Financial Statements 2009

Landsnet hf.
Gylfaflöt 9
112 Reykjavík

Reg. no. 580804-2410

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Endorsement by the Board of Directors and the CEO

General

Landsnet hf was established in August 2004 on the basis of the Electricity Act passed by the Icelandic parliament, the Althingi, in the spring of 2003. The role of Landsnet is to administer the transmission of electricity and system operation in accordance with the provisions of Chapter III of the Electricity Act No. 65/2003.

Results of the year 2009

According to the income statement, profit for the year amounted to ISK 1.5 billion and total profit for the year amounted to ISK 1 billion. The presentation is in accordance with the revised International Accounting Standards IAS 1, Presentation of Financial Statements, which entered into effect on 1 January 2009. Comparative figures have been changed accordingly. The change only affects the presentation of the financial statements and does not alter the financial ratio profit (loss) per share. According to the balance sheet, the Company's equity at year end amounted to ISK 8.3 billion.

Share capital at year end 2009 is divided between four shareholders as at the beginning of the year:

	Share
Landsvirkjun	64.73%
Rarik ohf.	22.51%
Orkuveita Reykjavíkur	6.78%
Orkubú Vestfjarða ohf.	5.98%

Statement of the Board of Directors and the CEO

According to the best of our knowledge, the financial statements are in accordance with the International Financial Reporting Standards as adopted by the EU and it is our opinion that the annual financial statements give a true and fair view of the financial performance of the Company for the financial year 2009, its assets, liabilities and financial position as at 31 December 2009 and its cash flows for the financial year 2009.

Further, in our opinion the financial statements and the endorsement by the Board of Directors and the CEO give a fair view of the development and performance of the Company's operations and its position and describes the principal risks and uncertainties faced by the Company.

The Board of Directors and the CEO have today discussed the annual financial statements of Landsnet hf for the year 2009 and confirmed them by means of their signatures.

Reykjavik, 11 February 2010.

The Board of Directors:

Friðrik Már Baldursson
Svana Helen Björnsdóttir
Katrín Helga Hallgrímsdóttir

CEO:

Þórður Guðmundsson

Independent Auditor's Report

To the Board of Directors and Shareholders of Landsnet hf.

We have audited the accompanying financial statements of Landsnet hf, which comprise the report by the Board of Directors, the balance sheet as at 31 December 2009, the income statement, statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory notes.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

Auditor's responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Landsnet hf as at 31 December 2009 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Reykjavik, 11 February 2010.

KPMG hf.

Matthías Þór Óskarsson

Income Statement for the year 2009

	Notes	2009	2008
Operating revenue			
Transmission	6	13.233.789	10.743.814
Other income	7	60.595	108.897
		13.294.384	10.852.711
Operating expenses			
Energy procurement costs		1.626.571	1.550.607
Transmission costs	9	3.282.830	2.831.349
System operation	9	640.432	575.815
Other operating expenses	9	793.627	728.452
		6.343.460	5.686.223
Operating profit		6.950.924	5.166.488
Financial income		157.093	118.477
Financial expenses		(5.786.569)	(20.282.106)
Net financial expenses	10	(5.629.476)	(20.163.629)
Share in net earnings of associated company	13	9.162	7.237
Profit (loss) before income tax		1.330.610	(14.989.904)
Income tax	11	140.625	2.210.258
Profit (loss)		1.471.235	(12.779.646)
Earnings (loss) per share			
Basic and diluted earnings (loss) per each ISK 1 share	19	0,25	(2,17)

Notes no. 1 to 29 are an integral part of these financial statements.

Financial Statements of Landsnet hf 2009 5 Amounts are in ISK thousand

Statement of Comprehensive Income for the year 2009

	Notes	2009	2008
Profit (loss)		1.471.235	(12.779.646)
Items under total profit recognised among equity			
Revaluation of transmission system		0	17.726.890
Current tax on revaluation of transmission system		0	(2.659.033)
Effect of changed tax rate on the revaluation of transmission		(424.017)	0
Total items under total profit recognised among equity		(424.017)	15.067.857
Total profit of the year		1.047.218	2.288.211

Notes no. 1 to 29 are an integral part of these financial statements.

Financial Statements of Landsnet hf 2009 6 Amounts are in ISK thousand

Balance Sheet as at 31 December 2009

	Notes	2009	2008
Assets			
Fixed assets in operation	12	62.171.360	61.405.502
Projects under construction	12	1.612.157	1.781.611
Intangible assets	12	1.479.350	1.716.814
Shares in other companies	13	50.558	48.832
Fixed assets		65.313.425	64.952.759
Inventories	15	483.285	480.439
Assets available for sale	12	427.693	0
Receivable from related companies		587.604	396.605
Trade and other receivables	16	999.859	853.021
Cash and cash equivalents	17	5.863.874	2.700.681
Current assets		8.362.315	4.430.746
Total assets		73.675.740	69.383.505
Equity			
Share capital	18	5.902.733	5.902.733
Revaluation account	18	13.709.886	14.743.274
Accumulated deficit		(11.290.636)	(13.371.242)
Equity		8.321.983	7.274.765
Liabilities			
Payable to related companies	20	47.180.690	34.808.942
Other long-term liabilities	20	12.003.482	6.676.851
Derivatives	22	2.769.177	2.991.625
Deferred income tax liability	14	502.804	219.412
Other obligations	21	582.404	475.723
Long-term liabilities and obligations		63.038.557	45.172.553
Loans from related companies		1.241.102	15.813.603
Current maturities		110.446	0
Trade and other payables	24	963.652	1.122.584
Short-term liabilities		2.315.200	16.936.187
Total liabilities		65.353.757	62.108.740
Total equity and liabilities		73.675.740	69.383.505

Notes no. 1 to 29 are an integral part of these financial statements.

Financial Statements of Landsnet hf 2009 7 Amounts are in ISK thousand

Statement of Changes in Equity for the year 2009

	Share capital	Revaluation account	Accumulated deficit	Total
Year 2008:				
Equity at 1 January 2008	5.902.733	0	(916.179)	4.986.554
Loss for the year			(12.779.646)	(12.779.646)
Revaluation of transmission system		17.726.890		17.726.890
Income tax effect of total revaluation		(2.659.033)		(2.659.033)
Total comprehensive income		15.067.857	(12.779.646)	2.288.211
Depreciation on revaluation recognised under accumulated deficit		(324.583)	324.583	0
Equity at 31 December 2008	5.902.733	14.743.274	(13.371.242)	7.274.765
Year 2009:				
Equity at 1 January 2009	5.902.733	14.743.274	(13.371.242)	7.274.765
Profit for the year			1.471.235	1.471.235
Effect of changed tax rate on revaluation		(424.017)		(424.017)
Total comprehensive income		(424.017)	1.471.235	1.047.218
Depreciation on revaluation recognised under accumulated deficit		(609.371)	609.371	0
Equity at 31 December 2009	5.902.733	13.709.886	(11.290.636)	8.321.983

Notes no. 1 to 29 are an integral part of these financial statements.

Financial Statements of Landsnet hf 2009 8 Amounts are in ISK thousand

Statement of Cash Flows for the year 2009

	Notes	2009	2008
Cash flow from operating activities			
Cash received from customers		13.155.078	10.683.265
Cash expenses		(3.836.827)	(3.839.947)
From operating activities excluding interest		9.318.251	6.843.318
Interest income received		157.093	118.478
Interest expenses paid and foreign exchange difference		(1.956.438)	(1.201.543)
Net cash from operating activities		7.518.906	5.760.253
Cash flow from investing activities			
Investment in property, plant and equipment	12	(938.923)	(1.304.077)
Proceeds from sale of property, plant and equipment	12	0	700
Investment in substations under construction	12	(1.718.812)	(275.605)
Investment in intangible assets	12	(465.216)	(1.204.552)
Change in unpaid construction costs, (decrease) increase		(269.288)	130.757
Proceeds from the sale of shares in an associated company		7.436	0
Net cash (to) from investment activities		(3.384.803)	(2.652.777)
Cash flow from financing activities			
Change in loans from related companies		(5.908.690)	3.019.900
Long-term loans		4.874.569	0
Change in short-term loans		0	(4.891.728)
Net cash (to) from financing activities		(1.034.121)	(1.871.828)
Net increase in cash and cash equivalents		3.099.982	1.235.648
Effect of exchange rate changes on cash and cash equivalents		63.210	480.774
Cash and cash equivalents at 1 January		2.700.681	984.259
Cash and cash equivalents at 31 December		5.863.874	2.700.681

Notes no. 1 to 29 are an integral part of these financial statements.

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Notes to the Financial Statements

1. Reporting entity

Landsnet hf has its headquarters in Iceland and is domiciled at Gylfaflöt 9 in Reykjavik, Iceland. The Company is a subsidiary of Landsvirkjun, which holds a 64.73% share. Landsnet was established in 2004 on the basis of the Electricity Act passed by the Icelandic parliament, the Althingi, in the spring of 2003. The role of Landsnet is to administer the transmission of electricity and system operation in accordance with the provisions of Chapter III of the Electricity Act No. 65/2003, which stipulates that the Company must not engage in any activities other than necessary to perform its duties under the Act.

2. Basis of preparation

a. Statement of compliance

The financial statements have been prepared in accordance with the International Financial Reporting Standards (IFRS) as adopted by the EU.

The financial statements were approved by the Board of Directors on 11 February 2010.

The accounting policies set out below have been applied consistently to all periods presented in these financial statements.

b. Basis of measurement

The financial statements have been prepared on the historical cost basis, except that the Company's transmission system is recognised at a revalued amount. The methods to measure fair value are discussed further in Note 4.

c. Functional and presentational currency

These financial statements are presented in Icelandic krónur (ISK), which is the Company's functional currency. All financial information presented in ISK has been rounded to the nearest thousand.

d. Use of estimates and judgements

The preparation of the financial statements in conformity with IFRS standards requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements is included in the following notes:

- Note 3c - Property, plant and equipment
- Note 3d - Intangible assets
- Note 3l (i) - Estimation of provision due to site restoration
- Note 14 - Income tax
- Note 22 - Derivatives

3. Significant accounting policies

The following accounting methods have been consistently applied to all disclosed periods in the financial statements, except that the Company has as of 1 January 2008 recognised its transmission network according to the revaluation method defined under IAS 16. Thus, the Company's transmission lines and substations are recognised at a revalued price in the balance sheet, which is their fair value at the revaluation date less revalued depreciation value from the date that the assets were acquired. Note 3c includes more details on the accounting policies applied in relation to the revaluation.

3. Significant accounting policies, contd.:

a. Foreign currency

Transactions in foreign currencies are translated to the functional currency of the Company at the exchange rates on the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies on the reporting date are retranslated to the functional currency at the exchange rate on that date. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate on the date that the fair value was determined. Foreign currency differences arising on retranslation are recognised in profit or loss.

b. Financial instruments

(i) Non-derivative financial instruments

Non-derivative financial instruments consist of investments in equity, trade and other receivables, cash and cash equivalents, loans, borrowings and trade and other payables.

Non-derivative financial instruments are recognised initially at fair value. For instruments not recognised at fair value through profit or loss, any directly attributable transaction costs are initially entered as an increase in their value. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

A financial asset and liability is recognised when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognised if the Company's contractual rights to the cash flows from the financial assets expire or if the Company transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Regular-way purchases and sales of financial assets are accounted for on the trade date, i.e. the date that the Company commits itself to purchase or sell the asset. Loans and receivables are recognised on the date that they are originated. Financial liabilities are derecognised if the Company's obligations specified in the contract expire or are discharged or cancelled.

Cash and cash equivalents comprise cash balances and call deposits.

Accounting for finance income and expense is discussed in Note 3(o).

(ii) Financial assets at fair value through profit or loss

An instrument is classified at fair value through profit or loss if it is held for trading or is designated as such upon initial recognition. Financial instruments are designated at fair value through profit or loss if the Company manages such investments and makes purchase and sale decisions based on their fair value. Upon initial recognition, attributable transaction costs are recognised in profit or loss when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

(iii) Other financial instruments

Financial instruments other than derivative financial instruments are recognised at the amortised cost value based on effective interest rates, less depreciation if detected.

(iv) Derivative financial instruments

The Company uses derivatives in order to hedge against currency and interest rate risk. Reference is made to Note 22 in relation thereto.

The Company has entered into currency and inerest rate swaps in order to hedge against the Company's currency and interest rate risk. Hedge accounting is not applied. Fair value changes on such derivatives are recognised among net income and expenses on financial assets and liabilities in the statement of comprehensive income.

(v) Share capital

Share capital is classified as equity.

3. Significant accounting policies, contd.:

c. Property, plant and equipment

(i) Fixed assets in operation

Items of property, plant and equipment other than transmission lines and substations are measured at cost less accumulated depreciation and impairment losses.

The cost includes expenditures directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the asset to a working condition for its intended use and the costs of dismantling and removing the items as well as restoring the site on which they are located.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property, plant and equipment.

In accordance with the provisions of the International Accounting Standard IAS 16, the Company's transmission lines and substations are recognised on the basis of the revaluation method. The Company's transmission lines and substations are thus stated at a revalued cost in the balance sheet, which is their fair value on the revaluation date less revalued depreciation from the assets' acquisition date. The revaluation of those assets will be performed on a regular basis and when the management believes that their fair value has changed significantly, among other things due to external factors. All value increases due to the revaluation are entered in a revaluation account among equity after income tax. Depreciation of the revalued price is recognised in the income statement. Upon sale or disposal of an asset, the part of the revaluation account pertaining to that asset is recognised in retained earnings.

(ii) Transmission structures under construction

Projects under construction are capitalised on the basis of the cost of purchased services, materials, direct wages and other costs directly attributable to the property. Assets that have not been put to use are not depreciated. Cost of capital for financing the cost of projects under construction is capitalised in the period that the asset is being constructed and is considered a part of the cost of the asset. Capitalised cost of capital is the Company's weighted average cost of capital.

(iii) Leased assets

The leases the Company holds are operating leases. Leased assets are not recognised in the Company's balance sheet.

(iv) Subsequent costs

The cost of replacing a part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Company and its cost can be measured reliably. The costs of day-to-day servicing of property, plant and equipment are recognised in profit or loss when incurred.

(v) Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant or equipment until the salvage value is reached. The estimated useful lives are as follows:

Substations	20 - 40 years
Transmission lines	50 years
Fibre-optic cables	20 years
Buildings	50 years
Other assets	4-10 years

Depreciation methods, useful lives and residual values are reviewed at each reporting date.

3. Significant accounting policies, contd.:

d. Intangible assets

(i) Developement cost

Expenditure on research activities is recognised in profit or loss when incurred. Developement cost is capitalised within fixed assets. This cost consists largely of expenses relating to exploration for transmission line sites, preparation for transmission structures and environmental impact assessments of proposed projects. The Company has concluded agreements whereby the prospective buyers of electricity shall bear all expenses of the project if it is cancelled. Cost of capital attributable to developement costs is not capitalised. Developement cost is not depreciated at this stage, but possible impairment losses have been considered, as discussed in Note (3i).

When the decision to construct a transmission structure has been made and all neccessary approvals have been obtained, the development cost of the transmission structure is capitalised in fixed assets as a project under construction.

At each accounting date, capitalised development cost is reviewed by management and impairment is recognised if premises for the recognition of development cost no longer exist.

(ii) Software and other intangible assets

Software and other intangible assets are measured at cost less accumulated amortisation and accumulated impairment losses.

(iii) Amortisation

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives for the current and comparative periods are as follows:

Software	4 years

e. Subsidiaries

The Company has one subsidiary, Landsnet ehf. The financial statements of the two companies are not consolidated and the holding is recognised at historical cost. The subsidiary has had insubstantial activity since its establishment.

f. Investment in associates

Associates are those entities in which the Company has significant influence, but not control, over financial and operating policies. Significant influence is presumed to exist when the Company holds between 20 and 50 percent of the voting power of another entity. Associates are accounted for using the equity method and are initially recognised at cost. The financial statements include the Company's share of the total recognised gains and losses of equity movements of associates on an equity-accounted basis from the date that significant influence commences until the date that the significant influence ceases. When the Company's share of losses exceeds its interest in an associate, the Company's carrying amount, including any long-term investments, is reduced to nil and recognition of further losses is discontinued except to the extent that the Company has undertaken an obligation for or made payments on behalf of the investee.

g. Inventories

Inventories are measured at the lower of cost and net realisable value. Net realisable value is the expected sales price in normal operation net of any cost of selling the product. The cost of inventories is based on the first-in-first-out (FIFO) principle of inventory valuation and includes cost incurred in acquiring the inventories and bringing them to their existing location and condition.

h. Trade receivables and other receivables

Trade receivables and other receivables are measured at cost net of any impairment losses.

3. Significant accounting policies, contd.:

i. Impairment

(i) Financial assets

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss.

(ii) Other assets

The carrying amount of the Company's other assets, except for inventories and deferred tax assets, is reviewed at each reporting date to determine whether there is any indication of an impairment loss. If any such indication exists, the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset or its cash-generating unit exceeds its estimated recoverable amount. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows of other assets or groups of assets (the "cash-generating unit"). Impairment losses are recognised in profit or loss. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amount of the other assets in the unit (group of units) on a pro rata basis. An impairment loss of revalued assets is recognised in revaluation account amongst retained earnings.

j. Employee benefits

(i) Defined contribution plans

The Company pays a contribution for part of its employees to defined contribution pension funds. The Company has no responsibility regarding the obligations of the pension funds. The contributions are recognised as an expense under salary and salary related expenses as incurred.

(ii) Defined benefit plans

Under an agreement between the Company and the Pension Fund for State Employees (LSR), the Company's obligations regarding employees who are members of LSR shall be settled yearly. LSR estimates specifically at year-end the present value of the pension obligation accrued during the year and deducts from that amount the contributions paid by employees and the Company to LSR due to pension rights accrued during the year. The difference is recognised in profit or loss and settled on a yearly basis. The actuarial estimation shall assume that the obligation accrued for the year is calculated to the present value at year-end using the interest rate normally used to estimate the obligations of pension funds, which is currently 3.5% per annum.

k. Share capital

When share capital recognised as equity is repurchased, the amount of the consideration paid, including directly attributable costs, is recognised as a deduction from equity. Repurchased shares are classified as treasury shares and presented as a deduction from total equity.

3. Significant accounting policies, contd.:

l. Provisions

A provision is recognised if, as a result of a past event, the Company has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are estimated by discounting the expected future cash flows at a pre-tax rate that reflects the current market assessment of the time value of money and the risks specific to the liability.

(i) Site restoration

The Company has estimated the cost of demolition of current line lots. The estimation is based on expert assessment. The demolition cost has been discounted based on the estimated useful life of the Company's power transmission lines. The discounted value is entered, on the one hand, as an increase for the relevant asset and, on the other hand, as an obligation in the balance sheet. Estimated demolition cost is discounted by the nominal yield of state-guaranteed securities, which is currently 7.94%.

m. Revenue

Income from the transmission of electricity is recognised in the income statement on the basis of measured delivery during the period. Other revenue is recognised as earned or delivered.

The Company's tariff is subject to the National Energy Authority's opinion. On the basis of Article 12 of the Electricity Act No. 65/2003, the National Energy Authority sets an annual limit on the Company's revenue from transmission of electricity to distribution system operators on the one hand and industrial users on the other hand. Article 12 of the Electricity Act states, among other things, the following:

The National Energy Authority shall set a revenue cap for the transmission company regarding the cost of the transmission of electricity to distribution systems on the one hand industrial users on the other hand. The revenue cap shall take into account whether industrial users lead to, or have led to, more profitable development and use of the transmission systems than would otherwise be the case.
The revenue cap shall be decided on the basis of the following criteria:
1. Cost relating to the Company's operation, including the cost of maintenance, the depreciation of important assets for the operation of the grid, lease cost due to transmission systems, cost due to energy losses, general operating expenses and system management costs.
2. The transmission company's yield shall be as close as possible to the market yield on unindexed five-year government bonds or comparable securities. The return is calculated as the percentage of EBIT and of the carrying amount of fixed assets necessary for the operation of the system.
3. Cost reduction requirements, based on normal cost according to the evaluation of the National Energy Authority, taking account of the Company's services.

The revenue cap shall be decided for three years at a time but reviewed on an annual basis. The review shall take into consideration whether any changes have taken place regarding the basis on which the revenue cap is determined. Excess recognition or lack of recognition of revenue may be adjusted between years. A regulation must stipulate a limit on the authorisation for the accumulation of rights.

The transmission company shall establish tariffs for its service in accordance with the revenue cap pursuant to paragraph 2. The tariff shall apply to distribution system operators on the one hand and industrial users on the other hand.

Two months before the tariff enters into force, it shall be submitted to the National Energy Authority. If the National Energy Authority believes that the presented tariff is in breach of the provisions of this Act or the of regulations, it shall send comments thereon to the transmission company within six weeks from the date it received the tariff. The tariff does not become valid until it has been adjusted on the basis of the National Energy Authority's assessment. The transmission company shall publish the tariff publicly.

3. Significant accounting policies, contd.:

m. Revenue, contd.:

If it is discovered that the transmission company's rate of return for the past three years was lower than 50% of the five-year nominal yield on government bonds or comparable securities nor the Company is generating profit, the determination of the revenue cap and the next year's tariff shall be based thereon. The same applies if it is discovered that the transmission company's rate of return for the past years was more than one-third higher over the same yield.

The Company's tariff is denominated partly in ISK and partly in USD.

n. Lease payments

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease.

An asset lease is expensed in the financial statements, the amount of which corresponds to financing cost and depreciation during the year, in relation to the use of electricity companies' transmission structures. The lease charge is regulated by the National Energy Authority.

o. Finance income and expenses

Finance income comprises interest income on funds invested, changes in the fair value of financial assets at fair value through profit or loss and foreign exchange rate differences recognised in profit or loss. Interest income is recognised as it accrues in profit or loss, using the effective interest method.

Finance expenses comprise interest expense on borrowings, reversal of discounting of obligations, foreign exchange losses, changes in the fair value of financial assets at fair value through profit or loss and impairment losses recognised on financial assets.

p. Income tax

Income tax on the profit for the year is deferred income tax. Income tax is recognised in profit or loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Deferred tax is recognised using the balance sheet method, providing for temporary differences between the carrying amount of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred tax is measured at the tax rates that are expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. The income tax rate will be 18% as of 1 January 2010 and the effect of the increase has been recognised in the financial statements.

q. Earnings (loss) per share

The Company presents basic and diluted earnings per share (EPS) data for its ordinary shares. Basic EPS is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period. Diluted EPS is the same as basic EPS, as the Company has not issued any call options or convertible bonds.

r. Segment reporting

Under the Electricity Act, the Company may only administer the transmission of electricity and system management in Iceland and operate an electricity trading market. The Company has not begun operating an electricity trading market and considers its present operation as one single segment, for which reason it does not provide segment reporting.

3. Significant accounting policies, contd.:

s. Change in accounting policies

As of 1 January 2009 the Company has changed its accounting methods according to the following:

(i) Presentation of financial statements

At the beginning of 2009, a revised IAS 1 Presentation of Financial Statements entered into effect, introducing the term 'total comprehensive income', which represents changes in equity during a period other than those changes resulting from transactions with owners in their capacity as owners. Total comprehensive income may be presented in either a single statement of comprehensive income, or in an income statement and a separate statement of comprehensive income. The presentation of comparative figures has been changed in accordance with the new presentation as required by the revised standard. The change only affects the presentation and does not alter the financial ratio earnings per share (EPS).

(ii) Determination and presentation of segment reporting

As of 1 January 2009, the Company determines and presents information on segments based on internal reporting to the Company's senior management. This change in accounting policies is due to the implementation of a new standard, IFRS 8 Segment Reporting. Previously, segment reporting was presented on the basis of IAS 14 - Segment Reporting. The implementation of the standard does not lead to changes in the Company's decision regarding segments.

t. New standards and interpretations thereof

The Company has implemented all International Financial Reporting Standards, amendments thereto and interpretations confirmed by the EU at year-end 2009 and that apply to its operations. The Company has not implemented standards, amendments thereto or interpretations entering into effect after year-end 2009 but allowed to be implemented sooner. The effect thereof on the Company's financial statements has not been fully determined but is considered to be insubstantial.

4. Determination of fair values

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

a. Trade and other receivables

The fair value of trade and other receivables is measured at the estimated discounted cash flow, based on market interests on the reporting date.

b. Derivatives

The fair value of derivative contracts is based on their listed market price, if available. If a listed market price is not available, then the fair value is estimated using accepted valuation techniques.

Valuation techniques include recent arm's lenght transactions between knowledgeable, willing parties, if available, reference to the current fair value of other instruments that are substantially the same, the discounted cash flow analysis and option pricing models. Valuation techniques incorporate all factors that market participants would consider in setting a price and are consistent with accepted methodologies for pricing financial instruments.

The fair value of derivative agreements not listed in active markets is determined using valuation methods reviewed on a regular basis by qualified employees. All valuation models used must be approved and tested in order to ensure that the results reflect those documents that were used.

4. Determination of fair values, contd.:

b. Derivatives, contd.:

The most reliable verification of the fair value of derivative agreements at the beginning is the purchase value, unless the fair value of the instrument can by verified by comparison with other listed and recent market transactions of a comparable instrument or based on an evaluation method where variables are solely based on market documents. When such documents are available, the Company recognises profit or loss at the initial registration date of the instruments.

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for similar instruments at the measurement date.

c. Non-derivative financial liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of intest at the reporting date.

5. Financial risk management

Overview

The Company has exposure to the following risks from its use of financial instruments:

- Credit risk
- Liquidity risk
- Market risk

This Note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk and its management of capital. Further quantitative disclosures are included throughout these financial statements.

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board of Directors seeks consultation regarding financial risk both from its employees and external consultants and discusses it regularly at Board meetings.

The Company's objective is to discover and analyse the risks it faces, set a benchmark for risk exposure and control it. The Company's risk management policy is regularily reviewed to analyse market changes and changes within the Company.

Credit risk

Credit risk is the risk of financial loss of the Company owing to the failure of a customer or counterparty to a financial instrument to meet its contractual obligations. The Company's credit risk is mainly due to trade receivables.

Trade and other receivables

The Company's exposure to credit risk is influenced mainly by the individual characteristics of each customer. Approximately 87% of the Company's transmission income derives from the Company's shareholders.

In general, the Company's customers are financially strong energy companies, which have conducted business with the Company since its establishment. The Company's largest customers are also shareholders in the Company. As of its establishment, the Company has not incurred losses on accounts receivable and its representatives have assessed its credit risk as insubstantial based on current operations. The Company's collection issues are reviewed on a regular basis.

5. Financial risk management, contd.:

Liquidity risk

Liquidity risk is the risk that the company will not be able to meet its financial obligations as they will fall due. The Company endeavours to ensure, to the extent possible, that it always has sufficient liquidity to meet its liabilities when due, without incurring unacceptable losses or risking damage to the Company's reputation.

The Company has entered into an agreement on a revolving credit facility with the parent company, Landsvirkjun, in the amount of USD 100 million. At year-end, undrawn credit under the facility amounted to USD 25 million. At year-end 2010, the facility will decrease to USD 85 million.

Market risk

Market risk is the risk that changes in the market prices of foreign exchange rates and interest rates will affect the Company's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising return.

The Company enters into interest and currency swaps in order to manage its market risk and hedge the currency combination of its income. The Company refers to Note 22 in this relation.

Currency risk

The Company is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the Company's functional currency. The Company's functional currency is the Icelandic króna (ISK). However, the Company derives part of its income in US dollars (USD) (2009: 65%) and a portion of its purchases is made in other currencies than ISK. The main currencies posing a foreign exchange risk are the USD and the Swiss Francs (CHF).

The Company does in general not hedge against foreign exchange risk but reviews on a regular basis the currency combination of its liabilities against the currency combination of its income.

The Company's borrowings in foreign currencies, mainly in USD and CHF, represent a foreign exchange risk, which is partly hedged. Interests on these loans are much lower than on the Company's ISK-denominated loans.

Interest rate risk

The Company's borrowings bear both variable and fixed interest. The majority of the Company's borrowings bear fixed interest, cf. Note 20.

Other market price risk

Other market price risk is limited because investment in bonds and shares is an insubstantial part of the Company's operations.

Capital management

It is the policy of the Company's Board of Directors to maintain a strong equity position in order to ensure stability in its operations' future development. The Company's operating budget envisages that the Company's equity ratio shall be at least 20%.

The Company is not subject to external rules on minimum capital requirements.

6. Revenue

Transmission revenue consists of:

	2009	2008
Energy transmission	11.438.387	8.990.365
Transmission losses and ancillary services	1.701.952	1.659.526
Service income and balancing energy	15.767	21.163
Input fees	77.683	72.760
	13.233.789	10.743.814

7. Other income

Other income consists of:

Income from work sold and rent	60.595	108.897

8. Personnel expenses

Payroll expenses are specified as follows:

Salaries	822.727	813.133
Defined contribution plan payments	95.548	93.857
Defined benefit plan payments	21.058	21.712
Other payroll expenses	75.426	64.365
	1.014.759	993.067

Payroll expenses consist of:

Transmission costs	402.471	442.226
System operation	348.230	314.579
Other operating expenses	264.058	236.262
	1.014.759	993.067

Average number of employees	99	96
Full-time equivalent units at year-end	93	90

Remuneration of the Board of Directors, CEO and two Executive Directors were as follows:

Remuneration of the Board of Directors	5.040	6.240
Remuneration and benefits of the CEO	19.827	19.166
Remuneration of two Excecutive Directors	32.760	32.021

9. Depreciation and amortisation

Depreciation and amortisation are specified as follows:

Depreciation of fixed assets in operation, see Note 12	2.271.781	1.860.562
Amortisation and impairment losses, see Note 12	108.358	39.341
Depreciation and amortisation recognised in the income statement	2.380.139	1.899.903

Depreciation and amortisation are allocated as follows to operating items:

Transmission costs	2.188.541	1.751.480
System operation	70.568	61.248
Other operating expenses	121.030	87.175
Depreciation and amortisation recognised in the income statement	2.380.139	1.899.903

Financial Statements of Landsnet hf 2009 21 Amounts are in ISK thousand

10. Financial income and expenses

Financial income and expenses are specified as follows:

	2009	2008
Interest income	157.093	118.477
Total finance income	157.093	118.477
Interest expenses	(2.107.496)	(2.095.549)
Indexation	(2.599.908)	(4.036.402)
Exchange rate difference	(1.211.693)	(15.408.950)
Changes in fair values of derivatives	(3.017)	1.073.891
Capitalised interest expense due to projects under construction	135.544	184.905
Total financial expenses	(5.786.570)	(20.282.105)
Net financial expenses	(5.629.477)	(20.163.629)

Net financial expenses due to the construction of a transmission infrastructure amounting to ISK 135.5 million is capitalised and has been reported as a reduction in financial expenses.

Capitalised financial expenses were 7.7% of capital tied in transmission structures under construction during the year (2008: 12.2%). This is the Company's average finance cost in the year 2009.

11. Income tax

Income tax recognised in the income statement is specified as follows:

	2009	2008
Calculated income tax for the year	(199.591)	2.248.485
Effect of changed tax rate	340.216	(38.227)
Income tax recognised in the statement of comprehensive income	140.625	2.210.258
Income tax recognised in equity:		
Income tax liability due to revaluation of fixed assets	0	2.659.033
Effect of increased tax rate on income tax liability due to revaluation	424.017	0
	424.017	2.659.033
Change in income tax asset/liability	(283.392)	(448.775)

Change in deferred income tax liability is specified as follows:

	2009	2008
Change in temporary differences	248.195	(97.259)
Change in carry-forward losses	(447.786)	2.345.744
Effect of changed income tax rate	(83.801)	(38.227)
Income tax liability due to revaluation of fixed assets	0	(2.659.033)
Change in deferred tax assets	(283.392)	(448.775)

Reconciliation of effective tax rate

	2009	2009	2008	2008
Profit (loss) before income tax		1.330.610		(14.989.904)
Income tax according to the current tax rate	15,0%	(199.591)	15,0%	2.248.485
Difference due to change in tax rate	(25,6%)	340.216	(0,3%)	(38.227)
Effective tax rate	(10,6%)	140.625	14,7%	2.210.258

Financial Statements of Landsnet hf 2009 22 Amounts are in ISK thousand

12. Property, plant and equipment

Property, plant and equipment are specified as follows:

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
Cost				
Balance at 1.1.2008	16.012.836	28.252.885	2.318.532	46.584.253
Revaluation	3.325.806	16.126.990	0	19.452.796
Additions	664.892	258.444	380.741	1.304.077
Sold and disposed of	0	0	(1.479)	(1.479)
Balance at 31.12.2008 and 1.1.2009	20.003.534	44.638.319	2.697.794	67.339.647
Additions	325.651	173.454	485.018	984.123
Transferred from projects under construction	1.500.466	982.123	0	2.482.589
Sold and disposed of	0	0	(2.014)	(2.014)
Transferred to assets available for sale	0	0	(427.693)	(427.693)
Balance at 31.12.2009	21.829.651	45.793.896	2.753.105	70.376.652
Depreciation and impairment losses				
Balance at 1.1.2008	891.354	1.258.427	198.367	2.348.148
Revaluation	294.988	1.430.918	0	1.725.906
Depreciation and impairment losses	622.514	1.115.426	122.622	1.860.562
Sold and disposed of	0	0	(472)	(472)
Balance at 31.12.2008 and 1.1.2009	1.808.856	3.804.771	320.517	5.934.144
Depreciation and impairment losses	708.528	1.422.169	141.084	2.271.781
Sold and disposed of	0	0	(634)	(634)
Balance 31.12.2009	2.517.384	5.226.940	460.967	8.205.291

Fixed assets in operation:

Carrying amount	Substations	Transmission lines	Other	Total
1.1.2008	15.121.482	26.994.458	2.120.165	44.236.105
31.12.2008 and 1.1.2009	18.194.678	40.833.548	2.377.277	61.405.502
31.12.2009	19.312.267	40.566.956	2.292.138	62.171.360

Basis of revaluation of fixed assets in operation

In accordance with the International Accounting Standard IAS 16, the Company's lines and substations are recognised according to the revaluation method. A revaluation was conducted on those assets in the year 2008. The revaluation was based on two methods. First, it was based on the estimated reconstruction cost of the transmission system, which was calculated by independent experts at the beginning of year and projected to year-end 2008. Second, the operating value was measured using a cash flow analysis. The valuation period was from 2009 to 2013, with the future operating value calculated thereafter. The year's revaluation was based on the operating value, the main premises of which were the Company's operating budgets for the years 2009-2013, a 30% equity ratio and that Landsnet's tariff for transmission to distributors would reflect price developments in Iceland while the tariff for industrial users would reflect price level changes in the United States. The estimation of weighted-average cost of capital (WACC) was based on comparable companies abroad. It is the opinion of the Company's management that nothing gives reason for a revaluation in the year 2009.

Had the Company not revalued lines and substations in the year 2008, the carrying amount of the same assets would have been approximately ISK 16.7 billion lower at year end 2009.

Financial Statements of Landsnet hf 2009 23 Amounts are in ISK thousand

12. Property, plant and equipment, contd.:

Assets available for sale

The Company has put its real estate at Bústaðavegur up for sale, which among other things previously housed the Company's Control Centre. A purchase offer has been approved, including certain conditions, which have not yet been lifted.

Rateable value and insurance value

The rateable value of the Company's real property amounts to upwards of ISK 3.5 billion. Assessed value for the same property's fire insurance amounts to ISK 6.1 billion. The insurance value of the Company's assets amounts to ISK 33.7 billion, excluding transmission lines and cables, which are insured by an emergency insurance fund. The Company's emergency insurance amounts to ISK 82.4 billion.

Intangible assets and projects under construction:	**Projects under construction**	**Intangible assets**
Cost		
Balance at 1.1.2008	1.506.006	577.535
Additions	275.605	1.204.552
Balance at 31.12.2008 and 1.1.2009	1.781.611	1.782.087
Additions	1.718.812	465.216
Transferred from intangible assets/projects under construction	(1.888.266)	(594.323)
Balance at 31.12.2009	1.612.156	1.652.980
Amortisation and impairment losses		
Balance at 1.1.2008	0	25.932
Write-downs and impairment losses in the year	0	39.341
Balance at 31.12.2008 and 1.1.2009	0	65.273
Depreciation and impairment losses	0	108.358
Balance at 31.12.2009	0	173.631
Carrying amount		
1.1.2008	1.506.006	551.603
31.12.2008 and 1.1.2009	1.781.611	1.716.814
31.12.2009	1.612.157	1.479.350

The carrying amount of intangible assets at year-end 2009 is divided into software in the amount of ISK 247 million (2008:235 million) and capitalised development cost amounting to ISK 1,232 million (2008:1,482 million).

Amortisation and impairment losses for 2009 are divided into the amortisation of software amounting to ISK 44.1 million and impairment loss on development cost amounting to ISK 64.3 million.

Financial Statements of Landsnet hf 2009 24 Amounts are in ISK thousand

13. Investment in other companies

The breakdown of investment in other companies is as follows:

	31.12.2009 Share	31.12.2009 Carrying amount	31.12.2008 Share	31.12.2008 Carrying amount
Landsnet ehf	100,00%	500	100,00%	500
Netorka ehf	37,18%	50.058	37,18%	48.332
Total investment in other companies		50.558		48.832

The Company's share in Landsnet ehf is stated at cost as the firm has not conducted any operations from its establishment. At the time of preparing Landsnet hf's financial statements, the financial statements of Netorka ehf were not available. However, the estimated share in Netorka's profit amounts to ISK 9 million for the year 2009 (2008: ISK 7 million). During the year 2009, the share capital of Netorka was decreased and paid to shareholders. Landsnet's share in the decrease amounted to ISK 7 million.

14. Deferred tax assets/tax liability

In December 2009, the Icelandic parliament decided to increase the income tax rate from 15% to 18% as of 1 January 2010. The change enters into effect for the tax assessment in the year 2011. The effect thereof has been recognised in the financial statements for 2009, with the increase in income tax liability amounting to ISK 84 million.

The breakdown of deferred tax liability is as follows:	31.12.2009	31.12.2008
Deferred tax assets/tax liability at 1 January	(219.412)	229.363
Calculated income tax for the year	140.625	2.210.258
Effect of changed tax rate on previous revaluation on transmission	(424.018)	(2.659.033)
Deferred tax liability at 31 December	(502.804)	(219.412)

The breakdown of deferred tax liability was as follows at year-end:

	31.12.2009	31.12.2008
Property, plant and equipment	(3.000.473)	(2.606.646)
Development cost	(90.473)	(57.206)
Investment in other companies	(1.979)	(275)
Other obligations	123.959	(38.233)
Tax losses carried forward	2.466.162	2.482.948
Deferred tax liability at 31 December	(502.804)	(219.412)

The carry-forward taxable loss amounted to ISK 13.7 billion. The loss is utilisable against taxable income over ten years from when the loss is incurred. The management believes that the Company's operation over the next ten years will generate taxable income and that the accumulated carry-forward taxable loss will be fully utilised. Carry-forward taxable loss at year-end 2009 will be utilisable as follows:

	31.12.2009	31.12.2008
Loss for the year 2006, applicable until year 2016	0	4.731
Loss for the year 2007, applicable until year 2017	0	909.954
Loss for the year 2008, applicable until year 2018	13.700.902	15.638.302
Total unadjusted taxable loss	13.700.902	16.552.987

15. Inventories

Inventories are specified as follows:	31.12.2009	31.12.2008
Spare parts and material inventories	483.285	480.439
	483.285	480.439

No write-down due to the Company's inventories is recognised in the financial statements.

Financial Statements of Landsnet hf 2009 25 Amounts are in ISK thousand

16. Trade and other receivables

Trade and other receivables:

	31.12.2009	31.12.2008
Nominal value of trade receivables	815.472	833.572
Other receivables	184.387	19.449
	999.859	853.021

17. Cash

Cash is specified as follows:

Bank balances	5.863.874	2.700.681

18. Equity

Share capital

The Company's total share capital according to its Articles of Association was ISK 5,903 million at year-end. The Company holds no treasury shares. Each share of ISK in the Company carries one vote. All share capital has been paid.

Revaluation account

The Company's revaluation account consists of the revaluation increase of the Company's fixed assets after income tax effects. Depreciation of the revalued price is entered in the income statement and transferred from the revaluation account to unadjusted loss.

Dividends

The Company paid no dividends in 2009 for the financial year 2008, nor in the year 2008 for the financial year 2007. No motion has been made regarding dividends to shareholders in the year 2010 for the financial year 2009.

19. Earnings (loss) per share

	2009	2008
Basic and diluted earnings (loss) per share:		
Profit (loss) to shareholders	1.471.235	(12.779.646)
Weighted average number of ordinary shares		
Shares at 1 January	5.902.733	5.902.733
Weighted average number of ordinary shares at 31 December	5.902.733	5.902.733
Basic and diluted earnings (loss) per share	0,25	(2,17)

20. Loans and borrowings

This Note provides information on the contractual terms of the Company's interest-bearing loans and borrowings, which are measured at amortised cost.

Long-term liabilities

Indexed bond loan from parent company in ISK, fixed interest of 4.21%	37.813.190	34.808.942
Loan agreement with parent company in USD, LIBOR + margin	9.367.500	0
Loan agreement in CHF, LIBOR + margin	7.107.049	6.676.851
Indexed bond loan in ISK, fixed interest of 5%	5.006.879	0
	59.294.618	41.485.793
Current maturities on long-term liabilities	(110.446)	0
	59.184.172	41.485.793

Financial Statements of Landsnet hf 2009 26 Amounts are in ISK thousand

20. Loans and borrowings, contd.:

Long-term liabilities, contd.:

The bond from the parent company is an inflation-indexed bullet bond maturing in 2020 with interest payable once per year. Indexed bond loans from third parties consist of a 15-year superannuation loan. The loan agreement with the parent company is denominated in USD with a three-year maturity; the revolving credit facility amounts to USD 100 million, of which USD 75 million have been drawn. The facility decreased to USD 85 million at year-end 2010.

	2009	2008
Short-term liabilities		
Short-term loan from parent company	1.241.102	15.813.603
Current maturities on long-term liabilities	110.446	0
Total interest-bearing short-term liabilities	1.351.548	15.813.603
Total interest-bearing liabilities	60.535.720	57.299.396

Terms of interest-bearing loans and borrowings

Debts in foreign currencies:

		31.12.2009		31.12.2008	
	Final maturity	Interest rate	Carrying amount	Interest rate	Carrying amount
Debt in CHF	2022	0,65%	7.107.049	3,10%	6.676.851
Debt in CHF	2008-2009		0	4,50%	3.556.943
Debt in JPY	2008-2009		0	2,70%	2.018.412
Debt in USD	2012	3,77%	9.367.500	4.0-5.7%	9.098.448
			16.474.549		21.350.654

Debt in ISK:				
Indexed	4.21 - 5%	2020 - 2034	44.061.171	35.948.742
Total interest-bearing loans and borrowings			60.535.720	57.299.396

Maturities by year of interest-bearing loans and borrowings:	31.12.2009	31.12.2008
Year 2010	110.446	0
Year 2011	740.538	0
Year 2012	9.220.265	333.843
Year 2013	838.789	667.685
Year 2014	845.273	667.685
Later	47.539.307	39.816.580
	59.294.618	41.485.793

21. Provision due to site restoration

Change in the provision due to site restoration is specified as follows:

Balance at 1.1.	475.722	447.154
Present value for the year reversed	61.482	28.568
Increase in provision	45.200	0
Balance at year-end	582.404	475.723

Financial Statements of Landsnet hf 2009 27 Amounts are in ISK thousand

21. Provision due to site restoration, contd.:

Change in provision due to site restoration is specified af follows, contd.:

Under IAS 16, the initial value of property, plant and equipment shall include their estimated cost of demolition after use. The estimated cost of demolition of lines has been assessed and then discounted based on assessed useful life. In return, an obligation has been written up under long-term liabilities. An increase in the obligation due to the discounting in addition to depreciation of demolition cost is expensed in the income statement.

22. Derivative financial instruments

The Company had entered into a derivative agreement with Kaupthing Bank hf, which was taken over by the Icelandic government in October 2008. According to point 1 of the Ruling of the Financial Supervisory Authority on the allocation of the assets and liabilities of Kaupthing Bank hf to New Kaupthing Bank hf (now Arion Bank hf) dated 21 October 2008, obligations and rights according to the derivative agreement were not transferred to the new bank. Kaupthing Bank hf, which is in receivership, therefore remained the counterparty to the agreement. The agreement had a five-year term and provided for the exchange of inflation-indexed Icelandic krónas and US dollars at the end of term in addition to interest accrued during the contractual term. Kaupþing Bank hf was to pay indexed ISK and Landsnet to pay USD. The agreement's term was from the end of November 2007 to March 2013. As stated in annual and interim financial statements, the Company has reviewed its legal position, including its payment obligation, under the agreement. The Company rescinded the agreement on 10 December 2009. Kaupthing Bank hf has objected to the rescission and may challenge its validity in court. In this relation, the Company is of the opinion that the balance of the derivative agreement must be stated in the financial statements until a final conclusion on the rescission has been reached.

23. Pension fund obligation

The Pension Fund for State Employees calculates at the end of each year the benefit plan obligation accrued for the year. Actuary assessment is based on the accrued obligation for the year being discounted at year-end on the basis of the annual interest rate generally used to assess pension fund obligations. The present annual rate is 3.5%. A total of ISK 18 million is expensed in relation thereto for 2009.

24. Trade and other payables

Trade and other payables are specified as follows:	**2009**	**2008**
Trade payables	746.092	941.144
Other payables	217.560	181.440
Trade and other payables total	963.652	1.122.584

25. Financial instruments

Credit risk

Highest possible loss due to credit risk

The Company's highest possible loss due to financial assets is their book value, which was as follows at year-end:

Receivables from related companies	587.604	396.605
Trade and other receivables	999.859	853.021
Cash and cash equivalents	5.863.874	2.700.681
	7.451.337	3.950.307

Financial Statements of Landsnet hf 2009 28 Amounts are in ISK thousand

25. Financial instruments, contd.:
Credit risk, contd.

Highest possible loss due to credit risk, contd.

The Company's most important customers are domestic energy companies. At year-end, receivebles from those companies amounted to ISK 1,523 million, including from Landsvirkjun, the parent company of Landsnet, in the amount of ISK 841 million.

No impairment loss has been recognised in relation to accounts receivable at year-end; nor has loss on receivables been expensed during the year, which is based on the management's experience.

Liquidity risk

The following are the contractual maturities of financial liabilities, including future interest payments:

31 December 2009

	Carrying amount	Contractual cash flow	Within 12 months	1-2 years	2-5 years	After 5 years
Non-derivative financial liabilities:						
Payable to related companies	47.180.690	65.747.113	1.937.528	1.947.393	14.497.390	47.364.802
Long-term liabilities	12.113.928	16.439.853	422.238	412.255	3.002.369	12.602.991
Trade and other payables	963.652	963.652	963.652	0	0	0
	60.258.270	83.150.618	3.323.418	2.359.648	17.499.759	59.967.793

31 December 2008

	Carrying amount	Contractual cash flow	Within 12 months	1-2 years	2-5 years	After 5 years
Non-derivative financial liabilities:						
Payable to related companies	50.622.545	69.880.509	17.323.450	3.019.694	4.529.541	45.007.824
Long-term liabilities	6.676.851	9.503.651	155.119	94.052	1.028.167	8.226.312
Trade and other payables	1.122.585	1.122.585	1.122.585	0	0	0
	58.421.981	80.506.745	18.601.154	3.113.746	5.557.708	53.234.136
Derivative financial liabilities:						
Foreign currency and interest rate swaps:	2.991.625	2.779.109	(159.359)	(483.426)	3.421.894	0
	2.991.625	2.779.109	(159.359)	(483.426)	3.421.894	0

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25. Financial instruments, contd.:

Currency risk

The Company's exposure to foreign currency risk, based on nominal amounts, was as follows:

	EUR	CHF	USD
31 December 2009			
Trade and other receivables			1.259.939
Loans from related companies			(9.367.500)
Other long-term liabilities		(7.107.049)	
Trade and other payables	(10.161)		
Net currency risk	(10.161)	(7.107.049)	(8.107.561)

In 2009, 65% of the Company's total revenue was in USD while purchases were mainly in ISK and EUR. In 2010, it is estimated that 61% of the Company's total revenue will be in USD.

	EUR	CHF	USD
31 December 2008			
Trade and other receivables			675.784
Loans from related companies		(3.556.943)	(9.098.448)
Other long-term liabilities		(6.676.851)	
Derivatives			(9.764.725)
Trade and other payables	(26.016)	(157.187)	(4.330)
Net currency risk	(26.016)	(10.390.981)	(18.191.719)

	Av. exch. rate for the year		Year-end exch. rate	
	2009	2008	2009	2008
Currency risk				
EUR	172,67	127,46	179,88	169,97
CHF	114,32	80,69	121,26	113,92
USD	123,59	88,07	124,90	120,87

Sensitivity analysis

A 10% strengthening of the ISK against the following currencies at 31 December would have increased (decreased) after-tax profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2008.

	2009	2008
EUR	833	2.211
CHF	582.778	883.233
JPY	0	171.565
USD	664.820	1.499.595

A 10% weakening of the ISK against the above currencies at 31 December would have had the equal but opposite effect on profit or loss after tax to the amounts shown above, given that all other variables remain constant.

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25. Financial instruments, contd.:

Interest rate risk

The breakdown of the Company's interest-bearing financial instruments at year-end was as follows:

	Carrying amount	
	31.12.2009	**31.12.2008**
Financial instruments with floating interest rate		
Financial liabilities	16.474.549	18.396.457
Derivative financial instruments*	0	2.991.625
	16.474.549	21.388.082
Financial instruments with fixed interest rate		
Financial liabilities	44.061.241	36.016.075

* As the Company has terminated its derivative agreement, it is not included in the sensitivity analysis since uncertainty prevails over its settlement.

Cash-flow sensitivity analysis for fixed-interest-rate instruments

The Company's liabilities carrying fixed interest rates are, on the one hand, an indexed bullet bond repayable in a single payment in 2020 to its parent company and, on the other, a 25-year superannuation bond loan. These liabilities are not recognised at fair value. Therefore, interest changes on the settlement date should not affect the Company's income statement.

Cash-flow sensitivity analysis for floating interest rate instruments

An increase in interest rates of 100 basis points at the reporting date would have increased (decreased) equity and profit or loss after tax by the amounts stated below. If interest rates had decreased by 100 basis points, the effect would have had the equal but opposite effect on profit or loss after tax. This analysis assumes that all other variables, in particular the exchange rates, remain constant. The analysis was performed in the same manner for the year 2008.

	Earnings	
	100bp increase	**100bp decrease**
31 December 2009		
Financial instruments with floating interest rates	(19.419)	12.783
Cash flow sensitivy (net)	(19.419)	12.783
31 December 2008		
Financial instruments with floating interest rates	(110.815)	110.815
Cash flow sensitivy (net)	(110.815)	110.815

Fair value

Fair value versus carrying amounts

The fair values and carrying amounts of financial assets and liabilities as reported in the balance sheet are specified as follows:

	31.12.2009		31.12.2008	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Loans and receivables	1.587.463	1.587.463	1.249.626	1.249.626
Cash and cash equivalents	5.863.874	5.863.874	2.700.681	2.700.681
Loans from related companies, long-term	47.180.690	50.352.953	34.808.942	35.555.121
Derivatives, debt	2.769.177	2.769.177	2.991.625	2.991.625
Other long-term liabilities	12.003.482	12.966.931	6.676.851	6.676.851
Loans from related companies, short-term	1.241.102	1.241.102	15.813.603	15.813.603
Trade and other payables	963.652	963.652	1.122.585	1.122.585
	71.609.440	75.745.152	65.363.913	66.110.092

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25. Financial instruments, contd.:

Classification and fair value of financial assets and liabilities

The following table shows the Company's classification of financial assets and liabilities and their fair value (before accrued interest).

	Financial assets and liabilities designated at fair value	Financial assets available for sale	Loans and receivables	Carrying amount
31 December 2009				
Investment in subsidiary	500	500		500
Receivables from related companies			587.604	587.604
Trade and other short-term receivables			999.859	999.859
Cash and cash equivalents			5.863.874	5.863.874
	500	500	7.451.337	7.451.837
Payables to related companies			47.180.690	47.180.690
Other long-term liabilities			12.003.482	12.003.482
Derivatives			2.769.177	2.769.177
Trade and other short-term payables			963.652	963.652
	0	0	62.917.001	62.917.001
31 December 2008				
Investment in subsidiary		500		500
Receivables from related companies			396.605	396.605
Trade and other short-term receivables			853.021	853.021
Cash and cash equivalents			2.700.681	2.700.681
	0	500	3.950.307	3.950.807
Payables to related companies			50.622.545	50.622.545
Other long-term debts			6.676.851	6.676.851
Derivatives	2.991.625			2.991.625
Trade and other short-term payables			1.122.584	1.122.584
	2.991.625	0	58.421.980	61.413.605

26. Operating leases

The Company as lessee

The Company leases a part of the transmission structures it uses from domestic energy companies. The lease agreements have an indeterminate lease term and the lease price is determined by the National Energy Authority.

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27. Other information

In accordance with the provisions of Article 12 of the Electricity Act No. 65/2003, the Company shall take into account if the connecting of new power stations or industries to the transmission system increases cost for other users of the system, and if the connection leads to more profitable construction or utilisation of the transmission system. At year-end 2007, the Company brought into use the Fljótdalur lines 3 and 4 in addition to the associated substations. Settlement has not been made to the relevant industries, but the Company will probably be required to pay the relevant party a system contribution where the transmission infrastructure in question will lead to the transmission system's more cost-effective development and utilisation. At year-end, information on the exact amount was not available, but the estimated amount for 2009 has been entered in the financial statements.

Under the Electricity Act, the revenue for Landsnet is set for a three year term at a time. The National Energy Authority sets the cap as well as regulating the Company. At year-end 2006, the National Energy Authority established Landsnet's revenue cap for the years 2007 to 2009 based on operating and administrative expenses in 2005 and 2005. The revenue cap for 2010–2012 has not yet been established by the National Energy Authority, but will be based on the operating return in 2007 and 2008. The revenue cap for 2006–2009 has not yet been accounted for.

28. Related parties

Definition of related parties

The Company has a related-party relationship with its parent company, subsidiary, associates, directors, excecutive officers and companies in their possession.

Transactions with senior management

(i) Payments to senior management

In addition to receiving salaries, the Chief Executive Officer and Managing Directors (Vice Presidents) of the Company enjoy various benefits and a contribution to a defined benefit pension fund. Management's salaries are accounted for in Note 8.

Other transactions with related parties

	2009	2008
Sale of goods and services:		
Landsnet's parent company and its subsidiaries	7.762.212	6.165.357
Cost:		
Landsnet's parent company and its subsidiaries	1.733.741	1.819.634
Landsnet's associate	1.285	977

29. Financial ratios

The company's key financial ratios:

	2009	2008
Financial performance:		
EBITDA	9.331.062	7.066.391

	31.12.2009	31.12.2008
Financial position:		
Current ratio – current assets/current liabilities	3,61	0,26
Equity ratio – equity/total assets	11,3%	10,5%
Return on equity	20,2%	(107,7%)

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