Financial Statements 2015

Landsnet hf.
Gylfaflöt 9
112 Reykjavík

Reg. no. 580804-2410

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Endorsement by the Board of Directors and the CEO

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

Results of the year 2015

According to the income statement, profit for the year amounted to ISK 4.0 billion and total profit amounted to ISK 22.7 billion. According to the balance sheet, the Company's equity at year end amounted to ISK 42 billion, including share capital in the amount of ISK 5.9 billion. Average number of employees was 124.

Share capital at year end 2015 is divided between four shareholders as at the beginning of the year:

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

The Company's Board of Directors is composed of two men and one woman. The Board thus meets the requirement of Article 63 of the Public Limited Companies Act that both genders must be represented on a board of directors composed of three members.

The Board of Directors proposes a dividend payment of ISK 400 million (approx. ISK 0.07 per share) to the shareholders in 2016 for the operating year 2015, but otherwise refer to the annual financial statements regarding changes in equity.

Fixed assets were revalued in 2015, the first such revaluation since 2008. Periodic revaluation had not been carried out during this period because of the high level of uncertainty surrounding the profitability of the Company's revenue cap and thereby its income. 2015 is the last year for which the Company is publishing its annual financial statements in ISK. The Annual Accounts Register has agreed that Landsnet will henceforward prepare its financial statements in US dollars (USD), the Company's new functional currency.

Corporate governance

The Board of Directors of Landsnet hf. emphasizes maintaining good management practices. The Board of Directors has laid down comprehensive guidelines wherein the competence of the Board is defined and its scope of work vis-à vis the CEO. These rules include i.e. rules regarding order at meetings, comprehensive rules on the competence of Directors to participate in the discussion and decision of issues presented to the Board, rules on secrecy, rules on information disclosure by the CEO to the Board and other issues. The Corporate Governance Statement, which is a appendix in the Financial Statements, provides further information.

Statement of the Board of Directors and the CEO

According to the best of the Board of Director's and the CEO's knowledge, the financial statements are in accordance with the International Financial Reporting Standards as adopted by the EU and it is the Board's and CEO's opinion that the annual financial statements give a true and fair view of the financial performance of the Company for the financial year 2015, its assets, liabilities and financial position as at 31 December 2015 and its cash flows for the financial year 2015.

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

The Board of Directors and the CEO have today discussed the annual financial statements of Landsnet hf. for the year 2015 and confirmed them by means of their signatures.

Reykjavik, 11 February 2016

The Board of Directors:

Geir A. Gunnlaugsson
Svana Helen Björnsdóttir
Ómar Benediktsson

CEO:
Guðmundur Ingi Ásmundsson

Independent Auditor's Report

To the Board of Directors and Shareholders of Landsnet hf.

We have audited the accompanying financial statements of Landsnet hf., which comprise the statement of financial position as at December 31, 2015, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of accounting policies and other explanatory information.

Management's responsibility for the financial statements

The Board of Directors and CEO are responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management and CEO determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's responsibility

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Landsnet hf. as at December 31, 2015, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Reykjavik, 11 February 2016.

Deloitte ehf.

Páll Grétar Steingrímsson
Rúnar Dór Daníelsson
Certified Public Accountants

Income Statement for the year 2015

	Notes	2015	2014
Operating revenue			
Transmission	5,6	16.069.414	14.227.404
Other income	7	113.241	123.002
		16.182.655	14.350.406
Operating expenses			
Energy procurement costs	8	2.168.318	1.763.886
Transmission costs	9,10	4.535.595	4.559.002
System operation	9,10	977.341	897.565
Other operating expenses	9,10	1.010.258	955.801
		8.691.512	8.176.254
Operating profit		7.491.143	6.174.152
Financial income		393.815	1.125.451
Financial expenses		(2.896.090)	(2.644.510)
Net financial expenses	11	(2.502.275)	(1.519.059)
Share in net earnings of associated company	16	19.730	38.303
Profit before income tax		5.008.598	4.693.396
Income tax	12,24	(998.777)	(931.155)
Profit		4.009.821	3.762.241
Earnings per share:			
Basic and diluted earnings per each ISK 1 share	22	0,68	0,64

Notes no. 1 to 34 are an integral part of these financial statements.

Financial Statements of Landsnet hf. 2015 5 Amounts are in ISK thousand

Statement of Comprehensive Income for the year 2015

	Notes	2015	2014
Profit		4.009.821	3.762.241
Items under total profit recognised among equity:			
Revaluation of transmission system		23.421.719	0
Current tax on revaluation of transmission system		(4.684.344)	0
Total items under total profit recognised among equity		18.737.375	0
Total profit of the year		22.747.196	3.762.241

Notes no. 1 to 34 are an integral part of these financial statements.

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Balance Sheet as at 31 December 2015

	Notes	31.12.2015	31.12.2014
Assets			
Fixed assets in operation	13	86.427.559	63.771.382
Projects under construction	13	3.020.789	809.211
Intangible assets	14	1.689.068	1.479.695
Investment in subsidiary	15	500	500
Investment in associates	16	726.939	707.209
Long-term note		117.670	11.643
Fixed assets		91.982.525	66.779.640
Inventories	17	560.261	549.804
Receivable from parent company	31	614.695	702.735
Trade and other receivables	18	1.009.969	1.121.663
Marketable securities	19	733.824	470.971
Cash and cash equivalents	20	8.072.134	12.234.663
Current assets		10.990.883	15.079.836
Total assets		102.973.408	81.859.476
Equity			
Share capital		5.902.733	5.902.733
Statutory reserve		609.515	227.774
Revaluation account		28.638.029	10.460.730
Retained earnings		6.805.393	2.617.237
Equity	21	41.955.670	19.208.474
Liabilities			
Long term liabilities from parent company	23	38.658.090	44.692.176
Other interest bearing long-term liabilities	23	9.204.636	9.955.162
Deferred income tax liability	24	7.334.845	2.674.787
Deferred income	25	380.490	354.109
Provision due to site restoration	26	906.703	819.766
Long-term liabilities and obligations		56.484.764	58.496.000
Loans from parent company	23	1.265.838	1.463.420
Current maturities	23	943.924	919.008
Income tax payable	24	1.023.063	587.811
Trade and other payables	28	1.300.149	1.184.763
Short-term liabilities		4.532.974	4.155.002
Total liabilities		61.017.738	62.651.002
Total equity and liabilities		102.973.408	81.859.476

Notes no. 1 to 34 are an integral part of these financial statements.

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Statement of Changes in Equity for the year 2015

	Share capital	Statutory reserve	Revaluation account	Retained earnings	Total
Year 2014:					
Equity at 1 January 2014	5.902.733	0	11.027.997	(1.484.497)	15.446.233
Total comprehensive income				3.762.241	3.762.241
Transfer to statutory reserve		227.774		(227.774)	0
Depreciation on revaluation recognised under accumulated deficit			(567.267)	567.267	0
Equity at 31 December 2014	5.902.733	227.774	10.460.730	2.617.237	19.208.474
Year 2015:					
Equity at 1 January 2015	5.902.733	227.774	10.460.730	2.617.237	19.208.474
Profit				4.009.821	4.009.821
Revaluation of transmission			23.421.719	0	23.421.719
Income tax effects of revaluation of transmission			(4.684.344)	0	(4.684.344)
Total comprehensive income			18.737.375	4.009.821	22.747.196
Transfer to statutory reserve		381.741		(381.741)	0
Depreciation on revaluation recognised under accumulated deficit			(560.076)	560.076	0
Equity at 31 December 2015	5.902.733	609.515	28.638.029	6.805.393	41.955.670

Notes no. 1 to 34 are an integral part of these financial statements.

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Statement of Cash Flows for the year 2015

	Notes	2015	2014
Cash flow from operating activities			
Operating profit		7.491.143	6.174.152
Adjustments for:			
Profit from sales of fixed assets	7	(1.215)	0
Depreciation and amortisation	10	2.922.433	2.967.730
Working capital from operation before financial items		10.412.361	9.141.882
Operating assets, decrease (increase)		189.277	(1.269.593)
Operating liabilities, (decrease) increase		(80.480)	194.992
Net Cash from operating activities before financial items		10.521.158	8.067.281
Interest income received		193.997	143.891
Interest expenses paid and foreign exchange difference		(2.013.846)	(1.980.531)
Taxes paid		(587.811)	0
Net cash from operating activities		8.113.498	6.230.641
Cash flow from investing activities			
Investment in transmission infrastructures		(3.891.858)	(2.672.056)
Other investments		(465.054)	(936.078)
Proceeds from sale of property, plant and equipment		3.494	0
Long-term note, change		(100.022)	11.643
Marketable securities, change		(257.801)	(254.526)
Net cash to investment activities		(4.711.241)	(3.851.017)
Cash flow from financing activities			
Change in loans from parent company		(6.894.839)	0
Payments of long-term liabilities		(967.210)	(907.061)
Net cash to financing activities		(7.862.049)	(907.061)
Net (decrease) increase in cash and cash equivalents		(4.459.792)	1.472.563
Effect of exchange rate changes on cash and cash equivalents		297.263	844.896
Cash and cash equivalents at 1 January		12.234.663	9.917.204
Cash and cash equivalents at 31 December	20	8.072.134	12.234.663

Notes no. 1 to 34 are an integral part of these financial statements.

Financial Statements of Landsnet hf . 2015 9 Amounts are in ISK thousand

Notes to the Financial Statements

1. Reporting entity

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

2. Basis of preparation

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

The financial statements were approved by the Board of Directors on 11 February 2016.

Details of the Company's accounting policies are included in note 34.

3. Functional and presentational currency

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

4. Use of estimates and judgements

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

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

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

- Note 13 and 34c - Fixed assets in operation
- Note 14 and 34d - Intangible assets
- Note 26 and 34j - Estimation of provision due to site restoration
- Note 24 and 34n - Income tax

Determination of fair values

A number of the Company's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the following methods. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability. Landsnet revaluates part of fixed assets to fair value, as stated in note 13, just as they do with marketable securities, as stated in note 19. Other assets and liabilities are not recognised at fair value.

Trade and other receivables

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

Non-derivative financial liabilities

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

See accounting policies in note 34k

Transmission revenue consist of:	**2015**	**2013**
Energy transmission	13.665.139	12.184.594
Transmission losses and ancillary services	2.260.928	1.906.911
Service income	49.225	41.777
Input fees	94.122	94.122
Transmission revenue total	16.069.414	14.227.404

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5. Revenue, contd.:

Landsnet's largest customers are also shareholders in the company. Further information on revenues from shareholders is provided in Note 31 on related parties.

6. Energy transmission

Energy transmission consist of:

	2015	2014
Energy transmission to power-intensive consumers	9.685.028	8.459.538
Energy transmission to distribution system operators	3.980.111	3.725.056
Energy transmission total	13.665.139	12.184.594

7. Other income

Other income consist of:

	2015	2014
Income from work sold	50.272	53.057
Rental income	32.622	26.385
Income from guarantees of origin and certification	23.213	38.961
Sales profit from fixed assets	1.215	0
Other income	5.919	4.599
Other income total	113.241	123.002

8. Energy procurement costs

Energy procurement costs consist of:

	2015	2014
Electricity purchases due to transmission losses	1.420.618	1.091.576
Purchase of ancillary services	747.700	672.310
Energy procurement costs total	2.168.318	1.763.886

9. Personnel expenses

See accounting policies in note 34i

Salaries and other personnel expenses consist of:

	2015	2014
Salaries	1.362.010	1.248.163
Defined contribution plan payments	168.490	159.491
Defined benefit plan payments	1.165	7.281
Other payroll expenses	122.595	126.856
Capitalised salaries	(139.349)	(185.366)
Personnell expenses total	1.514.911	1.356.425

Personnel expenses are specified as follows:

	2015	2014
Transmission costs	668.021	576.683
System operation	421.660	357.792
Other operating expenses	425.230	421.950
	1.514.911	1.356.425

	2015	2014
Average number of employees	124	125
Full-time equivalent units at year-end	110	113

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9. Personnel expenses, contd.:

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

	2015	2014
Remuneration of the Board of Directors	7.311	7.401
Remuneration and benefits of the CEO	15.983	17.015
Remuneration of Excecutive Directors	62.525	45.966

The Company underwent organisational changes in mid-2015, with the number of Executive VPs increased to five.

10. Depreciation and amortisation

See accounting policies in notes 34c and 34d

Depreciation and amortisation are specified as follows:

	2015	2014
Depreciation of fixed assets in operation, see Note 13	2.789.378	2.737.096
Amortisation and impairment losses, see Note 14	133.055	230.634
Depreciation and amortisation recognised in the income statement	2.922.433	2.967.730

Depreciation and amortisation are allocated as follows to operating items:

	2015	2014
Transmission costs	2.743.948	2.792.187
System operation	68.792	69.013
Other operating expenses	109.693	106.530
Depreciation and amortisation recognised in the income statement	2.922.433	2.967.730

11. Financial income and expenses

See accounting policies in note 34m

Financial income and expenses are specified as follows:

	2015	2014
Interest income	139.135	116.685
Net gain in fair value of marketable securities	59.913	27.206
Exchange rate difference	194.767	981.560
Total financial income	393.815	1.125.451
Interest expenses	(2.024.084)	(2.181.395)
Indexation	(963.657)	(511.459)
Change in present value of the provision due to site restoration	(86.938)	(43.698)
Capitalised interest expense due to projects under construction	178.589	92.042
Total financial expenses	(2.896.090)	(2.644.510)
Net financial expenses	(2.502.275)	(1.519.059)

Net financial expenses due to the construction of a transmission infrastructure amounting to ISK 179 million (2014: 92 million) is capitalised and has been reported as a reduction in financial expenses.

Capitalised financial expenses were 5,7% of capital tied in transmission structures under construction during the year (2014: 4,8%). This is the Company's average finance cost.

12. Income tax

See accounting policies in note 34n

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

	2015	2014
Calculated income tax for the year	24.286	(343.344)
Income tax payable	(1.023.063)	(587.811)
Income tax recognised in the income statement	(998.777)	(931.155)

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12. Income tax, contd.:

	2015	2014
Income tax recognised in equity:		
Income tax liability due to revaluation of fixed assets	4.684.344	0

Change in deferred income tax liability is specified as follows:

	2015	2014
Change in temporary differences	24.286	(152.137)
Change in carry-forward losses	0	(191.207)
Income tax liability due to revaluation of fixed assets	(4.684.344)	0
Change in deferred tax assets	(4.660.058)	(343.344)

Reconciliation of effective tax rate

		2015		2014
Profit before income tax		5.008.598		4.693.396
Income tax according to the current tax rate	20,0%	(1.001.720)	20,0%	(938.679)
Effects of associates	(0,1%)	3.946	(0,2%)	7.661
Other	(0,0%)	(1.003)	(0,0%)	(137)
Effective tax rate	19,9%	(998.777)	19,8%	(931.155)

13. Fixed assets in operation:

See accounting policies in note 34c

Basis of revaluation of fixed assets in operation

In accordance with the International Accounting Standard, the Company's lines and substations are recognised according to the revaluation method. These assets were revalued at year-end 2015. The revaluation was based on two methods. First, it was based on the estimated reconstruction cost of the transmission system, which was calculated by independent experts at the beginning of the year and projected to year-end 2015. Second, the operating value was measured using a cash flow analysis. The valuation period was 2016-2025, with the future operating value calculated thereafter. The year's revaluation was based on the operating value on the assumption that investment would equal the depreciation of the current asset base. The discounting of future cash flows was based on the weighted average cost of capital (WACC) determined for the Company with respect to power-intensive consumers and distribution system operators. The revaluation has been categorised as level 3 fair value.

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
Cost				
Balance at 1.1.2014	27.149.030	50.116.477	3.794.693	81.060.200
Additions	587.873	173.209	392.789	1.153.871
Transferred from projects under construction	2.051.466	105.521	0	2.156.987
Balance at 31.12.2014	29.788.369	50.395.207	4.187.482	84.371.058
Revaluation	11.085.036	12.336.683	0	23.421.719
Additions	463.877	338.581	103.163	905.621
Transfer	(138.032)	138.032	0	0
Transferred from projects under construction	252.845	867.648	0	1.120.493
Sold	0	0	(15.194)	(15.194)
Balance at 31.12.2015	41.452.095	64.076.151	4.275.451	109.803.697
Depreciation				
Balance at 1.1.2014	5.571.973	11.232.250	1.058.356	17.862.579
Depreciation	926.411	1.613.287	197.398	2.737.096
Balance at 31.12.2014	6.498.384	12.845.537	1.255.754	20.599.675
Depreciation	940.332	1.652.500	196.546	2.789.378
Sold	0	0	(12.915)	(12.915)
Balance 31.12.2015	7.438.716	14.498.037	1.439.385	23.376.138

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13. Fixed assets in operation, contd.:

	Substations	Transmission lines	Other	Total
Carrying amount				
1.1.2014	21.577.057	38.884.227	2.736.337	63.197.621
31.12.2014	23.289.985	37.549.670	2.931.728	63.771.382
31.12.2015	34.013.379	49.578.114	2.836.066	86.427.559
Carrying amount without revaluation				
1.1.2014	19.182.702	27.493.585	2.736.337	49.412.624
31.12.2014	21.021.349	26.742.393	2.931.728	50.695.470
31.12.2015	20.769.273	27.024.684	2.836.066	50.630.023

Rateable value and insurance value

The rateable value of the Company's real property amounts to upwards of ISK 3.2 billion (2014: ISK 3.2 billion). Assessed value for the same property's fire insurance amounts to ISK 5.8 billion (2014: ISK 5.5 billion) and book value amounts to ISK 3.9 billion (2014: ISK 4.0 billion). The insurance value of the Company's assets amounts to ISK 59.4 billion (2014: ISK 53.5 billion), excluding transmission lines and cables, which are insured by an emergency insurance fund. The Company's emergency insurance amounts to ISK 117.1 billion (2014: ISK 113.1 billion).

Projects under construction:

	2015	2014
Balance at 1.1.	809.211	1.086.550
Additions	3.248.842	1.765.113
Transferred to fixed assets in operation	(1.120.493)	(2.156.987)
Transferred from intangible assets	83.229	114.535
Balance at 31.12.	3.020.789	809.211

14. Intangible assets:

See accounting policies in note 34d and 34h

	Capitalised development cost	Software	Total
Cost			
Balance at 1.1.2014	1.551.422	427.499	1.978.921
Additions	349.717	82.153	431.870
Transferred to projects under construction	(114.535)	0	(114.535)
Balance at 31.12.2014	1.786.604	509.652	2.296.256
Additions	363.631	62.026	425.657
Transferred to projects under construction	(83.229)	0	(83.229)
Balance at 31.12.2015	2.067.006	571.678	2.638.684
Amortisation and impairment losses			
Balance at 1.1.2014	295.796	290.131	585.927
Amortisation and impairment losses	211.376	19.258	230.634
Balance at 31.12.2014	507.172	309.389	816.561
Amortisation and impairment losses	101.830	31.225	133.055
Balance at 31.12.2015	609.002	340.614	949.616

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14. Intangible assets, contd.:

Carrying amount

1.1.2014	1.255.626	137.368	1.392.994
31.12.2014	1.279.432	200.263	1.479.695
31.12.2015	1.458.004	231.064	1.689.068

Development costs are reviewed each year by the management of Landsnet hf. and are examined for any indications of impairment. If the management believes that impairment has occurred, that development cost is expensed as impairment.

15. Investment in subsidiary

See accounting policies in note 34e

The breakdown of investment in subsidiary is as follows:

	31.12.2015 Share	31.12.2015 Carrying amount	31.12.2014 Share	31.12.2014 Carrying amount
Landsnet ehf.	100,00%	500	100,00%	500

The Company's share in Landsnet ehf. is stated at cost as the firm has not conducted any operations from its establishment.

16. Investment in associates

See accounting policies in note 34f

The breakdown of investment in associates is as follows:

	2015 Share in net earnings	2014 Share in net earnings	31.12.2015 Carrying amount	31.12.2014 Carrying amount
Orkufjarskipti hf. 50%	19.730	38.303	726.939	707.209

17. Inventories

See accounting policies in note 34g

Inventories are spare parts and material inventories. No write-down due to the Company's inventories is recognised in the financial statements for the year 2015 nor for the year 2014.

18. Trade and other receivables

See accounting policies in note 34b

Trade and other receivables:

	31.12.2015	31.12.2014
Trade receivables	855.217	838.817
Other receivables	154.752	282.846
Trade and other receivables total	1.009.969	1.121.663

19. Marketable securities

See accounting policies in note 34b

Marketable securities held by the Company are listed on a stock exchange. They are liquid but cannot be classed as cash because their maturity is more than three months. The measurements of marketable securities are categorised as Level 1 fair value.

20. Cash and cash equivalents

See accounting policies in note 34b

Cash and cash equivalents:

Bank deposits in Icelandic kronas	1.930.314	1.648.951
Bank deposits in foreign currency	6.141.820	10.585.712
Cash and cash equivalents total	8.072.134	12.234.663

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21. Equity

See accounting policies in note 34b

Share capital

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

Revaluation account

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

Statutory reserve

Under the Public Limited Companies Act, 25% of the nominal value of the Company's share capital must be held in a statutory reserve, which is not permitted to be used to pay dividends to shareholders. 10% of each year's profit must be deposited in the reserve until it amounts to 10% of the nominal value of the share capital, when the percentage deposited becomes 5%.

Dividends

The Company paid no dividends in 2015 for the financial year 2014, nor in the year 2014 for the financial year 2013.

22. Earnings per share

See accounting policies in note 34o

	2015	2014
Basic and diluted earnings per share:		
Profit to shareholders	4.009.821	3.762.241
Weighted average number of ordinary shares at 31 December	5.902.733	5.902.733
Basic and diluted earnings per share	0,68	0,64

23. Interest-bearing loans and borrowings

See accounting policies in note 34b

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

	31.12.2015	31.12.2014
Long-term liabilities		
Indexed bond loan from parent company in ISK, fixed interest	38.658.090	44.692.176
Loan agreement in CHF, LIBOR + margin	4.971.593	5.639.308
Indexed bond loan in ISK, fixed interest	5.176.967	5.234.862
	48.806.650	55.566.346
Current maturities on long-term liabilities	(943.924)	(919.008)
Interest-bearing long-term liabilities total	47.862.726	54.647.338
Short-term liabilities		
Short-term loans from parent company specifies as follows:		
Accrued interest of long-term liabilities with parent company	1.265.838	1.463.420
Short-term loans from parent company total	1.265.838	1.463.420

The bond loan from the parent company is an inflation-indexed bullet loan maturing in 2020 with interest payable once per year. The Company made repayments on this debt in the amount of ISK 6,895 million during the year. Inflation-indexed bond loans from third parties consist of a 25-year superannuation loan maturing in 2034 and are listed on Nasdaq Iceland. The loan agreement denominated in Swiss francs (CFH) is a bond with equal instalments and maturing in 2022.

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23. Loans and borrowings, contd.:

Terms of interest-bearing loans and borrowings

Debts in foreign currencies:

		31.12.2015		31.12.2014	
	Final maturity	Weighted avg. rate	Carrying amount	Weighted avg. rate	Carrying amount
Debt in CHF	2022	0,05%	4.971.593	0,30%	5.639.308
Debt in ISK:					
Indexed	2020 - 2034	4,30%	43.835.057	4,30%	49.927.038
Total interest-bearing loans and borrowings			48.806.650		55.566.346

Maturities by year of interest-bearing loans and borrowings:

Year 2016/2015	943.924	919.008
Year 2017/2016	952.989	927.468
Year 2018/2017	962.513	936.356
Year 2019/2018	972.519	945.693
Year 2020/2019	39.641.122	955.504
Later	5.333.583	50.882.317
	48.806.650	55.566.346

24. Deferred tax liability

See accounting policies in note 34n

The breakdown of deferred tax liability is as follows:	2015	2014
Deferred tax liability at 1 January	2.674.787	2.331.443
Calculated income tax for the year	998.777	931.155
Deferred tax liability due to revaluation of fixed assets	4.684.344	0
Income tax payable	(1.023.063)	(587.811)
Deferred tax liability at 31 December	7.334.845	2.674.787

The breakdown of deferred tax liability was as follows at year-end:	31.12.2015	31.12.2014
Fixed assets in operation	7.286.054	2.604.009
Intangible assets	200.693	189.042
Other assets	20.302	20.913
Provision due to site restoration	(181.341)	(163.953)
Other obligations	(82.269)	(84.206)
Unrealized exchange rate difference	91.406	108.982
Deferred tax liability at 31 December	7.334.845	2.674.787

25. Deferred income

Deferred income is recognised with regard to connection charges paid by electricity buyers to the Company during the year. At year-end, deferred income amounted to ISK 395 millon (2014: 369 million). The part of deferred income that will be recognised in the income statement next year is recognised in current liabilities. Connection charges recognised in profit or loss for 2015 amounted to ISK 15 million (2014: 15 million).

26. Provision due to site restoration

See accounting policies in note 34j

Change in the provision due to site restoration is specified as follows:	2015	2014
Balance at 1.1.	819.766	775.163
Present value for the year reversed	86.937	43.699
Increase in provision	0	904
Balance at 31.12.	906.703	819.766

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26. Provision due to site restoration, contd.:

The initial value of property, plant and equipment includes the estimated cost of the demolition thereof after use. The estimated demolition cost of lines has been valuated and discounted based on life-cycle criteria. The discounted value is recognised as a provision under long-term liabilities. In the income statement, the change in the discounting provision, which is based on a 6.4% interest rate (2014: 6.9%), is reported under financial expenses, in addition to depreciation under operating expenses.

27. Pension fund obligation

See accounting policies in note 34i

The Pension Fund for State Employees calculates at the end of each year the benefit plan obligation accrued for the year. Actuary assessment is based on the accrued obligation for the year being discounted at year-end on the basis of the annual interest rate generally used to assess pension fund obligations. The present annual rate is 3.5%. A total of ISK 1 million is expensed in relation thereto for 2015 (2014: 7 million), but the accrued benefit plan obligation is paid in full each year.

28. Trade and other payables

See accounting policies in note 34b

Trade and other payables are specified as follows:	**31.12.2015**	**31.12.2014**
Trade payables	890.951	847.191
Other payables	409.198	337.572
Trade and other payables total	1.300.149	1.184.763

29. Financial instruments

Overview

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

- Credit risk
- Liquidity risk
- Market risk

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

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

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

Credit risk

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

Trade and other receivables

The Company’s main customers are electricity generating companies, distribution system operators and power-intensive consumers. The Company's largest customers are also shareholders in the Company. Approximately 86% (2014: 86%) of the Company's transmission income derives from the Company's shareholders.

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29. Financial instruments, contd.:

Highest possible loss due to credit risk

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

	31.12.2015	31.12.2014
Long-term note	124.031	23.286
Receivables from parent company	614.695	702.735
Trade and other receivables	1.003.607	1.110.020
Market securities	733.824	470.971
Cash and cash equivalents	8.072.134	12.234.663
Highest possible loss due to credit risk total	10.548.291	14.541.675

Impairment losses

No impairment loss has been recognised in relation to accounts receivable at year-end; nor has loss on receivables been expensed during the year, which is based on the management's experience. The Company's collection issues are reviewed on a regular basis.

Liquidity risk

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

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

31.12.2015	**Carrying amount**	**Contractual cash flow**	**Within 12 months**	**1-2 years**	**2-5 years**	**After 5 years**
Non-derivative financial liabilities:						
Long-term liabilities from parent comp.	39.923.928	46.795.618	1.627.506	1.627.506	43.540.606	0
Long-term liabilities	10.148.560	13.950.583	1.205.815	1.221.610	3.646.818	7.876.340
Trade and other payables	1.300.149	1.300.149	1.300.149	0	0	0
	51.372.637	62.046.350	4.133.470	2.849.116	47.187.424	7.876.340
31.12.2014						
Non-derivative financial liabilities:						
Long-term liabilities from parent comp.	46.155.596	55.981.420	1.881.541	1.881.541	5.644.622	46.573.716
Long-term liabilities	10.874.170	13.942.350	1.205.789	1.202.673	3.374.244	8.159.644
Trade and other payables	1.184.763	1.184.763	1.184.763	0	0	0
	58.214.529	71.108.533	4.272.093	3.084.214	9.018.866	54.733.360

Market risk

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

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29. Financial instruments, contd.:

Currency risk

Currency risk is the risk of a loss because of unfavorable changes in the rate of currencies. The Company is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than the Company's functional currency. The Company's functional currency is the Icelandic króna (ISK) and therefore a currency risk arises from the net cash flow and opening balance in currencies other than ISK. Supstantial part of the Company's income derives from US dollars. In 2015, 59.8% (2014: 58.8%) of the Company's total revenue was in USD while purchases were mainly in ISK but a portion of its purchases is made in other currencies than Icelandic króna (ISK), mainly in euro (EUR) and US dollars (USD). The main currencies posing a foreign exchange risk are the USD and the Swiss Francs (CHF). In 2016, it is estimated that 56.8% of the Company's total revenue will be in USD.

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

The Company's currency risk on borrowings denominated in Swiss Francs (CHF), is partly hedged against its revenues. The interest rates on these borrowings are on average lower than those on the Company's ISK-denominated borrowings.

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

	EUR	CHF	USD
31.12.2015			
Cash and cash equivalent	88.022	1.648.013	4.348.779
Trade and other receivables	568	0	334.498
Other long-term liabilities	0	(4.971.593)	0
Trade and other payables	(70.608)	0	(907)
Net currency risk	17.982	(3.323.580)	4.682.370
31.12.2014			
Cash and cash equivalent	7.177	8.476	10.509.162
Trade and other receivables	526	0	277.192
Other long-term liabilities	0	(5.639.308)	0
Trade and other payables	(80.814)	(5.569)	(3.788)
Net currency risk	(73.111)	(5.636.401)	10.782.566

	Av. exch. rate for the year		Year-end exch. rate	
	2015	2014	31.12.2015	31.12.2014
Currency risk				
EUR	146,30	154,86	141,32	154,27
CHF	137,08	127,50	130,50	128,29
USD	131,85	116,75	129,59	126,90

Sensitivity analysis

A 10% strengthening of the ISK against the following currencies at 31 December would have increased (decreased) after-tax profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2014.

	31.12.2015	31.12.2014
EUR	(1.439)	5.849
CHF	265.886	450.912
USD	(374.590)	(862.605)

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

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29. Financial instruments, contd.:

Interest rate risk

The Company´s interest rate risk arises from interest bearing assets and liabilities. The Company's borrowings bear both floating interest and fixed inflation-indexed interest. The majority of the Company's borrowings bear fixed inflation-indexed interest, cf. Note 23. At year end 2015, the proportion of liabilities with floating interest rates was 10%, same as at year end 2014.

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

	Carrying amount	
	31.12.2015	**31.12.2014**
Financial instruments with floating interest rate		
Financial assets	8.805.958	12.728.920
Financial liabilities	(4.971.593)	(5.639.308)
	3.834.365	7.089.612
Financial instruments with fixed interest rate		
Financial assets	124.031	0
Financial liabilities	(43.835.057)	(49.927.038)
	(43.711.026)	(49.927.038)

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

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

Cash-flow sensitivity analysis for floating interest rate instruments

An increase in interest rates of 100 basis points at the reporting date would have increased (decreased) equity and profit or loss after tax by the amounts stated below. If interest rates had decreased by 100 basis points, the effect would have had the equal but opposite effect on profit or loss after tax. This analysis assumes that all other variables, in particular the exchange rates, remain constant. The analysis was performed in the same manner for the year 2014.

	Earnings	
	100bp increase	**100bp decrease**
31.12.2015		
Financial instruments with floating interest rates	44.099	(84.334)
Cash flow sensitivy (net)	44.099	(84.334)
31.12.2014		
Financial instruments with floating interest rates	43.360	(77.010)
Cash flow sensitivy (net)	43.360	(77.010)

Fair value

Fair value versus carrying amounts

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

	31.12.2015		31.12.2014	
	Carrying amount	**Fair value**	**Carrying amount**	**Fair value**
Long-term liabilities from parent company	(38.658.090)	(40.631.127)	(44.692.176)	(47.580.197)
Other long-term liabilities	(10.148.560)	(10.293.830)	(10.874.170)	(11.907.963)
	(48.806.650)	(50.924.957)	(55.566.346)	(59.488.160)

The fair values of other financial assets and liabilities are equivalent to its carrying amounts.

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29. Financial instruments, contd.:

Interest rate in valuation of fair value

Where applicable, expected contractual cash flow is discounted using the interest rate on government bonds plus a 1% margin on the reporting date. Margin of 0,4% was used in discounting expected contractual cash flow in the year 2014.

Classification of financial assets and liabilities

The following table shows the Company's classification of financial assets and liabilities:

	Financial assets and liabilities designated at fair value	Loans and receivables	Financial liabilities at amortised cost	Carrying amount
31.12.2015				
Long-term note		117.670		117.670
Receivables from parent company		614.695		614.695
Trade and other receivables		1.009.969		1.009.969
Marketable securities	733.824			733.824
Cash and cash equivalents		8.072.134		8.072.134
	733.824	9.814.468	0	10.548.292
Loans from parent company			39.923.928	39.923.928
Other long-term liabilities			10.148.560	10.148.560
Trade and other payables		1.300.149		1.300.149
	0	1.300.149	50.072.488	51.372.637
31.12.2014				
Long-term note		11.643		11.643
Receivables from parent company		702.735		702.735
Trade and other receivables		1.121.663		1.121.663
Marketable securities	470.971			470.971
Cash and cash equivalents		12.234.663		12.234.663
	470.971	14.070.704	0	14.541.675
Loans from parent company			46.155.596	46.155.596
Other long-term liabilities			10.874.170	10.874.170
Trade and other payables		1.184.763		1.184.763
	0	1.184.763	57.029.766	58.214.529

Indexation risk

Indexation risk derives from changes in the Consumer Price Index, which affect the financial position and cash flows of inflation-indexed financial instruments. The majority of the company's loans are denominated in inflation-indexed ISK.

Cash-flow sensitivity analysis for the Consumer Price Index

An increase in the Consumer Price Index of 100 basis points at the reporting date would have increased (decreased) equity and profit or loss after tax by the amounts stated below. If the Consumer Price Index had decreased by 100 basis points, the effect would have had the equal but opposite effect on profit or loss after tax. This analysis assumes that all other variables, in particular the exchange rates, remain constant. The analysis was performed in the same manner for the year 2014.

	Earnings	
	100bp increase	100bp decrease
31.12.2015		
Inflation-indexed financial instruments	(392.074)	392.074
Cash flow sensitivy (net)	(392.074)	392.074

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29. Financial instruments, contd.:

31.12.2014

Inflation-indexed financial instruments	(416.024)	416.024
Cash flow sensitivy (net)	(416.024)	416.024

Other market price risk

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

Capital management

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

30. Operating leases

The Company as lessee

The Company leases a part of the transmission structures it uses from domestic energy companies. The lease agreements have an indeterminate lease term and the lease price is determined by the National Energy Authority. Expensed lease payments in 2015 amounted to ISK 132 million (2014: ISK 143 million).

31. Related parties

Definition of related parties

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

Transactions with senior management

(i) Payments to senior management

In addition to receiving salaries, the CEO and Managing Directors (Vice Presidents) of the Company receive a contribution to a defined benefit pension fund. They also receive a car allowance. Management's salaries are accounted for in Note 9.

Other transactions with related parties

	2015	2014
Sale of goods and services:		
Landsnet's parent company and its subsidiaries	8.484.277	7.428.440
Landsnet's other shareholders	5.383.422	4.900.660
Sale of goods and services to related parties total	13.867.699	12.329.100
Cost of goods and services:		
Landsnet's parent company and its subsidiaries	2.431.128	1.680.357
Landsnet's other shareholders	482.720	475.008
Cost of goods and services to related parties total	2.913.848	2.155.365

In addition to the costs outlined above, the Company paid ISK 1,939 million (2014: ISK 1,859 million) in interest to its parent company. The Company also received minor interest income from a long-term receivable from an affiliated company.

Balance:

Trade receivables and trade payables with related parties are as follows:

	31.12.2015		31.12.2014	
	Receivables	Payables	Receivables	Payables
Landsnet's parent company and its subsidiaries	614.695	0	702.735	0
Landsnet's other shareholders	549.584	0	543.582	0
	1.164.279	0	1.246.317	0

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31. Related parties, contd.:

Other receivables and payables with related parties are as follows:

	31.12.2015	31.12.2014
Interest-bearing long-term note to associate	124.031	23.286
Interest-bearing liabilities to parent company, see note 23	(38.658.090)	(44.692.176)
Accrued interest payable to parent company	(1.265.838)	(1.463.420)
	(39.799.897)	(46.132.310)

32. Financial ratios

The company's key financial ratios:

Financial performance:	2015	2014
EBIT	7.491.143	6.174.152
EBITDA	10.413.576	9.141.882

Financial position:	31.12.2015	31.12.2014
Current ratio – current assets/current liabilities	2,42	3,63
Equity ratio – equity/total assets	40,7%	23,5%
Return on equity	13,1%	21,7%

33. Basis of measurement

The financial statements have been prepared on the historical cost basis, except for:

- The Company's transmission system is recognised at a revalued amount, which was its fair value at revaluation date in the year 2015.
- Financial assets at fair value through profit and loss are recognised at fair value.

34. Accounting policies

The following accounting methods have been consistently applied to all disclosed periods in the financial statements. Costs have been reclassed between Transmission cost, System operation and Other operating expenses and comparison figures have been restated accordingly. Changes in presentation does not affect the Companys profit or loss nor equity.

The following table of contents shows the pages on which various accounting policies may be found.

a. Foreign currency 24
b. Financial instruments 25
c. Property, plant and equipment 26
d. Intangible assets 27
e. Investment in subsidiaries 27
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g. Inventories 27
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34. Accounting policies, contd.:

a. Foreign currency

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

b. Financial instruments

(i) Non-derivative financial instruments

The Company initially recognises loans, receivables and cash and cash equivalents on the date that they are originated. All other financial assets (including assets designanted as at fair value through profit or loss) are recognised initially on the trade date, which is the date that the Company becomes a party to the contractual provisions of the instrument.

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest is such transferred financial assets that is created or retained by the Company is recognised as a separate asset or liability.

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

The Company classifes non-deravative financial assets into the following catagories: financial assets at fair value through profit or loss and loans and receivables.

Financial assets at fair value through profit or loss

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

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables comprise trade and other receivables.
Cash and cash equivalents comprise cash balances and call deposits.

(ii) Non-derivative financial liabilities

The Company initially recognises debt securities issued and subordinated liabilities on the date that they are originated. All other financial liabilities (including liabilities designated as at fari valure through profit or loss) are recognised initially on the trade date, which is the date that the Company becomes a party to the contractual provisions of the instrument.

The Company derecognises a financial liability when its contractual obligations are discharged, cancelled or expire.

The Company classifies non-derivative financial liabilities into the other financial liabilities category. Such financial liabilities are recognised initially at fair value less any directly attributable transaction costs. Subsequent to initial recognition, these financial liabilities are measured at amortised cost using the effective interest method.

Other financial liabilities comprise loans and borrowings and trade and other payables.

(iii) Share capital

Share capital is classified as equity. Incremental costs directly attributable to the issue of shares are recognised as a deduction from equity.

34. Accounting policies, contd.:

c. Property, plant and equipment

(i) Fixed assets in operation

Items of fixed assets in operation other than transmission lines and substations are measured at cost less accumulated depreciation and impairment losses.

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

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

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

Any gain on disposal of an item of fixed assets in operating (calculated as the difference between the net proceeds from disposal and the carrying amount of the item) is recognised in profit or loss as other income but any loss on disposal of an item of fixed assets in operation is recognised in profit or loss as other operating expenses.

(ii) Transmission structures under construction

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

(iii) Leased assets

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

(iv) Subsequent costs

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

(v) Depreciation

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

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

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

34. Accounting policies, contd.:

d. Intangible assets

(i) Developement cost

Developement cost is capitalised within fixed assets. This cost consists largely of expenses relating to exploration for transmission line sites, preparation for transmission structures and environmental impact assessments of proposed projects. Cost of capital attributable to developement costs is capitalised except when there is a extended delay on the projects. Developement cost is not depreciated at this stage, but possible impairment losses have been considered, as discussed in Note 35h.

The Company has concluded agreements whereby the prospective buyers of electricity shall bear all expenses of the project if it is cancelled.

When the decision to construct a transmission structure has been made and all neccessary approvals have been obtained, the development cost of the transmission structure is capitalised in fixed assets as a project under construction.
At each accounting date, capitalised development cost is reviewed by management and impairment is recognised if premises for the recognition of development cost no longer exist.
Expenditure on research activities is recognised in profit or loss when incurred.

(ii) Software and other intangible assets

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

(iii) Amortisation

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets. The estimated useful lives of software are 4 years.

e. Investment in subsidiaries

The Company has one subsidiary, Landsnet ehf. The financial statements of the two companies are not consolidated and the holding is recognised at historical cost. The subsidiary has had no activity since its establishment. The share capital of the subsidiary is ISK 500 thousand.

f. Investment in associates

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

g. Inventories

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

h. Impairment

(i) Financial assets

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

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate.
Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss.

34. Accounting policies, contd.:

(ii) Other assets

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

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

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are 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 asset.

i. Pension payments

(i) Defined contribution plans

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

(ii) Defined benefit plans

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

j. Provisions

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

(i) Site restoration

The Company has estimated the cost of demolition of current line lots. The estimation is based on expert assessment. The demolition cost has been discounted based on the estimated useful life of the Company's power transmission lines. The discounted value is entered, on the one hand, as an increase for the relevant asset and, on the other hand, as an obligation in the balance sheet.

k. Revenue

Income from electricity transmission is recognised in the income statement on the basis of measured delivery during the year. Other revenue is recognised as earned or delivered. A revenue cap is set for the Company on the basis of Article 12 of the Electricity Act No. 65/2003.

l. Lease payments

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

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

34. Accounting policies, contd.:

m. Finance income and expenses

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

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

Foreign currency gains and losses are reported on a net basis.

n. Income tax

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

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

A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised. The income tax rate is 20%.

o. Earnings per share

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

p. Segment reporting

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

q. New standards and interpretations thereof

The Company has implemented all International Financial Reporting Standards, amendments thereto and interpretations confirmed by the EU at year-end 2015 and that apply to its operations. The Company has not implemented standards, amendments thereto or interpretations entering into effect after year-end 2015 but allowed to be implemented sooner. The effect thereof on the Company's financial statements has not been fully determined but is considered to be insubstantial.

Corporate Governance Statement

Role of Landsnet hf.

Under the Electricity Act No. 65/2003, Landsnet's role is to operate an electricity transmission system and administer its system management. The Company must ensure and maintain the capabilities of the transmission system on a long-term basis and ensure the electricity system's operational security. Landsnet's role is also to maintain a balance between electricity supply and demand at all times and manage the settlement of electricity flows countrywide. In addition, the Company is charged with promoting an efficient electricity market.

Corporate governance

The Board of Directors of Landsnet hf is committed to maintaining good corporate governance and complying with the Guidelines on Corporate Governance issued by the Icelandic Chamber of Commerce, NASDAQ OMX Iceland and the Confederation of Icelandic Employers in May 2015. The Board adopts Rules of Procedure defining the scope of its powers and duties vis-à-vis the President & CEO. The current Rules of Procedure were confirmed at the Annual General Meeting of Landsnet held on 27 June 2013 and are available for inspection at the Company's head office.

Internal control and risk management

To ensure that Landsnet's financial statements accord with generally accepted accounting practice, the Company has emphasised well-defined areas of responsibility, proper segregation of duties, regular reporting and transparency in its activities. The process of monthly reporting and reviews for individual departments is an important part of monitoring financial performance and other key performance indicators. Monthly financial results are produced and submitted to the Company's Board of Directors. The Board of Directors monitors the Company's financial risk and receives regular reports thereon. Information on risk management is provided in Note 29 to the annual financial statements.

Corporate values and Code of Ethics

Landsnet's employees are obliged to abide by the Company's values in all their activities. Its corporate values are informed by its role and future vision and provide the foundation for the corporate culture for which the Company strives. Landsnet's values are: respect, cooperation and responsible.

Landsnet's Code of Conduct was approved at a meeting of the Board of Directors on 25 July 2005 and is designed to encourage honesty, justice and fairness among staff towards each other, the Company and its customers. The Code is also intended to promote the trust and confidence of customers and the general public in Landsnet, as well as to limit the risk of reputational damage. The Board of Directors is of the view that a clear Code of Conduct that is duly observed in the Company's day-to-day activities forms the basis of its success and future growth. Landsnet's Code of Conduct applies to all its employees, including the Directors and the President & CEO. The Code of Conduct is available for inspection at Landsnet's head office.

Future vision and policy focus areas

Landsnet's future vision is an "electrified future in tune with society". Modern societies increasingly rely on a secure supply of electricity, making it necessary to strengthen the transmission system. Landsnet is committed to ensuring a secure supply of electricity in the future and maintaining a balance between generation and consumption. We will work to form as broad a consensus as possible on the way ahead, with due consideration for societal needs at any given time. We will treat the natural environment responsibly. Landsnet places priority on fostering a healthy electricity market environment and efficient use of financial resources.

Landsnet's corporate policy is based on the Company's role and future vision. The policy is reflected in our organisational and policy focus areas, which will guide our activities for the coming years.

Policy focus areas

Landsnet has defined a fourfold promise to society in the form of policy focus areas. These reflect our corporate policy and the milestones that must be achieved along the way to reach our future vision. The promises are:

1. A secure electricity supply – a high-quality, secure grid for the future

Landsnet is committed to ensuring that that all citizens, whether individuals, companies or public bodies, have access to electricity in the quantity and quality needed at all times. Future priorities are defined, including reliability, security and quality criteria. Landsnet will work towards a broad consensus on the rationale underlying decisions on infrastructure development and investment.

2. In harmony with society and the environment

Building a social consensus on Landsnet's role and aims will be an important enabler of progress. Such a consensus requires an understanding among the general public that the grid is one of the mainstays of our society. Landsnet therefore works towards raising awareness of its role, activities and importance as one of modern society's fundamental facilities. This requires a focus on corporate social responsibility intertwined with our policies. The company will seek to initiate and maintain a continuous dialogue with stakeholders – a dialogue characterised by honesty, responsibility, open-mindedness, mutual respect and a co-operative spirit.

3. Prudent use of funds – effective operations

Grid strengthening and a focus on bottleneck elimination will support a healthy investment environment for participants in the energy market and serve to reduce waste in the electricity sector as a whole. We take a "cradle to grave" approach to the grid when making decisions on investment and activities, with due consideration paid to the national interest. We manage and use the funds entrusted to us in a prudent manner, including proper stewardship of financial and other resources and cost-effective grid development, construction and operation. Our operations are streamlined.

4. A clear image

Landsnet seeks to build a clear corporate image of professionalism, trust and social responsibility. We strive to be a modern and forward-looking company that looks for a variety of solutions with an open mind in the overall public interest. We are committed to thorough, readily understandable and honest communication of information.

Organisational focus areas

Landsnet has defined a fourfold promise to society in the form of policy focus areas. These reflect our corporate policy and the milestones that must be achieved along the way to reach our future vision. The promises are:

1. Strategic management and organisation

Landsnet's organisational structure must support its role, policy and activities in a clear and targeted manner, including the company's promises to its customers and society at large. We place importance on a simple and effective organisational structure with strong main functional divisions and clear lines of responsibility that allow for a holistic overview of processes. In parallel, focus is placed on continuous improvements to simplify processes and step up efficiency and effectiveness.

2. A good workplace

Landsnet shows due care for all its employees. This includes providing them with opportunities to engage in exciting work and develop their skills in a professional and ambitious environment. We are committed to creating a good workplace whose culture and relations are shaped by our corporate values and whose employees are afforded opportunities to develop and progress. Importance is attached to cultivating a shared outlook among our staff on the company's values, purpose and role. Our corporate culture is characterised by service-mindedness and due care for the needs of our customers, staff, society and the environment.

Landsnet's management structure

The main units of Landsnet's management structure are the Board of Directors and the Executive Committee. Key roles are also performed by two committees appointed by the Board of Directors: the Audit Committee and the Remuneration Committee..

Relations between shareholders and the Board of Directors/management

Under the provisions of Act No. 75/2004 on the Establishment of Landsnet and the Electricity Act No. 65/2003, the Company's Directors shall be independent in all respects from other companies engaging in the generation, distribution or sale of electricity, whether these companies are owners of the Company or not. The purpose of these provisions is to meet the statutory requirement that the transmission system operator maintains utmost impartiality and non-discrimination in its activities.

With respect to the Company's special status under Chapter III of the Electricity Act and its strict duties to maintain impartiality and non-discrimination, it should be reiterated that shareholders are not permitted to interfere in individual affairs relating to Landsnet's activities.

As a rule, the shareholders' involvement must be limited to general policy decisions taken at regular shareholders' meetings, e.g. on financial targets.

Board of Directors

The Board of Directors of Landsnet hf is the supreme authority in the Company's affairs between Annual General Meetings. The Board is responsible for the Company's policy-making and major decisions between shareholders' meetings, as specified in, e.g., the Rules of Procedure of the Board of Directors. The Board supervises all Company operations, and works to ensure that its activities are in proper and good order at all times. The Board ensures sufficient supervision of the Company's financial management and that its accounts and financial statements are in good order. The Board engages the Chief Executive Officer of the Company, whose salary and employment terms are decided by the Remuneration Committee.

Landsnet's Board of Directors consists of the following three members:

Geir A. Gunnlaugsson, Chairman of the Board

Geir A. Gunnlaugsson was born in 1943. He read mechanical engineering at the University of Iceland, earned an MSc degree in mechanical engineering from the Technical University of Denmark and a PhD from Brown University, USA. He was professor of mechanical engineering at the University of Iceland in 1975-1986. He was chief executive of Icelandic Metals in 1983-1987, Marel in 1987-1999 and Hæfi, chairman of Reyðarál in 2000-2002 and chief executive of Promens in 2003-2006. Mr Gunnlaugsson has sat on the board of numerous businesses, both Icelandic and foreign, as well as other organisations and institutions, and has extensive experience in business management in Iceland and overseas. Mr Gunnlaugsson has been a member of Landsnet´s Board of Directors from 31 March 2011.

Svana Helen Björnsdóttir, Director

Svana Helen Björnsdóttir was born in 1960. She pursued studies in electrical engineering at the University of Iceland. She read electrical engineering at the Technische Universität Darmstadt in Germany, from which she earned a Dipl.-Ing./MSc degree in electrical power engineering in 1987. Ms Björnsdóttir also holds a diploma in operations management from the University of Iceland. She founded the information security company Stiki in 1992 and is the CEO of Stiki. She was chairman of the Federation of Icelandic Industries. Ms Björnsdóttir was at the same time chairman of Akkur SI. In addition, she was a member of the Executive Committee and a board member of the Confederation of Icelandic Employers. Ms Björnsdóttir has sat on the board of numerous businesses, both Icelandic and foreign, as well as other organisations and institutions, and has extensive experience in business management in Iceland and overseas. Ms Björnsdóttir has been a member of Landsnet´s Board of Directors from 31 March 2009.

Ómar Benediktsson, Director

Ómar Benediktsson was born in 1959. He holds a cand. oecon. degree in business administration from the University of Iceland. He served in managerial positions in tourism and aviation for 30 years. At the beginning of 2012, he became CEO of Farice ehf, which operates the submarine telecommunications network linking Iceland with the rest of the world. Farice is also a key player in developing Iceland's emerging data centre industry. Mr Benediktsson has sat on the board of numerous businesses, both Icelandic and foreign, as well as other organisations and institutions, and has extensive experience in business management in Iceland and overseas. Mr Benediktsson has been a member of Landsnet´s Board of Directors from 29 March 2012.

The Alternate Director is Svava Bjarnadóttir

The Board of Directors held 18 meetings in 2015. All of the meetings were attended by all Board members except for two meetings where one member was absent. Two meetings were attended by an Alternate Director.

Landsnet´s CEO and Executive Committee

Duties of the President & CEO

The President & CEO is responsible for the Company's day-to-day activities. He/she is empowered to make decisions on all Company affairs not entrusted to others under Act No. 2/1995 and/or the Company's Articles of Association. The President & CEO conducts the operations of the Company in accordance with rules and/or decisions of the Board of Directors, the Articles of Association and the law. The President & CEO's signature constitutes an obligation on the Company's part. He/she is an authorised signatory of the Company ("procuration holder"). The President & CEO may grant power of attorney to other employees of the Company to exercise designated powers of his/her duties of office, provided that prior approval is obtained from the Board of Directors.

The President & CEO is responsible for detecting, measuring, monitoring and controlling risks relating to the Company's operations. The President & CEO must maintain an organisation chart of the Company that clearly delineates areas of responsibility, employees' powers and communication channels within the Company. The President & CEO shall set internal control targets in consultation with the Board and monitor the effectiveness of internal control mechanisms. The President & CEO prepares meetings of the Board of Directors together with its Chairman and reports regularly to the Board on the Company's activities and position.

Guðmundur Ingi Ásmundsson, CEO & President
Mr Ásmundsson was born in 1955. He took a degree in electrical engineering from the University of Iceland in 1980 and a master's degree in electrical power engineering from the Technical University of Denmark in 1982. He joined Landsvirkjun in 1982 as an engineer in the Operations department, later becoming chief engineer and Head of System Operations from 1993. He served as Landsnet's System Manager from the Company's founding on 1 January 2005 and Director of System Operations from 1 November 2005. Mr Ásmundsson became Deputy CEO of Landsnet on 1 January 2008 and CEO & President on 1 January 2015.

Members of Landsnet's Executive Committe in addition to CEO consists of:

Einar S. Einarsson, Head of Corporate Services & Communication
Guðlaug Sigurðardóttir, Head of Finance (CFO)
Íris Baldursdóttir, Head of System Operation
Nils Gustavsson, Head of Constructions & Grid Services
Sverrir Jan Norðfjörð, Head of Technology & Development

Audit Committee

The Board of Directors appoints the Audit Committee. The current Audit Committee of Landsnet consists of:
María Sólbergsdóttir, accountant, Chairman
Ómar Benediktsson, Director of Landsnet's Board
Svava Bjarnadóttir, Alternate Director of Landsnet's Board

The Audit Committee has adopted Rules of Procedure, which define the Committee's role as follows:
The Audit Committee shall, among other things, have the following role, regardless of the responsibilities of the Board of Directors, management staff or others in this area:

- Oversight of procedures for the preparation of financial statements.
- Oversight of the structures and functioning of the Company's internal controls, internal auditing, if applicable, and risk management.
- Oversight of the auditing of the annual financial statements and consolidated financial statements.
- Assessment of the independence of the Company's auditor or audit firm; monitoring of the work of the auditor or audit firm.

The Audit Committee also makes proposals for improvements and deliberates on matters at the Board's request. The Audit Committee annually submits a proposal to the National Audit Office for a certified public accountant or audit firm for the Company.

A total of 4 meetings were held in 2015, all of which were attended by all Committee members.

Remuneration Committee

The Board of Directors of Landsnet hf performs the role of the Company's Remuneration Committee. Landsnet hf has formulated a Remuneration Policy, which was approved at the Company's Annual General Meeting on 31 March 2011. The Remuneration Policy can be viewed on the Company's website. The business of the Remuneration Committee is transacted at meetings of the Board of Directors when applicable.