Landsvirkjun

Group

Consolidated Financial Statements 2018

Landsvirkjun
Háaleitisbraut 68
103 Reykjavík
Iceland

Id.no. 420269-1299

Contents

Key figures - Unaudited

Management's presentation of the operation of Landsvirkjun

	2018	2017	2016	2015	2014
Operation					
Operating revenues	538,455	491,175	415,480	410,496	428,655
Realised aluminium hedges	(4,534)	(8,098)	4,890	10,956	9,629
Total operating revenues	533,921	483,077	420,370	421,452	438,284
Operating expenses	(144,041)	(137,503)	(118,630)	(99,932)	(106,126)
EBITDA	389,880	345,574	301,740	321,520	332,158
Depreciation and impairment loss	(125,448)	(127,086)	(118,571)	(115,554)	(114,045)
EBIT	264,432	218,488	183,169	205,966	218,113
Financial items	(80,178)	(64,844)	(60,045)	(73,418)	(69,838)
Associated companies	(179)	(228)	(5,448)	(1,921)	(1,419)
Profit before unrealised financial items	184,075	153,416	117,676	130,627	146,856
Unrealised financial items:					
Fair value changes in embedded derivatives	(49,410)	84,494	21,164	(59,925)	(88,484)
Fair value changes in other derivatives	24,878	(12,990)	(1,269)	5,466	(8,426)
Unrealised foreign exchange difference	21,014	(60,745)	(23,314)	47,657	60,271
	(3,518)	10,759	(3,419)	(6,802)	(36,639)
Profit before income tax	180,557	164,175	114,257	123,825	110,217
Income tax	(59,528)	(56,211)	(47,437)	(39,652)	(31,797)
Net Profit	121,029	107,964	66,820	84,173	78,420
Balance sheet					
Total assets	4,451,081	4,506,392	4,332,864	4,284,703	4,270,098
Equity	2,163,056	2,063,112	1,969,088	1,916,634	1,704,724
Liabilities	2,288,025	2,443,280	2,363,776	2,368,069	2,565,374
Net debt *	1,884,603	2,042,642	1,960,497	1,985,411	2,190,459
Cash flow					
Funds from operations (FFO)	316,336	282,774	235,602	240,354	258,226
Cash flow from operating activities	295,761	277,937	229,827	248,955	233,816
Investing activities	(150,864)	(253,740)	(172,277)	(77,486)	(88,271)
Financing activities	(151,876)	(45,282)	(59,305)	(235,465)	(220,687)
Liquidity					
Cash and cash equivalents at year end	116,278	126,544	144,534	142,127	207,070
Undrawn loans	353,155	421,363	472,448	360,824	200,000
Total liquidity	469,433	547,907	616,982	502,951	407,070
Key ratios					
Return on equity	5.9%	5.5%	3.5%	4.9%	4.7%
Equity ratio	48.6%	45.8%	45.4%	44.7%	39.9%
Interest cover (EBITDA/net interest expenses)	4.76x	5.53x	5.15x	4.60x	3.76x
FFO / net liabilities	16.8%	13.8%	12.0%	12.1%	11.8%
FFO / interest expenses	3.72x	4.35x	3.80x	3.27x	2.82x
Net debt / EBITDA	4.83x	5.91x	6.50x	6.18x	6.59x
Credit rating at year end without state guarantee					
Standard & Poor's	BBB	BBB	BBB-	BB+	BB
Moody's	Baa2	Baa3	Baa3	Ba1	Ba2

* Net debt are interest bearing long-term liabilities less cash and cash equivalents

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Quarterly statement 2018 - Unaudited

Management´s presentation of the operation of Landsvirkjun, contd.

	Q1	Q2	Q3	Q4	Total
Operating revenues					
Power sales	117,730	108,781	107,283	109,774	443,568
Realised aluminium hedges	(1,648)	(2,754)	(581)	449	(4,534)
Transmission	22,326	21,622	21,409	22,030	87,387
Other income	2,754	733	1,162	2,851	7,500
	141,162	128,382	129,273	135,104	533,921
Operating expenses					
Energy production costs	12,514	13,345	13,103	12,896	51,858
Transmission costs	9,866	8,821	10,914	9,843	39,444
Cost of general research	2,210	2,576	2,364	3,163	10,313
Other operating expenses	11,303	11,154	8,955	11,014	42,426
Depreciation and impairment loss	30,623	31,216	31,275	32,334	125,448
	66,516	67,112	66,611	69,250	269,489
Operating profit	74,646	61,270	62,662	65,854	264,432
Financial income and (expenses)					
Interest income	859	803	600	718	2,980
Interest expenses	(18,773)	(30,629)	(16,587)	(18,966)	(84,955)
Realised foreign exchange difference	115	(701)	(482)	2,865	1,797
	(17,799)	(30,527)	(16,469)	(15,383)	(80,178)
Associated companies	(921)	55	527	160	(179)
Profit before income tax and unrealised items	55,926	30,798	46,720	50,631	184,075
Unrealised financial items:					
Fair value changes in embedded derivatives	(39,556)	10,423	(3,629)	(16,648)	(49,410)
Fair value changes in other derivatives	16,879	(2,833)	3,527	7,305	24,878
Unrealised foreign exchange difference	(18,856)	28,893	4,586	6,391	21,014
	(41,533)	36,483	4,484	(2,952)	(3,518)
Profit before income tax	14,393	67,281	51,204	47,679	180,557
Income tax	(5,328)	(21,839)	(16,434)	(15,927)	(59,528)
Net Profit	9,065	45,442	34,770	31,752	121,029
Attributable to:					
Owners of the parent company	7,650	41,132	31,147	28,003	107,932
Subsidiaries minority interest	1,415	4,310	3,623	3,749	13,097
	9,065	45,442	34,770	31,752	121,029
From cash flow					
Cash flow from operating activities	81,142	68,097	73,454	73,068	295,761

Other key metrics for Landsvirkjun parent company	**2018**	**2017**	**2016**	**2015**	**2014**
Installed capacity at year end (MW)	2,145	2,000	1,957	1,957	1,957
Average price for industrial users* USD/MWh	28.3	26.6	23.9	24.5	25.9
Average price for retail sales comp.(excl. transm.) ISK/kWh	4.7	4.5	4.6	4.4	4.3
Sales in GWh	14,753	14,325	13,625	13,900	13,082
Research and development	14,824	20,004	16,829	19,529	30,606
Accident frequency: H200**	0.6	0.0	0.3	0.4	0.4

* Transmission is included in some power agreements

** H200 is the number of absence accidents per each 200,000 working hours

Consolidated Financial Statements of Landsvikjun 2018 4 Amounts are in USD thousand

Endorsement by the Board of Directors and CEO

Landsvirkjun’s objective is to operate in the energy sector and to engage in other business and financial operations according to the decision of the Board of Directors at each time. The Company’s consolidated financial statements include, in addition to the parent company, four subsidiaries, Landsnet hf., Orkufjarskipti hf., Icelandic Power Insurance Ltd. and Landsvirkjun Power ehf.

The financial statements of Landsvirkjun for the year 2018 are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and additional requirements in the Icelandic Financial Statement Act. The functional currency of the Company is US Dollar (USD) and amounts in the financial statements are rounded to the nearest thousand USD.

The Group’s operating revenues amounted to USD 533.9 million in the year 2018 compared to USD 483.1 million in the previous year. Thus, revenues increased by USD 50.8 million. Operating expenses amounted to USD 269.5 million in the year 2018 compared to USD 264.6 million in the year 2017. Thus, the Company's operating profit amounted to USD 264.4 million in the year 2018 compared to USD 218.5 million in the previous year.

Landsvirkjun has entered into derivative contracts in order to manage risk. Contracts have been made in order to hedge interest rate risk and foreign exchange risk. In addition, derivative contracts have been made in order to hedge risk due to fluctuations of aluminium prices in the global market as a part of revenues is linked to aluminium prices.

Financial expenses in excess of financial income amounted to USD 83.7 million in the year 2018, compared to USD 54.1 million the previous year. The change between years amounts to USD 29.6 million. The reason for this increase between years are higher interest expenses during the year 2018 due to transaction costs in relation to prepayments of loans which amounted to USD 10.5 million. The changes are also due to currency exchange differences and fair value changes in derivatives which are mostly unrealised and must be kept in mind when evaluating the Company's annual results. Profit before unrealised financial items amounted to USD 184.1 million during the year compared to USD 153.4 million in the year 2017. According to the income statement, profit for the year amounted to USD 121.0 million compared to USD 108.0 million in the previous year.

Equity at year end 2018 amounted to USD 2,163.1 million compared to USD 2,063.1 million at year end 2017 according to the balance sheet. The Company’s Board of Directors proposes that the profit for the year will be recognised as an increase in equity. The Company’s Board of Directors will during the Annual General Meeting propose a dividend payment to the owners of the Company but otherwise refers to the notes to the financial statements and statement of equity for further changes in equity. Landsvirkjun is a partnership owned by the State and Eignarhlutir ehf. The State owns 99.9% in the Company and Eignarhlutir ehf. 0.1%.

Cash and cash equivalents at year end amounted to USD 116.3 million and undrawn Revolving Credit and Loan Facilities amounted to USD 353.2 million. Cash and cash equivalents and undrawn Revolving Credit and Loan Facilities therefore amounted to USD 469.4 million at year end. Cash flow from operations amounted to USD 295.8 million. Landsvirkjun borrowed USD 267.2 million in the year and repaid debt amounting to USD 405.1 million. Cash and cash equivalents decreased by USD 10.3 million during the year.

Endorsement by the Board of Directors and CEO, contd.

Corporate Governance

The Board of Directors of Landsvirkjun endeavours to maintain good corporate governance taking into consideration the Guidelines on Corporate Governance issued by the Iceland Chamber of Commerce in collaboration with the Confederation of Icelandic Employers and Nasdaq OMX Iceland. The Board of Directors has laid down comprehensive guidelines wherein the competences of the Board is defined and its scope of work vis-à-vis the CEO. The Board of Directors has appointed an Audit Committee. In the year 2018, 15 Board meetings were held and 5 meetings in the Audit Committee. Meetings have been attended by the majority of the Board of Directors and the majority of the Audit Committee. According to the Financial Statements Act public interest entities shall provide information necessary for an understanding of the entity's development, performance, position and impact of its activity relating to environmental, social and employee matters, policy regarding human rights, how the entity counteracts corruption and bribery matters, and a brief description of the entity's business model etc. Information on the Company's policy and successes in these matters is provided in an appendix to the financial statements. Further information on the Parent Company’s corporate governance and risk management is included in notes 29 to 40 and appendix to the financial statements. Landsnet hf. has disclosed information on corporate governance and non-financial information in an appendix to its financial statements.

Statement by the Board of Directors and the CEO

According to the best knowledge of the Board of Directors and the CEO, the consolidated financial statements are in accordance with International Financial Reporting Standards as adopted by the EU and additional requirements in the Icelandic Financial Statement Act and it is the opinion of the Board of Directors and the CEO that the financial statements give a fair view of the Groups’s assets, liabilities and financial position as at 31 December 2018 and the Group’s results and changes in cash in the year 2018.

Furthermore, it is the opinion of the Board of Directors and the CEO that the financial statements and the Endorsement by the Board of Directors for the year 2018 give a fair view of the Group’s results, financial position and development and describe the main risk factors faced by the Group.

The Board of Directors and the CEO hereby confirm these consolidated financial statements with their signature.

Reykjavik, 28 February 2019.

The Board of Directors:

Jónas Þór Guðmundsson

Álfheiður Ingadóttir

Guðfinna Jóhanna Guðmundsdóttir

Gunnar Tryggvason

Jón Björn Hákonarson

The CEO:

Hörður Arnarson

Independent Auditors' Report

To the Board of Directors and owners of Landsvirkjun

Opinion

We have audited the consolidated financial statements of Landsvirkjun for the year ended December 31, 2018 which comprise the consolidated statement of comprehensive income, the consolidated statement of financial position, the consolidated statement of changes in equity, the consolidated statement of cash flow for the year then ended and the notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of Landsvirkjun as at December 31, 2018, and its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and additional requirements in the Icelandic Financial Statement Act.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the consolidated Financial Statements section of our report. We are independent of Landsvirkjun in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) and the Icelandic Institute of State Authorized Public Accountants, Code of Ethics (FLE Code) and we have fulfilled our ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key Audit Matters	How the matter was addressed in the audit
Power sales	
More than 70% of Landsvirkjun power sales comes from sales to industry. The revenue is based on delivered power and contractual prices that are based on certain parameters. Due to both the magnitude and variability of prices, we believe that power sales to industry are a key audit matter.	During our audit of power sales to industry we have confirmed that there is an effective internal control at Landsvirkjun regarding calculation and approval of invoices. We have also confirmed calculation of sales prices by comparing the calculation to contractual agreement and public information in addition to comparing delivered power to metering.
Valuation of power stations	
Included in property, plant and equipment are power stations which amount to 3,266 million USD at year-end. Power stations are measured at cost less accumulated depreciation and impairment. We consider the valuation of power stations to be a key audit matter due to their magnitude and management estimation of their expected useful life. As to the valuation of the assets, we refer to fixed assets in note 9 and accounting policies note 52.	We reviewed the impairment test of power stations prepared by management. During our audit we examined the valuation methodology and its consistency with prior year. We also examined management assumption for the valuation. This included: • Reviewing the operating plan which is the basis for the valuation. • Reviewing the assumptions for the weighted average cost of capital (WACC) used. We assessed if the valuation's calculations were in accordance with IFRS and assessed that the disclosures were appropriate.

Independent Auditors' Report, contd.

Valuation of transmission network	
The transmission network of Landsnet, subsidiary of Landsvirkjun, is recognised according to the revaluation method. At year-end its carrying amount was USD 688 million. Transmission network valuation is based on management estimations therefore we consider it to be a key audit matter. Revaluation is performed on a regular basis and it is measured using a cash flow analysis. The assets were revaluated at year-end 2015 and it is management estimate that there is no basis for revaluation at year-end 2018. As to the valuation of the assets, we refer to fixed assets in note 9 and accounting policies note 52.	Our audit was focused on management estimations of operating value of transmission lines and substations at the year-end 2018. We examined the valuation methodology and its consistency with prior year. We also examined management assumption for the valuation. This included: • Reviewing the operating plan which is the basis for the valuation. • Reviewing the assumptions for the weighted average cost of capital (WACC) used. We assessed if the valuation's calculations and disclosures were in accordance with IFRS. We have also examined management assumption related to depreciation methods in accordance with IFRS.

Other information

The Board of Directors and the CEO are responsible for the other information. The other information comprises key figures, the endorsement by the board of directors and CEO, statement of corporate governance and non-financial reporting.

Our opinion on the financial statements does not cover the other information and we do not express any form of assurance conclusion thereon, except the confirmation regarding report of the board of directors as stated below.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact. We have nothing to report in this regard.

In accordance with Paragraph 2 article 104 of the Icelandic Financial Statement Act no. 3/2006, we confirm to the best of our knowledge that the accompanying report of the board of directors includes all information required by the Icelandic Financial Statement Act that is not disclosed elsewhere in the financial statements.

Responsibilities of the Board of Directors and CEO for the Consolidated Financial Statements

The Board of Directors and the CEO are responsible for the preparation and fair presentation of the consolidated financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the EU and additional requirements in the Icelandic Financial Statement Act, and for such internal control as the Board of Directors and the CEO determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, the Board of Directors and the CEO are responsible for assessing Landsvirkjun's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Board of Directors and the CEO either intends to liquidate the company or to cease operations, or has no realistic alternative but to do so.

Independent Auditors' Report, contd.

Auditors' Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgement and maintain professional scepticism throughout the audit. We also:

• Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

• Obtain an understanding of internal control relevant to the audit 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 Landsvirkjun's internal control.

• Evaluate the appropriateness of accounting policies used and related disclosures, and the reasonableness of accounting estimates made by management.

• Conclude on the appropriateness of management's use of the going concern basis of accounting and whether a material uncertainty exists related to events or conditions that may cast significant doubt on ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements. If such disclosures are inadequate we are required to modify our unqualified opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause Landsvirkjun to cease to continue as a going concern.

• Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

• Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated and separate financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Board of Directors and the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Board of Directors and the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

Independent Auditors' Report, contd.

From the matters communicated with the Board of Directors and the Audit Committee, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Reykjavik, 28 February 2019.

Deloitte ehf.

Þorsteinn Pétur Guðjónsson
Auditor

Pétur Hansson
Auditor

Income Statement

	Notes	2018	2017
Operating revenues			
Power sales	4	443,568	401,514
Realised aluminium hedges		(4,534)	(8,098)
Transmission	4	87,387	81,026
Other income		7,500	8,635
		533,921	483,077
Operating expenses			
Energy production costs		145,486	141,539
Transmission costs		67,929	58,286
Cost of general research		10,313	21,378
Other operating expenses		45,761	43,386
		269,489	264,589
Operating profit	3	264,432	218,488
Financial income and (financial expenses)			
Interest income		2,980	2,548
Interest expenses		(84,955)	(65,060)
Foreign exchange difference		22,811	(63,077)
Fair value changes in embedded derivatives	31	(49,410)	84,494
Fair value changes in other derivatives		24,878	(12,990)
	7	(83,696)	(54,085)
Associated companies	14	(179)	(228)
Profit before income tax		180,557	164,175
Income tax	8	(59,528)	(56,211)
Net profit for the year		121,029	107,964
Attributable to:			
Owners of the Parent Company		107,932	98,084
Minority interest in subsidiaries		13,097	9,880
		121,029	107,964

Notes 1 to 60 are an integral part of these financial statements.

Consolidated Financial Statements of Landsvikjun 2018 11 Amounts are in USD thousand

Statement of Comprehensive Income

	2018	2017
Net profit for the year	121,029	107,964
Items that will not be reclassified subsequently to profit or loss		
Pension obligation after income tax, change	(2,293)	(2,647)
Items that may be reclassified subsequently to profit or loss		
Translation difference due to subsidiaries and associated companies	(2,492)	2,775
Total operating items moved to equity	(4,785)	128
Total Comprehensive Income for the year	116,244	108,092
Total Comprehensive Income attributable to:		
Owners of the Parent Company	103,419	98,021
Minority interest in subsidiaries	12,825	10,071
	116,244	108,092

Notes 1 to 60 are an integral part of these financial statements.

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Balance Sheet

Assets	Notes	2018	2017
Non-current assets			
Property, plant and equipment	9	4,013,546	3,810,257
Projects under construction	10	22,573	232,425
Development cost	11	140,698	130,319
Other intangible assets	11	48,067	48,413
Derivative financial instruments	13	13,342	66,200
Associated companies	14	11,070	11,778
Other non-current assets	15	762	163
Deferred tax asset	8	14	14
Total non-current assets		4,250,072	4,299,569
Current assets			
Inventories	17	5,530	5,625
Accounts receivables and other receivables	18	68,943	66,383
Derivative financial instruments	13	10,258	8,271
Cash and cash equivalents	19	116,278	126,544
Total current assets		201,009	206,823
Total assets		4,451,081	4,506,392
Equity and liabilities			
Equity			
Owners' contributions	20	586,512	586,512
Revaluation account	21	164,053	169,329
Restricted reserves	21	32,838	10,390
Translation difference	21	(40,756)	(38,536)
Other equity		1,289,803	1,216,571
Equity of the owners of the Parent Company		2,032,450	1,944,265
Minority interest		130,606	118,847
Total equity		2,163,056	2,063,112
Long term liabilities			
Interest bearing liabilities	22	1,808,579	1,889,372
Pension fund obligation	24	38,015	40,597
Deferred income tax liability	8	130,733	91,268
Obligation due to demolition	25	9,011	8,551
Prepaid income		2,847	3,043
Derivative financial instruments	13	11,538	4,110
		2,000,723	2,036,941
Current liabilities			
Accounts payable and other payables	26	73,102	93,028
Interest bearing liabilities	23	192,302	279,814
Income tax payable	8	18,586	18,038
Derivative financial instruments	13	3,312	15,459
		287,302	406,339
Total liabilities		2,288,025	2,443,280
Total equity and liabilities		4,451,081	4,506,392

Notes 1 to 60 are an integral part of these financial statements.

Consolidated Financial Statements of Landsvikjun 2018 13 Amounts are in USD thousand

Statement of Equity

	Owners' contribution	Revaluation account	Restricted reserves	Translation difference	Other equity	Equity attrib-utable to the owners of the Parent Company	Minority interest	Total equity
Changes in equity year 2017								
Equity at 1 January 2017..	586,512	175,712	1,039	(41,120)	1,138,169	1,860,312	108,776	1,969,088
Translation difference..				2,584		2,584	191	2,775
Pension obligation, change....................................					(2,647)	(2,647)		(2,647)
Net profit for the year..					98,084	98,084	9,880	107,964
Total Comprehensive Income..................................		0	0	2,584	95,437	98,021	10,071	108,092
Share of profit of subsidiaries and associated companies.....................................			9,351		(9,351)	0	0	0
Revaluation transferred to other equity..		(6,383)			6,383	0	0	0
Dividend paid to owners...					(14,067)	(14,067)	0	(14,067)
Equity at 31 December 2017	586,512	169,329	10,390	(38,536)	1,216,571	1,944,265	118,847	2,063,112
Changes in equity year 2018								
Equity at 1 January 2018..	586,512	169,329	10,390	(38,536)	1,216,571	1,944,265	118,847	2,063,112
Translation difference..				(2,220)		(2,220)	(272)	(2,492)
Pension obligation, change....................................					(2,293)	(2,293)		(2,293)
Net profit for the year..					107,932	107,932	13,097	121,029
Total Comprehensive Income..................................		0	0	(2,220)	105,639	103,419	12,825	116,244
Share of profit of subsidiaries and associated companies.....................................			22,448		(22,448)	0	0	0
Revaluation transferred to other equity..		(5,276)			5,276	0	0	0
Dividend paid to owners...					(15,234)	(15,234)	(1,066)	(16,300)
Equity at 31 December 2018	586,512	164,053	32,838	(40,756)	1,289,803	2,032,450	130,606	2,163,056

Notes 1 to 60 are an integral part of these financial statements.

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Statement of Cash Flow

	2018	2017
Operating activities		
Operating profit	264,432	218,488
Adjustments for:		
Depreciation and impairment loss	125,448	127,086
Pension obligation, change	(1,972)	(1,795)
Obligation due to demolition, change	460	1,467
Other changes	(56)	(210)
Working capital from operation before financial items	388,312	345,036
Operating assets, change	(2,581)	2,021
Operating liabilities, change	292	4,381
Cash flow from operating activities before financial items	386,023	351,438
Interest income received	3,062	2,566
Interest expenses and foreign exchange difference paid	(75,868)	(61,093)
Taxes paid	(17,456)	(14,974)
Cash flow from operating activities	295,761	277,937
Investing activities		
Power stations in operation	(37,299)	(8,752)
Power stations under construction	(68,474)	(165,055)
Transmission	(26,330)	(71,559)
Power plant preparation cost	(5,245)	(6,822)
Purchased shares in other companies	(622)	(41)
Other capital expenditures	(12,914)	(6,469)
Assets sold	107	621
Other receivables, change	(87)	4,337
Investing activities	(150,864)	(253,740)
Financing activities		
Dividend paid to owners	(14,246)	(14,067)
New loans	267,213	209,218
Amortisation of long-term debt	(405,102)	(227,708)
Currency swaps	259	(12,725)
Financing activities	(151,876)	(45,282)
Change in cash and cash equivalents	(6,979)	(21,085)
Effect of exchange difference on cash and cash equivalents	(3,287)	3,095
Cash and cash equivalents at the beginning of the year	126,544	144,534
Cash and cash equivalents at the end of the year	116,278	126,544

Notes 1 to 60 are an integral part of these financial statements.

Consolidated Financial Statements of Landsvikjun 2018 15 Amounts are in USD thousand

Notes

General Information

1. Landsvirkjun

Landsvirkjun is a partnership having its place of business in Iceland and its headquarters at Háaleitisbraut 68, Reykjavík. Landsvirkjun operates on the basis of the Act on Landsvirkjun No. 42/1983. The Company's objective is to engage in operations in the energy sector. The financial statements include the consolidated financial statements of the Company and its subsidiaries (referred to as "the Group") and share of profit or loss of associated companies.

2. Basis of preparation

a. Statement of IFRS compliance

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and additional requirements in Icelandic Financial Statements Act.

The Company's Board of Directors approved the financial statements on 28 February 2019.

Note 43 includes information on the Group's significant accounting policies and changes therein in the year.

b. Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following assets and liabilities, which have been measured at fair value; derivative financial instruments, trading financial assets and shares in other companies. Operating assets and assets held for sale are recognised at the lower of book value or fair value. Operating assets of the subsidiaries Landsnet hf. and Orkufjarskipti hf. are recognised at revalued cost. Transmission network of the subsidiary Landsnet hf. was revalued during the year 2015, see note 9.

c. Presentation and functional currency

The financial statements are presented in USD, which is the Parent Company's functional currency. All financial information presented in USD has been rounded to the nearest thousand, unless otherwise stated.

d. Management's use of estimate and judgements

The preparation of financial statements in conformity with IFRS 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 and the effect of the changes are entered in the periods that the changes are made and in subsequent periods if the change also affects those periods.

Information on management's estimates and decisions made in relation to the application of accounting methods that significantly affect the financial statements are presented in the following notes:

- notes 9 and 52 property, plant and equipment
- notes 11 and 53 development cost and other intangible assets
- notes 13, 29, 31, 32, 33 derivative financial instruments
- notes 8 and 51 income tax
- note 24 pension fund obligations

Notes, contd.

2. Basis of preparation, contd.:

e. Determination of fair value

The Group's accounting policies and disclosures can require measurement of fair values, for both financial and non-financial assets and liabilities.

To the extent possible the Group uses market information in determining fair values but if such information is not available management's evaluation is used.

For derivatives, other than embedded derivatives, counterparty information is used where applicable to measure fair values. Then treasury division compares this to its own assessment and confirms that such valuations meet the requirements of IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

Fair values are categorised into different levels in the fair value hierarchy based on assumptions used in the valuation techniques as follows.

- Level 1; quoted prices in active markets for identical assets or liabilities.
- Level 2; assumptions based on other than quoted prices included in Level 1 that can be acquired for the asset or liability, either directly (i.e. as prices) or indirectly (derived from prices).
- Level 3; assumptions for value of asset or liability that are not based on available market data.

If the assumptions used to measure fair value of an asset or a liability might be categorised in different levels of the fair value hierarchy, the fair value measurement is categorised in the lowest level.

If the categorisation of fair value during the accounting period changes, it is transferred between levels at the end of the period.

Further information on the assumptions made in measuring fair values is included in the following notes:

- note 13 derivative financial instruments
- note 31 embedded derivatives
- note 38 long-term debt
- note 52 property, plant and equipment

3. Segment reporting

Segment information is presented according to the nature of the operation and is based on the Group's organisation and internal disclosure.

Landsvirkjun Group's operating segments are specified as follows:

Electricity production

The operations of the Parent Company fall under the segment electricity production but Landsvirkjun's objective according to law is to operate in the energy sector and operate other business and financial operations according to decision of the Board of Directors at each time. Landsvirkjun's electricity production is based on hydroelectric power and geothermal heat. Landsvirkjun sells all its electricity production in Iceland, on the one hand to retail sales companies, and on the other to energy intensive industrial users. Furthermore, the operation of Icelandic Power Insurance Ltd. falls under this segment. The purpose of Icelandic Power Insurance Ltd. is to take care of insurances for Landsvirkjun's power stations.

Electricity transmission

The operations of Landsnet hf. fall under the segment electricity transmission. The purpose of Landsnet hf. is to operate the electricity transmission network and system management in Iceland according to provisions of Chapter III of the Energy Act No. 65/2003 and may thus not carry out other operations than are necessary in order to fulfill its obligations according to the Energy Act.

Notes, contd.

3. Segment reporting, contd.:

Other segments

Other segments include the operations of Orkufjarskipti hf. and Landsvirkjun Power ehf. The purpose of Orkufjarskipti hf. is to own and operate a telecommunications system which is necessary for the shareholders' electricity operations throughout the country and to rent access thereto in accordance with availability and law. Landsvirkjun Power ehf. takes care of sales of technical and operational advisory services to third parties and general research work, harnessing researches and projects for Landsvirkjun and related companies.

Almost all the operations of the Group are based in Iceland.

Operating segments year 2018	Electricity production	Electricity transmission	Other segments	Adjustments	Total
Income from third party	444,377	88,193	1,351		533,921
Income within the Group	15,029	65,946	5,021	(85,996)	0
Segment income	459,406	154,139	6,372	(85,996)	533,921
Segment operating expenses	(161,390)	(63,903)	(4,744)	85,996	(144,041)
EBITDA	298,016	90,236	1,628	0	389,880
Depreciation and impairment loss	(95,094)	(29,643)	(1,120)	409	(125,448)
Segment earnings, EBIT	202,922	60,593	508	409	264,432
Segment assets 2018	3,927,241	839,517	21,130	(347,878)	4,440,010
Associated companies	10,909	6,815	161	(6,815)	11,070
Total assets 2018	3,938,150	846,332	21,291	(354,693)	4,451,081
Segment liabilities 2018	1,889,722	476,027	4,056	(81,780)	2,288,025
Total liabilities 2018	1,889,722	476,027	4,056	(81,780)	2,288,025
Investing activities	114,375	34,279	1,609	0	150,263

Operating segments year 2017

Income from third party	400,091	81,669	1,317	0	483,077
Income within the Group	21,699	65,657	5,200	(92,556)	0
Segment income	421,790	147,326	6,517	(92,556)	483,077
Segment operating expenses	(164,151)	(60,972)	(4,936)	92,556	(137,503)
EBITDA	257,639	86,354	1,581	0	345,574
Depreciation and impairment loss	(97,782)	(28,483)	(1,230)	409	(127,086)
Segment earnings, EBIT	159,857	57,871	351	409	218,488
Segment assets 2017	4,025,516	843,935	22,893	(397,731)	4,494,613
Associated companies	11,616	7,367	162	(7,367)	11,778
Total assets 2017	4,037,132	851,302	23,055	(405,098)	4,506,392
Segment liabilities 2017	2,076,465	514,339	4,351	(151,875)	2,443,280
Total liabilities 2017	2,076,465	514,339	4,351	(151,875)	2,443,280
Investing activities	182,473	74,722	1,484	0	258,679

Consolidated Financial Statements of Landsvikjun 2018 18 Amounts are in USD thousand

Notes, contd.

4. Operating revenues

Power sales are specified as follows:

	2018	2017
Wholesale	90,760	81,222
Industrial users	352,808	320,292
Power sales total	443,568	401,514

Revenues from transmission are specified as follows:

	2018	2017
Transmission	75,554	68,744
Transmission losses, grid service and other transmission revenues	11,833	12,282
Transmission total	87,387	81,026

In notes no. 43 and 46 is further accounted for the registration of revenues of the Group.

5. Total number of employees

Total number of employees is specified as follows:

	2018	2017
Average number of employees during the year, full-time equivalents	470	464
Full-time equivalent units at year-end	429	422

6. Total salaries of employees

Total salaries of employees are specified as follows:

	2018	2017
Salaries	56,522	54,276
Contribution to defined contribution plans	8,226	7,579
Defined pension benefit payments	2,930	2,853
Other change in pension obligations	(1,972)	(1,795)
Other salary related expenses	5,454	5,249
	71,160	68,162
Transferred to assets	(8,823)	(9,958)
	62,337	58,204

Salaries and salary related expenses are allocated as follows in the income statement:

	2018	2017
Energy production costs	24,291	22,143
Transmission costs	13,272	12,657
Other operating expenses	33,597	33,362
Transferred to assets	(8,823)	(9,958)
	62,337	58,204

Salaries of the Boards of Directors, CEO, Deputy CEO and Executive Directors are specified as follows:

	2018	2017
Salaries of the Board of Directors of the parent company	195	189
Salaries of the Boards of Directors of two subsidiaries (same as in 2017)	174	158
Salaries and benefits of the CEO of the parent company*	379	304
Salaries of five Directors and the Deputy CEO (same as in year-end 2017)	1,578	1,702
Salaries and benefits of the CEO and 7 Man. Dir. of subsid. (same as in year-end 2017)	1,700	1,435

*The monthly salaries of the CEO of the parent company without benefits have not changed from July 2017.

Consolidated Financial Statements of Landsvikjun 2018 19 Amounts are in USD thousand

Notes, contd.

7. Financial income and (expenses)

Financial income and (expenses) are specified as follows:

	2018	2017
Interest income	2,980	2,548
Interest expenses	(84,536)	(69,881)
Guarantee fee	(5,413)	(7,452)
Indexation	(1,408)	(1,883)
Capitalised interest costs	6,402	14,156
Total interest expenses	(84,955)	(65,060)
Realised foreign exchange difference	1,797	(2,332)
Unrealised foreign exchange difference	21,014	(60,745)
Total foreign exchange difference	22,811	(63,077)
Fair value changes in embedded derivatives	(49,410)	84,494
Fair value changes in other derivatives	24,878	(12,990)
Total financial income and (expenses)	(83,696)	(54,085)

Capitalised finance cost amounted to 3.8% (2017: 3.8%) of invested cash in power stations under construction in the year 2018 and 5.1% (2017: 5.2%) of invested cash in transmission under construction.

8. Income tax

Income tax is specified as follows:

	2018	2017
Change in income tax asset / liability	(39,465)	(36,737)
Income tax payable	(18,586)	(18,038)
Income tax recognised among comprehensive income	(1,382)	(1,489)
Foreign exchange and translation difference	(150)	100
Other changes	54	(46)
Income tax expensed	(59,528)	(56,211)

Consolidated Financial Statements of Landsvikjun 2018 20 Amounts are in USD thousand

8. Income tax, contd.:

Effective tax rate

		2018		2017
Profit for the year		121,029		107,964
Income tax for the year		59,528		56,211
Profit before income tax		180,557		164,175
Income tax acc. to the parent company's tax rate	37.6%	67,889	36.0%	59,103
Effect of different tax rates within the Group	(4.6%)	(8,252)	(3.5%)	(5,819)
Effect of incr. in tax rate in 2018 from 36% to 37.6%	0.0%	0	1.0%	1,650
Non-taxable and non-deductible items	(0.1%)	(110)	0.8%	1,277
Effective income tax	33.0%	59,528	34.2%	56,211

Income tax due to items recognised in other comprehensive income is specified as follows:

	2018	2017
Income tax due to pension obligation recognised in other comprehensive income	(1,382)	(1,489)
	(1,382)	(1,489)

Changes in the tax asset / liability during the year is specified as follows:

	Deferred tax asset		Deferred tax liability	
	2018	2017	2018	2017
Balance at the beginning of the year	14	0	(91,268)	(54,517)
Reclass from deferred tax asset to deferred tax liability	0	(4)	0	4
Change in temporary difference	(24)	4	(39,468)	(36,778)
Change in carry forward loss	26	14	(149)	122
Foreign exchange and translation difference	(2)	0	152	(100)
Balance at year end	14	14	(130,733)	(91,268)

The Group's deferred tax asset / liability is specified as follows:

Carry forward loss	36	14	187	363
Property, plant and equipment and intangible assets	0	0	(144,035)	(110,692)
Derivative financial instruments	0	0	(4,765)	(13,989)
Other items	(22)	0	17,881	33,050
Balance at year end	14	14	(130,733)	(91,268)

The Group's carry forward tax losses may be utilised for 10 years from when it is incurred and are specified as follows:

Carry forward loss of the year 2013, usable until the year 2023	0	18
Carry forward loss of the year 2014, usable until the year 2024	0	138
Carry forward loss of the year 2015, usable until the year 2025	411	532
Carry forward loss of the year 2016, usable until the year 2026	441	491
Carry forward loss of the year 2017, usable until the year 2027	146	706
Carry forward loss of the year 2018, usable until the year 2028	119	-
Carry forward loss at year end	1,117	1,885

Deferred tax asset is recognised as assets as management considers it likely that it will be utilised against future taxable profit. Carry forward loss is recognised in Icelandic krona and, therefore, the exchange rate of the USD affects the carry forward loss at each year end.

Consolidated Financial Statements of Landsvikjun 2018 21 Amounts are in USD thousand

Notes, contd.

9. Property, plant and equipment

Property, plant and equipment is specified as follows:

Cost value	**Power stations**	**Trans-mission**	**Communi-cation equipment**	**Other assets**	**Total**
Total value at 1.1.2017	5,079,432	888,983	24,653	71,690	6,064,758
Effect of exchange rate changes	0	0	2,016	17	2,033
Additions during the year	8,978	11,353	1,463	2,681	24,475
Transferred from projects under construction and development cost	205,662	81,675	0	0	287,337
Sold and disposed of	0	0	(1)	(1,209)	(1,210)
Total value at 31.12.2017	5,294,072	982,011	28,131	73,179	6,377,393
Effect of exchange rate changes	0	0	(2,997)	0	(2,997)
Additions during the year	37,990	6,113	1,702	7,091	52,896
Transferred from projects under construction	264,867	11,644	0	0	276,511
Sold and disposed of	0	0	0	(528)	(528)
Total value at 31.12.2018	5,596,929	999,768	26,836	79,742	6,703,275
Depreciation and impairment loss					
Total value at 1.1.2017	2,151,660	258,177	8,729	31,488	2,450,054
Effect of exchange rate changes	0	0	730	0	730
Depreciation for the year	86,681	26,301	1,246	2,922	117,150
Sold and disposed of	0	0	0	(798)	(798)
Total value at 31.12.2017	2,238,341	284,478	10,705	33,612	2,567,136
Effect of exchange rate changes	0	0	(1,173)	0	(1,173)
Depreciation for the year	92,756	27,061	1,138	3,290	124,245
Sold and disposed of	0	0	0	(478)	(478)
Total value at 31.12.2018	2,331,097	311,539	10,670	36,424	2,689,730
Book value					
1.1.2017	2,927,772	630,806	15,924	40,202	3,614,704
31.12.2017	3,055,731	697,533	17,426	39,567	3,810,257
31.12.2018	3,265,832	688,229	16,166	43,318	4,013,546
Book value without revaluation					
1.1.2017	2,927,772	367,655	15,305	40,202	3,350,934
31.12.2017	3,055,731	446,573	16,844	39,567	3,558,715
31.12.2018	3,265,832	447,335	15,722	43,318	3,772,207

Official assessment of fixed assets and insurance value

The official assessment of the Company's real estates amounted to USD 499 million at year end 2018 (2017: USD 501 million). Insurance value of the Company's assets amounts to USD 5,470 million (2017: USD 5,270 million) and catastrophe insurance value amounts to USD 1.048 million (2017: USD 1.148 million).

Consolidated Financial Statements of Landsvikjun 2018 22 Amounts are in USD thousand

Notes, contd.

9. Property, plant and equipment, contd.:

Assumptions relating to revaluation of property, plant and equipment

In accordance with provision of IFRS the Group's transmission network and communication equipment were revalued during the year 2008 and powerlines and connection masts of Landsnet hf. at year end 2015. Two methods were applied when performing the revaluation. On one hand it is done by looking at the assets' replacement cost which was calculated by independent experts at the beginning of the year 2015 and projected to the end of the year 2015. On the other hand the value of the asset in operation is calculated by cash flow analysis. The forecast period was from the year 2016 until 2025 and after that terminal value of the operations was calculated. The revaluation was based on operational value of the current assets and assumed the investments would be equal to depreciations of current assets. Discounting of future cash flows was based on weighted average cost of capital (WACC) which Landsnet hf. is allocated for large industrial users and distribution companies. The revaluation is classified at level 3 in the fair value hierarchy.

10. Projects under construction

Projects under construction are specified as follows:

	2018	2017
Balance at 1.1.	232,425	282,318
Transferred to development costs	(2,771)	(7,305)
Additions during the year	69,430	242,777
Transferred to property, plant and equipment	(276,511)	(285,365)
Balance at 31.12.	22,573	232,425

In the beginning of the year 2018 Theistareykir geothermal power station and Burfell II hydro power station were still under construction. The former part af Theistareykir was taken into operation in December 2017 and the latter part in April 2018. Burfell II was taken into operation at the end of September 2018.

11. Development cost and other intangible assets

Development cost and other intangible assets are specified as follows:

	Capitalised development costs	Water and geothermal rights	Software	Total
Cost value				
Total value at 1.1.2017	217,179	45,611	10,032	272,822
Additions during the year	9,742	0	427	10,169
Transf. to projects under construction and power pl.	(18,908)	0	0	(18,908)
Transferred from projects under construction	7,305	0	0	7,305
Total value at 31.12.2017	215,318	45,611	10,459	271,388
Additions during the year	8,131	0	334	8,465
Transferred from projects under construction	2,771	0	0	2,771
Total value at 31.12.2018	226,220	45,611	10,793	282,624
Depreciation and impairment loss				
Total value at 1.1.2017	75,779	0	6,942	82,721
Amortisation during the year	0	0	715	715
Impairment loss during the year	9,221	0	0	9,221
Total value at 31.12.2017	85,000	0	7,657	92,657
Amortisation during the year	0	0	680	680
Impairment loss during the year	523	0	0	523
Total value at 31.12.2018	85,523	0	8,337	93,860

Consolidated Financial Statements of Landsvikjun 2018 23 Amounts are in USD thousand

11. Development cost and other intangible assets, contd.:

Book value				
1.1.2017	141,401	45,611	3,090	190,102
31.12.2017	130,319	45,611	2,802	178,732
31.12.2018	140,698	45,611	2,456	188,765

Development cost is reviewed every year by management and checked whether there are indications of impairment. In testing for possible impairment the Parent Company's forecast on expected cash flow over the useful life of the assets was used. In the evaluation expected cash flow was discounted with the rate of 5.14% (2017: 5.0%) of weighted average required rate of return. If management concludes that impairment has occurred the relevant development cost is expensed as impairment.

12. Depreciation and impairment loss

The Group's depreciation and impairment is specified as follows:	**2018**	**2017**
Power stations	92,756	86,681
Transmission	27,061	26,301
Telecommunication equipment	1,138	1,246
Other assets	3,290	2,922
Depreciation of assets in operation	124,245	117,150
Impairment loss on development cost	523	9,221
Amortisation of software	680	715
	125,448	127,086

The Group's depreciation and impairment is allocated as follows by sectors:

Energy production costs	93,628	87,514
Transmission costs	28,485	27,258
Cost of general research	0	8,995
Other operating expenses	3,335	3,319
	125,448	127,086

13. Derivative financial instruments

Derivative financial instruments in the balance sheet are specified as follows:

Assets:		
Embedded derivatives in electricity sales agreements	6,674	54,390
Aluminium hedges	10,177	1,141
Currency swaps	6,749	18,940
	23,600	74,471
Derivative financial instruments are divided as follows:		
Long-term component of derivative agreements	13,342	66,200
Short-term component of derivative agreements	10,258	8,271
	23,600	74,471
Liabilities:		
Embedded derivatives in electricity sales agreements	2,640	946
Aluminium hedges	1,786	17,251
Currency swaps	10,424	693
Interest rate swaps	0	679
	14,850	19,569

Consolidated Financial Statements of Landsvikjun 2018 24 Amounts are in USD thousand

Notes, contd.

13. Derivative financial instruments, contd.:

Derivative financial instruments are divided as follows:

	2018	2017
Long-term component of derivative agreements	11,538	4,110
Short-term component of derivative agreements	3,312	15,459
	14,850	19,569

The assumptions for valuation of embedded derivatives are discussed in note 31.

The fair value of other derivatives than embedded derivatives is based on Landsvirkjun's evaluation and available evaluation of counterparties, where applicable, and verified by the treasury department with comparative calculations based on market information.

14. Associated companies

Shares in associated companies recognised according to the equity method are specified as follows:

		2018	
	Share	Share in return	Book value
Farice ehf., Kopavogur, Iceland	33.2%	(131)	10,587
Heimsþing ehf., Reykjavik, Iceland	33.3%	0	2
SER eignarhaldsfélag ehf., Reykjavik, Iceland	35.4%	(54)	307
Sjávarorka ehf., Reykjavik, Iceland	33.6%	0	13
LP-Verkis, Georgia	40.0%	(9)	8
Hecla SAS, France	28.5%	15	153
		(179)	11,070

		2017	
	Share	Share in return	Book value
Farice ehf., Kopavogur, Iceland	33.2%	(130)	11,202
SER eignarhaldsfélag ehf., Reykjavik, Iceland	35.4%	(13)	398
Sjávarorka ehf., Reykjavik, Iceland	33.6%	(1)	15
LP-Verkis, Georgia	40.0%	(31)	18
Hecla SAS, France	28.5%	(53)	145
		(228)	11,778

15. Other non-current assets

Other long-term assets in the balance sheet are specified as follows:

	2018	2017
Shares in other companies	685	163
Long-term receivables	77	0
	762	163

16. Landsvirkjun's subsidiaries

Landsvirkjun's subsidiaries are the following:

	Share	
Icelandic Power Insurance Ltd., Bermuda	100.0%	100.0%
Landsnet hf., Reykjavik, Iceland	64.7%	64.7%
Landsvirkjun Power ehf., Reykjavik, Iceland	100.0%	100.0%
Orkufjarskipti hf., Reykjavik, Iceland	100.0%	100.0%

17. Inventories

Inventories are specified as follows:

Spare parts and consumables	5,530	5,625
	5,530	5,625

Consolidated Financial Statements of Landsvikjun 2018 25 Amounts are in USD thousand

Notes, contd.

18. Accounts receivables and other receivables

Accounts receivables and other receivables are specified as follows:

	2018	2017
Accounts receivables	64,934	61,098
Other short term receivables	4,009	5,285
	68,943	66,383

In assessing impairment of accounts receivables, historical information is used as guidance as well as current economic prospects. At year-end 2018, 94% of accounts receivables were under 30 days old (2017: 93%).

19. Cash and cash equivalents

Cash and cash equivalents are specified as follows:

	2018	2017
Bank deposits	64,910	106,536
Market securities	51,368	20,008
	116,278	126,544

20. Equity

The Parent Company is a partnership owned by the Icelandic State and Eignarhlutir ehf. The Icelandic State owns 99.9% in the Company and Eignarhlutir ehf. 0.1%. Eignarhlutir ehf. is owned by the State. Landsvirkjun is an independent taxable entity. The Group’s equity ratio at year end 2018 was 48.6% compared to 45.8% at year end 2017.

21. Revaluation account, translation difference and restricted reserves

The revaluation account consists of a revaluation of the transmission network and telecommunication equipment after income tax effects. The translation difference is the foreign exchange difference arising due to Landsvirkjun’s subsidiaries and associated companies with other functional currencies than the Parent Company's. Restricted reserves contain the share in profit of equity accounted investees, from 1 January 2016, (subsidiaries and associated companies) recognised in the income statement which exceeds dividends from these companies, or the dividend that has been decided to distribute.

22. Liabilities

Interest bearing long term debt is specified as follows:

	2018	2017
Interest bearing long term debt 1.1.	2,169,186	2,105,031
New loans	267,213	209,218
Amortisation of long-term debt	(405,102)	(227,708)
Foreign exchange changes	(44,559)	75,085
Changes in CPI indexation and amortisation of discount	14,143	7,560
Interest bearing long term debt 31.12.	2,000,881	2,169,186

Interest bearing long term debt is specified as follows by currencies:

		2018		2017	
	Due date	Average interest	Remaining balance	Average interest	Remaining balance
Liabilities in ISK	2019-2034	3.7%	273,367	3.7%	295,793
Liabilities in CHF	2019-2022	0.0%	20,849	0.0%	27,044
Liabilities in EUR	2019-2026	0.0%	309,111	0.9%	392,671
Liabilities in USD	2019-2035	3.8%	1,397,554	3.3%	1,453,678
			2,000,881		2,169,186
Current maturities of long-term debt			(192,302)		(279,814)
Total long-term debt			1,808,579		1,889,372

Consolidated Financial Statements of Landsvikjun 2018 26 Amounts are in USD thousand

22. Liabilities, contd.:

Interest rate terms on loans at year end are from 0.0-5.0%. Nominal interest rates for the period were on average 3.7% (2017: 3.5%), taking into account the state guarantee fee and excluding expenses in relation to prepayments of loans which amounted to USD 10.5 million. The Company's payments due to guarantees for long-term loans are calculated according to the Act No. 121/1997 on state guarantees.

23. Maturities of long-term debt

According to loan agreements, maturities of long-term debt are as follows:

	2018	2017
2018	-	279,814
2019	192,302	193,063
2020	260,771	338,640
2021	215,459	209,145
2022	163,293	106,736
2023	165,740	-
Later	1,003,316	1,041,788
	2,000,881	2,169,186

24. Pension fund obligations

The Company's obligation to refund the indexation charges on retirement payments to current and former employees, which hold pension rights with state and communal pension funds amounted to USD 38.0 million at year end 2018 according to an actuary's evaluation, which is based on estimated future changes in salaries and prices. Interest rates in excess of price increase are assessed at 3.5% and salary increase in excess of price increase is assessed at 1.5% per year on average. Premises on life expectancy and mortality are in accordance with the provisions of Regulation No. 391/1998 on obligatory pension benefits and operation of pension funds. The calculated retirement age is 68 years for current employees and 65 years for non-employees with vested benefits. This is consistent with criterion used by the Pension Fund for State Employees.

Change in the obligation is specified as follows:	2018	2017
Balance at 1.1.	40,597	35,383
Expensed during the year	925	887
Payments during the year	(2,896)	(2,683)
Actuarial change	3,674	4,137
Effect of foreign exchange rate changes	(4,285)	2,873
Balance at 31.12.	38,015	40,597

Pension fund obligation, 5 year statement:	2018	2017	2016	2015	2014
Present value of the obligation	38,015	40,597	35,383	27,663	26,345

25. Obligation due to demolition

Change in the obligation due to demolition is specified as follows:	2018	2017
Balance at 1.1.	8,551	7,023
Reversal of discount in the year	460	1,467
Increase in obligation	0	61
Balance at 31.12.	9,011	8,551

In accordance with IFRS, the initial value of fixed operating assets shall include estimated cost of their demolition after their use. Estimated demolition cost of power lines has been assessed and discounted on the basis of the useful life. In return, an obligation has been written up among long-term liabilities. A change in the obligation is recognised in the income statement amounting to the discounted value.

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Notes, contd.

26. Accounts payable and other payables

Accounts payable and other payables are specified as follows:	2018	2017
Accounts payable	25,479	52,611
Accrued interests	20,797	20,870
Other short term liabilities	26,826	19,547
	73,102	93,028

27. Related parties

Definition of related parties

Owners, associated companies, members of Boards of Directors, key management and companies and institutions owned by them are among the Company’s related parties.

Transactions with related parties	**2018**	**2017**
Other income		
Associated companies	17	54
Interest income		
Associated companies	2	0
Expenses		
Associated companies	0	0
Receivables		
Associated companies	10	15

Transactions with related parties are on the same basis as transactions with non-related parties. Transactions with the State or companies or institutions owned by the State are not specified as a separate item but such transactions are comparable to transactions with non related parties. The Group applies an exemption from disclosure requirements of IAS 24 as the Parent Company is owned by the State. See further information in note 20.

28. Fees to auditors

Fees to auditors of the Group in the year 2018 amounted to USD 376 thousand (2017: USD 341 thousand), whereof USD 239 thousand (2017: USD 212 thousand) was for the audit of financial statements.

29. Risk management

The Company’s Board of Directors has approved a risk management policy, which is based on the following factors:

- That risk is defined and its origin is known
- Generally accepted methods are used in evaluating risk
- Effective management is applied in accordance with authorisations
- Effective monitoring of risk factors is ensured
- That information provided to the risk management committee and the Board of Directors is accurate and provided on a regular basis

The Company has implemented a formal process in risk management in order to identify the most important factors. Management and employees of Landsvirkjun identify financial and non-financial risks for Landsvirkjun and evaluate their significance. The results are recorded in the Company's risk register and used to decide on appropriate action and management, with respect to possible effects on image, financial position, health and safety, environment and compliance.

Consolidated Financial Statements of Landsvikjun 2018 28 Amounts are in USD thousand

Notes, contd.

29. Risk management contd.:

The board's risk committee, which consists of three board members, confirms the effectiveness of the Company's risk management and assists the board with supervision of key risks and the Company's actions in managing risks.

The Company's executive risk committee revalues and approves processes relating to the Company's risk management. It is a venue for consultation regarding risk management and ensures that the Company operates in accordance with risk policy. The executive risk committee consists of the CEO, Deputy CEO and CFO. The CEO is the chairman of the executive risk committee.

30. Financial risk

The treasury division is entrusted with analysing, managing and providing information regarding Landsvirkjun's financial risks. The Company's financial risk is divided into market risk, liquidity risk and counterparty risk. The Company's market risk consists mainly of three risk categories:

- Aluminium price risk due to power agreements linked to the price of aluminium
- Interest rate risk due to the Company's liabilities
- Foreign exchange risk due to liabilities and cash flow

Landsvirkjun has been focused on reducing market risk in recent years. For this purpose the ratio of USD and fixed interests has been significantly increased. Efforts have been made to reduce the ratio of aluminium linked revenue in power sales and new sales agreements have not been linked to aluminum price.

31. Aluminium price risk

The Company is exposed to market risk due to changes in aluminium price as about a quarter of its income (before aluminium hedges) is linked to aluminium price. Thus, the Company has entered into derivative agreements in order to secure its income base and reduce fluctuations. Such agreements consist in most cases of fixing the aluminium price at a certain level. Therefore, the Company can lose income if the aluminium price goes up, but at the same time guarantees higher income should the aluminium price go down. About 67% of the estimated cash flow of 2019 and 25% of 2020 has been hedged. At year end 2018, fair value of the hedges was positive by USD 8.4 million (2017: negative USD 16.1 million).

Embedded derivatives

Landsvirkjun's contracts for sale and purchase of electricity which are linked to aluminium price form embedded derivatives which are recognised in the Company's financial statements. Embedded derivatives in electric power contracts are recognised in the balance sheet at fair value on the reporting date. Fair value changes are recognised in the income statement among financial income and expenses.

	2018	2017
Fair value of embedded derivatives is specified as follows:		
Fair value of embedded derivatives at the beginning of the year	53,444	(31,050)
Fair value changes during the year	(49,410)	84,494
Fair value of embedded derivatives at year end	4,034	53,444
Division of embedded derivatives is specified as follows:		
Long term component of embedded derivatives	5,228	47,194
Short term component of embedded derivatives	(1,194)	6,250
Total embedded derivatives	4,034	53,444

Consolidated Financial Statements of Landsvikjun 2018 29 Amounts are in USD thousand

Notes, contd.

31. Aluminium price risk contd.:

The main assumptions Landsvirkjun uses in the valuation of embedded derivatives are as follows:

Calculations are based on the forward price of aluminium, as disclosed in the LME and are based on the maximum time length of forward aluminium prices, or 123 months. Management's opinion is that aluminium price expectations after ten years will reflect the aluminium price at the time the agreements were made and therefore fair value changes will not arise for that period.

The calculations are limited to the revision time of electric power sales agreements or length of agreements. However the time length can never be more than the aforementioned 123 months.

According to provisions on energy buyers' purchase obligation the calculation is based on a secured minimum purchase.

In November 2019 a renewed power sales agreement will take effect where its link to aluminium price will be discontinued. As a result market risk in revenues due to changes in aluminium prices will decrease.

Expected cash flow of contracts is discounted using USD rates according to Bloomberg, no spread added. At year end 2018, rates for discounting were in the range of 2.6 - 2.8% (2017: 1.6 - 2.4%).

Sensitivity analysis of aluminium price risk

The following tables show effects of changes in aluminium prices on fair value of financial instruments linked to aluminium prices in the income statement. Amounts are in thousands of USD, pre tax.

31/12/2018	**Aluminum price USD/MT**	
	-100	+100
Embedded derivatives	(8,832)	8,742
Aluminium hedges	5,066	(4,860)
	(3,766)	3,882

31/12/2017	**Aluminum price USD/MT**	
	-100	+100
Embedded derivatives	(13,667)	13,667
Aluminium hedges	5,695	(5,917)
	(7,972)	7,750

32. Foreign exchange risk

Foreign exchange risk is the risk of loss due to unfavourable changes in foreign exchange rates. Landsvirkjun's foreign exchange risk is due to cash flows, assets and liabilities in addition to transactions in other currencies than the functional currency.

Landsvirkjun's functional currency is the USD and therefore a foreign exchange risk arises from the cash flow and open balances in currencies other than the USD. The Company's revenues are mainly in USD. Other revenues are mainly in ISK and NOK but foreign exchange risk due to those currencies is limited due to netting in the cash flow in ISK and income in NOK is relatively low. Currency risk due to amortisation and interest payments for future years has been limited with the use of cross currency swaps.

The Company's reporting risk related to changes in exchange rate arises mainly due to its debt in EUR which is mainly long-term. The following table shows Landsvirkjun's position in currencies other than the functional currency.

Notes, contd.

32. Foreign exchange risk contd.:

Landsvirkjun's foreign exchange risk relating to monetary assets and liabilities at year end is specified as follows:

2018	EUR	ISK	CHF	Other currencies
Long term receivables	0	1,895	0	0
Accounts receivables and other receivables	1,378	22,615	0	1,930
Cash and cash equivalents	2,051	25,241	79	3,136
Interest bearing liabilities	(309,111)	(273,367)	(20,849)	0
Derivatives	103,075	238,178	0	0
Accounts payable and other payables	(1,032)	(68,977)	0	(399)
Risk in balance sheet	(203,639)	(54,415)	(20,770)	4,667

2017	EUR	ISK	CHF	Other currencies
Long term receivables	0	2,214	0	0
Accounts receivables and other receivables	736	24,420	0	1,994
Cash and cash equivalents	2,903	18,310	199	3,172
Interest bearing liabilities	(392,671)	(295,793)	(27,044)	0
Derivatives	57,483	255,307	0	0
Accounts payable and other payables	(3,980)	(81,396)	(1)	(352)
Risk in balance sheet	(335,529)	(76,938)	(26,846)	4,814

Exchange rates of the main currencies against the USD for the years 2018 and 2017 are specified as follows:

	Average rate		Rate at year end	
	2018	2017	2018	2017
EUR	0.85	0.89	0.87	0.84
GBP	0.75	0.78	0.78	0.74
CHF	0.98	0.98	0.98	0.98
JPY	110.49	112.26	110.06	112.55
NOK	8.14	8.27	8.68	8.20
ISK	108.38	106.78	116.33	104.42

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32. Foreign exchange risk contd.:

Sensitivity analysis

The change of the functional currencies of the companies in the Group by 10% against the following currencies, would have changed the Group's results and equity by the following amounts before tax. Sensitivity against EUR has decreased due to amortisation of debt and a cross currency swap entered into this year. The analysis includes monetary assets and liabilities and assumes that all other variables, especially interest rates, remain unchanged.

	Profit (loss) / Equity	
2018	Strengthening	Weakening
EUR	20,364	(20,364)
ISK	5,442	(5,442)
CHF	2,077	(2,077)
Other currencies	(499)	499
2017	Strengthening	Weakening
EUR	33,553	(33,553)
ISK	7,694	(7,694)
CHF	2,685	(2,685)
Other currencies	(468)	468

The fair value of cross currency swaps was negative by USD 3.7 million at the end of December 2018 (2017: positive by USD 18.2 million).

33. Interest rate risk

Landsvirkjun faces interest rate risk as the Company has interest bearing assets and liabilities. The Company's interest bearing assets and liabilities carry both fixed and floating interest rates and cross currency swaps with exchange of currency and interest are used to manage interest rate risk. No interest rate swaps were in effect at year end 2018 (2017: negative by USD 0.7 million). The Company's risk consists of a possible increase in floating interest rates on debt which can lead to an increase in financial expenses.

At year end 2018, the proportion of loans with fixed interest rates including swap agreements was 73% (2017: 68%). At year end 2018, the estimated market value of the Company's long-term liabilities was USD 145 million higher than their book value (2017: USD 173 million higher) discounted by the underlying currencies yield curve without spread. The following table shows the division of financial assets and liabilities between floating and fixed interest.

Financial instruments with fixed interest	**2018**	**2017**
Interest bearing liabilities	(1,130,884)	(1,125,864)
Cross currency and interest rate swaps	(337,367)	(339,124)
Long term receivables	77	0
	(1,468,174)	(1,464,988)
Financial instruments with floating interest		
Cash and cash equivalents	116,278	126,544
Interest bearing liabilities	(869,997)	(1,043,322)
Cross currency and interest rate swaps	334,941	357,662
	(418,778)	(559,116)

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33. Interest rate risk, contd.,

Sensitivity analysis of interest risk

The following tables show the effect of changes in interest rates on book value and cash flows for one year. The amounts are in USD thousand before tax.

31/12/2018	Cash flow		Book value	
	-100 bps	+100 bps	-100 bps	+100 bps
Embedded derivatives	0	0	475	(439)
Other derivatives	(2,319)	3,176	(657)	2,392
Interest bearing liabilities	5,435	(8,044)	0	0
Cash and cash equivalents	(1,163)	1,163	0	0
	1,953	(3,705)	(182)	1,953

31/12/2017	Cash flow		Book value	
	-100 bps	+100 bps	-100 bps	+100 bps
Embedded derivatives	0	0	2,887	(2,690)
Other derivatives	(3,301)	3,525	(247)	848
Interest bearing liabilities	6,885	(9,645)	0	0
Cash and cash equivalents	(1,265)	1,265	0	0
	2,319	(4,855)	2,640	(1,842)

34. Liquidity risk

Liquidity risk consists of risk of losses should the Company not be able to meet its obligations at maturity date. Landsvirkjun limits liquidity risk with effective liquidity management by ensuring that there is sufficient cash at all times to be able to meet obligations. In order to keep balance between liabilities and expected revenues an emphasis is placed on a secure liquidity position in the form of cash and access to revolving credit facilities.

The Company's cash and cash equivalents amounted to USD 116 million at year end 2018 (2017: USD 127 million) but taking into account undrawn credit facilities (USD 250 million and ISK 12,000 million) Landsvirkjun has access to a total of USD 469 million (2017: USD 548 million). Cash flow from operations, a well distributed maturity profile in addition to strong liquidity and access to credit facilities secure the Company's liquidity at least throughout the year 2020.

Notes, contd.

34. Liquidity risk, contd.,

Contractual payments due to financial instruments, including interests, are specified as follows:

2018	Book value	Contractual cash flow	Within one year	1 - 2 years	2 - 5 years	More than 5 years
Non-derivative financial instruments						
Long term receivables	77	86	0	0	86	0
Cash and cash equiv.	116,278	116,278	116,278	0	0	0
Short term receivables	68,943	68,943	68,943	0	0	0
Interest bearing liabilities ..	(2,000,881)	(2,358,526)	(234,138)	(322,096)	(676,137)	(1,126,155)
Current liabilities	(91,688)	(91,688)	(91,688)	0	0	0
	(1,907,271)	(2,264,907)	(140,605)	(322,096)	(676,051)	(1,126,155)
Derivative financial instruments						
Cross currency swaps	(3,675)	(13,310)	(2,730)	(6,201)	(4,321)	(58)
Aluminium derivatives	8,391	7,695	7,096	599	0	0
Embedded derivatives in electr. sales agr.	4,034	5,373	(1,214)	(1,362)	562	7,387
	8,750	(242)	3,152	(6,964)	(3,759)	7,329

2017	Book value	Contractual cash flow	Within one year	1 - 2 years	2 - 5 years	More than 5 years
Non-derivative financial instruments						
Cash and cash equiv.	126,544	126,544	126,544	0	0	0
Short term receivables	66,383	66,383	66,383	0	0	0
Interest bearing liabilities ..	(2,169,186)	(2,554,443)	(315,905)	(249,237)	(780,515)	(1,208,786)
Current liabilities	(111,066)	(111,066)	(111,066)	0	0	0
	(2,087,325)	(2,472,582)	(234,044)	(249,237)	(780,515)	(1,208,786)
Derivative financial instruments						
Cross currency swaps	18,247	15,576	(610)	1,716	14,470	0
Interest rate swaps	(679)	(696)	(696)	0	0	0
Aluminium derivatives	(16,110)	(14,804)	(13,068)	(1,736)	0	0
Embedded derivatives in electr. sales agr.	53,444	60,451	6,319	6,771	13,866	33,495
	54,902	60,527	(8,055)	6,751	28,336	33,495

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Notes, contd.

35. Financing

Landsvirkjun places emphasis on securing access to capital and having diverse sources of funding. Thus, the Company has been able to access capital through the issuance of bonds in the domestic and foreign capital markets, with borrowing from the European Investment Bank (EIB) and the Nordic Investment Bank (NIB) and through project financing in Europe and Japan. In addition, the Company has access to credit facilities from its relationship banks.

In 2018, Landsvirkjun issued for the first time a Green Bond for a total amount of USD 200 million through a US private placement (USPP) and was the first issuer in Iceland to issue a bond in a Green Bond format. Landsnet drew on a loan from the Nordic Investment Bank (NIB) amounting to USD 40 million. Total borrowings in 2018 amounted to USD 267 million (2017: USD 209 million). Total amortisation of debt was USD 405 million (2017: USD 228 million) but Landsvirkjun prepaid loans and bonds amounting to USD 95 million in the year.

Landsvirkjun´s interest-bearing debt amounted to USD 2.001 million at year-end 2018 (2017: USD 2.169 million). The risk associated with refinancing is reduced by the equal distribution of amortisations and by the suitable lifetime of outstanding debt. The weighted average lifetime of interest-bearing debt is 5.1 years (2017: 5.3 years) and the ratio of interest-bearing debt with maturity within a 12-month period is 9.6% (2017: 13%).

In recent years, Landsvirkjun has placed an emphasis on changing its loan portfolio and no longer takes on debt with a state guarantee. In addition, the Company has worked systematically to remove state guarantees of outstanding debt where possible. The principal of state guarantee debt is decreasing and the last debt enjoying a state guarantee is due in 2026. At year-end 2018, 40% of Landsvirkjun's debt was state guaranteed. Landsvirkjun pays a guarantee fee to the Icelandic state for the Company´s debt which has a state guarantee.

36. Green Bonds

In connection with the United Nations´ Sustainable Development Goals, Landsvirkjun issued a USPP in Green Bond format of USD 200 million in March 2018. This was the company´s first Green Bond and Landsvirkjun was the first Icelandic company to issue a Green Bond. The bond was issued under Landsvirkjun´s Green Bond Framework and the proceeds of the transaction have been fully allocated to the build up of Theistareykir Power Station and the expansion of Burfell Power Station. Both projects are in compliance with the Green Bond Framework´s eligibility criteria and restrictions on $CO2$ emission.

Annual reporting under the Green Bond Framework and further information can be found on Landsvirkjun´s website: https://www.landsvirkjun.com/finance/funding/green-bond.

37. Counterparty risk

Counterparty risk is the risk that a counterparty to an agreement does not comply with provisions of the agreement. Landsvirkjun's counterparty risk arises first and foremost due to the Company's power agreements, derivative contracts and cash and cash equivalents. Though the amounts involved can be considerably high, the risk is limited by the Company´s requirements for take or pay clauses in power agreements and also through requirements for counterparty guarantees. Landsvirkjun requires that counterparties have an investment grade credit rating when it comes to keeping cash and cash equivalents and entering into derivative contracts. In note no. 50 the assessment of assets is explained in more detail.

37. Counterparty risk contd.:

The Company's counterparty risk is specified as follows at year end:

	2018	2017
Derivative financial instruments	23,600	74,471
Long term receivables	77	0
Accounts receivables and other receivables	68,943	66,383
Cash and cash equivalents	116,278	126,544
	208,898	267,398

38. Comparison of fair value and book value of long-term debt

	2018		2017	
	Book value	Fair value	Book value	Fair value
Interest bearing long term liabilities	2,000,881	2,146,307	2,169,186	2,342,525

The fair value of other financial assets and liabilities is measured as book value.

Fair value of interest bearing liabilities is calculated by discounting expected cash flows with the underlying currencies' yield curve.

Interest rates are specified as follows:	2018	2017
Interest bearing liabilities in ISK	1.1 to 1.4%	1.9 to 2.0%
Interest bearing liabilities other than in ISK	-0.8 to 2.8%	-0.7 to 2.6%

39. Fair value classification

The table shows the level categorisation for items in the financial statements recognised at fair value.

	Level 2	Level 3	Total
2018			
Embedded derivatives		4,034	4,034
Other derivatives	8,982	(4,266)	4,716
Revaluation of property, plant and equipment		241,338	241,338
Shares in other companies		685	685
	8,982	241,791	250,773
2017			
Embedded derivatives		53,444	53,444
Other derivatives	(13,228)	14,686	1,458
Revaluation of property, plant and equipment		250,960	250,960
Shares in other companies		163	163
	(13,228)	319,253	306,025

Main assumptions for valuation of derivatives can be seen in notes 13 and 31.

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Notes, contd.

40. Classification of financial instruments

Financial assets and liabilities are divided into defined groups. The classification affects how evaluation of the relevant financial instrument is measured. Those groups to which the Company's financial assets and liabilities pertain and their basis for evaluation are specified as follows:

- Assets and liabilities held for trading - are recognised at fair value through profit and loss.
- Equity instruments - are recognised at fair value through profit and loss.
- Loans and receivables - are recognised at amortised cost.
- Other financial liabilities - are recognised at amortised cost.

Financial assets and liabilities are divided into the following groups of financial instruments:

2018	Assets and liabilities held for trading	Equity instruments	Loans and receivables	Other financial liabilities	Book value
Derivative financial instruments	23,600				23,600
Shares in other companies		685			685
Long term receivables			77		77
Accounts receivables and other receivables			68,943		68,943
Cash and cash equivalents			116,278		116,278
Total assets	23,600	685	185,298	0	209,583
Interest bearing liabilities				2,000,881	2,000,881
Derivative financial instruments	14,850				14,850
Accounts payable and other payables				91,688	91,688
Total liabilities	14,850	0	0	2,092,569	2,107,419
2017					
Derivative financial instruments	74,471				74,471
Shares in other companies		163			163
Accounts receivables and other receivables			66,383		66,383
Cash and cash equivalents			126,544		126,544
Total assets	74,471	163	192,927	0	267,561
Interest bearing liabilities				2,169,186	2,169,186
Derivative financial instruments	19,569				19,569
Accounts payable and other payables				111,066	111,066
Total liabilities	19,569	0	0	2,280,252	2,299,821

41. Capital management

Landsvirkjun places emphasis on maintaining a strong equity base supporting further development of the Company.

42. Subsequent events

Nothing has come forth after the balance sheet date, which would require adjustments or changes to the financial statements for the year 2018.

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Notes, contd.

43. Significant accounting policies

The Group has adopted International Financial Reporting Standards, amendments thereto and interpretations adopted by the European Union at year-end 2018. It is the management's opinion that the implementation of new and amended standards and interpretations do not have significant effects on the consolidated financial statements. The Group has not adopted new or amended standards which have been issued but not entered into effect.

New and amended IFRS Standards that are effective for the current year

The Group has implemented IFRS 15 Revenue from Contracts with Customers (see A) and IFRS 9 Financial Instruments (see B) which were effective for the annual period that begins on or after 1 January 2018. The Group has not implemented new standards, interpretations or amendments to standards that are not currently effective. IFRS 16 Leases (see C) is effective for annual periods that begin on or after 1 January 2019. It is management's estimate, that the application of other new standards and interpretations or amendments that have been endorsed but are not yet effective do not have a material effect on the consolidated financial statements of the Group. Changes to significant accounting policies of the Group are described below:

A. IFRS 15 Revenue from Contracts with Customers

The objective of IFRS 15 is to establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. IFRS 15 introduced a 5-step approach to revenue recognition where the core principles are that an entity will recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration which the entity expects to be entitled to in exchange for those goods or services. Revenue recognition in IFRS 15 is based on the transfer of control which is different from the previous standards where revenue recognition was based on the transfer of risk and rewards. The Group has decided not to restate comparative amounts and therefore the requirements of IFRS 15 were applied from 1.1.2018. The transition to IFRS 15 did not affect equity as at 1.1.2018.

Revenues are recognised based on the nature of products sold and services delivered as follows:

Electricity generation

Electricity generation revenues are generated by the sale of electricity that is generated by hydroelectric power, wind power and geothermal heat.

Electricity generation revenues are generated by the delivery of electricity at an agreed price. The service obligation is to deliver electricity over time and the contractual price is the fee that Landsvirkjun expects to receive, on either the daily price or the contractual price. The service obligation is met over time and reflects consideration based on contracual price for each delivered unit which is the amount that is recognised as revenues. The right to make an invoice for the sale of electricity arises when electricity is generated and delivered and the right to make an invoice has been created for a fee which will, in most circumstances, be the same as the value for the customer.

Furthermore, the operation of Icelandic Power Insurance Ltd. is included in this segment. The purpose of Icelandic Power Insurance Ltd. is to manage insurances for Landsvirkjun´s power stations.

43. Significant accounting policies, contd.:

Electricity transmission

Landsnet carries out the transmission of electricity and system operation in accordance with the provisions of Chapter III of the Electricity Act no. 65/2003. Revenues for the transmission of electricity are based on the measurement of delivered units according to a valid tariff at each time. That tariff is dependent on a revenue cap defined in art. 12 of the Electricity Act and is subject to surveillance by the National Energy Authority. Revenues from transmission losses and system operation are also recognised based on the measurement of delivered units according to the valid tariff. That tariff is based on purchase price according to auctions and is not dependent on the revenue cap but subject to surveillance by the Natonal Energy Authority. The right to recognise revenue and issue an invoice for the transmission of electricity is established when the electricity is transmitted and delivered.

Other

Other segments include the operations of Orkufjarskipti hf. and Landsvirkjun Power ehf. The purpose of Orkufjarskipti hf. is to own and operate a telecommunication infrastructure which is necessary for shareholders´ electricity operations throughout the country and to rent access thereto in accordance with availability and law. Landsvirkjun Power ehf. takes care of sales of technical and operational advisory services to third parties and general research work, harnessing researches and projects for Landsvirkjun and related companies. Revenues are recognised for other income when a performance obligation according to an agreement has been fulfilled.

B. IFRS 9 Financial Instruments

IFRS 9 includes new requirements for recognition and measurement of financial instruments and a new impairment model for financial assets that is based on expected loss. New requirements for hedge accounting are introduced. The new standard replaces IAS 39 Financial Instruments: Recognition and Measurement.

IFRS 9 divides all financial assets into three measurement catagories - those measured at amortised cost, those measured at fair value through profit or loss and those measured at fair value through other comprehensive income. The standards classification rules are dependent on what is the financial assets business model and cash flow characteristics. Embedded derivatives in a contract where the host is a financial asset are never separated. Instead, the contractual cash flows of the financial assets are assessed in their entirety.

Financial assets are measured at amortised cost if they meet the following two conditions and are not designated at fair value through profit and loss:
- the financial assets business model is to hold the financial asset to collect the contractual cash flows; and
- the contractual terms of the financial assets give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

If the objective of the business model for a financial asset is both to hold the financial asset to collect the contractual cash flows and selling the financial asset, the financial asset is measured at fair value through other comprehensive income. The Group can make an irrevocable election at initial recognition to measure equity instruments, that are not held for trading nor a contingent consideration recognised by an acquirer in a business combination to which IFRS 3 Business Combinations applies, at fair value through other comprehensive income.

43. Significant accounting policies, contd.:

All financial assets which are not measured at amortised cost or at fair value through other comprehensive income are measured at fair value through profit or loss. All derivatives are measured at fair value through profit or loss. At initial recognition the Group has the option to designate a financial asset as measured at fair value through profit or loss if doing so eliminates or significantly reduces a measurement or recognition inconsistency.

The transition to IFRS 9 did not affect the measurement of financial assets in the consolidated financial statements of the Group i.e. financial assets measured at amortised cost. Financial assets that previously were classified at amortised cost and fair value through profit or loss are classified in the same way under IFRS 9.

The impairment model in IFRS 9 is based on the premise of providing for expected losses and applies to all of the following: (i) financial assets measured at amortised cost, (ii) financial assets mandatorily measured at fair value through other comprehensive income; (iii) lease receivables, (iv) contract assets within the scope of IFRS 15, and (v) certain loan commitments and financial guarantee contracts. The impairment model does not apply to financial assets measured at fair value through profit or loss and equity instruments measured at fair value through other comprehensive income.
The transition to the new impairment model did not have a material effect on the consolidated financial statements and did not affect retained earnings at the beginning of the period.

C. IFRS 16 Leases

IFRS 16 provides a single lessee accounting model to account for lease agreements in the financial statements of both the lessee and the lessor. At its effective date IFRS 16 succeeds the current requirements in IAS 17 and related interpretations. IFRS 16 makes a distinction between a lease and a service agreement on the basis that if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The standard removes the difference in accounting treatment between finance lease (on balance sheet) and operation lease (off balance sheet) and introduces a single lessee accounting model, requiring lessees to recognise right of use assets and lease liabilities for all leases unless the lease term is 12 months or less or the underlying asset has a low value. In addition IFRS 16 requires extensive disclosure for lease agreements. The standard applies to annual reporting periods beginning on or after 1 January 2019.

Based on management estimate, the transition to IFRS 16 will result in a recognised lease liability for the lease of real estate and land in the balance sheet as at 1 January 2019 amounting to USD 6.5 million and the same amount for the right of using an asset.

The Group will not do a full retrospective implementation of the requirements of the standard and therefore comparative amounts will not be restated. As the lease liability will be equal to the right of use asset, no transition effect will be recorded through equity.

44. Basis of consolidation

Subsidiaries are entities controlled by the Company. A company controls an entity when it has the power to govern the investment, is exposed to, or has rights to variable returns from its involvement in the investment and has the ability to affect those returns through its power over the investment. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. Financial performance of subsidiaries have been taken into account. When the Company's share of losses exceeds its interest in a subsidiary, the carrying amount of that interest is reduced to nil and the recognition of further losses is discontinued except to the extent that the Company has an obligation or has made payments on behalf of the subsidiary. In case of a profit on the operation of a subsidiary in subsequent periods, a share in their profit is not recognised until the share in a loss has been fully set off.

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Company's interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

Assets and liabilities of subsidiaries with another functional currency than the Parent Company are translated to USD at the exchange rate ruling at the accounting date. Income and expenses of that operation are translated to USD at the average exchange rate of the year. The exchange rate difference arising from the translation to USD is entered as a specific item in the statement of comprehensive income and under equity. Amounts in the statement of cash flow are translated to USD at the average exchange rate of the year. The exchange rate difference arising from the translation to USD is entered as a specific item in the statement of cash flow.

45. Associated companies

Associated companies are those companies in which the Group 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% of the voting power of another entity, including any other possible voting power.

The consolidated financial statements include share in the profit or loss of associated companies accounted for using the equity method, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds the book value of an associated company the book value is reduced to nil and the recognition of further losses is discontinued except to the extent that the Group has an obligation or has made payments on behalf of the associated company. If in subsequent periods there is a profit on the operation of associated companies, the share in the profit is not recognised until the previous share in losses has been set off.

46. Operating revenues

Revenues from sales and transmission of electricity consists of sales to power intensive industries and public utilities based on measured delivery of electricity during the period. Other service income is recognised when earned or upon delivery.

47. Interest income and expenses

Interest income and expenses are recognised in the income statement using the effective interest method. Interest income and expenses include bank rates, premium, realised interest rate swaps and other differences arising on initial book value of financial instruments and amounts on the date of maturity using the effective interest method.

Effective interest is the imputed rate of interest used in determining the current value of estimated cash flow over the estimated useful life of a financial instrument or a shorter period if applicable, so that it equals the book value of the financial asset or liability in the balance sheet. When calculating the effective interest rate, the Company estimates cash flow taking into account all contractual aspects of the financial instrument.

48. Other financial income and expenses

Other financial income and expenses include profit or loss on assets and liabilities held for trading and all realized and unrealized fair value changes and changes in foreign exchange rates.

49. Foreign currency transactions

Transactions in foreign currencies are recognised at the exchange rate ruling at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are recognised at the exchange rate ruling at the end of the year. The foreign currency gain or loss thereon relating to USD is recognised in the income statement. Non-monetary assets and liabilities measured at cost value in a foreign currency are translated to USD at the exchange rate ruling at the date of the transactions. Tangible assets and liabilities recognised in foreign currencies at fair value are translated to USD at the exchange rate ruling at the date of determination of fair value.

50. Impairment

a) Financial assets

The impairment model in IFRS 9 is based on the premise of providing for expected losses. IFRS 9 requires that the same impairment model apply to all of the following: (i) financial assets measured at amortised cost, (ii) financial assets mandatorily measured at fair value through other comprehensive income; (iii) lease receivables within the scope of IAS 17 Leases, (iv) contract assets within the scope of IFRS 15 Revenue from Contracts with Customers, and (v) certain loan commitments and financial guarantee contracts. This is model is a change from the impairment model under the previous standard, IAS 39, which required impairment to be recognised based on incurred losses.

Expected impairment loss for financial assets is estimated based on what stage of the impairment model the relevant financial assets is classified:

Stage 1: expected credit loss is estimated based on 12 months expectation of default,
Stage 2: expected credit loss is estimated based on lifetime default,
Stage 3: objective evidence of impairment is in place about the expected credit loss of the financial asset.

At initial recognition, financial assets are classified in stage 1, with the exception of purchased or originated credit impaired financial assets. Financial assets are classified in stage 2 when there is a significant increase in credit risk from initial recognition. An estimate of significant increase in credit risk is performed at each financial reporting date. The Group has elected to classify trade receivables that do not include significant finance component, in stage 2 at initial recognition in accordance with the simplified approach in the standard.

At each financial reporting date, management estimates if there is an objective evidence of impairment of financial assets (stage 3). Financial assets are impaired if there is an objective evidence, as a result of one or more events that occurred after the initial recognition of the asset, that indicated that the expected cash flow from the assets will be lower than previously expected.

Impairment of financial assets at amortised cost is the difference between the book value of the assets and the expected cash flow, discounted with original effective interest rate. Impairment for assets held for sale is estimated based on the fair value of the financial assets at each balance sheet date.

Impairment is reversed if there is an objective evidence that an event has occurred after the impairment was recognised that changes the previous estimate of impairment. Reversal of impairment loss for financial assets at amortised cost and debt instruments classified as available for sale are recognised in profit or loss. Reversal of impairment loss for equity instruments that are classified as assets available for sale, is recognised in other comprehensive income.

Change in estimated impairment for financial assets is recognised in profit or loss in the period when the estimate is performed.

50. Impairment, contd.:

b) Other assets

The carrying amounts of the Company's other assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Intangible assets with unspecified useful lives are tested annually for impairment.

An impairment loss is expensed if the carrying amount of the asset or its cash generating unit exceeds its recoverable amount. A cash generating unit is the smallest group of assets that generates cash inflows that are largely independent of the cash inflows of other assets or cash generating units. Impairment loss is first recognised in the income statement and then to reduce the carrying amounts of the fixed assets in the cash generating unit.

The recoverable amount of an asset or cash generating unit is the greater of its value in use and its net fair value. Value in use is based on the estimated future cash flows, discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the assets.

For other assets, an impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation.

51. Income tax

Income tax on the results for the year consists of current income tax and deferred income tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity or in statement of comprehensive income, in which case income tax is recognised among those items.

Current income tax is the expected tax payable on the taxable income for the year, using tax rates enacted at the reporting date, in addition to adjustments made to current income tax of previous years.

A deferred income tax asset (liability) is recognised in the financial statements. Its calculation is based on the difference in balance sheet items, according to the tax return, on the one hand, and the consolidated financial statements, on the other hand. The difference thus arising is due to the fact that the tax assessment is based on premises other than the Group's financial statements and is in main respect a temporary difference as expenses are entered in the financial statement in another period than in the tax return. Calculation of deferred tax is based on the expected tax ratio when temporary differences are estimated to be reversed based on current law at the reporting date.

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against the asset. The tax asset is calculated at each reporting date and decreased to the extent that is considered likely that it will not be utilised against future taxable profit.

52. Property, plant and equipment

Property, plant and equipment are initially measured at cost.

The cost of renewing single items of fixed asset is capitalised if it is considered likely that the proceeds on the asset will revert to the Company and the cost can be measured reliably. All other cost is expensed in the income statement as it is incurred.

The Group's transmission and telecommunication systems are recognised at a revalued cost in the balance sheet, which is their fair value less depreciation from the date of revaluation. The revaluation of those assets is carried out on a regular basis. All value increase due to the revaluation is recognised in the revaluation account among equity after income tax effect. Depreciation of the revalued cost is recognised in the income statement. Upon the sale, depreciation or disposal of an asset, the part of the revaluation account pertaining to the asset is transferred to retained earnings.

Other operating assets are capitalised at cost less accumulated depreciation and impairment.

Initial value of fixed assets includes the estimated cost of demolition following their use. Estimated demolition cost of power lines has been measured at a discounted value based on the useful life and an obligation in relation thereto has been recognised among long-term liabilities. A change in the obligation due to the discounted value is recognised through the income statement in addition to depreciation of demolition cost.

Cost value consists of all cost incurred due to the acquisition of the asset. Cost value of fixed assets constructed in own account is the aggregate cost of construction, such as cost of material and salaries in addition to all other costs the Company incurs in making the asset operative.

If single items of fixed assets have different estimated useful lives, they are divided in accordance with their different useful lives.

Interest expense on loans used to finance the cost value of projects are capitalised at the time of construction.

Profit or loss on the sale of fixed assets is the difference between the sales value and the book value of the asset and is recognised in the income statement.

Notes, contd.

52. Property, plant and equipment, contd.:

Depreciation

Depreciation is calculated as a fixed annual percentage based on the estimated useful lives of the operating assets.

Depreciation method, estimated useful life and residual value are revalued at each accounting date.

Depreciation ratios and useful life are specified as follows:

	Depreciation	Useful life
Power stations:		
Power houses and other structures	1.67%	60 years
Machinery	2.5-6.67%	15-40 years
Dams and waterways	1.67-3.33%	30-60 years
Thermal stations	1.67-6.67%	15-60 years
Windmills	5.00%	20 years
Substations	2.5-5%	20-40 years
Power lines	1.67-5%	20-60 years
Optical fibre	4-10%	10-25 years
Other telecommunication equipment	6-20%	5-17 years
Office buildings	2.00%	50 years
Equipment	10-25%	4-10 years
Vehicles	10-20%	5-10 years

53. Intangible assets

Intangible assets are recognised at cost value, less accumulated impairment loss and amortisation.

Expenditure for general research cost is expensed in the period it incurs. Development cost for future power projects is capitalised among fixed assets, such as cost of materials, salary cost and all cost incurred by the Company in relation to capitalised development cost. Development cost is only capitalised if there is probability of future economic benefit and the Company intends and is able to conclude, use or sell it. The useful life of development cost is assessed to be unlimited until a decision is made concerning its use or sale, thus the cost is not depreciated at this stage but account is taken for possible impairment loss if a project changes.

Water and geothermal rights are capitalised in the balance sheet at cost value as intangible assets with unlimited useful life since it cannot be determined when these rights will no longer be financially viable.

Other intangible assets are stated at cost less accumulated amortisation and impairment loss.

Subsequent cost is only capitalised if it increases the estimated future economic benefit of the asset it relates to. All other cost is expensed in the income statement when incurred.

Amortisation is calculated on a straight line basis, based on the estimated useful lives of intangible assets from the date that they become applicable. Amortisation and estimated useful life is specified as follows:

	Amortisation	Useful life
Software	25%	4 years

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54. Financial instruments

a) Non-derivative financial assets

Non-derivative financial assets are recognised when the Company becomes a part of contractual provisions of the relevant financial instrument.

Financial assets are derecognised if the Company's contractual right to cash flow due to the asset expires or the Company transfers the assets to another party without holding back control or almost all the risk and gain involved in the ownership. The component of the transferred financial assets arising or retained by the Company is recognised as a specific asset or liability.

Financial assets and financial liabilities are offset and the net amount presented in the balance sheet when, and only when, the Company has a legal right to offset the amounts and intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

The Group classifies non-derivative financial assets into the following categories: financial assets at fair value through profit or loss, loans and receivables and financial assets available for sale.

i) Financial assets measured at fair value through profit or loss

A financial asset is classified at fair value through profit or loss if it is classified as held-for-trading or is designated as such on initial recognition. Upon initial recognition attributable transaction costs are recognised in profit or loss when incurred. Financial assets at fair value through profit or loss are measured at fair value in the balance sheet, and changes therein are recognised in the income statement.

Financial assets at fair value through profit or loss are shares in other companies and marketable securities.

ii) Financial assets at amortised cost

Financial assets is measured at amortised cost if it meets the following two conditions and is not designated at fair value through profit or loss: (i) the financial assets business model is to hold the financial asset to collect the contractual cash flows; and (ii) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Such financial assets are initially recognised at fair value plus all transaction costs. After initial recognition the financial assets are measured at amortised cost net of any write down for impairment.

Financial assets at amortised cost include bonds, cash and cash equivalents, trade receivables and other receivables. Cash and cash equivalents includes funds and non-restricted bank balances with maturity date of three months or less.

iii) Financial assets at fair value through other comprehensive income

If the financial assets are held within a business model where the objective is achieved by both collecting contractual cash flows and selling financial assets the financial instrument is measured at fair value through other comprehensive income. It is permitted to make a irrevocable election at initial recognition to measure equity instruments at fair value through other comprehensive income, if they are not held for trading or contingent consideration recognised by an acquirer in a business combination to which IFRS 3 Business Combinations applies.

b) Non-derivative financial liabilities

Non-derivative financial liabilities are initially measured at fair value plus direct transaction costs. Subsequent to initial recognition the liabilities are recognised at the amortised cost value based on effective interests.

The Group derecognises a financial liability when the contractual obligations due to the debt instrument expire.

The Company's non-derivative financial liabilities are loans, accounts payables and other payables.

54. Financial instruments, contd.

c) Derivative financial instruments

The Company enters into derivative financial instruments to hedge its foreign currency, interest rate and aluminium price risk exposures. Derivative financial instruments are recognised initially at fair value. Direct transaction cost is recognised in the income statement as it incurs. Subsequent to initial recognition, derivative financial instruments are recognised at fair value in the balance sheet and fair value changes are recognised in the income statement among financial income and expenses. Hedge accounting is not applied to derivative instruments that economically hedge monetary assets and liabilities denominated in foreign currencies.

i) Separable embedded derivatives

Embedded derivatives where host contract is not a financial instruments are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, other instruments with the same provisions as the embedded derivative would be defined as a derivative and the hybrid contract is not stated at fair value in the income statement.

Changes in the fair value of separable embedded derivatives are recognised in the income statement among financial income and expenses.

55. Inventories

Inventories are stated at the lower of the cost value or the net sales value. Cost value of inventories is based on "the First In First Out method" and includes cost incurred upon the purchase of the inventories and in bringing them to the sales location and in a saleable state.

56. Cash and cash equivalents

Cash and cash equivalents consist of cash, short-term market securities and demand deposits.

57. Equity

The Group's equity is divided into owners' contribution, revaluation account, translation difference, restricted reserves, other equity and minority interest. The Parent Company's initial capital amounts to USD 587 million.

58. Employees' benefits

a) Defined contribution plan

Cost due to contribution to defined benefit plans is expensed in the income statement among salaries and salary related expenses when incurred.

b) Defined benefit plan

The Company's obligation due to defined benefit plans is calculated by estimating the future value of defined pension benefits accrued by current and former employees in current or previous periods. The benefits are discounted in order to determine their present value. An actuary has calculated the obligation on the basis of a method, which is based on accrued benefits. Actuarial changes in the obligation are recognised among operating items under equity in the statement of comprehensive income. Other changes are recognised in the income statement.

59. Provisions

Obligations are recognised in the balance sheet when the Company has a legal obligation or entered into obligations due to past events, it is considered probable that they will be settled and they can be reliably measured. The obligation is assessed on the basis of estimated future cash flow, discounted on the basis of interests reflecting market interests and the risk inherent with the obligation.

60. Operating segments

A segment is a distinguishable component of the Group, which is subject to risks and returns, including income and expenses related to other segments of the Group. In determining the distribution of resources to segments and evaluating the results, the return of the segments is reviewed by management on a regular basis.

Segment operating results, assets and liabilities consist of items that can be directly linked to each segment, in addition to the items that can be reasonably divided into segments.

Appendix I: Statement of Corporate Governance

Corporate Governance

Organisation

Landsvirkjun's operations are subject to Act No. 42/1983, with subsequent amendments. The Board of Directors of Landsvirkjun has established working procedures for the Board for further compliance with the law.

Role, goals, vision and values

Landsvirkjun is an energy company owned by the Icelandic State. Landsvirkjun's role is to maximise the yield of energy resources entrusted to the Company with emphasis on sustainable use, valuable products and efficiency. In order to uphold its role with ambition the Company has defined the following goals: Practise efficient electricity production and development, serve a diverse client base, connect prices to European electricity markets, constantly develop skills and capabilities of the employees, and to encourage unity and support from stakeholders via open and clear communication.

Landsvirkjun's future vision is to be a progressive electricity company in the field of renewable energy. The company operates in an international competitive market and strives to be amongst the best power producer in generating and selling energy.

The values of the company are progressiveness, prudence and reliability.

The Board of Directors

According to law, the Board of Directors of Landsvirkjun is appointed by the Minister of Finance for a one year term at a time and it is responsible for the financial matters and operation of Landsvirkjun. The Board of Directors of Landsvirkjun consists of the following Directors: Jónas Þór Guðmundsson, Supreme Court Attorney, who is also the Chairman of the Board, Álfheiður Ingadóttir, biologist, Vice Chairman of the Board, Jón Björn Hákonarson, Chairman of Fjardabyggd town council, Guðfinna Jóhanna Guðmundsdóttir, lawyer and Gunnar Tryggvason, engineer.

Audit committee

Chapter IX of the Financial Statements Act No. 3/2006, cf. Act No. 80/2008, applies to the audit committee of Landsvirkjun. The working procedures for the committee are established by the Company's Board of Directors for further compliance with the law. The audit committee of Landsvirkjun exercises advisory functions for the Board and operates on the basis of the Board's authorisation. The committee has not executive power. The Company's audit committee consists of three individuals; two board members, Jónas Þór Guðmundsson and Gunnar Tryggvason, and Heimir Haraldsson, auditor and chairman of the committee. The audit committee can get advice at each time if necessary to conduct its supervisory duties.

Remuneration committee and risk management committee

The remuneration committee consist of three board members, Jónas Þór Guðmundsson, Álfheiður Ingadóttir and Jón Björn Hákonarson. The risk management committee consists of Jónas Þór Guðmundsson, Álfheiður Ingadóttir and Guðfinna Jóhanna Guðmundsdóttir. The Board of Directors of Landsvirkjun has set the committees work procedures.

Appendix I: Statement of Corporate Governance, contd.

CEO, Deputy CEO and Executive Directors

The CEO is Hörður Arnarson. The Board of Directors and the CEO exercise executive power in the Company. Deputy CEO is Ragna Árnadóttir. The Deputy CEO’s role is to stand in for the CEO in his absence and manage the CEO's office, which handles collective matters of the Company and policy development, and ensures good corporate governance. The CEO's office consists of supporting departments which are responsible for processing collective matters of Landsvirkjun.

The executive Board consists of the CEO, Deputy CEO and heads of each division. There were five heads of divisions at the end of the year.

Finance division. The Company’s CFO is Rafnar Lárusson. The role of the division is to create basis for profitable operation and contribute to maximum results in all units of the Group.

Project planning division. The Head of project planning division is Gunnar Guðni Tómasson. The role of the division is to manage Landsvirkjun’s power plant constructions from development to fully operative power plants. The division monitors costs, quality and work progress and ensures that projects are delivered fully operative in accordance with the Company’s presumptions, estimates and needs.

Marketing and business development division. Head of marketing and business development is Stefanía G. Halldórsdóttir. The role of the division is to maximise the Company’s revenue by analysing new business opportunities, product development, promotion and sales of products and services, negotiating contracts and follow up of existing contracts.

Energy division. Head of the energy division is Einar Mathiesen. The role of the division is to guarantee that energy production and distribution is in accordance with agreements with customers, guided by safety and efficiency, as well as ensuring maximum output of Landsvirkjun's processing systems.

Development division. Head of development division is Óli Grétar Blöndal Sveinsson. The role of the division is to manage the preparation of new power projects and to conduct research and monitoring of the existing power system. The division shall ensure the economic implementation of new power projects, increase flexibility in power production, and manage innovation in power production and to have a long-term vision of utilisation of energy resources.

Appendix II: Non-financial information

Business Model

Landsvirkjun is an energy company owned by the Icelandic State and produces electricity from renewable energy sources, hydroelectric power, geothermal power and wind. The Company produces over 70% of the country´s electricity and is by far the largest producer of electricity in Iceland.

Landsvirkjun operates in an international competitive market, where various industrial companies are offered competitive agreements, with a long-term secure delivery of electricity. The Company's share in the world market is negligible.

Furthermore, Landsvirkjun operates in the local wholesale market, where the customers are companies which resell electricity to homes and business entities.

Social responsibility - policy and emphasis 2018

Preparations for the implementation of the international standard GRI started in 2018, to support strategic planning, goal setting and disclosure of social responsibility (non-financial disclosure) of Landsvirkjun.

An element of the preparatory work was to start working on materiality analysis, to define the issues that should be emphasized in the coming years in the area of social responsibility. A general policymaking meeting with the management and other employees of the Company was held at the end of October 2018. At the meeting, the GRI Standards were introduced, the Standards indicators related to economic, environmental and social issues were reviewed and ranked by importance. Further consultation with Landsvirkjuns´ stakeholders regarding the focus of social responsibility will take place in 2019.

Landsvirkjun continues to support the Principles of the UN Global Compact in the areas of the environment, labour, human rights and anti-corruption. The Company reports annually on its progress in these areas and the relevant information is available in Landsvirkjun's annual report for 2018.

In addition, Landsvirkjun supports three of the UN' Sustainable Development Goals. The goals were systematically pursued in 2018. The three objectives focus on measures against climate change, sustainable energy and gender equality. The work towards advancing the goals is discussed in the relevant sections of Landsvirkjun's annual report for 2018.

Non-financial key performance indicators

Landsvirkjun started the implementation of the international GRI Standards in 2018. The Standards will be used in the definition of long and short term non-financial indicators in line with the Company's key focus areas related to corporate social responsibility.

Information on the Company's work on gender equality and environmental performance can be found in the relevant sections below.

Appendix II: Non-financial information, contd.

Communication and collaboration

The operation of Landsvirkjun can have an extensive effect on the society, in particular in communities close to the Company´s power stations. One of the Company´s aims is to create support and solidarity with open communication with stakeholders. In all segments and in all construction projects, a stakeholders´ analysis is performed and communication plan developed with the aim to have the optimal communication relating to the operation. In 2018, annual meetings of sustainability projects were held in East and Northeast Iceland, as well as many other meetings, both open and consultation meetings. Further information on meetings and communications in 2018 can be found in Landsvirkjun's annual report.

Each year, Landsvirkjun supports a variety of projects that deliver social benefits, both through Landsvirkjun's community fund and in other ways. During the year, Landsvirkjun became, among others, sponsor of the first Icelandic business accelerator for social innovation, named Snjallræði. Further information on the project can be found in Landsvirkjun's annual report.

Risk Management

Landsvirkjun follows a formal risk management procedure for identifying and managing financial and non-financial risk in the Company´s operations. The effects of the operations can be significant but by mapping the main risk factors of the Company and through appropriate management, efforts are made to reduce the probability of incidents and their possible effects on the Company's image, financial position, health and security and environment.

Environment

Landsvirkjun has a certified environmental management system in accordance with ISO 14001. The Company approved an environmental policy in 2006 and systematically works on preventing and reducing the environmental effects of its operations. Furthermore, the Company follows a plan of implementation in accordance with the Company's environmental policy.

<u>Climate</u>

Landsvirkjun´s objective is to be carbon-neutral in 2030. Annually, data on Landsvirkjun´s CO2 emission is compiled and also the indirect emission in the value chain. In the last 10 years the emission has been reduced in Landsvirkjun´s operation. Additional information can be found in Landsvirkjun´s Annual Report, Green Accounts.

From the year 2007, Landsvirkjun has been providing information about the operation´s carbon footprint. Dissemination of information has been supported by the international GHG Protocol Corporate Standard. This year Landsvirkjun will take an additional step following the standard for the calculation of the Company´s emissions accounting.

In order to achieve its goal of carbon-neutral operations, Landsvirkjun, along with reducing emissions, has been working on mitigation measures. The main mitigation measures are land reclamation and forestry of a total of 23,250 hectares. Further information can be found in Landsvirkjun's annual report.

Appendix II: Non-financial information, contd.

Other measures taken by Landsvirkjun in 2018 to mitigate climate impact include the following:
- **Internal carbon prices**. During the year, Landsvirkjun initiated work to assess internal carbon prices in its operation.
- **Green bonds.** During the year, Landsvirkjun, first of all Icelandic companies, issued a Green bond. The proceeds from the issue was used for the development of Theistareykir Power Plant and the expansion of Búrfell Power Station.
- **Increased energy efficiency and electricity production with renewable energy sources.** The annual utilization of discharge electricity at Búrfell Power Station was on average about 86%, but after the expansion of the plant, the utilization rate is 94% and has therefore increased by 8%, or 300 GWh.
- **Electricity exchange in transport.** Landsvirkjun is an active participant in electricity exchange in transport in Iceland. The company is a member of Samorka, an association of energy and utility companies in Iceland, a shareholder in Íslensk NýOrka and a member of a cooperative forum on energy exchange called the Green Energy. The Company's goal is that 25% of the company's car fleet will be electrically powered by 2020. At the end of 2018, 22% of Landsvirkjuns´ cars were clean energy cars.
- **Reduce carbon dioxide emissions in construction with ecological concrete.** In 2018, Landsvirkjun launched an experimental project, in parallel with the expansion of Búrfell Power Station, where ecological concrete was used with a lower proportion of cement than in conventional concrete. The environmentally-friendly concrete, which was used to form the entrance wall of the plant, is an Icelandic design which partly uses silica and basalt metal instead of cement. The benefits are about 25-30% lower carbon footprint than the concrete used in other parts of the construction.

Environmental Incidents

Landsvirkjun's goal is to prevent all environmental incidents in the operation of the Company. There were no environmental incidents during Landsvirkjun's operation in 2018.

CDP

In 2018, Landsvirkjun delivered for a third time a report on its carbon emissions to CDP, previously the Carbon Disclosure Project, and thus obtained a better view of the situation compared to comparable companies in other countries. Between 2017 and 2018, Landsvirkjun's rating rose from C to B, which is a better performance than the average for energy companies that report to CDP.

Further information on Landsvirkjun's environmental performance in 2018 can be found in Green Accounts for 2018 and in the annual report.

Human resources

Gender equality

In the past two years, special emphasis has been placed on gender equality within Landsvirkjun, which is in line with Landsvirkjun's support for the United Nation´s sustainable development goal number 5 on gender equality. The development of gender equality objectives and measures began in 2018, based on the analysis of gender equality and from results from employee workshops in the autumn of 2017.

In March 2018, a three-year equality action plan was presented, with goals, measures and 17 improvement projects that will bring the company closer to the goals that have been set in equality matters. The projects include i.e., the recruitment process, working environment and response to sexual and gender-based harassment.

Appendix II: Non-financial information, contd.

The preparation for equal pay certification took place during the year, and formal equal pay assessment was carried out in December. At the end of the year, it was confirmed that the gender pay gap according to PwC's assessment was less than 1% for the second consecutive year, but no other Icelandic company has achieved this before. Landsvirkjun's human resources and gender equality policy was revised in parallel with the equal pay certification.

Safety

Landsvirkjun is at the forefront with regards to occupational safety, health and protection. Landsvirkjun's policy is an accident free operation. Furthermore, the Company is certified in accordance with Occupational Health and Safety Assessment Series OHSAS 1800, but companies with this certification are required to constantly work on reforms relating to safety, health and general wellbeing of employees.

Landsvirkjun follows the indicator of zero annual accident frequency (no accidents). Two accidents occurred during the year, and thus the goal was not achieved.

Human rights

Human rights

Landsvirkjun did not issue a human rights policy as planned during the year. However, great emphasis was placed on improving gender equality in the Company´s operation during the year, and Landsvirkjun's human resource policy was updated with increased emphasis on the matter.

The rules on chain responsibility were approved by Landsvirkjun's Board of Directors in 2016. These rules are aimed at ensuring that every person working for Landsvirkjun, such as contractors, subcontractors or temporary work agencies, will enjoy various rights. A contractor shall ensure and be responsible for that all employees receive salaries, benefits, sickness and accidents insurances and other rights in accordance with the contract, collective agreements and law in effect at each time.

In 2019, it will be assessed whether there is a need for a special human rights policy in addition to the existing rules and is intended to ensure the human rights of all parties involved in Landsvirkjun's operation.

The Company´s policies on corruption and bribery matters

The Code of Ethics for Landsvirkjun´s employees was issued and implemented in December 2013. It contains nine categories, including employee safety, importance of honesty and respect in communication, treatment of confidential information and conflict of interest. Following this, a code of ethics for suppliers and service providers was implemented, which is based on the code of ethics for employees and principles of UN Global Compact on human rights, labour, environment and anti-corruption. The code provides clear guidelines on what is expected with regard to sound operating and management governance and were implemented into the relevant procedures in 2015.