	**6,215**
As of 31 December 2017	**2,695**	**1,886**	**504**	**52**	**48**	**11**	**342**	**5,485**

Licences

As of 31 December 2017, licences consist primarily of the licences listed below:

In August 2000, Telefónica Germany GmbH & Co. OHG acquired a UMTS licence (3G) that will expire on 31 December 2020. In May 2010, Telefónica Germany GmbH & Co. OHG acquired frequency usage rights in the 2.0 GHz band that will expire in December 2025. As part of the E-Plus Group acquisition on 1 October 2014, another UMTS licence, which will expire on 31 December 2020, as well as additional frequency usage rights in the 2.0 GHz band that will expire in December 2025, were acquired. The carrying amount as of 31 December 2017 amounted to EUR 646 million (2016: EUR 853 million). The 3G licences are amortised on a straight-line basis over the respective useful life. The residual lives are three to eight years.

In May 2010, Telefónica Germany GmbH & Co. OHG also acquired frequency usage rights used for LTE (4G), among others, that will expire in 2025. With the acquisition of E-Plus on 1 October 2014, additional frequency usage rights were acquired by the Telefónica Deutschland Group that can be used for LTE and run until December 2025. In June 2015, Telefónica Germany GmbH & Co. OHG won an auction for two paired blocks in the 1.8 GHz range, which will be used from 1 January 2017 and are limited until December 2033. Furthermore, LTE licences exist with terms until December 2025/December 2033. The carrying amount of the usage rights as of 31 December 2017 amounted to EUR 1,686 million (2016: EUR 1,396 million). The 4G licences are amortised on a straight-line basis over the respective useful life. The residual lives are eight to sixteen years.

In June 2015, Telefónica Germany GmbH & Co. OHG won an auction for two paired blocks in the 900 MHz range (2G), which will be used from 1 January 2017 and have a term until December 2033. The carrying amount of the usage rights as of 31 December 2017 amounted to EUR 363 million.

Customer base

The customer base is primarily a result of the acquisition of the E-Plus Group by Telefónica Deutschland. The customer base acquired in the E-Plus acquisition on 1 October 2014 is amortised mainly over a remaining period of six to seven years.

Software
Software mainly includes licences for IT and office applications. In financial years 2017 and 2016, additions related mainly to CRM and billing systems as well as data warehouse and enterprise resource planning systems. Software disposals primarily relate to software that reached the end of its useful life.

Brand names
The brand names acquired in the E-Plus Group acquisition on 1 October 2014 are amortised over a remaining period of 17 years.

Construction in progress/prepayments on intangible assets
In financial year 2015, the Telefónica Deutschland Group acquired additional frequencies that were reported in construction in progress/prepayments on intangible assets. At the mobile phone frequency auction, the Telefónica Deutschland Group acquired two paired blocks in the 700 MHz range, two paired blocks in the 900 MHz range and two paired blocks in the 1.8 GHz range. The acquired frequencies at 900 MHz and 1.8 GHz could already be used starting 1 January 2017. During the reporting period, due to the active use, a total of EUR 863 million were reclassified from construction in progress/prepayments on intangible assets to service concession arrangements, licences and software due to their active use. The use of the acquired frequencies at 700 MHz is dependent on the broadcasting companies, among other things.

4.3. Property, plant and equipment

(Euros in millions)	Land and buildings	Plant and machinery	Furniture, office equipment tools and other items	PP&E in progress	Property, plant and equipment
Cost					
As of 1 January 2016	**738**	**8,216**	**231**	**68**	**9,252**
Additions	7	650	34	51	742
Disposals	(10)	(649)	(19)	(0)	(678)
Reclassifications	(6)	10	(0)	(4)	–
Other	18	140	–	–	158
As of 31 December 2016	**747**	**8,366**	**245**	**114**	**9,473**
As of 1 January 2017	**747**	**8,366**	**245**	**114**	**9,473**
Additions	10	581	46	39	676
Disposals	(25)	(165)	(33)	–	(223)
Reclassifications	(4)	10	1	(7)	0
Other	(6)	18	–	–	12
As of 31 December 2017	**722**	**8,809**	**260**	**146**	**9,938**
Accumulated depreciation					
As of 1 January 2016	**(526)**	**(4,071)**	**(147)**	**–**	**(4,745)**
Additions	(61)	(816)	(32)	–	(908)
Disposals	9	368	19	–	397
Reclassifications	5	(6)	1	–	0
As of 31 December 2016	**(573)**	**(4,525)**	**(159)**	**–**	**(5,256)**
As of 1 January 2017	**(573)**	**(4,525)**	**(159)**	**–**	**(5,256)**
Additions	(59)	(766)	(37)	–	(862)
Disposals	24	164	33	–	222
Reclassifications	0	(0)	–	–	–
As of 31 December 2017	**(607)**	**(5,127)**	**(163)**	**–**	**(5,896)**
Net book value					
As of 31 December 2016	**174**	**3,841**	**87**	**114**	**4,217**
As of 31 December 2017	**114**	**3,683**	**98**	**146**	**4,041**

Property, plant and equipment primarily comprise land and buildings, technical equipment and machinery, furniture, tools and other items in progress.

The additions to property, plant and equipment related to the decommissioning and asset retirement obligations increased by EUR 16 million, mainly due to the higher cost estimates based on new insights as well as changing interest rates. In the previous year, the decommissioning and asset retirement obligations increased by EUR 158 million mainly due to changed costs estimates.

Property, plant and equipment from finance leases amounted to EUR 124 million as of 31 December 2017 and EUR 163 million as of 31 December 2016. The change of EUR 39 million resulted primarily from depreciation. The most significant finance leases are disclosed in Note 4.10 Interest-Bearing Debt, Finance leases.

PP&E in progress resulted mainly from the expansion of the network.

4.4. Trade and other receivables

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	**Non-current**	**Current**	Non-current	Current
Trade receivables	76	1,272	84	1,591
Receivables from related parties (Note 12 Related Parties)	–	77	–	42
Other receivables	–	58	–	19
Allowances for bad debts	(7)	(142)	(7)	(192)
Trade and other receivables	**69**	**1,265**	**77**	**1,460**

With respect to trade and other receivables, there are no indications that lead us to conclude that there is any impairment requirement beyond the existing impairment.

The breakdown of trade receivables is as follows:

Trade receivables include receivables from finance leases. For further information refer to Note 4.10 Interest-Bearing Debt, Finance leases.

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	**Non-current**	**Current**	Non-current	Current
Trade receivables billed	76	715	84	975
Trade receivables unbilled	–	557	–	615
Trade receivables	**76**	**1,272**	**84**	**1,591**

The following table shows the development of the allowances for the years ending as of 31 December 2017 and 2016.

	2017		2016	
(Euros in millions)	**Non-current**	**Current**	Non-current	Current
1 January	**(7)**	**(192)**	**(13)**	**(194)**
Additions	–	(73)	–	(83)
Release	–	–	–	–
Utilisation	–	123	6	86
31 December	**(7)**	**(142)**	**(7)**	**(192)**

In 2017 and 2016, the Telefónica Deutschland Group sold instalment receivables in order to optimise the working capital and to access an alternative source of funding. The nominal value of the transaction is concluded in 2017 amounted to EUR 624 million (2016: EUR 517 million), with the carrying amount being EUR 618 million (2016: EUR 511 million). The buyer of the receivables bears the risk of these receivables. The receivables sold were derecognised in full at the time of the sale.

The allowance includes guarantees granted in the amount of the fair value of EUR 3 million (2016: EUR 2 million).

4.5. Other financial assets

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	Non-current	Current	Non-current	Current
Investments in start-ups	18	–	21	–
Interest rate swaps	6	4	12	2
Reimbursement rights	57	–	9	–
Silent factoring deposit	10	12	17	19
Deposits	0	–	1	–
Loans	2	1	–	4
Other financial assets	**94**	**17**	**60**	**25**

Current other financial assets primarily include the current portion of the security deposit for silent factoring.

This silent factoring deposit was pledged as collateral to cover the maximum risk to be borne by the Telefónica Deutschland Group and the guarantee of the servicing of the receivables over the term of the sold receivables. The Telefónica Deutschland Group receives fixed interest on the deposit. If the underlying receivables fail, a certain amount must be reimbursed.

Interest rate swaps relate to the two issued bonds (for further information see Note 4.10 Interest-Bearing Debt).

The reimbursement claims arose to cover the pension and partial retirement obligations, but do not represent plan assets in accordance with IAS 19. The recognised fair values are based on the values received from the insurance company, which are based on the insurance company's internal calculation models.

The loan mainly include loans to start-ups, which include options for conversion to equity instruments and transaction costs that are directly attributable to the acquisition of a credit facility.

For further information on the investments in start-up companies, see Note 9 Measurement Categories of Financial Assets and Financial Liabilities.

With regard to other financial assets, there were no indications of impairment as at 31 December.

4.6. Other non-financial assets and other non-financial liabilities

Other non-financial assets were comprised as follows as at 31 December 2017:

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	Non-current	Current	Non-current	Current
Prepayments	129	107	128	61
Prepayments to related parties	–	0	–	1
Other tax receivables	–	79	–	1
Other non-financial assets	**129**	**186**	**128**	**63**

Non-financial assets primarily relate to prepayments for fees charged for leased lines and VAT. For prepayments to affiliated companies, please refer to Note 12 Related Parties.

Other non-financial liabilities were comprised as follows as at 31 December 2017:

(Euros in millions)	As of 31 December 2017 Current	As of 31 December 2016 Current
Payroll taxes and social security	10	13
Current tax payables for indirect taxes	119	64
Other current taxes	3	3
Other non-financial liabilities	**132**	**79**

4.7. Inventories

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Merchandise	109	89
Allowances	(4)	(4)
Inventories	**105**	**85**

Inventories comprise smartphones and accessories in particular.

The total cost of inventories recognised as an expense in the Consolidated Income Statement in financial year 2017 was EUR 1,145 million (2016: EUR 1,070 million).

Consistent with common industry practices, the suppliers of inventories retain the title until the items are paid for in full.

4.8. Cash and cash equivalents

Cash and cash equivalents mainly includes deposits in connection with cash pooling agreements with Telfisa Global B.V., Amsterdam, Netherlands (Telfisa Global B.V.), receivables from banks with an original term of up to three months and cash in hand.

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Cash at bank and in hand	14	13
Cash pooling	573	600
Cash and cash equivalents	**587**	**613**

There were no indications of impairment as of 31 December 2017.

4.9. Equity

Subscribed capital
As of 31 December 2017, Telefónica Deutschland Holding AG had share capital of EUR 2.975 million, which is consistent with the prior year and is divided into 2,974,554,993 no par value registered shares, each accounting for a pro rata amount of share capital of EUR 1.00. In general, each no par value share has one vote at the Annual General Meeting. The registered share capital is fully paid.

As of 31 December 2017, Telefónica Deutschland Holding AG did not hold any of its own shares.

In accordance with section 6 para. 2 of the articles of association, the shareholders do not have the right to securitise shares. In general, each no par value share grants one vote at the Annual General Meeting. The shares are freely transferable.

Authorised capital
Telefónica Deutschland Holding AG had authorized capital 2016/I of EUR 1,487,277,496 as of 31 December 2017.

Conditional capital
The share capital of Telefónica Deutschland Holding AG is conditionally increased by up to EUR 558,472,700 by issuing up to 558,472,700 new non-par value registered shares (Conditional Capital 2014/I).

Additional paid-in capital

As a result of cash and non-cash capital increases in connection with the acquisition of the E-Plus Group, which were entered in the commercial register on 18 September and 7 October 2014, additional paid-in capital increased in 2014 by EUR 4,800 million (unchanged) as of 31 December 2017, in the amount of EUR 4,800 million.

Retained earnings

Legal reserve

Retained earnings contain a legal reserve in accordance with section 150 (2) of the German Stock Corporation Act (Aktiengesetz – AktG) of EUR 0.014 million (2016: EUR 0.014 million).

Proposed dividend for financial year 2017 to be paid in 2018

On 24 October 2017, the Management Board of Telefónica Deutschland resolved to propose a total cash dividend of EUR 773 million or EUR 0.26 per share at the next Annual General Meeting, which is scheduled for 17 May 2018.

Dividend distribution in the financial year

On 9 May 2017, the Annual General Meeting of Telefónica Deutschland resolved to distribute a dividend of EUR 0.25 for each no par value share for financial year 2016, in total around EUR 744 million.

Dividend distribution in the previous year

On 19 May 2016, the ordinary Annual General Meeting of Telefónica Deutschland resolved to distribute a dividend of EUR 0.24 for each no par value share for financial year 2015, in total around EUR 714 million.

4.10. Interest-bearing debt

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	Non-current	Current	Non-current	Current
Bonds	504	613	1,107	12
Promissory notes and registered bonds	299	4	299	4
Loans	450	0	298	0
Finance leases	15	19	17	15
Contribution and compensation obligations	–	2	–	6
Interest-bearing debt	**1,268**	**637**	**1,721**	**37**

For the maturity profile of the listed liabilities, see the disclosures in the Management Report, Risk Management and Financial Instruments. Long-term interest-bearing debt with a remaining term greater than 5 years remains in the amount of EUR 402 million.

Bonds

This item includes two bonds for which interest rate swaps were recognised in the reporting year and in the previous year and were reported under other financial assets (see Note 4.5 Other financial assets).

These bonds (except for EUR 350 million of the nominal value) are accounted for by using the effective interest method after deduction of the disagio and transaction costs. EUR 350 million of the nominal value of the bonds is accounted for as a fair value hedge with interest rate swaps.

The senior unsecured seven-year bond issued on 10 February 2014 has a nominal value of EUR 500 million. The bond will mature on 10 February 2021 and was issued by O2 Telefónica Deutschland Finanzierungs GmbH, Munich. The coupon for the fixed interest bond is 2.375 % and the issue price 99.624 %. The issue spread was 100 basis points over the seven-year euro mid-swap rate, resulting in a yield of 2.434%. O2 Telefónica Deutschland Finanzierungs GmbH, Munich, has transferred the net issuing proceeds of the bond to Telefónica Germany GmbH & Co. OHG, Munich, in the form of a loan. An interest rate swap was concluded for a partial amount of EUR 150 million of the bond's nominal value. On the basis of this interest rate swap contract, the Telefónica Deutschland Group pays a variable interest rate based on the three-month Euribor on a nominal amount and receives a fixed interest rate of 1.268% on the same amount in return.

In November 2013, the Telefónica Deutschland Group, via its subsidiary O2 Telefónica Deutschland Finanzierungs GmbH, Munich, issued an unsecured five-year bond (Senior Unsecured Bond) with a nominal value of EUR 600 million and a maturity on 22 November 2018. The annual nominal interest rate of the bond is 1.875 %. Based on the issue price of 99.162 %, the bond yields an annual return of 2.053 %. O2 Telefónica Deutschland

Finanzierungs GmbH, Munich, has transferred the net issuing proceeds of the bond to Telefónica Germany GmbH & Co. OHG, Munich, in the form of a loan. An interest rate swap was concluded for a partial amount of EUR 200 million of the nominal value of the bond. On the basis of this interest rate swap contract, the Telefónica Deutschland Group pays a variable interest rate based on the three-month Euribor on a nominal amount and receives a fixed interest rate of 0.927 % on the same amount in return.

All factors that market participants would normally consider, are included in the measurement of the fair value of the interest rate swaps, including the credit risks of the contract parties. The fair value of the interest swaps results from discounting of the expected future payments over the remaining term of the contract using current market interest rates and yield curves.

The adjustments to the carrying amount of the non-current financial liabilities result in a cumulative loss of EUR 8 million (EUR 12 million cumulative loss in 2016 and EUR 4 million profit in 2017), while the corresponding clean prices of the interest rate swaps result in a cumulative profit of EUR 8 million (EUR 12 million cumulative profit in 2016 and EUR 4 million loss in 2017). Under the interest rate swaps, the Telefónica Deutschland Group pays a variable quarterly interest rate amounting to the three-month Euribor and receives fixed interest rates of 0.927% and 1.268%. The hedged nominal value of the financial liabilities amounts to EUR 350 million. Thus, 19% (2016: 19%) of the bonds of the company were switched from fixed interest to variable interest. The fair value of the dirty prices from the interest rate swaps that secure financial debt amounted to EUR 10 million as at 31 December 2017 (2016: EUR 14 million) and was recognised as a financial asset. The fair value of the bonds is determined by discounting the expected future cash flows at currently applicable interest rates with comparable conditions and residual terms.

Promissory notes/registered bonds

On 13 March 2015, the Telefónica Deutschland Group completed an initial placement of promissory notes and registered bonds with a volume of EUR 300 million.

The promissory notes placed with a volume of EUR 172 million have unsecured tranches with terms of five, eight and ten years, with both fixed and floating interest rates. The average interest rate of tranches with a fixed interest rate was 1.38% p.a. The interest on the variable tranches is based on Euribor money market terms plus an agreed margin.

The registered bonds placed have terms of 12, 15 and 17 years and a fixed interest rate. The tranches amount to EUR 3 million, EUR 33 million and EUR 92 million, respectively, and bear interest at 2.000%, 2.250% and 2.375%.

All tranches were issued at par.

Loans

The Group signed a EUR 750 million revolving credit facility (RCF) on 22 March 2016. The term of this credit facility was extended by one year until March 2022 for the first time in February 2017. The RCF can therefore still be extended by a maximum of one further year. The RCF bears a variable interest rate at Euribor money market conditions plus an agreed margin. As of 31 December 2017, the credit facility had not been used.

On 13 June 2016 the Group signed a financing agreement with the European Investment Bank (EIB) to the value of EUR 450 million. As of 31 December 2017, this loan had been utilised in the form of two fixed-interest tranches totalling EUR 450 million. The funds provided by the EIB are due by December 2024 and May 2025 and will be repaid in equal instalments starting in December 2019 and May 2020 respectively. The benchmark interest rate for the fixed-interest tranches is determined according to the principles defined by the bodies of the EIB for loans of the same type.

On 31 July 2017, the Telefónica Deutschland Group concluded a bilateral revolving credit facility with Telfisa Global B.V., which amounted to EUR 500 million. It serves general business purposes and has a term of one year. As of 31 December 2017, the credit facility had been fully repaid.

Finance leases

The obligations arising from finance leases mainly result from agreements for network elements concluded under sale and leaseback transactions and classified as finance leases in accordance with their contract design as well as agreements for the leasing of IT equipment.

In connection with these finance leases, the Telefónica Deutschland Group recognised the assets attributable to the network elements under property, plant and equipment in the Consolidated Financial Statements as of 31 December 2017 and in the previous year (for further information see Note 4.3 Property, plant and equipment).

The breakdown of minimum lease payment obligations is as follows:

As of 31 December 2017

(Euros in millions)	Future minimum lease payment obligations	Unamortised interest expense	Present value of future minimum lease payment obligations
Due within one year	19	1	19
Due between 1 and 5 years	15	0	15
Due in more than 5 years	–	–	–
Total	**34**	**1**	**33**

As of 31 December 2016

(Euros in millions)	Future minimum lease payment obligations	Unamortised interest expense	Present value of future minimum lease payment obligations
Due within one year	16	1	15
Due between 1 and 5 years	17	0	17
Due in more than 5 years	–	–	–
Total	**33**	**1**	**32**

Receivables from finance leases

The Telefónica Deutschland Group subleases mobile phones to its end customers through a lease agreement. The Group thus acts as a lessor to the customers. The customer contracts included fixed lease payments over a term of two years. As of 31 December 2017, receivables exclusively comprise receivables from existing contracts. New contracts are no longer being concluded for this lease model.

The following table shows the expected minimum lease payments by end customers:

As of 31 December 2017

(Euros in millions)	Future minimum lease payments	Unrealised interest income	Present value of outstanding minimum lease payments
Due within one year	8	0	8
Due between 1 and 5 years	–	–	–
Due in more than 5 years	–	–	–
Total	**8**	**0**	**8**
Accumulated allowance			(2)
Total after accumulated allowance			**6**

As of 31 December 2016

(Euros in millions)	Future minimum lease payments	Unrealised interest income	Present value of outstanding minimum lease payments
Due within one year	99	0	99
Due between 1 and 5 years	8	0	8
Due in more than 5 years	–	–	–
Total	**107**	**0**	**107**
Accumulated allowance			(10)
Total after accumulated allowance			**97**

The allowance of receivables from finance leases is recognised as an expense. The credit risk is determined on the basis of past experience.

Renewal and purchase options expected to be exercised are included in the calculation of the minimum lease payments to be made and those expected.

The receivables from finance leases are included in the trade receivables.

Contribution obligations

This item includes contribution obligations to partners in investments in start-ups that hold puttable shares.

Transition of debt movements to cash flow from financing activities

(Euros in millions)	As of 31 December 2016	Cash flow from financing activities	Acquisitions	Fair Value Amendments	Other movements	As of 31 December 2017
Bonds	1,119	–	–	(4)	2	1,117
Promissory notes and registered bonds	303	–	–	–	0	303
Loans	298	150	0	–	2	450
Finance leases	32	(17)	18	–	–	33
Contribution and compensation obligations	6	–	–	–	(4)	2
Interest-bearing debt	**1,758**	**133**	**18**	**(4)**	**0**	**1,905**
Financing as part of frequency auctions	111	(111)	–	–	–	–
Total	**1,869**	**22**	**18**	**(4)**	**0**	**1,905**

4.11. Trade and other payables and deferred income

(Euros in millions)	As of 31 December 2017		As of 31 December 2016	
	Non-current	Current	Non-current	Current
Trade payables to third parties	–	733	–	897
Accruals	17	842	15	783
Payables to related parties (Note 12 Related Parties)	–	374	–	425
Trade payables	**17**	**1,989**	**15**	**2,105**
Other creditors non-trade	1	125	2	81
Other payables to related parties (Note 12 Related Parties)	–	40	–	41
Other payables	–	69	–	58
Other payables	**1**	**235**	**2**	**181**
Trade and other payables	**19**	**2,224**	**17**	**2,286**
Deferred income	**255**	**527**	**338**	**664**

In financial year 2017, payables from silent factoring totalling EUR 64 million are now shown under Other creditors non-trade instead of Trade payables to third parties. In the prior year liabilities from Silent Factoring totalled EUR 48 million.

Accruals relate mainly to outstanding invoices for goods and services and for non-current assets.

Other creditors non-trade mainly consists of liabilities due to personnel and payables from silent factoring.

Other liabilities mainly comprise debtors with credit balances.

For the maturity profile of the listed liabilities, see the disclosures in the Management Report, Risk Management and Financial Instruments.

Deferred income primarily includes advance payments received for prepaid credit and other advance payments received for future service performance. It also includes the payment from MS Mobile Service GmbH (Drillisch) received in connection with the Mobile Bitstream Access Mobile Virtual Network Operator (MBA MVNO) agreement.

Other advance payments received for future service performance and the payment received from Drillisch are broken down by maturity according to their expected utilisation. Advance payments received for prepaid credit are classified exclusively as current.

4.12. Provisions

(Euros in millions)	As of 31 December 2017 Non-current	As of 31 December 2017 Current	As of 31 December 2016 Non-current	As of 31 December 2016 Current
Pension obligations	151	–	106	–
Restructuring	43	64	20	127
Asset retirement obligation	378	73	400	57
Other provisions	28	6	35	5
Provisions	**599**	**142**	**561**	**190**

Pension obligations

The Telefónica Deutschland Group has defined benefit plans. These primarily include defined benefit rights against an external provident fund (Gruppen-Unterstützungskasse), which is managed in accordance with its articles of association, and direct commitments.

The overriding investment policy and strategy for the defined benefit plans are based on the goal of generating returns from the plan assets as well as from the reimbursement rights deriving from insurance policies which, together with the contributions, are sufficient to meet the pension obligations.

The plan assets are invested in insurance policies that are taken out directly by the Telefónica Deutschland Group or indirectly by the provident fund. The reimbursement rights from insurance policies result from those insurance policies, which were not pledged to the employees.

The requirements for the financing of pension obligations arise from the financing strategy of the provident fund and are anchored in its guidelines. The guidelines define that the expected defined benefit obligation will be settled by the provident fund. They are fully financed by the Telefónica Deutschland Group. The Telefónica Deutschland Group provides the provident fund with the necessary financial resources.

However, under its articles of association, the fund must cease or reduce its payments if the company does not make, or no longer makes, the necessary financial resources available to the fund. In this case, the employees can bring their legal right to post-employment benefits against the Telefónica Deutschland Group.

The amount of the committed benefits for the defined benefit pension plans essentially depends on the basic salary of the individual employee during the period of employment. The benefits paid include old age pensions, payments for the inability to work and benefits in the event of death to surviving relatives.

In order to minimise the biometric risks of the committed benefits (such as an early benefits claim through invalidity or death of the beneficiary), the pension or promised retirement capital is covered to the full extent (congruent) or in part by insurance policies. In addition, the pledging of the insurance policies to the pension beneficiary acts as security for the claims of the beneficiary in the event of the insolvency of the sponsoring company.

This defined benefit plan is subject to actuarial and financial risks such as life expectancy and interest rate risk as well as inflation risk. In addition, all reinsurance policies are essentially with an insurance company.

In financial year 2017, the employer's share of the statutory pension insurance amounted to EUR 39 million (2016: EUR 41 million).

Telefónica Deutschland Group has additional defined contribution plans. The expense for defined contribution plans recognised for the period amounted to EUR 2 million (2016: EUR 3 million).

The following table contains the key data for the defined benefit plans:

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Present value of defined benefit obligation from funded plans	(108)	(168)
Present value of defined benefit obligation from unfunded plans	(128)	(65)
Present value of defined benefit obligation	**(235)**	**(233)**
Fair value of plan assets	84	128
(Deficit)/Surplus	**(151)**	**(106)**
Net benefit provision	**(151)**	**(106)**
Reimbursement rights	**57**	**8**

The development of the present value of the defined benefit obligations in 2017 and 2016 was as follows:

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Present value of the defined benefit obligation as of 1 January	**(233)**	**(198)**
Current service costs (personnel expenses)	(9)	(6)
Interest expense (financial result)	(4)	(5)
Remeasurement of defined benefit obligation	8	(31)
thereof: actuarial gains/(losses) arising from changes in financial assumptions	*5*	*(31)*
thereof: experience adjustments	*3*	*1*
Benefits paid	3	3
Other	–	3
Present value of the defined benefit obligation as of 31 December	**(235)**	**(233)**

The development of the fair value of the plan assets was as follows in 2017 and 2016:

(Euros in millions)	2017	2016
Fair value of plan assets as of 1 January	**128**	**122**
Return on plan assets excluding amounts included in interest income (expense)	0	(2)
Interest income (financial result)	2	3
Employer contributions	6	9
Benefits paid	(2)	(2)
Other	(50)	(2)
Fair value of plan assets as of 31 December	**84**	**128**

The fair value of the reimbursement rights from insurance contracts developed in 2017 and 2016 as follows:

(Euros in millions)	2017	2016
Fair value of reimbursement rights from insurance contracts as of 1 January	**8**	**8**
Return on reimbursement rights excluding amounts included in interest income (expense)	(0)	(0)
Interest income	0	0
Employer contributions	0	0
Benefits paid	(0)	(0)
Other	50	(0)
Fair Value of reimbursement rights from insurance contracts as of 31 December	**57**	**8**

The amounts recognised under "Other" in 2016 for defined benefit obligations and the plan assets originate from the transfer of pension obligations and the related plan assets.

The amounts listed under 'Other' in 2017 for plan assets and for reimbursements rights are a result of the ban on set offs reimbursement rights that have not been pledged against plan assets.

In 2017, as in the previous year, there was no asset ceiling.

The main actuarial assumptions on which the determination of the present value of the defined benefit obligation as of the reporting date is based are provided in the following table (factors represent averages).

	As of 31 December 2017	As of 31 December 2016
Discount rate	1.75%	1.65%
Nominal rate of pension payment increase	1%; 1.75%	1%; 1.75%
Fluctuation rate	(0% – 20%)	(0% – 20%)

The mortality tables on which the actuarial calculation of the DBO as at the reporting date is based are the Heubeck Mortality Tables 2005G (Heubeck Richttafeln 2005G).

(In years)	As of 31 December 2017	As of 31 December 2016
Life expectancy at age 65 for a retiree currently	21	21
Life expectancy of a currently aged 40 deferred member at age 65	24	24

An increase or decrease in the main actuarial assumptions would have had the following effects on the present value of the defined benefit obligations as of 31 December 2017:

(Euros in millions)	Increase in parameters	Decrease in parameters
Discount rate (+0.25%/-0.25%)	(13)	14
Pension increase (+0.50%/-0.50%)	10	(9)
Turnover rate (+1.00%/-1.00%)	(0)	0
Life expectancy (+1 year)	8	–

Increases and reductions in the discount rate and increases to pension payments do not have the same impact on the determination of the DBO due to the interest rate effects. If several assumptions are changed at the same time, the overall effect will not necessarily correspond to the sum of the individual effects due to the changes in the assumptions. In addition, the sensitivity of a change in the DBO only reflects each specific order of magnitude in the change of assumptions (for example 0.25%). If the assumptions change by a different order of magnitude, the effect on the DBO does not necessarily have to be linear.

The following table contains information regarding the analysis of the due date of expected payments:

(Euros in millions)	1 January to 31 December 2017	1 January to 31 December 2016
Benefits expected to be paid within year 1	2	2
Benefits expected to be paid within year 2	3	2
Benefits expected to be paid within year 3	3	3
Benefits expected to be paid within year 4	3	3
Benefits expected to be paid within year 5	3	3
Benefits expected to be paid within 6 to 10 years	24	22

The average expected term of the defined benefit obligation for the 2017 financial year is 22.8 years (2016: 23.2 years).

The best estimate of the contributions that will be paid into the plans in the financial year ending 31 December 2017 amounts to EUR 9 million (2016: EUR 9 million) .

Other provisions

(Euros in millions)	Restructuring	Asset retirement obligation	Others	Total
As of 1 January 2017	**147**	**457**	**40**	**644**
Additions	86	21	5	112
Utilisation	(123)	(29)	(9)	(160)
Release	(4)	–	(5)	(9)
Reclassifications	1	–	2	3
Accrued interest	–	1	–	1
As of 31 December 2017	**106**	**450**	**33**	**590**
thereof non-current	*43*	*378*	*28*	*448*
thereof current	*64*	*73*	*6*	*142*

The provision for restructuring primarily includes measures resulting from the transformation of the Telefónica Deutschland Group in connection with the integration of E-Plus that aim to increase profitability through synergies. The amount of EUR 106 million as of 31 December 2017 (2016: EUR 147 million) is allocated to personnel adjustments, the deactivation of a part of the mobile network, the suspension of contracts with sales representatives and other measures.

The majority of the provision recognised as of 31 December 2017 is attributable to severance payments in connection with personnel adjustments.

Furthermore, a decline resulted from the scheduled utilisation of EUR 123 million, which was partly offset by additions of EUR 86 million. As in the previous year, these additions are recognised in other expenses and personnel expenses (for further information see Note 5.3 Personnel expenses and 5.4 Other expenses).

The provisions for asset retirement obligations include the calculated costs for the dismantling and removal of assets (e.g. mobile equipment such as operating facilities and technology), largely based on the agreements with service providers.

The timing of utilisation and the associated outflow of cash depends on the implementation of the current network consolidation strategy.

5. Selected Explanatory Notes to the Consolidated Income Statement

5.1. Revenues

(Euros in millions)	1 January to 31 December 2017	2016
Rendering of services	6,149	6,419
Other revenues	1,147	1,084
Revenues	7,296	**7,503**

Revenues from the rendering of services include mobile service revenues as well as revenues from fixed line/DSL business. The other revenues include handset revenues and miscellaneous other revenues.

None of the Telefónica Deutschland Group's customers' accounts for more than 10 % of total revenues.

The breakdown of revenues according to mobile business and fixed line/DSL business is shown in the following table:

(Euros in millions)	1 January to 31 December 2017	2016
Mobile business	6,415	6,498
Mobile service revenues	5,287	5,437
Handset revenues	1,128	1,061
Fixed line/DSL business revenues	862	981
Other revenues	19	23
Revenues	**7,296**	**7,503**

Mobile service revenues
The mobile service revenues are largely based on basic fees and the fees levied for voice (including incoming and outgoing calls), messaging (including SMS and MMS) and mobile data services as well as the revenues from service contracts. Alongside roaming revenues, mobile service revenues include access and interconnection fees that are paid for by other service providers for calls and SMS messages delivered via our network.

Handset revenues
Handset revenues include the income from the sale of mobile phones as part of the "O_2 My Handy" model, the hardware portion of bundled packages (hardware bundled offerings) for the former E-Plus brands and cash sales. In addition, handset revenues include further components from mobile business such as activation fees and accessories.

With the "O_2 My Handy" model, the customer can choose whether to pay the entire price of the mobile phone up front or to make an initial payment to start with and pay the remaining purchase price in twelve or 24 monthly instalments. Revenues from the "O_2 My Handy" model are discounted according to their term.

Regarding the hardware bundled offers provided by the former E-Plus brands, the customer was able to choose between the purchase or lease of a device.

Fixed line/DSL business revenues
Fixed line/DSL business revenues comprise mainly revenues from DSL services for private customers, DSL activation fees for private customers, revenues from DSL products and non-recurring items (e.g. fees for change of address, number transfers, etc.), revenues from wholesale ULL (also known as wholesale DSL), revenues from the sale of the company's own DSL network, from services and from hardware to other service providers who re-bundle these and sell them on to end customers, and data traffic revenues from carriers in connection with the sale and trade of minutes between carriers to connect

their customer calls via the networks of other operators. DSL revenues also include fixed line revenues.

Other revenues
Other revenues relate to new business, such as advertising and financial services, e.g. the mobile service offering "O_2 More Local", O_2 banking and new innovative products from the Telefónica NEXT business field.

5.2. Other income

(Euros in millions)	2017	2016
		1 January to 31 December
Own work capitalised and ancillary income	128	146
Gain on disposal of assets	31	356
Other income	**159**	**502**

Own work capitalised includes direct labour costs as well as the allocable portion of indirect costs in connection with investments in non-current assets.

The gains on the disposal of assets in financial year 2016 resulted from the sale of passive tower infrastructure to Telxius S.A. For further information, see Note 7 Disposal Groups.

5.3. Personnel expenses

In financial year 2017, personnel expenses amounted to EUR 642 million (2016: EUR 646 million). Of these, EUR 552 million related to wages and salaries (2016: EUR 562 million), EUR 78 million to social security (2016: EUR 77 million), and EUR 11 million to pensions (2016: EUR 6 million). Personnel expenses from share-based payments are presented in Note 13 Share-Based Payments; personnel expenses relating to pension plans are presented in Note 4.12 Provisions.

In addition, restructuring expenses of EUR 44 million (2016: EUR 46 million) are recognised in personnel expenses. For further information, see Note 4.12 Provisions.

5.4. Other expenses

(Euros in millions)	2017	2016
		1 January to 31 December
Other third-party services	2,168	2,331
Other operating expenses	94	77
Allowance for current assets	80	91
Advertising	291	340
Other expenses	**2,633**	**2,838**

As of 31 December 2017, other expenses included restructuring expenses of EUR 38 million (2016: EUR 43 million) (for further information see Note 4.12 Provisions).

Other third-party expenses essentially comprise commissions.

5.5. Depreciation and amortisation

(Euros in millions)	2017	2016
	1 January to 31 December	
Depreciation of property, plant and equipment	862	908
Amortisation of intangible assets	1,008	1,210
Depreciation and amortisation	**1,869**	**2,118**

5.6. Financial result

(Euros in millions)	2017	2016
	1 January to 31 December	
Interest income from financial assets	5	11
Interest expenses from financial liabilities	(37)	(44)
Accretion of provisions and other liabilities	(2)	(4)
Other exchange gains/ (losses)	0	(0)
Financial result	**(34)**	**(36)**

Interest income from financial assets primarily includes the interest income in connection with "O_2 My Handy" receivables, receivables from finance leases and interest income from late payments.

Interest expenses from financial debt primarily comprise the interest for the bonds issued in November 2013 and February 2014, the revolving credit facility signed on 22 March 2016, the financing agreement signed on 13 June 2016 with the European Investment Bank (EIB), as well as for the promissory notes and registered bonds issued in March 2015.

Interest from finance lease obligations is also included.

5.7 Income tax

Consolidated income tax group

As of 31 December 2017, the consolidated income tax group of the Telefónica Deutschland Group consisted of 17 (2016: 21) companies.

Current and deferred taxes

(Euros in millions)	2017	2016
	1 January to 31 December	
Current tax expense	(0)	(0)
Deferred tax expense	(262)	(90)
Income tax/ (expense)	**(262)**	**(90)**

The movements in deferred tax assets are as follows:

(Euros in millions)	2017	2016
As of 1 January	**427**	**505**
Deferred tax expense	(262)	(90)
Amount of deferred taxes recognised directly in equity as shown in the Consolidated Statement of Comprehensive Income	(3)	11
As of 31 December	**162**	**427**

Tax loss carry forwards and temporary differences

Tax losses carried forward for which no deferred tax assets are reported as of 31 December 2017 amounted to EUR 14,439 million for corporate income tax and EUR 14,060 million for trade tax (2016: EUR 13,781 million and EUR 13,614 million). For temporary differences of EUR 263 million in 2017 (2016: EUR 0 million) no deferred tax assets were recognised. For entities respectively the income tax group which had a negative taxable income in the previous year or in the current period, deferred tax assets of EUR 162 million (EUR 427 million the previous year) were capitalised, as the future realisation of this tax claim is to be supported by the tax income projection.

The capitalisation of tax loss carry forwards at the end of the projection period is based on more conservative estimates of future income than those which would have been anticipated for other non-accounting-related purposes.

The breakdown of deferred tax assets and deferred tax liabilities from temporary differences and tax losses carried is as follows:

	As of 31 December 2017		As of 31 December 2016	
(Euros in millions)	**Deferred tax assets**	**Deferred tax liabilities**	Deferred tax assets	Deferred tax liabilities
Goodwill and other intangible assets	853	(685)	1,129	(797)
Tangible assets	–	(210)	6	(246)
Trade and other receivables	10	(16)	12	(36)
Other current financial assets	8	(8)	8	(13)
Financial liabilities, trade and other payables	28	(7)	19	(6)
Provisions including pension provisions	88	(18)	105	(0)
Other current financial liabilities	23	(6)	64	(4)
Tax loss carry forwards	102	–	184	–
Deferred tax assets (liabilities)	**1,112**	**(951)**	**1,527**	**(1,101)**
Netting	(951)	951	(1,101)	1,101
Deferred tax assets (liabilities)	**162**	**–**	**427**	**–**

The deferred taxes in the amount of EUR 1,112 million (last year: EUR 1,527 million) are classified in general as non-current deferred tax assets and EUR 951 million (last year: EUR 1,101 million) as non-current deferred tax liabilities.

Reconciliation of earnings before tax to income tax expense recognised

	1 January to 31 December	
(Euros in millions)	**2017**	2016
Loss before tax	**(118)**	**(86)**
Tax expense at prevailing statutory rate (32 %)	38	28
Non-deductible expenses	(11)	(19)
Tax free income	–	–
Change in unrecognised temporary differences and tax loss carry forwards	(289)	(98)
Other	(0)	(0)
Income tax	**(262)**	**(90)**
Current tax expense	(0)	(0)
Deferred tax expense	(262)	(90)
Income tax (expense)	**(262)**	**(90)**

6. Business Combinations

Two transactions affecting the basis of consolidation were conducted by the Telefónica Deutschland Group in financial year 2017 (for more information, please see Note 10 Group Companies of the Telefónica Deutschland Group. This change in the basis of consolidation did not have a material effect on the consolidated financial statements of the Telefónica Deutschland Group.

7. Disposal Groups

Disposal group in 2016: Sale of passive tower infrastructure to Telxius

Telxius Telecom S.A., which was a wholly owned subsidiary of Telefónica S.A. at the time of the sale, acquired all of the shares in Telxius Towers Germany GmbH (formerly Telefónica Germany Vermögensverwaltungs-gesellschaft mbH), a formerly wholly owned subsidiary of E-Plus Mobilfunk GmbH, in accordance with a share purchase and transfer agreement dated 21 April 2016.

Telxius Towers Germany GmbH was formed as part of the spin-off of cellular towers and the corresponding assets and liabilities and lease agreements. The purpose of the company is the leasing of passive tower infrastructure for the operation of mobile communications networks.

The disposal of Telxius Towers Germany GmbH had the following impact on the Group's net assets and financial position in financial year 2016:

(Euros in millions)	As of 21 April 2016
Intangible assets	(23)
Property, plant and equipment	(277)
Trade and other receivables	(0)
Prepaid expenses	(4)
Provisions	83
Trade and other payables	0
Deferred income	8
Net assets and liabilities	**(214)**
Service receivables from Telxius	1
Liabilities to Telxius	(17)
Effect on net assets excluding cash and cash equivalents	**(231)**
Fee included in cash and cash equivalents	587
Cash and cash equivalents disposed of	(0)
Net cash inflow	**587**

Subsequent to the spin-off, the Telefónica Deutschland Group has been leasing the infrastructure back from Telxius Towers Germany GmbH under the terms of a corresponding lease. Furthermore, the parties agreed that the Group will be able to charge certain service fees to Telxius Towers Germany GmbH during a transitional phase.

A net capital gain of EUR 352 million was reported in the Consolidated Income Statement in connection with this disposal. The gain on the disposal of the interest, which is reported in other operating income, is offset by consulting fees that are reported in other operating expenses.

8. Earnings per share

Basic earnings per share are calculated by dividing the profit for the year after tax attributable to the ordinary shareholders of the parent company by the weighted average number of ordinary shares outstanding during the reporting period.

Diluted earnings per share are calculated by adjusting the profit after tax attributable to the ordinary shareholders of the parent company and the weighted average number of ordinary shares outstanding in the reporting period for the effects of any dilutive effects inherent in converting potential ordinary shares.

Both basic as well as diluted earnings per share attributable to the ordinary shareholders of the parent company are calculated based on the following data in accordance with IAS 33.

	1 January to 31 December	
(Euros in millions)	**2017**	2016
Total profit (loss) attributable to equity holders of the parent for basic = diluted earnings	(381)	(176)
Weighted average number of ordinary shares issued (in million units)	2,975	2,975
Earnings per share in EUR (basic = diluted)	**(0.13)**	**(0.06)**

In addition, the share capital of Telefónica Deutschland Holding AG is conditionally increased (see Note 4.9 Equity). Shares from the conditional capital of a stock corporation are not part of the calculation of the earnings per share as they can be contingently issued.

9. Measurement Categories of Financial Assets and Financial Liabilities

In the following tables, the fair values of all financial assets and financial liabilities of the Telefónica Deutschland Group are disclosed in accordance with the measurement categories as determined by IAS 39 and in line with the requirements of IFRS 13.

As of 31 December 2017, the carrying amount of the financial assets and financial liabilities represents an appropriate approximation for the fair value (with the exception of the portion of the bonds that is not hedged – see below).

In addition, the tables show the categorisation of the financial assets and financial liabilities in accordance with the importance of the input factors that were used for their respective measurement. For this purpose, three levels or measurement hierarchies are defined:

- Level 1: Primary market value: Quoted prices (unadjusted) in active markets for identical assets and liabilities;
- Level 2: Significant other observable input parameters: Inputs observable, either directly or indirectly, which are subject to certain limitations;
- Level 3: Significant unobservable input parameters: All unobservable inputs, which might include the entity's own data as a starting point and which should be adjusted if reasonably available information indicates that other market participants would use different data.

As of 31 December 2017
Financial assets

(Euros in millions)	Hedges (not a measurement category according to IAS 39)	Available-for-sale financial assets	Held-to-maturity financial assets	Loans and receivables	Measurement hierarchy Level 1 (Quoted prices)	Level 2 (Other directly observable market inputs)	Level 3 (Inputs not based on observable market data)	Total carrying amount	Total fair value	Not in the scope of IFRS 7
Non-current trade and other receivables (Note 4.4)	–	–	–	69	–	69	–	69	69	–
Other non-current financial assets (Note 4.5)	6	18	–	12	–	18	–	36	18	57
thereof: derivatives	*6*	–	–	–	–	*6*	–	*6*	*6*	–
thereof: investments in start-ups	–	*18*	–	–	–	–	–	*18*	–	–
thereof: other	–	–	–	*12*	–	*12*	–	*12*	*12*	*57*
Current trade and other receivables (Note 4.4)	–	–	–	1,263	–	1,263	–	1,263	1,263	2
Other current financial assets (Note 4.5)	4	–	–	13	–	4	–	17	17	–
thereof: derivatives	*4*	–	–	–	–	*4*	–	*4*	*4*	–
thereof: other	–	–	–	*13*	–	*13*	–	*13*	*13*	–
Cash and cash equivalents (Note 4.8)	–	–	–	587	–	587	–	587	587	–
Total	**10**	**18**	**–**	**1,944**	**–**	**1,955**	**–**	**1,973**	**1,955**	**59**

As of 31 December 2016*
Financial assets

(Euros in millions)	Hedges (not a measurement category according to IAS 39)	Available-for-sale financial assets	Held-to-maturity financial assets	Loans and receivables	Measurement hierarchy Level 1 (Quoted prices)	Level 2 (Other directly observable market inputs)	Level 3 (Inputs not based on observable market data)	Total carrying amount	Total fair value	Not in the scope of IFRS 7
Non-current trade and other receivables (Note 4.4)	–	–	–	77	–	77	–	77	77	–
Other non-current financial assets (Note 4.5)	12	21	–	18	–	30	–	51	30	9
thereof: derivatives	*12*	–	–	–	–	*12*	–	*12*	*12*	–
thereof: investments in start-ups	–	*21*	–	–	–	–	–	*21*	–	–
thereof: other	–	–	–	*18*	–	*18*	–	*18*	*18*	–
Current trade and other receivables (Note 4.4)	–	–	–	1,458	–	1,458	–	1,458	1,458	1
Other current financial assets (Note 4.5)	2	–	–	23	–	25	–	25	25	–
thereof: derivatives	*2*	–	–	–	–	*2*	–	*2*	*2*	–
thereof: other	–	–	–	*23*	–	*23*	–	*23*	*23*	–
Cash and cash equivalents (Note 4.8)	–	–	–	613	–	613	–	613	613	–
Total	**14**	**21**	**–**	**2,189**	**–**	**2,203**	**–**	**2,224**	**2,203**	**11**

*The prior year's presentation was amended to improve ease of reading.

As of 31 December 2017, EUR 6 million of other non-current financial assets and EUR 4 million of current financial assets are include in a hedge. These relate to the swaps that the Group entered into in connection with the bond issuance (for further information, see Note 4.5 Other financial assets).

The fair value of other non-current financial assets is determined by discounting future cash flows at current market interest rates.

In addition, EUR 18 million of other non-current financial assets (see Note 4.5 Other financial assets) are classified as available-for-sale financial assets. These relate to investments in start-ups (for further information, see Note 4.5 Other financial assets). These assets were measured at cost, as reliable measurement on the basis of market prices was not possible. These entities generate start-up losses, and the existing business plans contain numerous unreliable assumptions. For this reason, the measurement was made in accordance with IAS 39.46c. The reduction of EUR 3 million concerns investments in start-up companies in the amount of EUR 2 million and a divestment of EUR 5 million recognised in the current year in relation to the investments in start-up companies.

All other financial assets as of 31 December 2017 were categorised as loans and receivables.

Please see the respective notes for further information.

The age structure of the financial assets that are overdue and not impaired was as follows:

(Euros in millions)	**As of 31 December 2017**	As of 31 December 2016
Overdue for 1–90 days	1	15
Overdue for 91-180 days	2	1
Overdue for more than 180 days	19	14
Total	**22**	**30**

With regard to financial assets that are neither overdue nor impaired, there are no indications of circumstances that could have a negative impact on their value as of the respective reporting date.

As of 31 December 2017

Financial liabilities

(Euros in millions)	Hedges (not a measurement category according to IAS 39)	Liabilities at amortised cost	Finance leases	Measurement hierarchy Level 1 (Quoted prices)	Level 2 (Other directly observable market inputs)	Level 3 (Inputs not based on observable market data)	Total carrying amount	Total fair value	Not in the scope of IFRS 7
Non-current interest-bearing debt (Note 4.10)	155	1,098	15	537	778	–	1,268	1,315	–
Non-current trade and other payables (Note 4.11)	–	17	–	–	17	–	17	17	1
Current interest-bearing debt (Note 4.10)	202	419	17	615	25	–	637	639	–
Current trade and other payables (Note 4.11)	–	2,161	–	–	2,161	–	2,161	2,161	62
Total	**357**	**3,695**	**31**	**1,152**	**2,981**	**–**	**4,084**	**4,133**	**64**

As of 31 December 2016*

Financial liabilities

(Euros in millions)	Hedges (not a measurement category according to IAS 39)	Liabilities at amortised cost	Finance leases	Measurement hierarchy Level 1 (Quoted prices)	Level 2 (Other directly observable market inputs)	Level 3 (Inputs not based on observable market data)	Total carrying amount	Total fair value	Not in the scope of IFRS 7
Non-current interest-bearing debt (Note 4.10)	360	1,343	17	1,164	614	–	1,721	1,778	–
Non-current trade and other payables (Note 4.11)	–	15	–	–	15	–	15	15	2
Current interest-bearing debt (Note 4.10)	–	22	15	–	37	–	37	37	–
Current trade and other payables (Note 4.11)	–	2,218	–	–	2,218	–	2,218	2,218	68
Total	**360**	**3,599**	**32**	**1,164**	**2,884**	**–**	**3,991**	**4,048**	**70**

*The prior year's presentation was amended to improve ease of reading.

As of 31 December 2017, EUR 155 million of non-current interest-bearing debt and EUR 202 million of current interest-bearing debt is included in a hedge. This relates to a portion of the bonds, which are each accounted for with an interest rate swap as a fair value hedge (for further information see Note 4.10 Interest-bearing debt).

The fair value of the bonds (non-current and current interest-bearing debt) is determined based on primary market values (unadjusted quoted prices in active markets, level 1). The fair value of the other non-current interest-bearing debt is determined by discounting the future payment streams using current market interest rates.

The non-current and current trade and other payables are categorised as financial liabilities at amortised cost.

Please see the respective notes for further information.

10. Group Companies of the Telefónica Deutschland Group

In accordance with sections 285 and 313 of the German Commercial Code (HGB), the following table lists the companies making up the Telefónica Deutschland Group as of 31 December 2017.

For detailed information, please refer to the list of shareholdings published with the Annual Financial Statements of Telefónica Deutschland Holding AG in the German Federal Gazette.

Company name, registered office	Country	Consolidation	Share in % as of 31 December 2017
Parent company			
Telefónica Deutschland Holding AG, Munich	Germany	n/a	n/a
Subsidiaries			
Telefónica Germany Management GmbH, Munich[2]	Germany	Full financial year	100%
Telefónica Germany GmbH & Co. OHG, Munich[1]	Germany	Full financial year	100%
Telefónica Germany 1. Beteiligungsgesellschaft mbH, Munich[2]	Germany	Full financial year	100%
TGCS Rostock GmbH, Munich[2]	Germany	Full financial year	100%
Telefónica Germany Next GmbH, Munich[2]	Germany	Full financial year	100%
Minodes GmbH, Berlin	Germany	From May 2017	100%
Telefónica Germany Retail GmbH, Düsseldorf[2]	Germany	Full financial year	100%
co-trade GmbH, Munich	Germany	From October 2017	100%
Wayra Deutschland GmbH, Munich[2]	Germany	Full financial year	100%
O2 Telefónica Deutschland Finanzierungs GmbH, Munich	Germany	Full financial year	100%
TGCS Bremen GmbH, Munich[2]	Germany	Full financial year	100%
TGCS Hamburg GmbH, Munich[2]	Germany	Full financial year	100%
TGCS Nürnberg GmbH, Munich[2]	Germany	Full financial year	100%
E-Plus Service GmbH, Düsseldorf[2]	Germany	Full financial year	100%
TGCS Essen & Potsdam GmbH, Potsdam[2]	Germany	Full financial year	100%
TGCS Berlin GmbH, Düsseldorf[2]	Germany	Full financial year	100%
Erste MVV Mobilfunk Vermögensverwaltungsgesellschaft mbH, Düsseldorf[2]	Germany	Full financial year	100%
AY YILDIZ Communications GmbH, Düsseldorf[2]	Germany	Full financial year	100%
Ortel Mobile GmbH, Düsseldorf[2]	Germany	Full financial year	100%
TFS Potsdam GmbH, Potsdam[2]	Germany	Full financial year	100%
Shortcut I GmbH & Co. KG, Hamburg	Germany	Full financial year	90%
Joint Operations			
TCHIBO Mobilfunk Beteiligungs-GmbH, Hamburg	Germany	Full financial year	50%
TCHIBO Mobilfunk GmbH & Co. KG, Hamburg	Germany	Full financial year	50%
Other investments[3]			
MNP GbR, Düsseldorf[4]	Germany	Full financial year	33%
tado GmbH, Munich	Germany	Full financial year	14%
Sum Up Holdings Ltd, Grand Cayman	Cayman Islands	Full financial year	4%
Zen Guard GmbH, Berlin	Germany	Full financial year	6%
So1 GmbH, Berlin	Germany	Full financial year	16%
Stocard GmbH, Mannheim	Germany	Full financial year	17%

[1] These entities are using the exemption provisions pursuant to section 264b HGB.

[2] These entities are using the exemption provisions pursuant to section 264 (3) HGB.

[3] Other investments are not included in the consolidation.

[4] The company reported total equity of EUR 102 thousands as of 31 December 2016 . Net income amounted to EUR -33 thousand for financial year 2016.

In the first quarter of the financial year, Telefónica Germany Customer Services GmbH was renamed to TGCS Rostock GmbH, TGCS Bremen Contact Center GmbH to TGCS Bremen GmbH, TGCS Hamburg Contact Center GmbH to TGCS Hamburg GmbH, TGCS Nürnberg Contact Center GmbH to TGCS Nürnberg GmbH, E-Plus Customer Operations GmbH to TGCS Berlin GmbH, E-Plus Financial Services GmbH to TFS Potsdam GmbH, and E-Plus Customer Support GmbH to TGCS Essen & Potsdam GmbH.

In the second quarter of the financial year, Telefónica Germany Next GmbH took over Minodes GmbH.

In the third quarter of the financial year, E-Plus Services Treuhand GmbH was merged with E-Plus Mobilfunk GmbH with retroactive effect to 1 January 2017. This merger was followed by the accretion of the assets and legal relationships of E-Plus Service GmbH & Co. KG to E-Plus Mobilfunk GmbH. In a second step, E-Plus Mobilfunk GmbH was renamed to E-Plus Service GmbH. Furthermore, Go Clever GmbH and Cash & Phone GmbH were merged with Telefónica Germany GmbH & Co. OHG with retroactive effect to 1 January 2017.

In the fourth quarter of the financial year, Telefónica Germany Retail GmbH took over co-trade GmbH.

11. Joint Operations

Telefónica Germany GmbH & Co. OHG jointly controls TCHIBO Mobilfunk Beteiligungs-GmbH, Hamburg, and TCHIBO Mobilfunk GmbH & Co. KG, Hamburg, jointly with TCHIBO GmbH, Hamburg.

The business objective of TCHIBO Mobilfunk Beteiligungs-GmbH is the holding of interests in other companies. The business objective of TCHIBO Mobilfunk GmbH & Co. KG, where TCHIBO Mobilfunk Beteiligungs GmbH is its personally liable shareholder, is the marketing and sales of mobile communications services to be rendered by third parties and the marketing and sales of hardware.

As part of the joint operation in TCHIBO Mobilfunk GmbH & Co. KG, Telefónica Germany GmbH & Co. OHG reimburses the company for sales and marketing services provided by the latter, on the one hand, and otherwise supplies the company with mobile communications devices.

12. Related Parties

Related parties within the meaning of IAS 24 are defined as natural persons and companies that can be influenced by the Telefónica Deutschland Group, that can exercise a material influence over the Telefónica Deutschland Group, or that are materially influenced by another related party of the Telefónica Deutschland Group.

Transactions with related parties include transactions between the Telefónica Deutschland Group and the Telefónica, S.A. Group.

Telefónica Deutschland Holding AG is the parent company of the Telefónica Deutschland Group. It is included in the Consolidated Financial Statements of the ultimate parent company, Telefónica, S.A., Madrid, Spain (Telefónica, S.A.; its group: the Telefónica, S.A. Group). The direct parent company of the Telefónica Deutschland Group is Telefónica Germany Holdings Limited, a wholly owned subsidiary of O2 (Europe) Limited, Slough, United Kingdom (O2 (Europe) Limited), and an indirect subsidiary of Telefónica, S.A. The companies of the Telefónica, S.A. Group are related parties as Telefónica, S.A. controls the Telefónica Deutschland Group.

Note 10 provides an overview of the companies making up the Telefónica Deutschland Group. In 2016 and 2017, the following were related parties from the perspective of the Telefónica Deutschland Group:

- Telefónica, S.A. and its subsidiaries, and significant investments of Telefónica, S.A. Group (see Note 12.1 Transactions with the Telefónica, S.A. Group),
- Members of the Management Board and Supervisory Board of the Telefónica, S.A. Group and members of the Management Board and Supervisory Board of the Telefónica Deutschland Group (see Note 12.2 Transactions with the Management Board and Supervisory Board).

The extent of the transactions conducted with the Telefónica, S.A. Group and other related parties can be seen in the overviews below.

Intercompany charges are based on cost-plus or similar allocation methods.

12.1. Transactions with the Telefónica, S.A. Group

Receivables from and liabilities to the Telefónica, S.A. Group

The Telefónica Deutschland Group reports the following receivables from and liabilities to the companies belonging to the Telefónica, S.A. Group:

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Receivables from the Telefónica, S.A. Group	**650**	**643**
that are recognised in the following items in the Consolidated Statement of Financial Position:		
Cash and cash equivalents (cash pooling)	573	600
Trade and other receivables	77	43
Liabilities to the Telefónica, S.A. Group	**415**	**466**
that are recognised in the following items in the Consolidated Statement of Financial Position:		
Trade and other payables	415	466
Interest-bearing debt	0	0

Cash and cash equivalents (cash pooling)

The receivables from the Telefónica, S.A. Group as a result of cash pooling relate to the cash pooling agreement with Telfisa Global B.V.

Trade and other receivables

These receivables result from transactions in goods and services such as roaming and commissions for insurance services, as well as licence agreements between Telefónica Deutschland Group and the Telefónica, S.A. Group. As of the reporting dates of 31 December, the line item contains receivables from Telefónica, S.A. of EUR 2 million in 2017 and EUR 1 million in 2016.

Trade and other payables

This item primarily relates to liabilities sold by the suppliers of Telefónica Germany GmbH & Co. OHG to Telefónica Factoring España, S.A., in which Telefónica, S.A. has an interest. In addition, the item includes licence agreements, social security benefits and lease benefits for the entire Telefónica, S.A. Group.

As of the reporting dates of 31 December, the item contains other payables to Telefónica, S.A. of EUR 3 million in 2017 (2016: EUR 7 million).

Interest-bearing debt

The interest bearing debt is related to the loan agreement concluded with Telfisa Global B.V.

Revenues, other income and expenses relating to the Telefónica, S.A. Group

	Revenues, other income and interest income 1 January to 31 December		Expenses 1 January to 31 December	
(Euros in millions)	2017	2016	2017	2016
Telefónica, S.A. Group	44	400	(176)	(192)

Revenues and other income are primarily generated from goods and services such as roaming, mobile phone insurance, wholesale voice, etc. and, in the previous year, additionally from the sale of passive tower infrastructure.

Expenses include group fees totalling EUR 36 million in 2017 and EUR 55 million in 2016, together with expenses relating to the purchase of goods and services, rent, as well as other expenses in connection with transactions with the Telefónica, S.A. Group, e.g. insurance and IT services.

12.2. Transactions with Management Board and Supervisory Board

a) Management Board

In financial year 2017, the members of key management personnel included the following members of the Management Board:

— Markus Haas (CEO)

— Markus Rolle (from 1 August)

— Wolfgang Metze (from 1 August)

- Alfons Lösing (from 1 August)
- Cayetano Carbajo Martín (from 1 August)
- Guido Eidmann (from 1 August)
- Valentina Daiber (from 1 August)
- Nicole Gerhardt (from 1 August)
- Rachel Empey (until 31 July),

The remuneration system of Telefónica Deutschland Group for the members of the Management Board and the Supervisory Board is described in further detail in the Combined Management Report, Remuneration Report.

In the financial years to which the accompanying Consolidated Financial Statements relate, the members of the Management Board have not carried out any transactions with the Telefónica Deutschland Group other than as part of the normal trading and business activity of the Telefónica Deutschland Group.

In accordance with section 314 (1) no. 6a HGB, the total remuneration granted to the Management Board of Telefónica Deutschland Holding AG for the financial year ended 31 December 2017 amounted to EUR 4,147 thousand. The total remuneration in the reporting year contains no share-based payments regarding the transfer of shares without consideration.

The Telefónica Deutschland Group has not currently granted the members of its Management Board any security or loans and have not assumed any guarantees for them.

The total remuneration granted to the Management Board in accordance with section 314 (1) no. 6a HGB in 2016 amounted to EUR 4,105 thousands. The total remuneration in financial year 2016 contains no share-based payments regarding the transfer of shares without consideration.

Salaries and other benefits according to IAS 24.17 that were granted to active Management Board members are composed as follows:

	1 January to 31 December	
(Euros in thousands)	2017	2016
Remuneration	**4,611**	**3,980**
thereof:		
Short-term employee benefits	3,884	3,558
Other long-term employee benefits	367	255
Share-based payments[1]	93	(22)
Service cost	268	189

[1] Due to forfeited share options, income from share-based payments was recognised in the previous year

Due to the conditional rights to the free transfer of shares (bonus shares) for Telefónica, S.A.'s share options for the Management Board members (for further information see the Management Report, Remuneration system for Board Members) the following changes took place:

(In units)	2017	2016
Share options as of 1 January	**111,242**	**266,661**
Forfeited share options	(65,990)	(133,176)
Change in composition of Management Board	37,345	–
Actual share assignment	(22,252)	(22,243)
Share options as of 31 December	**60,345**	**111,242**

The defined benefit pension obligations for the Management Board members in financial year 2017 amounted to EUR 2,248 thousand and EUR 4,185 thousand in 2016.

As of 31 December 2017 and 2016, the pension obligations for members of the former management and their surviving dependants amounted to EUR 14,448 thousand and EUR 12,443 thousands, respectively.

For further details of the pension obligations of the Telefónica Deutschland Group, please refer to Note 4.12 Provisions.

As of 31 December 2017 and 2016, the total remuneration expense for members of the former management and their surviving dependants amounted to EUR 182 thousand in 2017 and EUR 197 thousand in 2016.

b) Supervisory Board

Name	Member of the Supervisory Board	Remuneration in thousands of Euros
Eva Castillo Sanz	since 5 October 2012	80
Laura Abasolo García de Baquedano	since 12 May 2015	2
Angel Villá Boix	since 18 September 2012 to 4 October 2017	2
Patricia Cobian González	since 18 September 2012	2
Michael Hoffmann	since 5 October 2012	70
Enrique Medina Malo	since 18 September 2012	2
Sally Anne Ashford	since 18 September 2014	20
Peter Erskine	since 19 May 2016	20
Julio Linares López	since 16 October 2017	4
Christoph Braun	since July 2016	40
Thomas Pfeil	since 3 June 2013	20
Dr. Jan Erik Walter	since 3 June 2013	20
Marcus Thurand	since 3 June 2013	20
Christoph Heil	since 3 June 2013	20
Claudia Weber	since 3 June 2013	20
Joachim Rieger	since 31 October 2014	25*
Jürgen Theirfelder	since 31 October 2014	25*

*In addition to the remuneration set out in Section 20 of Telefónica Deutschland Holding AG's Articles of Association, Mr Joachim Rieger and Mr Jürgen Thiefelder receive annual remuneration for their work as Supervisory Board members of the subsidiaries TCGS Potsdam GmbH and Telefónica Germany Retail GmbH of EUR 4,500 each, which is already included in the table.

The members of the Supervisory Board received remuneration for their activities of EUR 382 thousands in 2017 and EUR 372 thousands in 2016.

Members of the Supervisory Board who are also employees of the Telefónica Deutschland Group also receive remuneration from their employment relationship, including entitlements from share-based payment agreements, subject to compliance with the requirements for participation in each individual case, and are entitled to pension schemes. This remuneration comprises the following with effect from appointment to the Supervisory Board:

(Euros in thousands)	2017	2016
Remuneration	**721**	**707**
thereof:		
Short-term employee benefits	693	683
Share-based payments	7	3
Service cost	21	21

As of 31 December 2017, the Telefónica Deutschland Group has not granted the members of its Supervisory Board any securities or loans, and has not assumed any guarantees on their behalf.

13. Share-based Payments

As of 31 December 2017, the Telefónica Deutschland Group had made various agreements regarding share-based payments. The financial effects of the share-based remuneration systems are, however, of minor importance for the Telefónica Deutschland Group:

- In financial year 2017, personnel expenses arising from share-based payment transactions amounted to EUR 7 million (2016: EUR 3 million).
- As of 31 December 2017, liabilities arising from share-based payment transactions amounted to EUR 0 million (2016: EUR 0 million).

14. Information Regarding Employees

The following table presents the breakdown of the Telefónica Deutschland Group's average headcount grouped with respect to their status under employment law:

Average headcount	2017	2016
Office staff	9,024	8,821
thereof from joint operations	12	11
Temporary staff	381	452
Total	**9,405**	**9,272**

15. Financial Instruments and Risk Management

As of the reporting date, Telefónica Deutschland Group faces a variety of risks from financial instruments. In this regard, please refer to the statements regarding risk management and financial instruments in the Combined Management Report.

16. Capital Management

The Telefónica Deutschland Group strives to guarantee the sustainability of its business and to maximise its enterprise value by permanently monitoring its capital costs, equity ratio and OIBDA.

As of 31 December 2017, the equity ratio amounted to 58.8% compared with 61.5% as of 31 December 2016. In financial year 2017, OIBDA amounted to EUR 1.785 million and EUR 2.069 million in 2016.

17. Contingent Assets and Liabilities

Indirect claims against the frequency allocation at 800 MHz, 1.8 GHz, 2.0 GHz and 2.6 GHz could result in the reassignment of the 800 MHz, 1.8 GHz, 2.0 GHz and 2.6 GHz frequencies purchased at the 2010 frequency auction. The above frequencies were (indirectly) contested, as there was pending litigation from several cable network operators, broadcasting companies and Airdata AG against the terms and conditions, on which the frequency allocation was based. This litigation was primarily aimed at the allocation conditions for 800 MHz, but also alternatively involved the rescission of the entire allocation decision (i.e. also affecting 1.8 GHz, 2.0 GHz and 2.6 GHz). The actions have now been dismissed in the court of last instance. This ends the legal disputes before the administrative courts. The possibility of additional legal proceedings due to as yet unasserted third-party claims against frequency allocations in 800 MHz in connection with the aforementioned legal action cannot be ruled out. If the appeals are successful, this could result in the reassignment of the frequencies for 800 MHz acquired at the 2010 frequency auction.

As one of the leading network operators in Germany, Telefónica Deutschland Group is exposed to the risk of claims concerning patent violations. In this context, patent owners could assert claims for licence payments and/or for the prohibition of the use of certain patent-violating technologies. This risk is mitigated by Telefónica Deutschland Group's exemption and compensation claims against its relevant suppliers. Besides compensation claims for legal costs, patent owners currently have potential licence claims that come under consideration on the basis of the provisional/court-assessed values in dispute. These claims are almost completely offset by the potentially mitigating exemption and compensation claims. The amount of the legal costs and licence claims is estimated in the low millions.

Telefónica Deutschland Group could be subject to claims or other proceedings arising in the ordinary course of business. The possible effects are of minor significance for the Group's net assets, financial position and results of operations.

18. Operating Leases, Purchase and Other Contractual Obligations

The following expected maturity dates apply for the obligations from operating leases, purchase and contractual obligations:

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Less than 1 year	554	535
1 to 5 years	1,451	1,265
Over 5 years	774	992
Obligation from operating leases	**2,779**	**2,793**

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Less than 1 year	1,351	1,129
1 to 5 years	698	47
Over 5 years	154	692
Purchase and other contractual obligations	**2,203**	**1,868**
Total	**4,982**	**4,661**

The following amounts are recognised in the Consolidated Income Statement:

	1 January to 31 December	
(Euros in millions)	2017	2016
Expenses for operating leases	642	543

The expenses for operating leases essentially include rental expenses for office buildings and shops, antenna sites, cars and network equipment (i.e. leased lines and cell sites). Some of the contracts contain renewal options. These relate primarily to lease contracts for network towers.

The Telefónica Deutschland Group provides absolute guarantees to secure rental obligations primarily for antenna sites. These guarantees are granted by external financial counterparts and are offered in the course of normal commercial activity.

The guarantees amounted to EUR 111 million as of 31 December 2017 compared with EUR 105 million in 2016.

The Telefónica Deutschland Group has entered into various sublease agreements for office buildings, cell sites and shops. The estimated payment schedule for subleases is as follows:

(Euros in millions)	As of 31 December 2017	As of 31 December 2016
Less than 1 year	13	15
1 to 5 years	17	20
Over 5 years	4	5
Income from subleases	**35**	**40**

The following amounts are recognised in the Consolidated Income Statement:

(Euros in millions)	1 January to 31 December 2017	2016
Income from subleases	22	24

19. Total Auditor's Fees

The services listed below performed by the Group's auditor, which was Ernst & Young GmbH Wirtschaftsprüfungsgesellschaft until 2016 and PricewaterhouseCoopers GmbH Wirtschaftsprüfungsgesellschaft from 2017, were recognised in the Consolidated Income Statement.

Because the Telefónica Deutschland Group conducts all of its business in Germany, the entire amount is incurred in Germany.

(Euros in millions)	1 January to 31 December 2017	2016
Types of fee:		
Audit fees	2	2
Other audit-related services	0	0
Total fee	**2**	**2**

The auditor's fees include especially the fees for auditing the Consolidated Financial Statements of Telefónica Deutschland Holding AG and fees for auditing the annual financial statements of the subsidiaries. Other audit-related services were performed in financial year 2017 only to a minor extent.

20. Events after the Reporting Period

Telefónica Germany GmbH & Co. OHG has mandated Landesbank Baden-Württemberg (LBBW) and DZ Bank AG for the placement of a promissory note loan targeting a volume of EUR 200 million consisting of various tranches with tenors of up to 15 years. Placement has started in January 2018 and closing is scheduled to take place in the 1st quarter of 2018. The financing agreement will only be finalised after successful placement in February, payment will only be made on 28 February or in March.

No additional events subject to disclosure requirements occurred after the 2017 end of the financial year.

21. Declaration of Compliance with the German Corporate Governance Code

The Management Board and the Supervisory Board last submitted a declaration of compliance in accordance with section 161 of the German Stock Corporation Act (AktG) on 12 /13 /14 /16 October 2017. The complete wording of the declaration of compliance is available on Telefónica Deutschland's website at **www.telefonica.de/declaration-of-compliance-2017**.

Munich, 12 February 2018

Telefónica Deutschland Holding AG

The Management Board

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