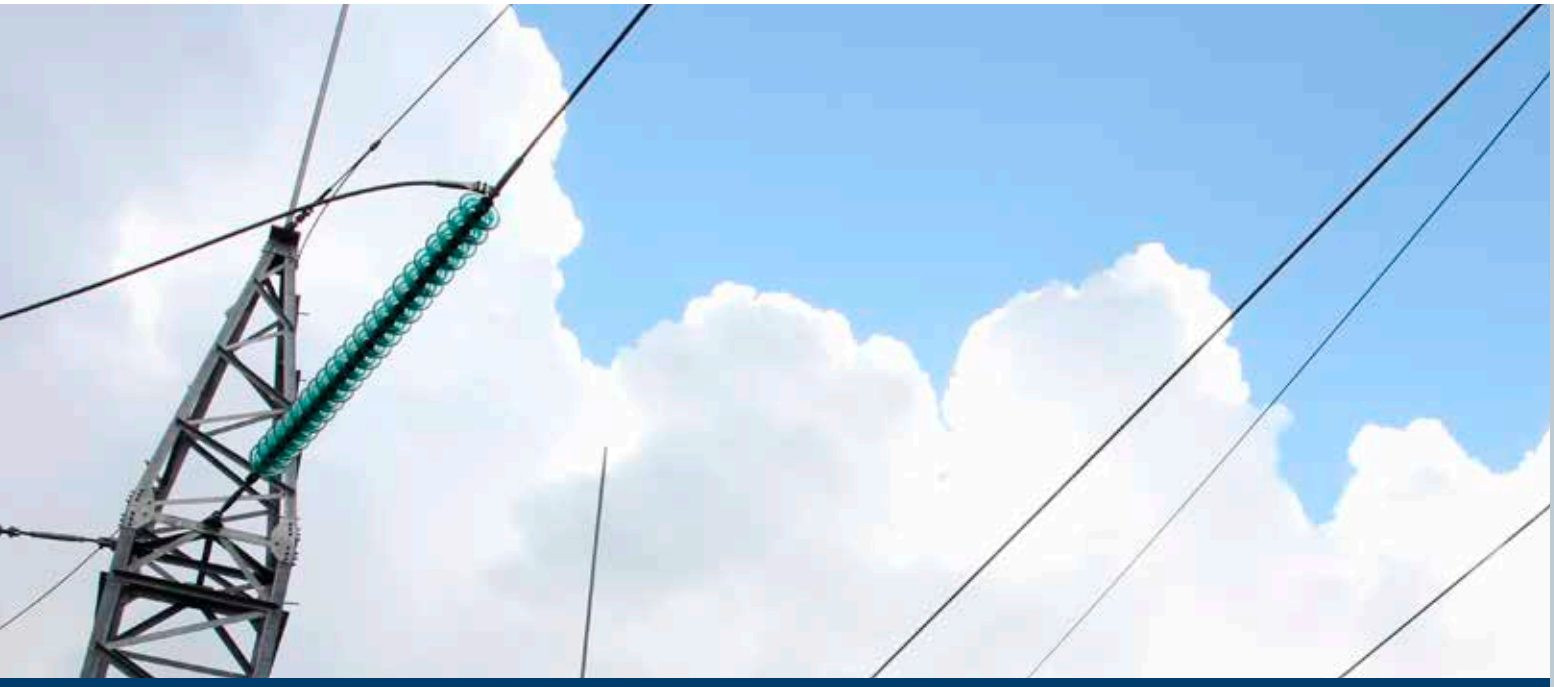
ANNUAL REPORT 2013

LANDSNET



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VOTTUN HF. ÍST ISO 9001
VOTTUN HF. ÍST ISO 14001
VOTTUN HF. OHSAS 18001

Certification

Landsnet's integrated and certified management system covers quality, environmental protection, electrical safety and occupational health and safety. Integrated management of these areas delivers better co-ordination of our work processes and more effective management of the company.

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Computer-generated images	Hornsteinar
English translation	Páll Hermannsson
Printing	Svansprent

“The current situation is unacceptable and will only deteriorate further while the cost for society increases if steps are not taken in the next immediate years to strengthen and further develop the grid

A pressing need for policy formulation

Statement by the Chairman and the President & CEO

Landsnet achieved a good performance in 2013, delivering an operating profit of ISK 2,183 million. Revenue was ISK 13,874 million and turnover was up 12% year-on-year. The tariff for distributors has remained stable in recent years and well below Iceland's inflation trend. The tariff for power-intensive consumers, which is denominated in US dollars, was raised at the beginning of 2013 following a tariff reduction phase in the preceding years, which was mostly in repayment of exchange-rate-driven profit that exceeded Landsnet's revenue cap after the collapse of the Icelandic króna in late 2008. The transmission tariff was corrected in accordance with the revenue cap and has in USD terms come down to a level comparable to that of early 2008. While no new transmission agreements were concluded in the year, transmission under existing agreements increased by 2.9%.

The company's interest-bearing debt stands at approximately ISK 56,003 million, of which 88.5% is denominated in ISK. About 79% of the total long-term debt consists of a start-up loan from our parent company on which no payments are due until 2020, an important factor for our cash position. A new funding policy was approved in the year that better reflects our revenue streams and provides the basis on which we will be remodelling our capital structure in the coming years.

Our financial performance for the year was in line with the revenue cap to which the company's profitability is subject. Our permitted return on equity is determined within this revenue cap and on the basis of a certain equity ratio decided by the regulator. The revenue cap is decided by the National Energy Authority in accordance with the provisions of the Electricity Act. The equity ratio allowed under the revenue cap is higher than our current equity ratio. This enables us to build our equity level in accordance with the revenue cap criteria, a key factor in bringing our equity position to a similar level to that of our counterparts in neighbouring countries. Our equity ratio stood at 19.9% at year-end and is approaching the company's initial equity ratio for the first time since its founding.

Clouds on the horizon

The number of grid disturbances in the year was similar to that of recent years. Outage minutes were considerably fewer than in the preceding year, or 17 minutes. Nonetheless, there are clouds on the horizon for the grid's general operation, as evidenced by the fact that the system had to be split into islands a total of 23 times in the year to protect it against shocks and minimise operational risk. Curtailments due to system constraints were active for a large portion of the year. This situation is unacceptable and will only deteriorate further while the cost for society increases if steps are not taken in the next immediate years to strengthen and further develop the grid.

System weaknesses are clearly evident from the substantial curtailments of transmission between North and South Iceland and the frequent splitting of the grid due to instability during the year, which affected voltage quality for numerous consumers. Problems in the grid's operation outside south-west Iceland have been on the increase and have reached a stage where our customers have sustained serious damage due to voltage and power fluctuations following grid disturbances. Landsnet had to pay tens of millions ISK in compensation last year as a result, with the scale and frequency of such incidents growing year by year.

Bottlenecks between North and South Iceland are curbing power generation capacity below potential, as generating companies are unable to co-ordinate the operation of water reservoirs in the most efficient way possible in their day-to-day activities or when required for the water resource management of individual areas. This reduces efficiency in the power system and prevents the grid from being able to react to major disturbances resulting from faults in the grid or power

stations. Increasing energy losses in the grid are also costly.

We have placed a strong emphasis on improving supply reliability in the regional networks. Such efforts have included strengthening the East Iceland network through voltage raising and the expansion of substations. In the West Fjords, we are constructing new substations at Ísafjörður and Bolungarvík, as the existing ones were in avalanche areas. In connection with this project, we are also building a new 10 MW automatic reserve station at Bolungarvík. A new sub-sea transmission cable was laid from the Icelandic mainland to the Westman Islands during the year, as the older cable was in a poor state. A new substation is due to be built at Akranes in the south-west of Iceland and more substations are scheduled for construction around the country over the next few years. We will continue with projects aimed to bring the supply reliability of the regional networks to par with other parts of the grid. Investment in the regional networks in 2011-2014 amounts to around ISK 7 billion.

We have tackled challenges in the grid's operation through innovation and smart grid solutions, which have helped to mitigate serious operational issues and minimise power outages. Examples of this include:

- A new Static VAR System at Grundartangi that balances out voltage fluctuations in the grid and increases its stability and transmission capacity
- Renewal of protection systems in the Regional Network
- Splitting the grid into islands to reduce the impact of disturbances using Wide Area Protection Systems and telecommunications
- In-depth analysis and planning for operational difficulties
- Research and development projects aimed to introduce risk management in the grid's real-time operation, including a number of projects in partnership with foreign transmission system operators and universities.

Whilst we have managed to reduce severe system impacts through the above measures, the system is reaching a critical point where substantial strengthening of the main grid is necessary if its operational security is not to be significantly compromised in the coming years.

The government must resolve the impasse

It has been Landsnet's aim in recent years to upgrade the grid considerably. Owing to disputes over underground cables versus overhead lines, however, we have not been able to upgrade the system in the north and east of Iceland as planned. As a result, our investment in recent years has been focused mostly on resolving local transmission constraints as opposed to main grid constraints, which have a much wider impact.

Last year saw a rise in power consumption in East Iceland due to a 100 MW switchover to renewable energy at fishmeal plants, which is pushing the transmission capacity limit of the Regional Network. Clearly, this consumption will be subject to heavy curtailment until the grid is upgraded. This is a pity, not least as the switchover from imported oil to domestic renewable energy is one of the major environmental issues of recent years. In view of these developments, we have redoubled our efforts to assess the environmental impact of constructing transmission infrastructure across the Sprengisandur highland plateau. Preparations also continue for the construction of new transmission lines between the Blanda and Fljótsdalur Power Stations.

In the absence of a definitive policy on undergrounding, further grid upgrading cannot be expected to start in the near future. Therefore, it is important for the government to formulate a policy on this important issue as soon as possible.

Landsnet is not opposed to undergrounding; our position is based on the Electricity Act's requirement that the most economically efficient option must always be taken. Like other stakeholders, we therefore call for a government policy on this major issue to enable us to build a grid fit for the future.

Geir A. Gunnlaugsson, Chairman of the Board

Þórður Guðmundsson, CEO & President

Key figures

	2009	2010	2011	2012	2013
System demand (GWh)	15,906	16,165	16,287	16,652	17,108
Transmission losses (GWh)	354	331	324	339	378
Transmission losses as a ratio of consumption	2.2%	2.0%	2.0%	2.0%	2.2%
Operating revenue	13,294	12,846	11,903	12,344	13,874
Investing activities	3,385	1,338	830	2,211	6,408
Investing activities as a ratio of operating revenue	25.5%	10.4%	7.0%	17.9%	46.2%
Earnings before interest and taxes (EBIT)	6,951	6,341	5,440	5,306	6,568
EBIT as a ratio of operating revenue	52.3%	49.4%	45.7%	43.0%	47.3%
General operating costs*	2,337	2,401	2,550	3,187	3,209
General operating costs as a ratio of operating revenue	17.6%	18.7%	21.2%	25.8%	23.1%
Profit	1,471	3,563	840	800	2,183
Profit as a ratio of operating revenue	11.1%	27.7%	7.1%	6.5%	15.7%
Assets	73,676	70,513	74,679	74,873	77,608
Equity	8,322	11,622	12,462	13,263	15,446
Liabilities	65,354	58,891	62,217	61,610	62,162
Return on equity**	20.2%	42.8%	7.2%	6.4%	16.5%
Equity ratio***	11.3%	16.5%	16.7%	17.7%	19.9%
Length of overhead transmission lines	3,071	3,054	3,055	3,055	3,061
Length of underground and sub-sea cables	109	146	147	147	158
Full-time equivalent positions at year-end	93	95	94	106	114

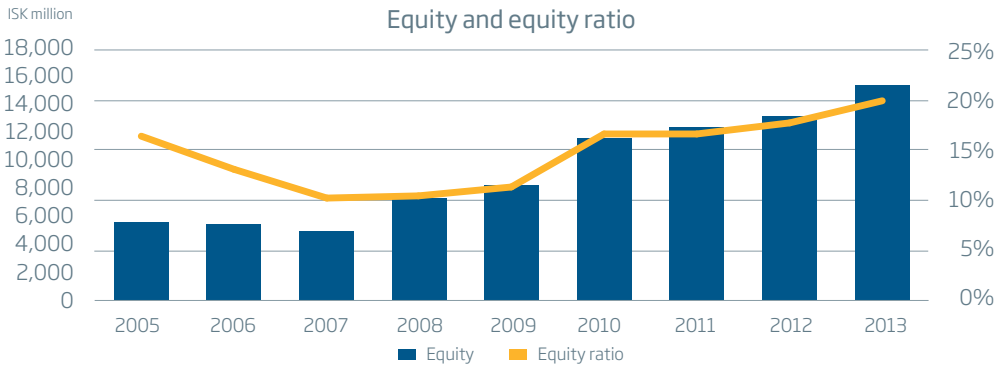
Amounts in ISK million

Calculation of key figures

* General operating costs = operating expenses – depreciation and amortisation – ancillary services and losses

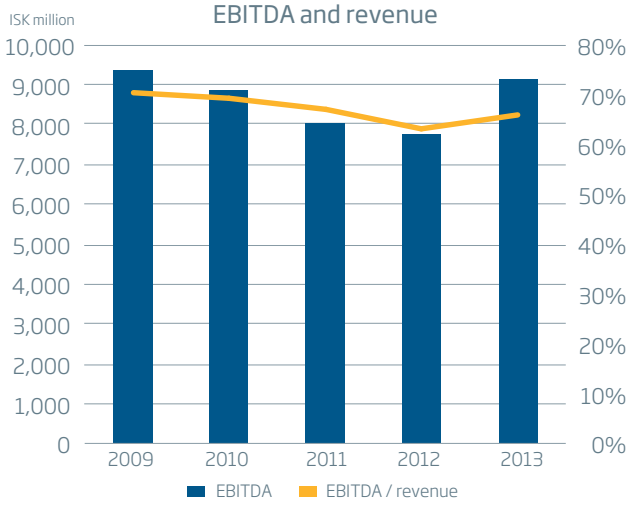
** Return on equity = profit/equity at beginning of year

*** Equity ratio = equity/assets

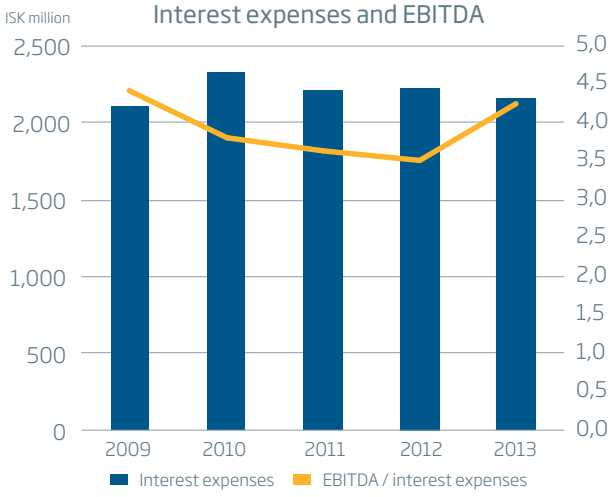


Transmission and transmission losses

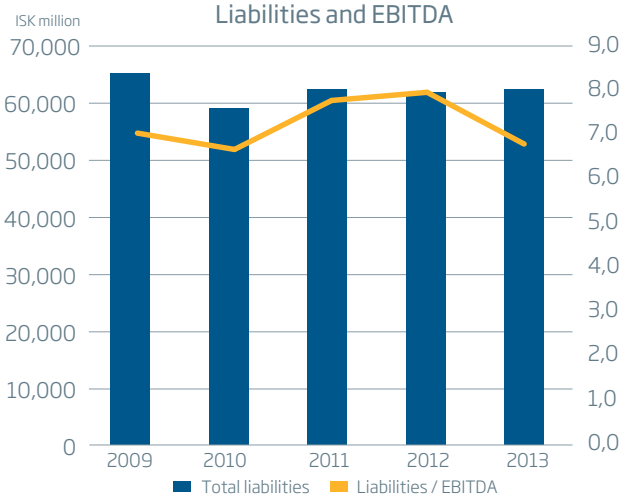
EBITDA and revenue



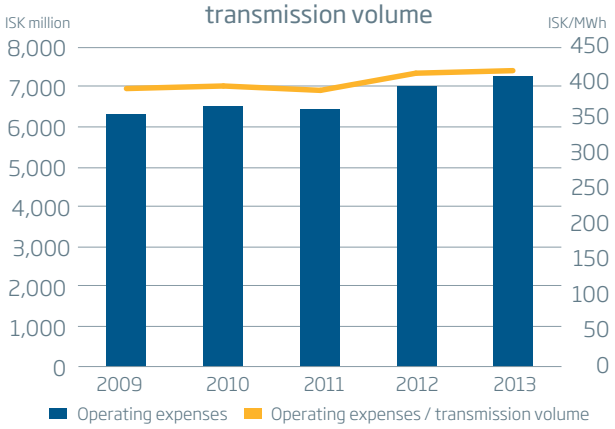
Interest expenses and EBITDA



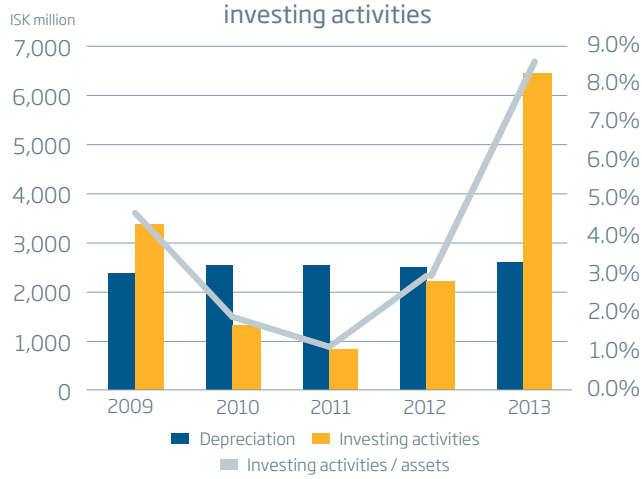
Liabilities and EBITDA



Operating expenses and transmission volume



Depreciation and investing activities



We transmit electricity

Our role is to be the Transmission System Operator of the Icelandic power system. Landsnet operates under a concession arrangement and is subject to regulation by the National Energy Authority, which determines the revenue cap on which the company's tariff is based. Our responsibilities are:

- Ensuring and maintaining the grid's capacities on a long-term basis and ensuring the grid's operational security
- Maintaining a balance between electricity supply and demand
- Managing the settlement of electricity flows countrywide and promoting an active electricity market

In harmony with the environment

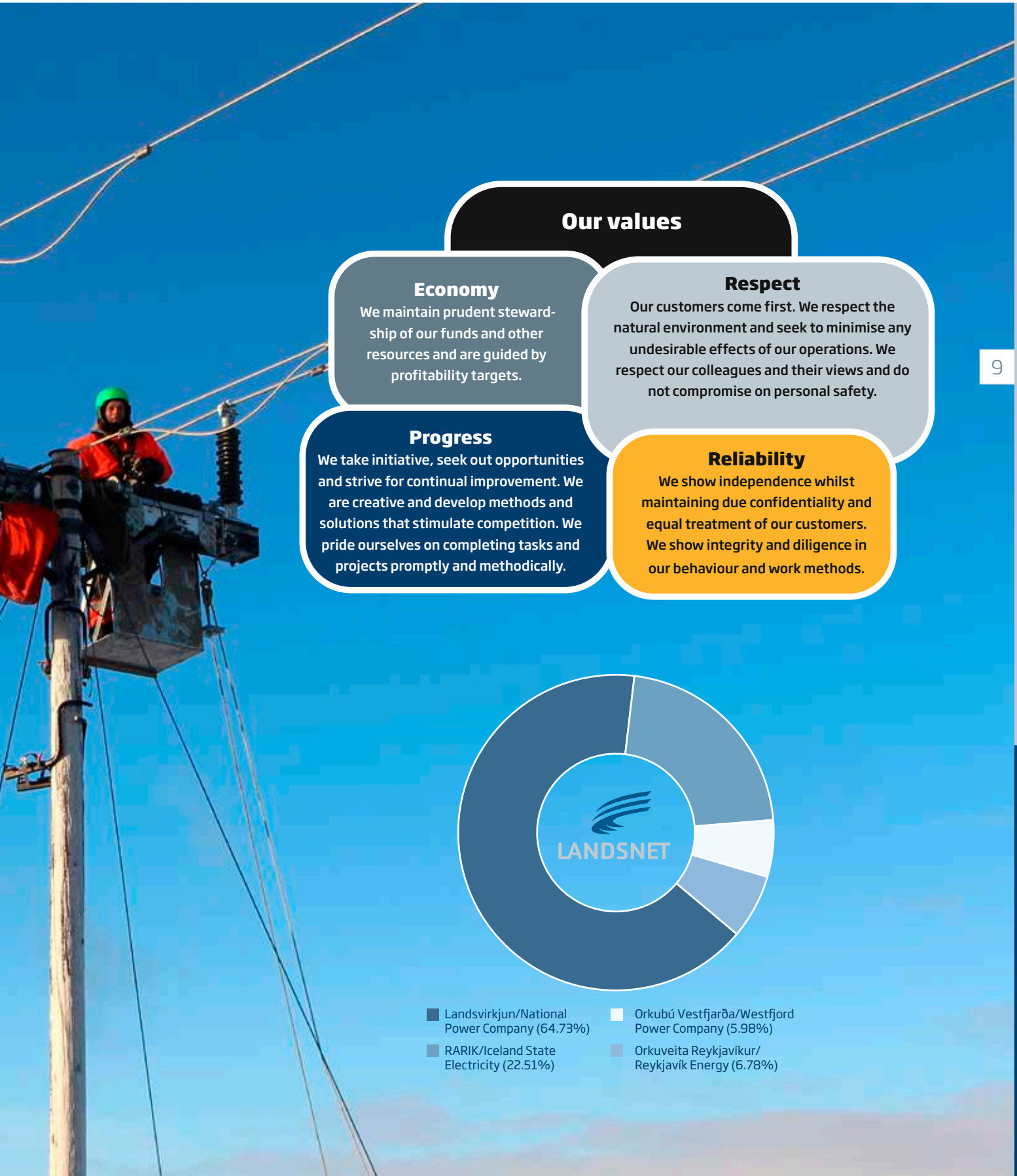
Landsnet's future vision is to be a reliable transmission system operator, supporting value creation in society whilst operating in harmony with the environment.

To achieve this vision, we have adopted the following policy focus areas:

- Ensuring security of supply and increasing value creation in society
- Promoting efficient and cost-effective development of the grid that meets stakeholders' long-term expectations
- Respecting the environment through sound practices and innovative infrastructure development
- Developing Landsnet as a company and building consensus and understanding of our role and policies

Landsnet's policy

- To meet the electricity market's long-term needs by developing a next-generation grid based on eco-friendly solutions
- To be a leader in the introduction of smart grid solutions focusing on renewable energy sources, increased value creation and sustainability
- To be leader in the development of an information highway for electricity market players
- To foster energy-market innovation that supports value creation in society, including the presentation of such innovation and of the company's plans



Our values

Economy
We maintain prudent steward-ship of our funds and other resources and are guided by profitability targets.

Respect
Our customers come first. We respect the natural environment and seek to minimise any undesirable effects of our operations. We respect our colleagues and their views and do not compromise on personal safety.

Progress
We take initiative, seek out opportunities and strive for continual improvement. We are creative and develop methods and solutions that stimulate competition. We pride ourselves on completing tasks and projects promptly and methodically.

Reliability
We show independence whilst maintaining due confidentiality and equal treatment of our customers. We show integrity and diligence in our behaviour and work methods.

- Landsvirkjun/National Power Company (64.73%)
- Orkubú Vestfjarða/Westfjord Power Company (5.98%)
- RARIK/Iceland State Electricity (22.51%)
- Orkuveita Reykjavíkur/ Reykjavík Energy (6.78%)

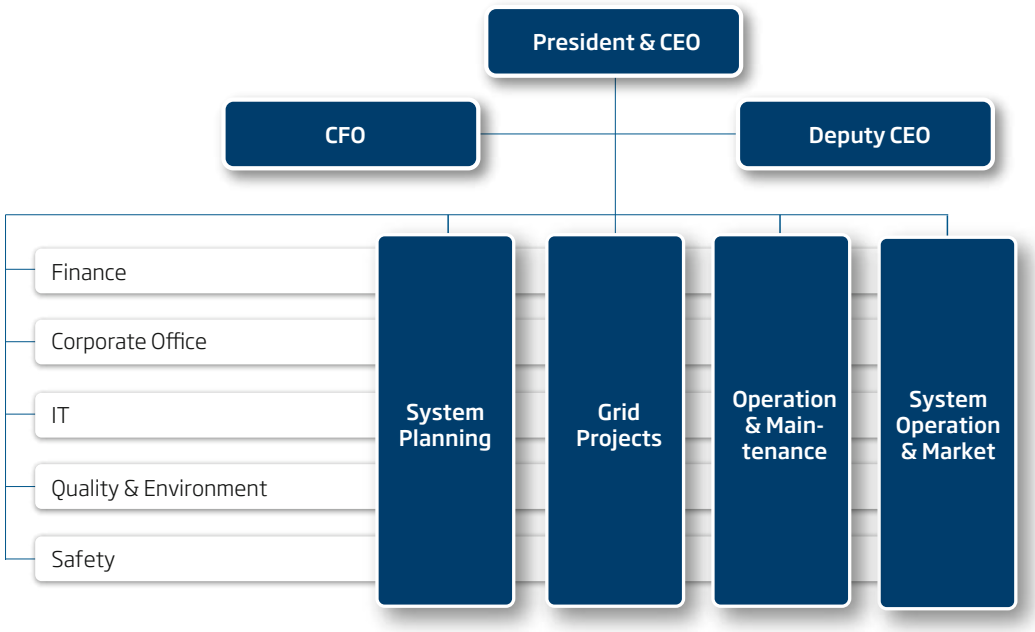
Landsnet's Board of Directors

Landsnet's Board of Directors is composed of Geir A. Gunnlaugsson, previously chief executive of Marel and Promens, Svana Helen Björnsdóttir, Executive Chairman of Stiki, and Ómar Benediktsson, CEO of Farice.

Mr Gunnlaugsson has been a member of Landsnet's Board since 2011 and is Chairman of the Board. Ms Björnsdóttir was elected to the Board in 2009 and Mr Benediktsson in 2012. The Alternate Director is Svava Bjarnadóttir, Partner and Consultant at Strategía ehf.

The Board is elected for a term of one year at a time. To meet statutory requirements of utmost impartiality in our activities, our Directors must be independent in all respects from other companies engaging in the generation, distribution or supply of electricity.

Landsnet's organisation chart



Landsnet's Executive Committee consists of Þórður Guðmundsson, President & CEO, Guðmundur I. Ásmundsson, Deputy CEO, and Guðlaug Sigurðardóttir, CFO.

Mr Guðmundsson has been CEO of Landsnet since the company commenced operations at the beginning of 2005. He was previously Director of the Transmission division of Landsvirkjun. Mr Ásmundsson has been Deputy CEO since 2008, having previously served as Director of Landsnet's System Operations. Ms Sigurðardóttir joined Landsnet as Chief Financial Officer in 2008, having previously held positions at KPMG Iceland, the fisheries companies Meitillinn and VSV and the Municipality of Árborg.

System Operation & Market controls the electricity system and co-ordinates operations in the grid and related units. This includes developing and operating protection equipment. The division also handles the development of market solutions, the drafting of terms and conditions relating to trade and operations, customer relations, the issuance of guarantees of origin and the settlement of electricity flows countrywide.

System Planning has the role of developing in a cost-effective manner a transmission system that meets market demands and ensures and maintains its long-term capability. It is responsible for forecasting future changes in the electricity market and providing effective solutions in a timely fashion.

Grid Projects is responsible for ensuring electricity supply to consumers wherever requested. When the transmission capacity of existing infrastructure is fully utilised, or a new customer requires increased power supply, Landsnet must either enhance existing infrastructure or construct new transmission capacity to meet agreements on increased transmission.

Operation & Maintenance (O&M) is responsible for ensuring our transmission infrastructure's capability of meeting security-of-supply obligations. This includes managing assets, maintenance and refurbishment of structures in service. O&M operates in all parts of the country.

Senior management team

Landsnet's senior management team at the energisation of the reactive power compensator at Klafastaðir:

Nils Gústavsson, Head of Grid Projects, Elfa Hrönn Guðmundsdóttir, Human Resource Manager, Þorgeir J. Andrésson, Head of Corporate Office, Sæmundur Valdimarsson, Head of IT, Hildur B. Hrólfsdóttir, Quality and Environmental Manager, Guðmundur Ingi Ásmundsson, Deputy CEO, Guðlaug Sigurðardóttir, CFO, Sverrir Jan Norðfjörð, Head of System Planning, Þórður Guðmundsson, President & CEO, Guðlaugur Sigurgeirsson, Head of Operation & Maintenance (O&M), and Lúðvík B. Ögmundsson, Safety Manager. Not pictured is Íris Baldursdóttir, Head of System Operation & Market.

“Our staff came under considerable pressure due to severe faults coupled with new assets being brought into service

Activities in 2013

The year 2013 began for Landsnet in the same way as 2012 ended – with extensive repairs of transmission lines. Overall, however, it was an average year as regards grid disturbances. Our staff came under considerable pressure due to severe faults coupled with new assets being brought into service. Despite this pressure, we managed to complete all routine maintenance of substations and transmission lines. Maintenance and operational activities were successful, with all scheduled inspections and repairs completed.

Disturbances

Grid disturbances totalled 52 during the year while disturbance-related faults numbered 56, which means that more than one fault occurred in some instances. Most of these took place in January, September and December and were weather-related. Energy not supplied due to grid disturbances totalled 595.8 GWh, which corresponds to 17.9 outage minutes. Energy not supplied due to disturbances in non-Landsnet systems totalled 160 MWh.

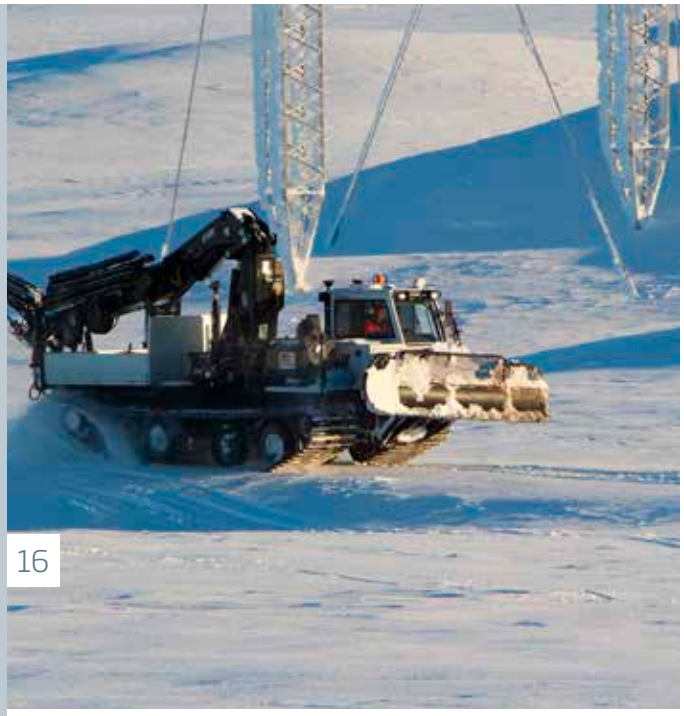
Main grid disturbances in 2013

- **On 26 and 27 January**, a storm hit the country with very strong winds and icing conditions in the West Fjords and north-east Iceland, which resulted in an outage of the Bolungarvík Line 1 and the Breiðadalur Line 1. The latter line sustained considerable damage as one phase conductor broke, as did a number of wooden poles and crossbars. Energy not supplied on this occasion was 391 MWh.

- **On 23 February**, heavy industrial load of 330 MW in south-west Iceland tripped, which resulted in our Wide Area Protection system separating the grid into four islands. When the south-west and north-west networks were being interconnected, a generator in the north-east island tripped, causing underfrequency in that island. This triggered an outage in the north-west extending from Blanda eastward to Hólar. The re-energisation shortly after the outage resulted in a very high-voltage situation in North and East Iceland for a short while. Energy not supplied was assessed at 62 MWh.

- **On 15 and 16 September**, a fierce storm struck the country with wind sweeping in from the north, precipitation and icing conditions in the north-east of the country. At the same time, heavy winds with sudden gusts were blowing in the area south of the Vatnajökull ice cap. Crews were stationed at strategic locations in case lines started tripping and sustaining damage. We also took appropriate measures in the grid and adjusted transmission to minimise the risk exposure in the event of tripping. When the storm struck land, tripping began. The Laxá Line 1 was the first to trip, followed by the Sigalda 4/Prestbakki Line 1 two consecutive times in a short period. The violent weather made it difficult to keep the lines in operation; they had tripped 7-8 times before the weather calmed down. There was also much icing on the Krafla Line 1, causing it to trip. When the weather subsided, inspection of the Laxá Line 1 revealed that at least five wooden poles were broken. Energy not supplied on this occasion totalled 4 MWh.

- **On 25 September**, industrial load in south-west Iceland caused a sudden trip and a partial outage for other power-intensive companies in the area. Approximately 700 MW in total went out of service in one instant, which had an extensive impact on the electricity system. Our system protections then separated the grid into two islands, which saved the north-east island. Frequency peaked at 52.97 Hz in the south-west island, which sustained a serious voltage spike. After the power-intensive plants' load was reduced, various generating units in the south-west island tripped, including two in the River Þjórsá-River Tungnaá area, six on the River Sog and three on the Reykjanes peninsula. Frequency and voltage changes affected some consumers – for example, traffic lights in Reykjavík went off and back-up power generators switched on in a number of places. Five hours later, the disturbance was over and all services had returned to normal. Energy not supplied as a result totalled 46.50 MWh.



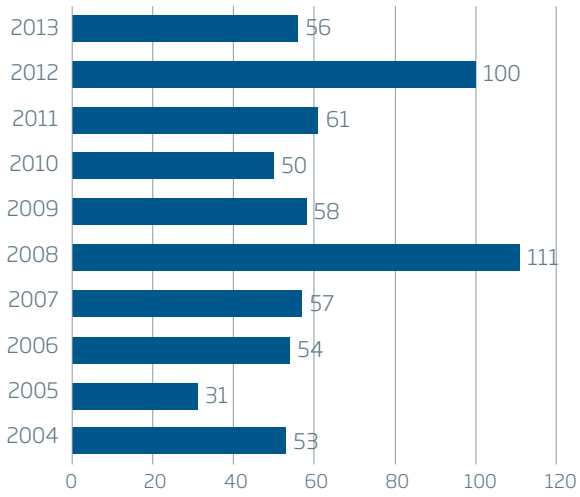
» **On 13 December**, the Sigalda Line 4/Prestbakki Line 1 tripped in heavy wind with gusts reaching and exceeding 45 m/s. Our Wide Area Protection system split the grid into two islands. Under-frequency occurred in the south-west island, which caused a power-intensive customer to trip load. Energy not supplied was approximately 11 MWh.

» **On 23 and 24 December**, a severe storm swept through the West Fjords with blizzards and heavy precipitation combining with a strong, steady wind and gusts reaching and exceeding 40 m/s. In the wake of the storm, the Geiradalur Line 1 tripped, causing an outage throughout the West Fjords. Power was restored shortly afterwards, but the line tripped again in short order. The Geiradalur Line 1 tripped a total of four times again until midnight on 23 December, when the decision was made to start reserve power units. The West Fjords were reconnected to the grid on 24 December. Energy not supplied totalled 6.65 MWh.

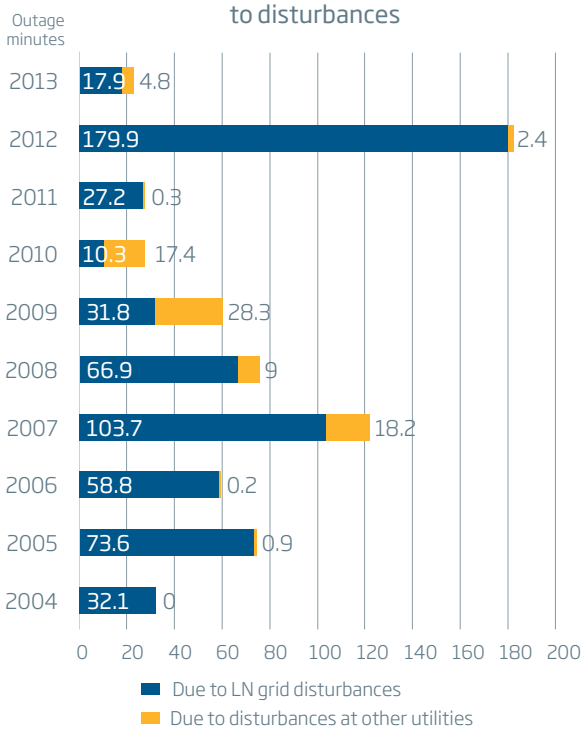
» **On 25 and 26 December**, severe icy weather conditions in East Iceland caused considerable damage to transmission lines, which led to grid disturbances that lasted more or less into mid-January 2014. The Stuðlar Line 2 tripped on Christmas Day, as did the Kópasker Line 1 twice at short intervals. The day after, the Vopnafjörður Line 1 tripped due to severe icing. Inspection of the Stuðlar Line 2 revealed that 10 wooden poles were broken. In addition, one phase conductor and a wooden pole were broken on the Vopnafjörður Line 1. Conditions to carry out repairs were very unfavourable, with heavy snow, continual icing and heavy fog. Our linesmen together with contractors and assistants performed no mean feat in getting the lines back up and running in very challenging conditions. Energy not supplied totalled approximately 1.9 MWh..

» **On 30 December**, a storm battered the West Fjords with strong winds and icing conditions, resulting in the Breiðadalur Line 1 tripping. Energy not supplied was assessed at 1.78 MWh.

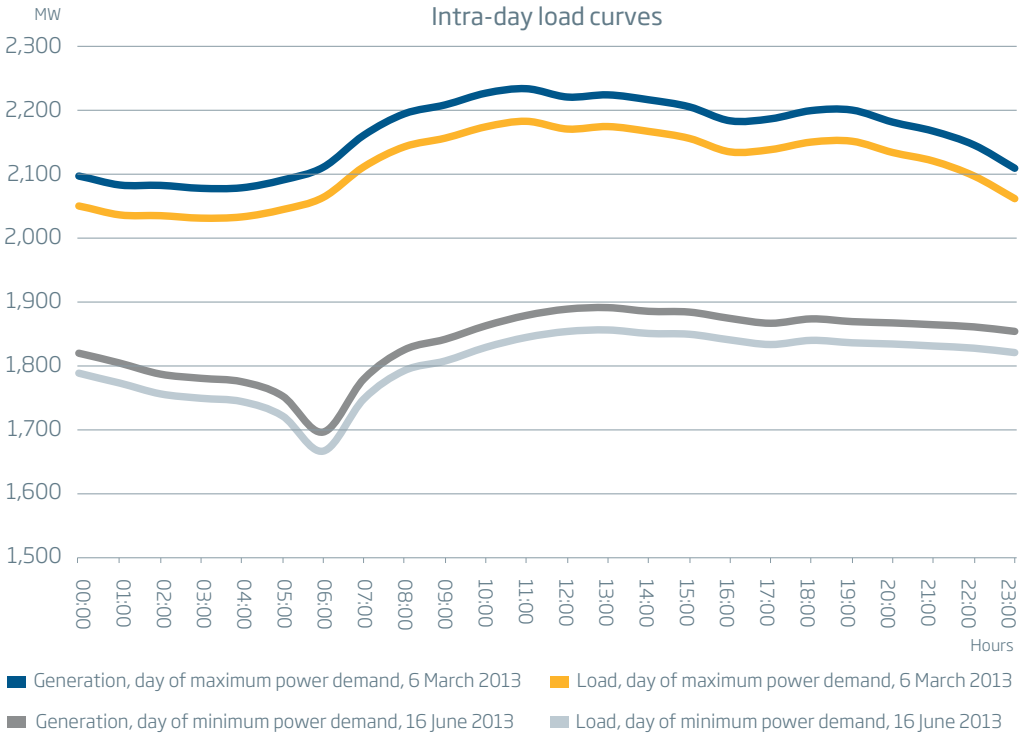
Number of grid disturbances



Outage minutes due to disturbances



Intra-day load curves



Peak load in the year

The year's peak in power fed into the grid was recorded on 6 March 2013 at 2236 MW, a year-on-year increase of 3.94%. Total system demand in 2013 was 17,113 GWh, up 3.03% on the previous year. Transmission losses totalled 374 GWh, or 2.14% of generation, up by 9.25%.

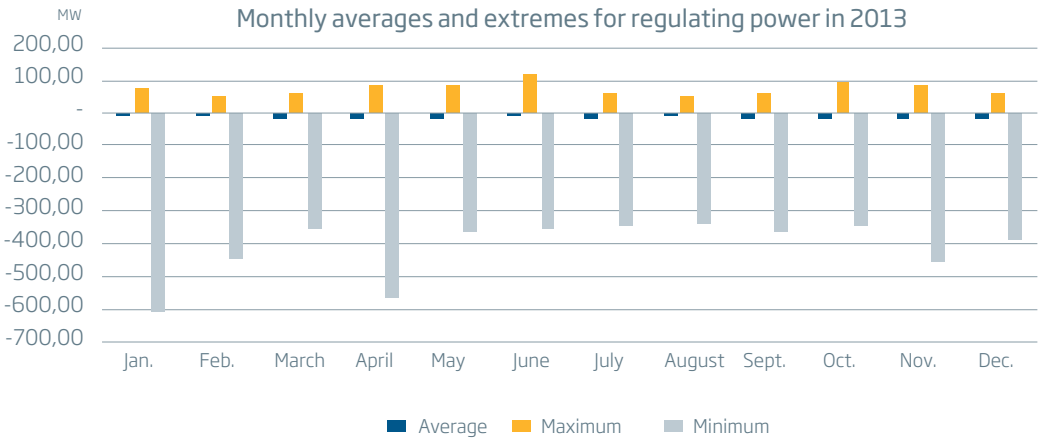
Increased transmission losses and operational risk

Transmission through the Regional Network was at or over the maximum capacity limit for a large part of the year. The reason was increased load in East Iceland coupled with high levels of inter-regional transmission due to the low reservoir water levels of hydro power stations. In 23 instances, the grid had to be separated into so-called islands ("island operation")[1] to avoid further disturbances in its operation. This caused increased transmission losses as well as heightened operational risk compared with recent years for Landsnet. We carried out system operation simulations to analyse and test different types of island operation in an aim to mitigate risk during high transmission levels through the Regional Network.

Market developments

Our autumn round of tendering to buy electricity to cover transmission losses and regulating power[2] revealed substantial increases in electricity prices. This was followed by increases of our respective tariff rates. In addition, increased curtailable transmission[3] has put our curtailment procedures and relations with distribution system operators and power-intensive consumers to the test.

Landsnet is required by law to ensure the availability of sufficient spinning reserves[4] at any given time, to control frequency and voltage and ensure a minimum supply of regulating power[5] in the regulating power market. Contracts with generating companies ensured the availability of 100 MW of spinning reserves in 2013. We continued experimenting with "telephone bids" in the regulating power market in an aim to stimulate competition. We also developed an arrangement facilitating the participation of suppliers in offering power in the regulating power market. Tenders were invited for guaranteed regulating power, 40 MW for up-regulation and 40 MW for down-regulation. Three tenderers submitted bids, following which a number of new generating units entered the regulating power market. Their participation in the market has been a success.



1) Can be two or more smaller operational units.
2) Ensures minimum supply in the regulating power market, see footnote 5.
3) Electricity consumption that Landsnet may curtail in certain instances, e.g. due to disturbances, system constraints, etc.
4) Operating reserve ('back-up power') connected to the grid and immediately available.
5) The power procured by Landsnet to balance differences between forecast energy use and actual energy use in the electricity system as a whole.

In recent years, we have been working on the launch of an Icelandic spot market for electricity trading, named ISBAS. The launch of a spot power market is a big step and it is important for market participants to see an advantage in taking an active part right from the outset. Once the decisions and commitments of prospective market participants are in place, we will be able to launch the ISBAS market within half a year based on the preparations already undertaken.

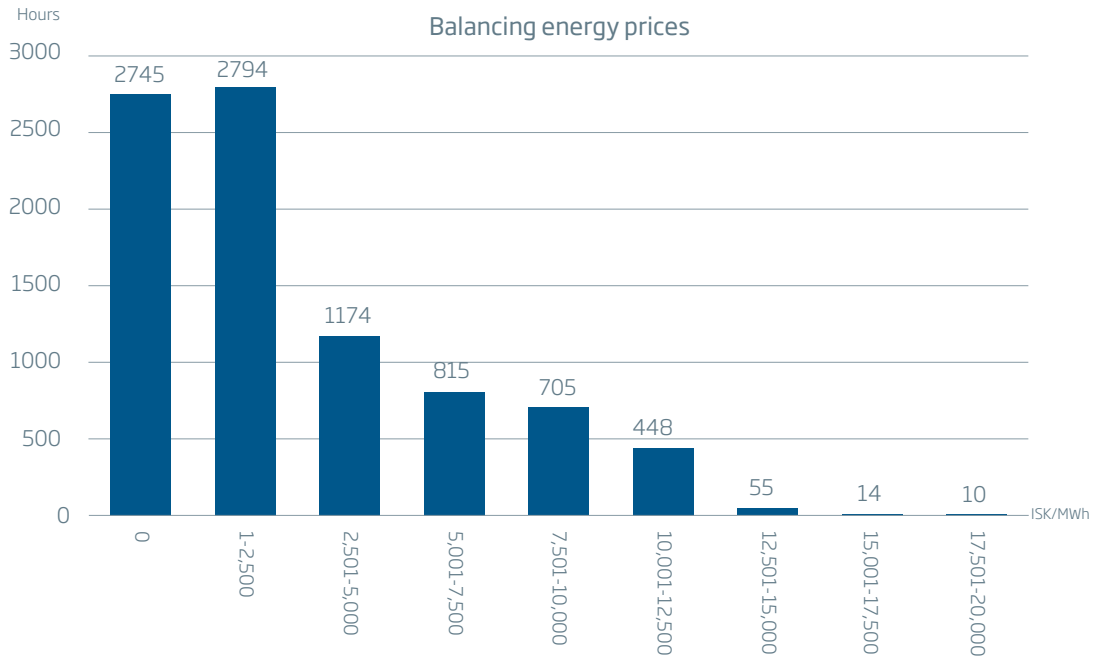
Grid Code[1)]

In 2013, we reviewed the Terms for Sales Metering and Settlements and the Terms for Connections to the Grid. We also finalised the Terms for Curtailable Transmission, which were approved by the Ministry of Industry and Innovation and took effect on 1 October 2013.

Protections and system protections

We continuously work on keeping all grid protection systems within an acceptable life cycle to ensure maximum functionality. In 2013, we managed to renew a large part of the protection equipment at the Rangárvellir and Eyvindará substations, in addition to a considerable amount of control and protection equipment brought into service as part of new infrastructure projects. This includes a Static VAR System at Klafastaðir and the renewal of protection equipment for the Norðurál Lines 1 and 2, an extension to the substation at Stuðlar, a new substation at Búðarháls and a new line exit at Hólar in Hornafjörður. We started renewing the current transformers (CTs) at Brennimelur, Geitháls, Sultartangi and Sigalda due to the increased load on the grid in recent years.

Protection systems are of major importance for the grid's operation. In addition to conventional protections, we have in recent years been installing and developing Wide Area Protection capabilities, which divide the grid into islands when operating conditions become difficult. These are an ever more important aspect of the grid's management as its load is increasing and inter-regional transmission is near maximum levels for a large portion of the year. We installed Wide Area Protections at the Sigalda substation and equipment in the Regional Network on the north and east routes from the Brennimelur substation to the Fljótsdalur substation to be able to locate faults with more precision.



1) A set of terms used by Landsnet for electricity transmission, the transmission system's design, system management and various commercial matters.

Grid development

At the beginning of 2013, we completed the preparations for a number of new infrastructure projects, thereby laying the foundations for one of the most active investment years in the company's history. The projects cover a wide range of investments, encompass all regions of the country and involve maintenance as well as strengthening and expansion of the grid. An effort was made to start the preparations earlier than has been customary, in particular systems analysis, specific studies of weather conditions, option analysis, line routeing and planning-related work. Emphasis was placed on following the correct procedures to shorten the projects' preparation time after the decision to develop new infrastructure.

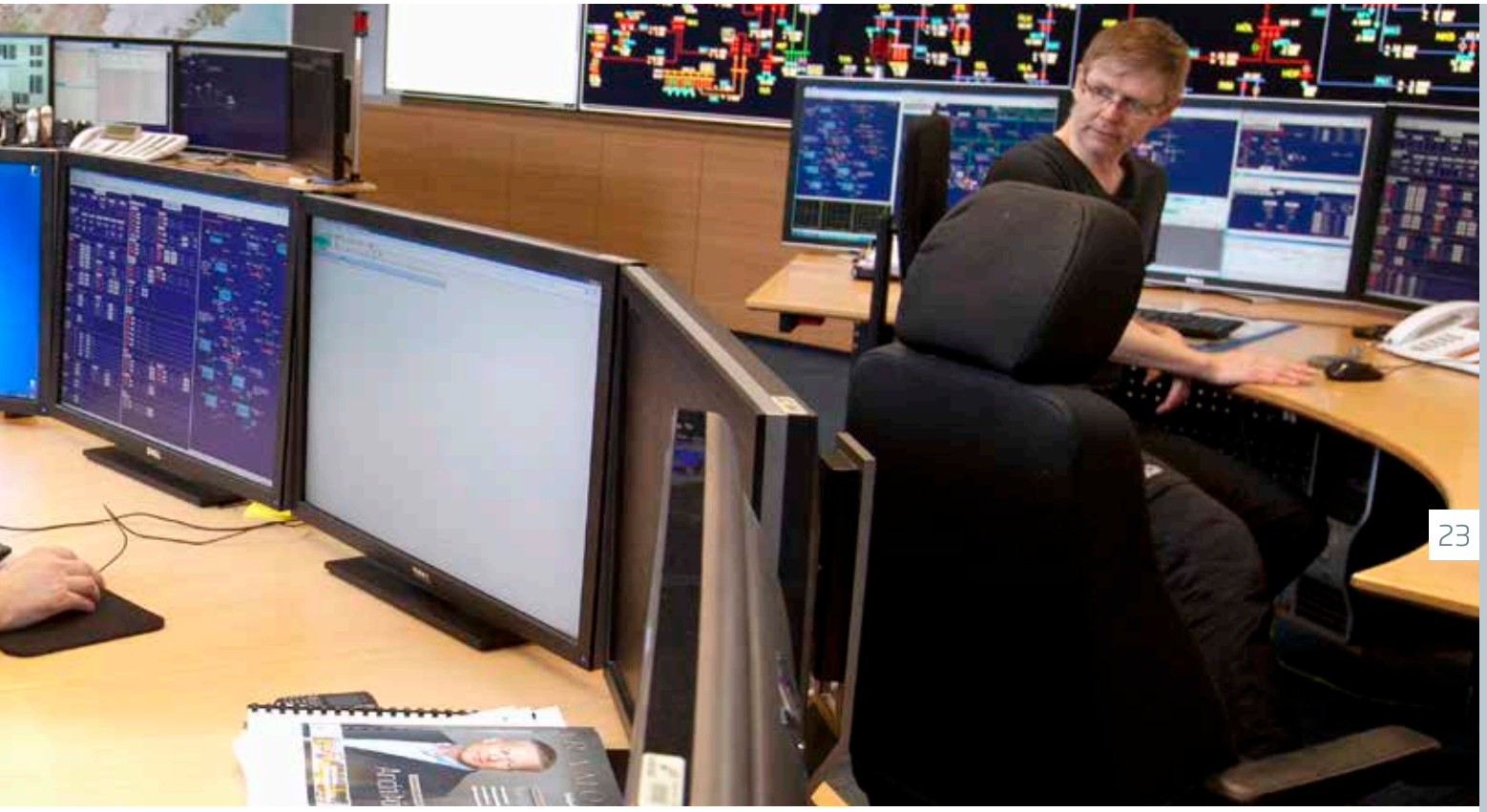
Basic research and data collection

Landsnet and its predecessors have through the years had basic research carried out on environmental factors that affect the grid's development and operation. This has produced a unique database on which we can base our decisions regarding future grid development. Such basic research will continue, with due regard to the importance of the continuity of such work.

Focus points for the year included the development of forecasting models for ice build-up on power lines. Among other things, we use special equipment installed on important transmission lines to expedite fault location and tension recorders to measure icing rates. The ice can weigh as much as large SUVs hanging on the conductors at every tower! We expect to be able to use the icing forecasting model to define load criteria and in day-to-day grid monitoring.

System analysis and design

As usual, we worked on a wide range of projects devoted to system analysis and system design, in



addition to specific assessments in response to inquiries by customers and stakeholders. This included an analysis for regional network strengthening, an analysis for the landing sites and necessary grid strengthening for a potential sub-sea cable to Europe, work on solutions to transmission constraints in the main grid and an analysis of connection possibilities for a number of new power stations.

Risk assessment

We carried out a risk assessment for our entire activities, including operational risk, project risk, financial risk and counterparty risk. This was the first such comprehensive risk assessment of the company, which involved the participation of a large proportion of our staff. We place a major emphasis on the safety of our staff, and the risk assessment was no exception in this respect.

Operational risk is defined as the risk of negative impact on Landsnet's performance. This includes aspects relating to generation fed into the grid, the grid itself, information and surveillance systems, management, the legal environment, contracts, etc.

Project risk is defined as the risk of the results and performance of independent projects undertaken by/for the company not being to its satisfaction in some way.

Counterparty risk is the risk of financial loss in the event that a customer or a counterparty to a financial instrument is unable to meet its agreed or contractual obligations.

Financial risk primarily concerns financial aspects of the company's activities, i.e. the risk of financial loss on both on- and off-balance-sheet items, including due to

changes in the market price of such items. This includes changes in interest rates, exchange rates and inflation. The company's defined financial risk consists of liquidity risk, interest-rate risk, exchange rate risk and indexation risk.

Green Certificates

In April 2012, we began issuing guarantees of origin of electricity, so-called Green Certificates, which serve as confirmation that certain electricity is generated using renewable energy sources, e.g. hydropower or geothermal power.

Markets for guarantees of origin of electricity are widespread in Europe. Our issuance of Green Certificates far exceeded expectations in 2013, with upwards of 13 million certificates issued in the year, up from just under 5.4 million in the preceding year, a 59% year-on-year increase.

By issuing Green Certificates, we lend important support to the market environment of electricity suppliers. For each MWh of electricity generated from a renewable energy source, a guarantee of origin may be sold regardless of the sale of the electricity itself. This creates a new tradable commodity, which Icelandic generating companies have already sold in substantial quantities in the European market. In light of healthy sales, Landsnet decided to reduce the Green Certificate tariff from ISK 7 per certificate issued to ISK 4.30. The reduced tariff took effect on 1 October 2013.

We have partnered with other European issuers to promote Green Certificates and the regulatory framework governing their use in Iceland. Our staff have also taken an active part in the Association of Issuing Bodies (AIB), which promotes the use of the standardised European Energy Certificate System. Our employees have played a key role both in implementation and policy formulation on technical aspects within the AIB.

Purchasing and inventory control

Due to extensive infrastructure investment and grid maintenance, 2013 was a busy year in purchasing and inventory control. We held 16 tender exercises during the year, in addition to numerous price queries. Active infrastructure investment in the year was reflected in the number of purchase orders, which were up 15% from 1,594 in 2012 to 1,822 in 2013.

The year saw extensive activity at our depot terminal at Geitháls, a through-point for most of the equipment used in our infrastructure construction and maintenance. For example, at the beginning of the year we had to replenish our stocks of wood poles in the wake of the damage wreaked by storms in previous months. This involved the import of around 500 wood poles in the spring.

IT ever more important

Information technology and telecommunications play an ever larger role in our operational and grid security, with a major emphasis placed on leveraging technology to the optimal level.

Last year we lay the final touches on upgrading our Energy Management System. Our operational separation from Landsvirkjun was also finalised when Landsnet introduced its own financial system, telephone exchanges and payroll system. We concluded our selection of a new document management system, which is expected to increase efficiency and transparency and open up new possibilities of co-operation between departments and teams. A new intranet was launched at the end of the year, work on which had begun in 2012.

Two audits were carried out in the year. The first was a security audit, which used various methods to assess the company's information security. The latter was an audit and analysis of the functionality of our software systems, data flows between these and functional overlaps. The results were mostly positive. We will take appropriate steps in 2014 to address cases where room for improvement was identified.

Possible tower design

A 3D image of new transmission towers designed for Landsnet for better visual integration with Icelandic landscapes. The towers are shown here with the Sprengisandur highland route as a backdrop, with the Hágöngur mountains in the distant background. The towers' location in the photo does not reflect any intended line routeing.

Improvements to the grid

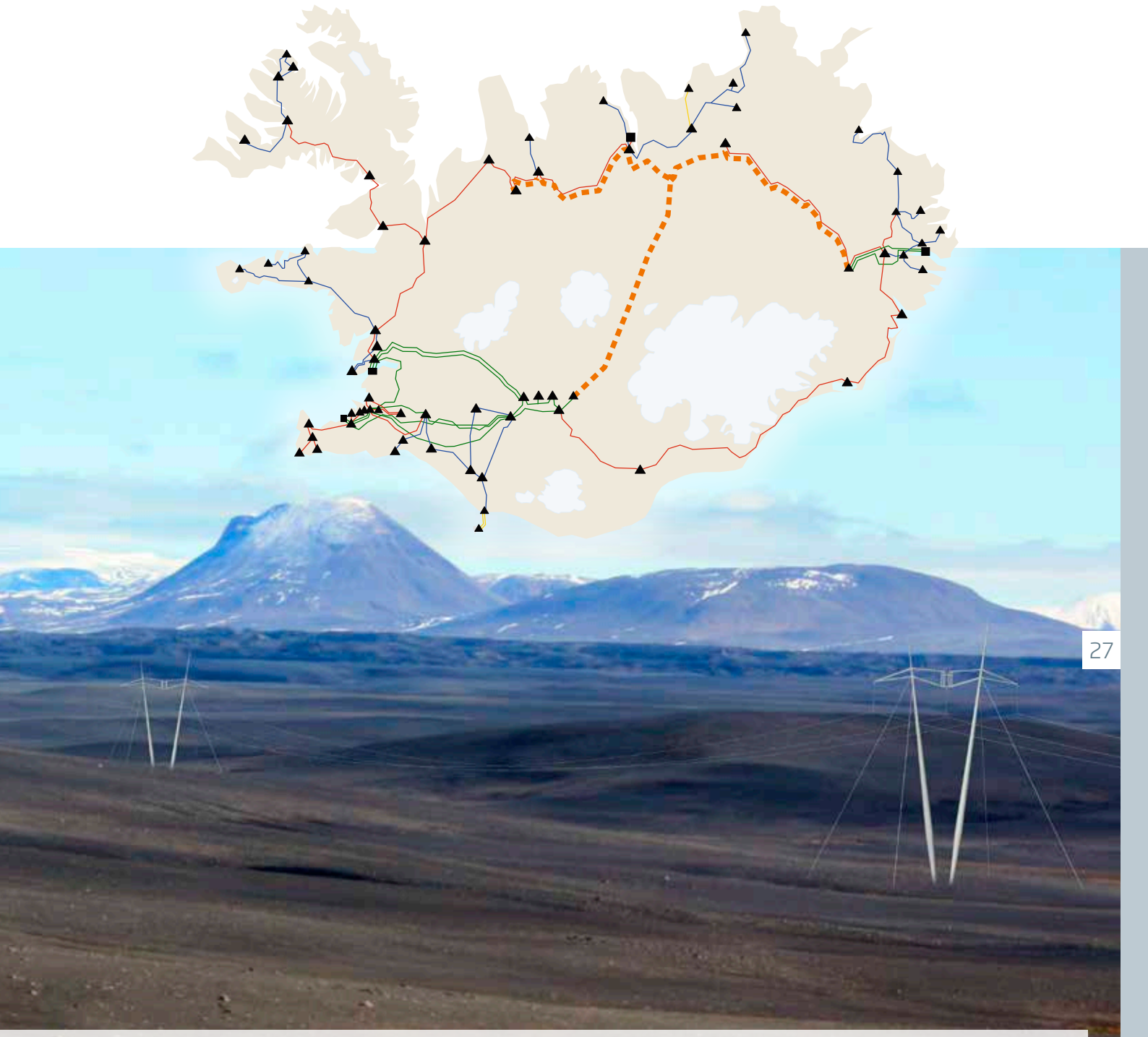
Bottlenecks in the main grid are making it ever more difficult for Landsnet to transmit power between regions of the country and ensure sufficient operational security. This situation is set to deteriorate further due to increasing transmission. A new report compiled for Landsnet shows that if further grid development is not undertaken in the next few years, various difficulties will arise, costing billions of ISK for Iceland's economy.

The following two steps are the most urgent to turn this situation around: (1) constructing a Suðurnes Line 2 to ensure security of supply on the Reykjanes peninsula and (2) strengthening the connection between North and South Iceland. The Suðurnes Line has been in preparation for almost a decade and now it looks to be moving ahead, a major benefit for the Reykjanes population and economy.

North-South connection expedited

The Regional Ring Network has reached the limit of its carrying capacity and no longer meets power demand in North and East Iceland. Previous plans envisaged upgrading the network in stages, but its development now needs to be reprioritised due to substantially increased power transmission, partly as a result of the switchover of fishmeal plants in East Iceland to renewable energy and a significant increase in power generation in North Iceland as set out in the Master Plan approved by Iceland's parliament.

In light of changed assumptions, we have started preparations for a North-South connection over the Sprengisandur highland plateau, from which we plan to strengthen the Regional Network westward and eastward to the Blanda and Fljótsdalur power stations. This will serve to increase the



grid's transmission capacity, operational security, flexibility and efficiency and provide a way out of the unsatisfactory circumstances in which the grid is currently operated.

Changed preparation procedures

Our Grid Plan will undergo its first strategic environmental assessment in 2014. This will involve public discussion of our option scenarios from environmental perspectives, including comparison of routeing options for the strengthening of the North-South connection. Work is ongoing to flesh out the details of individual infrastructure projects, which includes comparing different options on the basis of visibility analysis and other environmental considerations. By presenting the results of these analyses, stakeholders are provided with a clearer picture of the options available, regardless of what Landsnet intends to propose as the best solution.

For the main grid's strengthening to be realised, with its resultant macroeconomic benefits, the government must, firstly, formulate a policy on underground cables around which consensus can be built and, secondly, impose some order on the licensing processes for our infrastructure projects. The current situation is that projects get stranded in many parts of the process as planning authority is widely dispersed, in contrast to the system in Norway, for example, where planning authority over electrical power projects is placed under one central body.

“The year 2013 was one of the most active in Landsnet’s history in terms of infrastructure development. Our investment amounted to more than ISK 6 billion, a record number since 2007

Main infrastructure projects in 2013

The year 2013 was one of the most active in Landsnet's history in terms of infrastructure development. The company's investment amounted to more than ISK 6 billion, a record number since 2007.

Búðarháls

The Búðarháls Power Station was connected to the grid in late 2013 following the construction of a substation at Búðarháls and a 6km long 220 kV transmission line, the Búðarháls Line 1. The works started in 2012 with the construction of a substation building and a service track for the Búðarháls Line and work on the tower foundations. In the summer of 2013, the transmission towers were erected, the conductor stringing was carried out and the installation of equipment for the substation was completed. The structures formally entered service at the beginning of 2014 when the Minister of Industry connected the Búðarháls Power Station to the grid.

New transformer at Fljótsdalur

At the beginning of 2013, we concluded an agreement with the Italian company Tamini on the purchase of a new 220/132 kV, 100 MVA transformer to be installed at the Fljótsdalur substation. The manufacture of the transformer started in February 2013 and it is due to be delivered in April 2014. Foundations were put in place for a reserve transformer at Fljótsdalur. The new transformer is scheduled to be connected at the end of July 2014, after which the existing transformers at Fljótsdalur will be taken out of service for repairs.

New delivery point at Höfn

A new 132 kV point of delivery at Höfn in Hornafjörður was added to the grid in co-operation with Iceland State Electricity (RARIK) in reaction to a request for electricity supply to the local fishmeal plant. We added a 132 kV breaker bay at the Hólar substation, raised the voltage of a line from Hólar to Ægissíða north of Höfn, which RARIK had operated at a voltage of 11 kV, and laid a 132 kV cable from the end of the line to RARIK's reserve power station at Höfn. The Mayor of Hornafjörður inaugurated the new transmission assets at the beginning of 2014.

Reserve power station and substation at Bolungarvík

Construction on a new joint substation of Landsnet and the Westfjord Power Company and a Landsnet reserve power station at Bolungarvík began in 2013. The existing substations are in an avalanche risk area. The tender design for the building, machinery and electrical equipment took place at the start of the year. Tenders were then invited for these project components in the spring. The construction works began in the autumn and the project is scheduled to be mostly completed by the start of summer 2014. We entered into a contract with the Swedish company Attacus for the purchase of six 1.8 MW diesel generators. Their installation is scheduled to begin in August 2014 and to be completed in September. The aim is to bring the new substation into service in October 2014.

New static VAR system for Grundartangi

In 2013, we completed the installation of a static VAR system at Klafastaðir for the Grundartangi industrial site. The system entered the testing phase in December and was formally connected to the grid at the beginning of 2014 by the Minister of Industry. It increases the transmission capacity to Grundartangi and enables us to meet increased power demand there without adding transmission lines. The compensator will also enhance the grid's voltage control significantly, which will have a positive effect on power quality and the operation of the whole grid.

New sub-sea cable to the Westman Islands

In the summer of 2012, we began preparations for the installation of a new sub-sea cable to the Westman Islands – the VM3. Following a failure in the autumn of 2012 in one of the two sub-sea cables providing the islands with power, every effort was made to expedite the project in an aim to energise the new cable by the autumn of 2013. This target was achieved. An agreement was concluded between Landsnet and the Swedish company ABB at the beginning of 2013 on the manufacturing and installation of the sub-sea cable and the manufacturing of underground cables connecting with it. The sub-sea cable was installed in the summer and formally launched into service on 9 October. A 30-minute documentary was produced on this project.

New substation at Ísafjörður

Construction on a new substation at Ísafjörður commenced during the year. The existing substation is old, located in an avalanche risk area and in need of renewal, in addition to which the construction of avalanche barriers requires its relocation. The new substation will be located next to the Westfjord Power Company's heating works at the head of the Skutulsfjörður fjord. The first phase of the substation building was completed at year-end and the project is scheduled for completion in spring 2014. In relation to the avalanche barriers at Ísafjörður, we received a request for the relocation of the Ísafjörður Line 1, work on which began in autumn 2012. This work had to be suspended in December 2012 due to weather, but restarted as soon as the ground frost thawed in spring 2013. The project was completed in August.

Increased capacity of the Sigalda Line 3

We worked on the design and preparation of tender documents for increasing the transmission capacity of the Sigalda Line 3, a 220 kV line between the Sigalda and Búrfell Power Stations. The conductor on the line will be replaced and the towers strengthened. The changes will double the line's transmission capacity and will take place in stages over the next few years.

Underground cable to Þeistareykir

The installation of and site restoration for the Þeistareykir Line 2, a 66 kV underground cable, from the Kópasker Line 1 at Höfuðreiðarmúli to Þeistareykir was completed in difficult conditions in snow and harsh weather in the first half of the year. The cable was brought into service in October and will provide electricity in the works area during the construction of the Þeistareykir Power Station. After the power station comes on line, the cable will connect the Laxá Power Station to the grid.

Expansion of Stuðlar substation

The expansion of our substation at Stuðlar near Reyðarfjörður fjord in East Iceland entered the testing phase towards the end of the year and was formally brought into service by the Mayor of Fjarðabyggð at the start of 2014. This was the first project in our action plan to increase the transmission capacity and reliability of the regional network in East Iceland after the switchover of local seafood processing companies to renewable energy. A 66 kV outdoor substation already existed at Stuðlar, but the expansion added a 132 kV outdoor substation on the same site as well as two 132/66 kV power transformers with a combined transmission capacity of about 65 MVA. Concurrently, we raised the voltage on the Stuðlar Line 1 to 132 kV. The line, an underground cable extending from our substation at Hryggstekkur in Skriðdalur valley to the Stuðlar substation, had been operated at 66 kV since entering service.

Suðurnes Line 2

Preparations continued for installing the Suðurnes Line 2, with the preparation of the tender documents already well advanced. A new type of transmission towers has been developed for the line section from Hrauntungur to Hraunhellur. The National Energy Authority has reviewed and approved the project. We expect to start work on line tracks and foundations for the line in the summer of 2014 and to complete the stringing in 2015.

Expansion of Vatnshamrar substation

To improve security of supply in West Iceland, we expanded the substation at Vatnshamrar during the year. A 132/66 kV power transformer and two new breaker bays were installed. The new transformer came from the substation at Hryggstekkur, where it was no longer needed after the voltage raising at Stuðlar. In parallel, we made changes to the Vatnshamrar Line 2 on a section extending to the Andakíll Power Station. The terminal tower inside the substation was removed and the last section of the line was undergrounded.

Renewal of 220 kV current transformers

We replaced 220 kV current transformers at a number of substations as the previous ones had limited current-carrying capacity and poor insulation values during high salinity conditions. At Sultartangi, this required considerably more extensive works and involved taking the Hrauneyjafoss Line 1 out of service for five weeks.

Conduits for underground cables in the Norðfjörður Tunnel

Landsnet plans to take advantage of the Icelandic Road and Coastal Administration's planned construction of the Norðfjörður Tunnel to place conduits for underground cables in the tunnel. The two parties entered into an agreement on the project in 2013. Landsnet will pay for the installation of the conduits in accordance with the progress of the project.

Selfoss Line 3

We prepared a new 28km long 66 kV underground cable connection between the towns of Selfoss and Þorlákshöfn in South Iceland. The operational reliability of the western part of the 66 kV network in South Iceland is not satisfactory, but the new connection will increase security of supply considerably for these towns, as well as for the town of Hveragerði.

Strengthening of the Tálknafjörður Line 1

In the autumn, we commenced work on strengthening the Tálknafjörður Line 1, which has been subject to frequent disturbances in recent years. The work largely consisted of increasing the insulation level of the line and reducing short-circuits between conductors.

A job well done

The laying of a sub-sea cable to the Westman Islands in record time in the summer of 2013 is an example of a well-executed project to upgrade the South Iceland regional network. Regional network strengthening aims to increase security of supply within the regions. However, the full benefits of such upgrades are not always achieved immediately due to grid constraints. This situation will continue for some time.

Strengthening of regional networks

Our regional networks have long been subject to a lower security of supply than the main grid. We have taken targeted measures to remedy this situation, spending over ISK 5 billion on regional network strengthening between 2010 and 2013. Approximately ISK 6 billion are earmarked for such projects in 2014-2016.

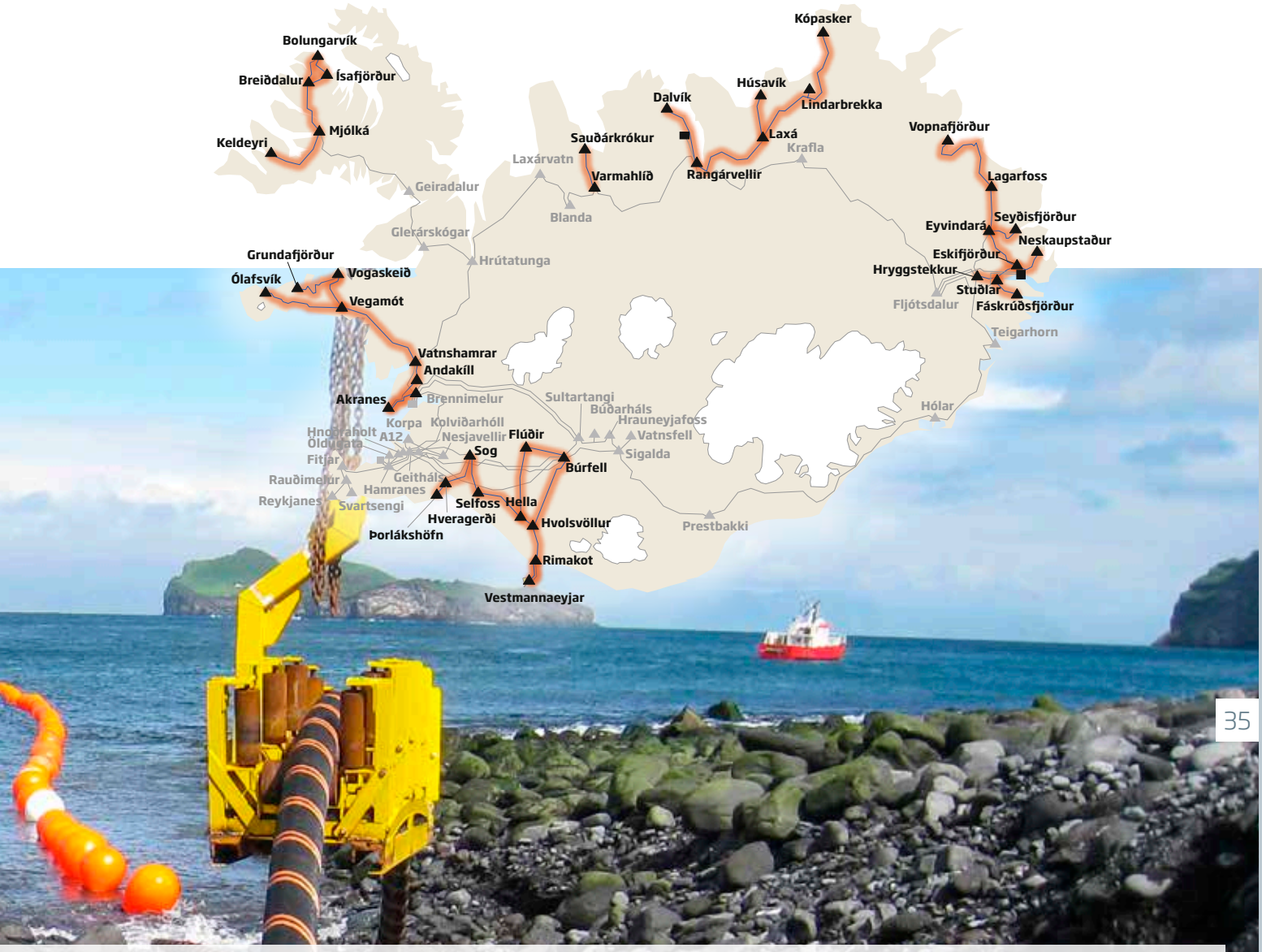
Forthcoming projects

In West Iceland, we are preparing a ring connection between the towns of Ólafsvík and Grundarfjörður through the installation of an underground cable and new substations. A new substation will also be constructed at the town of Akranes.

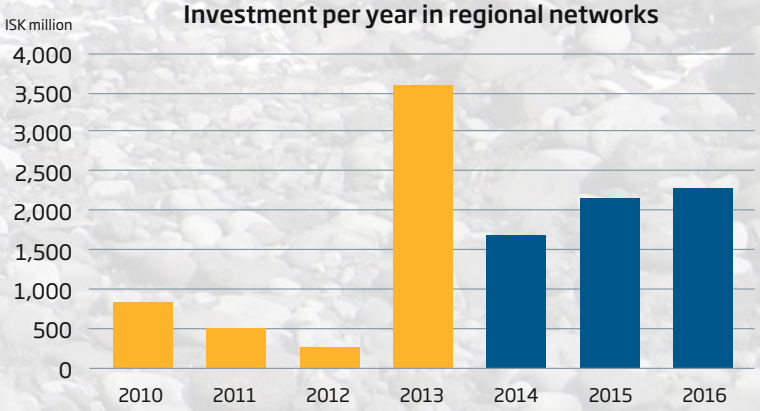
For South Iceland, preparations are underway for the installation of a cable between the towns of Selfoss and Þorlákshöfn, which will improve security of supply for Selfoss, Hveragerði and Þorlákshöfn. Preparations have also begun for the construction of a new substation in the Westman Islands and for raising the operating voltage of the new sub-sea cable from 33 to 66 kV. Also on the drawing table is the further strengthening of the South Iceland network to make it fit to meet foreseeable load increases. This includes an underground cable between the towns of Hella and Hvolsvöllur to replace the Hella Line 2, and renewal of the Hvolsvöllur substation.

In the West Fjords, our transformer at Mjólká has reached the limit of its capacity, making it necessary to add a new transformer soon to increase transmission capacity into the region as well as security of supply. We are also considering a ring connection in the southern West Fjords, with a view to taking advantage of the prospective Dýrafjörður Tunnel.

We aim to further strengthen the regional networks for the future, with increased emphasis on doubling connections between areas to improve security of supply. This takes into account the industrial sites proposed in municipal land-use plans and the Master Plan for Hydro and Geothermal Energy Resources in Iceland.



Investment per year in regional networks



The regional networks are most often run at a voltage of 66 kV. Underground cables are usually installed when these networks are renewed, as the cost thereof is deemed more or less equivalent to that of overhead lines at this voltage level. In the past 10 years, almost 90km of underground cables have been laid at voltages of 132 kV, 66 kV and 33 kV, nearly 40km thereof in the regional networks.

“Grid strengthening increases Iceland’s ratio of renewable energy use, partly because more transmission capacity enables the replacement of fossil fuel systems with green electricity

Environment

The grid is one of the key pillars of sustainable and eco-friendly energy use in Iceland. Grid strengthening increases Iceland's ratio of renewable energy use, partly because more transmission capacity enables the replacement of fossil fuel systems with clean electricity, as exemplified recently by fishmeal plants in East Iceland. It is thus directly conducive to achieving government objectives to reduce greenhouse gas emissions. The grid's operation also has some contrary effects on the environment. Although the emission of pollutants in our day-to-day activities is relatively minor, new infrastructure projects do have various environmental impact. This includes the manufacturing of components for the grid and various soil disturbance, e.g. due to line tracks and the construction of transmission towers. Other environmental impact is more subjective, such as the visual effects of structures, which are mostly reversible.

Certified environmental management system

Our policy is to minimise any undesirable environmental impact. To this end, we use a structured management approach with environmental considerations intertwined in all our activities. In 2013, Landsnet passed the certification audit of its environmental management system for compliance with the ISO 14001 standard, which has placed our processes for important environmental governance under more organised control.

Environmental requirements for new infrastructure projects

Our tender documents for all investment projects include stringent environmental requirements, in which our project managers are well versed. We present our environmental and safety requirements to our contractors' employees before the commencement of any works. During the works period, such aspects of the project are overseen by inspectors and the project manager. Upon completion of line works, our staff together with key stakeholders carry out a special audit of the project's standard of finish from an environmental standpoint. Our experience with these procedures has been positive and shows that most contractors are open to such co-operation and

Hildur B. Hrólfsdóttir, Landsnet's Quality and Environmental Manager, Þórður Guðmundsson, CEO & President, Ari Arnalds, Quality Manager at Vottun hf., and Lúðvík B. Ögmundsson, Landsnet's Safety Manager, upon receiving our certification for environmental and occupational safety management.

welcome proposals for improvements. Improving environmental performance is a long-term commitment requiring a new mind-set and skills for all those involved. Despite good intentions, deviations may occur in our activities in this respect. Landsnet is responsible for making good such damage and repairing any environmental disturbance to the extent possible. Three environmental audits were carried out at the end of investment projects in 2013.

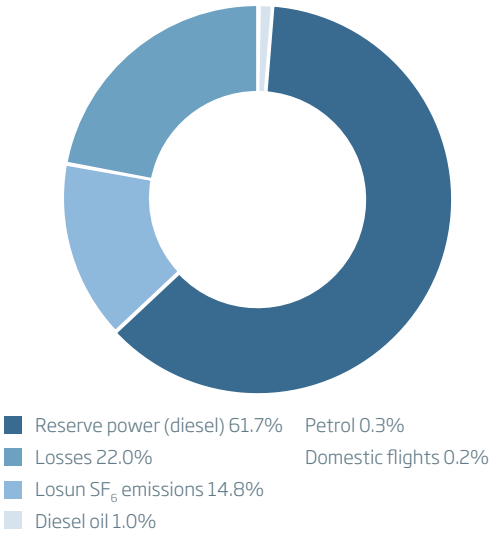
Landsnet's carbon footprint

Our activities leave a carbon footprint. The lion's share of greenhouse gas emissions from the grid's operation is due to the purchasing of reserve power, system energy losses and leakage of the insulating gas sulphur hexafluoride (SF_6). Together these factors account for 98.5% of our carbon footprint, so they should be our primary focus. Emissions due to the purchasing of reserve power are primarily due to electricity generation by diesel-powered generators. Approximately 84% of all back-up power in the grid in 2013 was generated in the West Fjords.

Our carbon footprint from power losses is due to generation to make up grid losses, which are mainly due to the increased role of geothermal power. Sulphur hexafluoride (SF_6) is a very stable molecule and serves as an excellent flame retardant or insulating gas in electrical equipment, but is also a very potent greenhouse gas. In 2013, SF_6 leakage from electrical equipment accounted for 0.51% of the total gas in the system (unconfirmed, preliminary results). This leakage level corresponds to tightness requirements for new equipment (0.5%). Total grid transmission during the year was 17,487 Gwh. Our carbon footprint in 2013 (excluding carbon sequestration through re-vegetation) was 19,874 CO_2 equivalent tonnes or 1136 kg of CO_2 equivalents per transmitted Gwh – or equivalent to 8,000 diesel passenger cars with an average fuel efficiency of 8 L/100km, each driven 12,000km per year.

Our emission calculations are based on real data on SF_6 leakage and purchases of fossil fuels for vehicles and equipment. Figures on the carbon footprint of reserve power are based on data on MWh generated and the fuel consumption of diesel generators. The results are converted to carbon dioxide equivalents using factors from the Environment Agency of Iceland, which are also used in record-keeping regarding the UN Framework Convention on Climate Change. The number of domestic flights undertaken by our staff is also used to estimate greenhouse gas emissions. International flights and the carbon footprint of grid infrastructure materials are not included in these results (e.g. steel, aluminium and concrete).

Landsnet's carbon footprint in 2013



The pie chart shows the breakdown of greenhouse gas emissions (kg CO_2 equivalents) by source.

Soil conservation

We worked on soil conservation in approximately 162 hectares of land in the valley Víðidalur á Fjöllum in co-operation with the Soil Conservation Service of Iceland. At an altitude of around 460m above sea level and believed to have been fully vegetated into the 1500s, the land is now heavily eroded and barren of vegetation. Conditions for re-vegetation were fairly favourable in the year and vegetation is beginning to stage a comeback. Young people employed by Landsnet over the summer months also distributed fertilizer and seeds south of the Langjökull glacier.


.U2.A11
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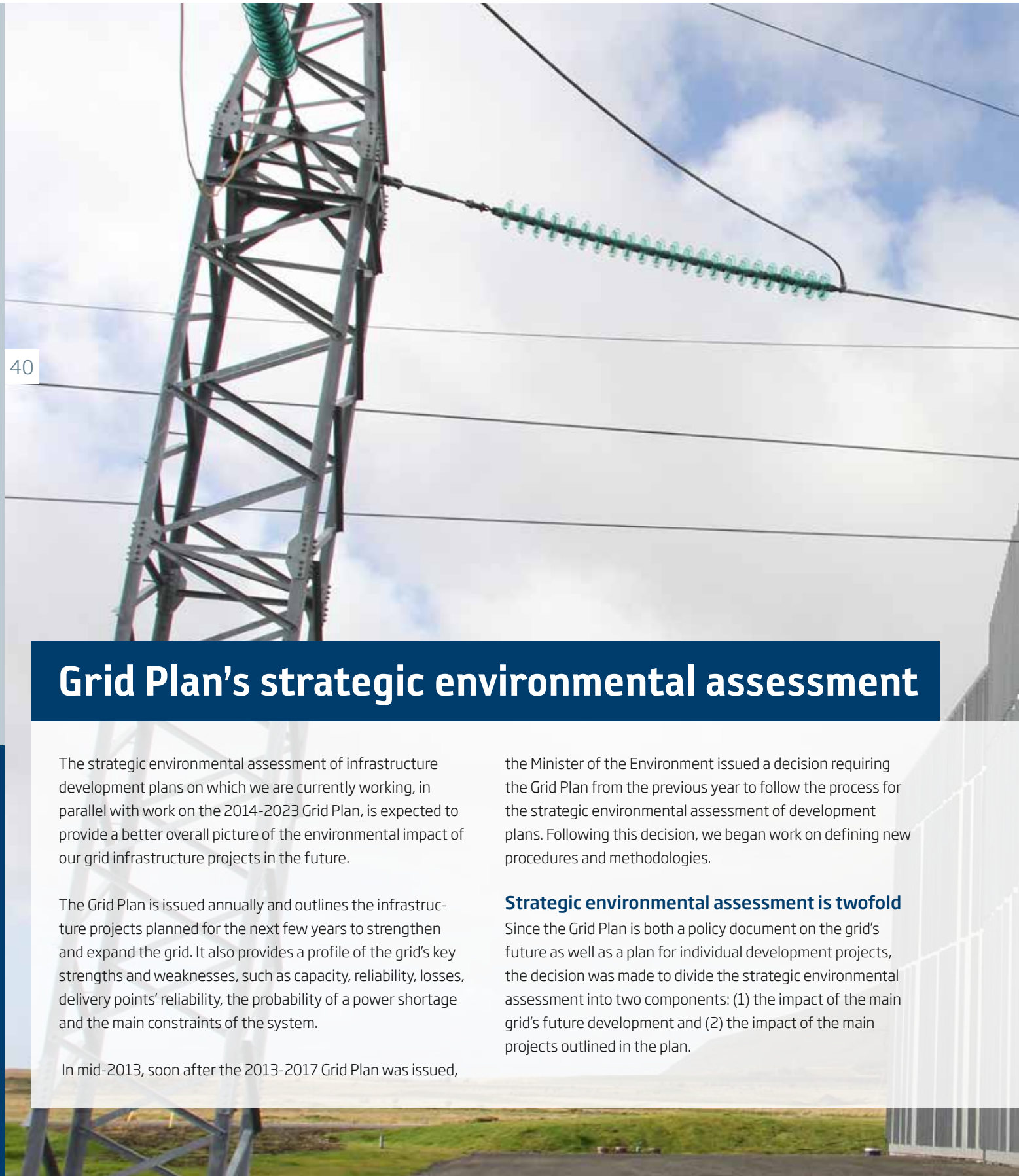
Eco-friendly innovation project

Our new static VAR system at Grundartangi is a good example of a grid infrastructure project where environmental factors were given prominence. The new project enables us to transmit more power into the area without adding transmission lines. Its design also aims to minimise the environmental impact.



Grid Plan's strategic environmental assessment

The strategic environmental assessment of infrastructure development plans on which we are currently working, in parallel with work on the 2014-2023 Grid Plan, is expected to provide a better overall picture of the environmental impact of our grid infrastructure projects in the future.

The Grid Plan is issued annually and outlines the infrastructure projects planned for the next few years to strengthen and expand the grid. It also provides a profile of the grid's key strengths and weaknesses, such as capacity, reliability, losses, delivery points' reliability, the probability of a power shortage and the main constraints of the system.

In mid-2013, soon after the 2013-2017 Grid Plan was issued, the Minister of the Environment issued a decision requiring the Grid Plan from the previous year to follow the process for the strategic environmental assessment of development plans. Following this decision, we began work on defining new procedures and methodologies.

Strategic environmental assessment is twofold

Since the Grid Plan is both a policy document on the grid's future as well as a plan for individual development projects, the decision was made to divide the strategic environmental assessment into two components: (1) the impact of the main grid's future development and (2) the impact of the main projects outlined in the plan.

The primary purpose is to ensure that due account is taken of environmental considerations in decision-making for the plan, that negative environmental impact is mitigated or prevented and information is provided on the possible environmental impact of the plan's implementation. The assessment is based on comparison between options, e.g. voltage levels, routeing and system alternatives on the one hand and a "zero option" (status quo) on the other hand (see table).

The hope is that this new procedure will enable the consultation process for new projects to start sooner and focus on main options rather than individual projects, thereby building better consensus on the grid's necessary future development.

Voltage options Decision on voltage used in the grid	• 132 kV • 220 kV • 400 kV	**Routeing decision** Routes of transmission infrastructure	• New lines, untouched area • New lines within infrastructure corridor • Existing line corridors
System alternative Decision on technical implementation	• Overhead lines • Underground • Other solutions	**Zero option** Status quo decision	• No grid infrastructure development undertaken

“Ensuring that all our staff and others working on our projects return safe and sound to their homes after each day’s work

Safety and security come first

Landsnet has always placed a high priority on personal safety and operational security. There is much at stake in achieving exemplary safety and security in our activities and, accordingly, we have developed a strong safety and security culture.

Work accidents

Our commitment to safety is reflected in our zero-tolerance approach, the key objective of which is to ensure that all our staff and others working on our projects return safe and sound to their homes after each day's work.

We failed to achieve our stated objective in 2013, as three lost-time injury events[1] occurred during the year. Two of these were minor but one was fairly serious. However, things turned out better than first thought.

Our "H factor"[2] which indicates the frequency of injuries, was 2.07 based on 200,000 hours worked at year-end 2013. This factor is on a downward trend, primarily due to more hours worked at Landsnet. However, one accident is one too many and effective measures must be taken in response. We place great emphasis on recording all incidents, however minor, to be able to react with preventive measures. The recording of safety incidents has grown year-on-year, which is very positive as more and better information will serve to facilitate prevention and reaction to future events.

Safety and security standards

Landsnet passed the certification audit for the OHSAS 18001 occupational health and safety management standard during the year and now operates in accordance with this standard. The aim thereof is to increase safety awareness among our staff and improve our safety performance. We have also had positive experience with the certified electrical safety management system RÖSK, which we have been using for some time. This system is of key importance for personal safety as well as operational security in all work on the transmission system.

That's the way you do it

At the beginning of 2013, we issued the instructional manual *That's the Way You Do It* on safety procedures and arrangements at Landsnet premises. The goal of this publication is to establish certain criteria for designers and operators, including for the design of new structures, in order to co-ordinate safety practices.

Landsnet Emergency Management

The Landsnet Emergency Management (LEM) team keeps a close watch over risks and hazards that may affect our activities, including natural phenomena such as volcanic eruptions, flooding, solar storms, epidemics, etc.

LEM's activities went according to plan in the year. Numerous issues were taken up for resolution, possible emergency scenarios were discussed and solutions sought. Two emergency management exercises were held in the year. One of these was a table exercise with the participation of two power-intensive users, focusing on Terrestrial Trunked Radio (TETRA) communications. The other was a large-scale live exercise with the participation of nearly the entire energy sector, the police, the district commissioners and many others. It focused on the response to serious natural disasters with resultant damage to Iceland's electricity system. There was general satisfaction with the exercise, which identified many important opportunities to improve emergency preparedness.

Electricity System's Emergency Partnership (ESEP)

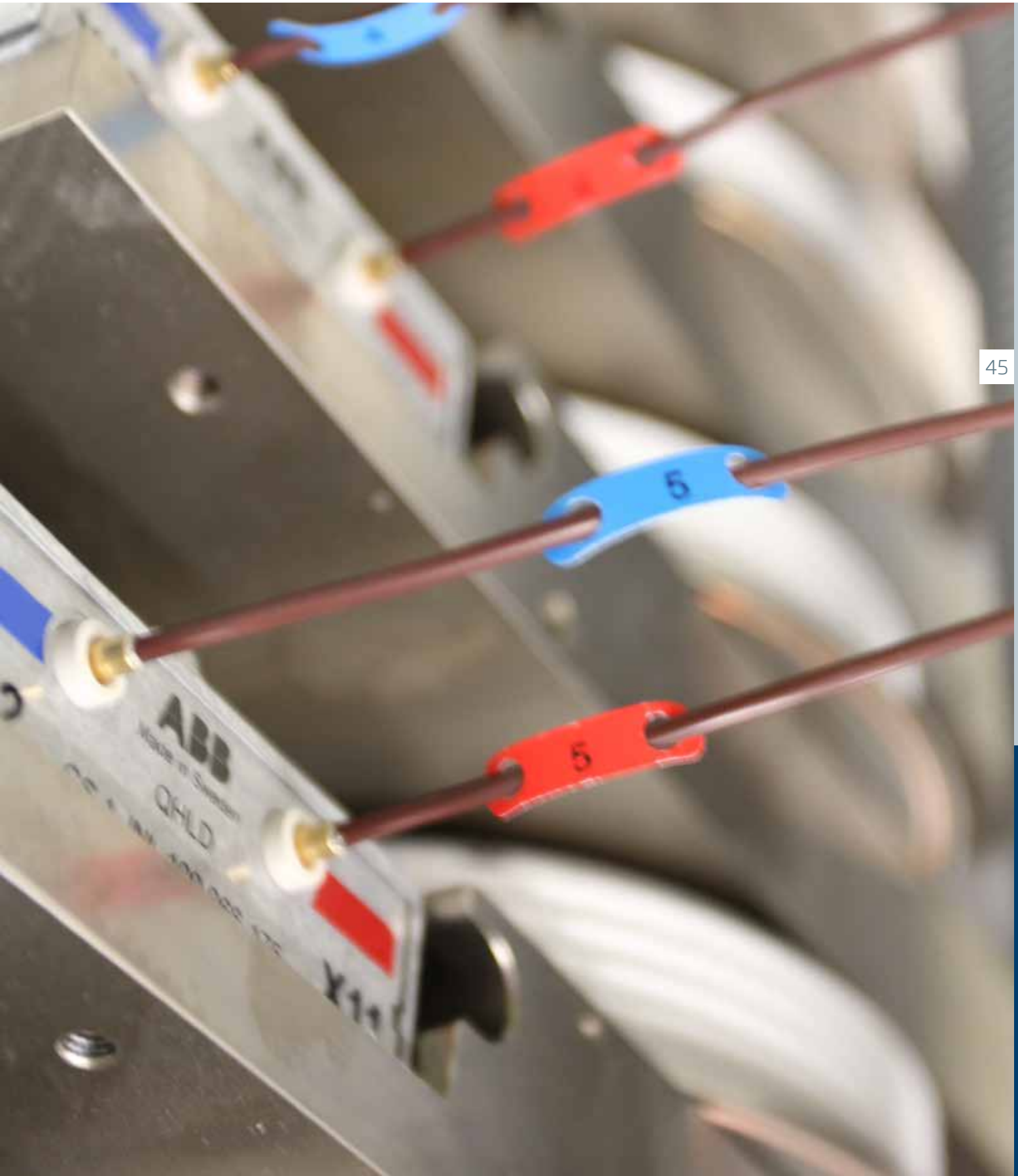
The Electricity System's Emergency Partnership (ESEP) has gradually gained in strength. Two joint meetings were held during the year, with numerous experts giving presentations relating to the electricity system. ESEP's objective is to substantially strengthen co-operation on emergency preparedness over the coming years and to hold joint exercises for the ESEP partners. Communications must be seamless when an emergency strikes. To this end, ESEP encourages increased use of TETRA in all communications within the energy sector.

1) Accidents that lead to absence from work.
2) H = frequency (from the Norwegian word "hyppighet").

A natural disaster exercise at Landsnet's Control Centre. Exercise no. 1311 on 6 November 2013.

NordBER

NordBER is the Nordic contingency planning and crisis management forum for transmission system operators and energy authorities. Its central aim is to conduct a dialogue between the partner countries and provide cross-border assistance in serious emergencies. It also organises joint Nordic exercises and seeks to identify potential risks facing the Nordic electricity sector. Landsnet and the National Energy Authority are partners in NordBER, whose activities mostly take place at three annual consultation meetings. A number of working groups are also active all year round to discuss, among other things, risk and sensitivity analysis, crisis management exercises, telecommunications security and natural hazards. NordBER's activities are growing at a significant rate and the Nordic Council has adopted resolutions on its importance, as have the national audit offices of three partner countries. Its activities have been planned for the next two years, with increased focus on joint exercises between the Nordic countries, some of which are already being prepared.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On duty every day of the year

At the heart of the grid is Landsnet's Control Centre, where staff are on duty 24/7 year round to manage transmission flows and ensure that power is delivered seamlessly and at full quality to customers – whatever the circumstances.

European study of grid reliability

The year saw the formal launch of the research project GARPUR – *Generally Accepted Reliability Principle with Uncertainty Modelling and through Probabilistic Risk Assessment* – organised by Landsnet and Reykjavik University in partnership with 17 European universities, research institutes and transmission system operators (TSOs).

GARPUR is the most extensive research project undertaken in this field globally. Its key aim is to revolutionise the prevailing methodology in grid reliability calculations and develop new and more effective criteria enabling European TSOs to better deal with the substantial changes that have taken place in the development and operation of electricity systems in Europe and work on their further development.

Landsnet in a key role

The project's origin may be traced to Landsnet's co-operation with the Norwegian TSO, Statnett, on projects relating to reliability criteria in grid design and management. Landsnet plays a key role in testing the methodologies and reliability criteria in the project, being a world leader in

real-time analysis of the stability of electricity systems through the use of smart grid solutions.

In recent years, we have placed focus on introducing technological innovations, including in IT, measurement technology and electronic technology, to assess the condition and status of the grid in real time and facilitate its more precise management. Iceland and the Icelandic grid were deemed to be an ideal testing ground for the results of the GARPUR project.

The project's scheduled duration is four years. In addition to Landsnet and Reykjavik University, the other participants are the TSOs in Norway, Belgium, France, Bulgaria, the Czech Republic and Denmark and research institutes in Norway, Belgium, Finland, the Netherlands, the United Kingdom, the Czech Republic, France, Germany, Israel and Denmark.

The project's total cost is estimated at ISK 1.7 billion. It has been awarded an ISK 1.2 billion research grant from the EU's Seventh Framework Programme.

“We have been developing our human resources in a targeted manner since 2010

Our people

We have been developing our human resources in a targeted manner since 2010 in an aim to ensure that our staff are as well equipped as possible to meet the company's future challenges. Focus has been placed on training and knowledge, restructuring HR processes and providing more accessible, relevant and targeted information for management staff.

Growing need for new staff

Our employees numbered 114 at year-end 2013, of which 79% were men and 21% women. Men comprised 67% of senior management and women 33%. Our staff are well educated and have expertise in their respective fields. Employees holding vocational education in an electrical field or a university degree in engineering and technology comprise the largest portion of our staff. Other disciplines in which our staff have been trained include business administration, computer science, economics, social science and law. We recruited 12 new employees in the year. Increased staff turnover may be expected in the coming years due to age-related retirement; about a fifth of our staff are 60 or older.

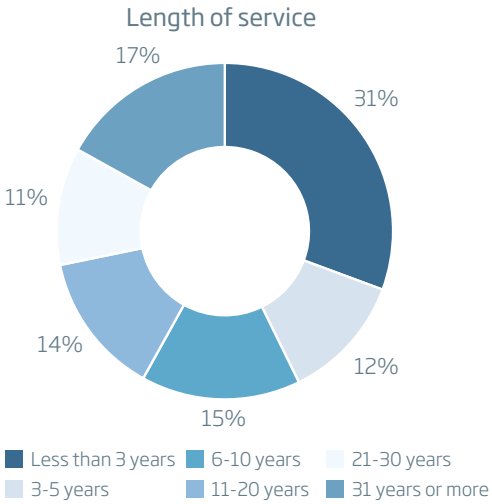
We continued to prepare new Landsnet premises in the town of Akureyri, which will improve our services in North Iceland. We place a high premium on good co-operation with other energy companies and contractors. As external expertise in the transmission system is decreasing and its operation is becoming ever more specialised, we clearly need to build our internal capabilities to be able to operate without external assistance.

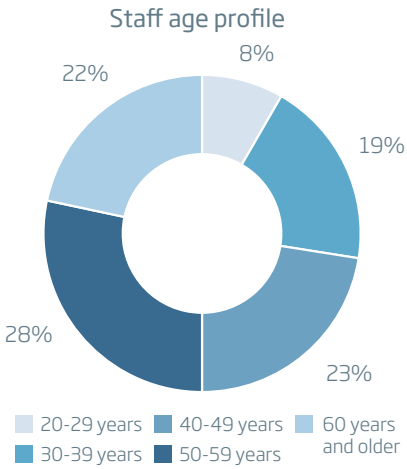
76 summer jobs

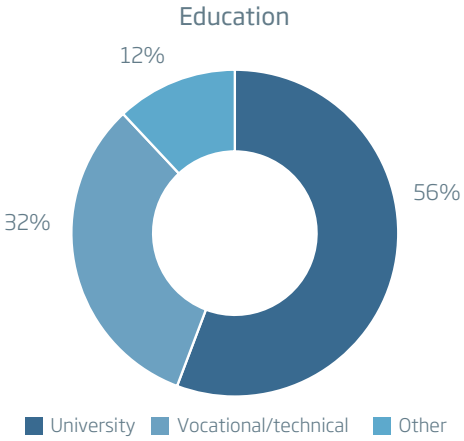
We employed 55 upper secondary school students and 21 university students in summer jobs in 2013. An emphasis is placed on affording university students with opportunities to perform real-world tasks in their respective fields of study. We thereby aim to contribute more to society.

Improving health

The health of our staff is improving. The sickness absence rate was down from 1.89% in 2012 to 1.73% in 2013. This is the second consecutive year in which the rate drops. Our aim is to be below 2%. We have endeavoured to promote good health among our people and offer them various medical services.







Satisfaction with training and education

Our employees are generally satisfied with the diverse training opportunities offered by Landsnet to enhance their professional and personal skills.

The Landsnet Academy

A major effort has been made to develop staff training and education in recent years to foster continual improvement and ensure that our employees have the capabilities and knowledge to tackle the tasks of the day and the company's future challenges.

Particular emphasis is placed on targeted instruction informed by the company's defined training and education goals. Needs analysis is used to assess the training needs of different teams and departments and training plans are devised for individuals as well as groups, teams and departments. This is followed by issuing a "Landsnet Academy Training Plan" that reflects the company's specific activities and is designed to disseminate the considerable and specialised knowledge that our staff possess.

Training in Iceland and overseas

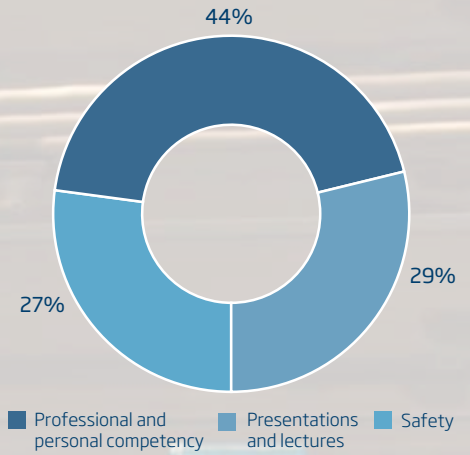
A total of 42 training courses were held for departments, groups and teams within the company during the year. Of these courses, 16 concerned safety and security and 26 aimed to enhance employees' professional and personal skills. This included instruction on avalanche barriers and wilderness first aid as well as courses in retirement preparation; project management; self-expression and public speaking; and driving and the use of snowmobiles. Furthermore, 17 presentations and lectures were given on various topics. Our staff also attended training events individually, both in Iceland and abroad, through participation in symposia and courses.

All new members of staff are provided with induction training. The training needs of new recruits in the first few months of employment are defined and every new employee is assigned a "mentor" to assist with orientation to the job. The objectives of induction training are:

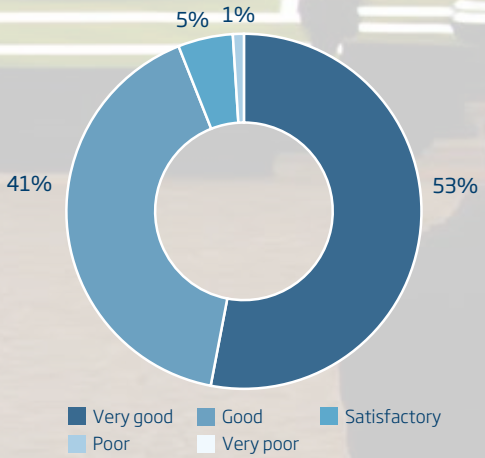
- To familiarise new staff with our activities and enable them to assimilate to the company's policies and values.
- To provide new staff with education and training in using equipment, tools and procedures required in their work to be able to attain the required level of performance as soon as possible.
- To provide new staff with specialised training defined as necessary for them to be able to perform well.
- To ensure that our staff are confident and comfortable in their work and receive support whenever needed.

Our employees' appraisal of courses and training offered in 2013 indicates a generally high level of satisfaction, with 94% of the participants rating the course attended as good or very good and 84% rating the course as useful or very useful for their work.

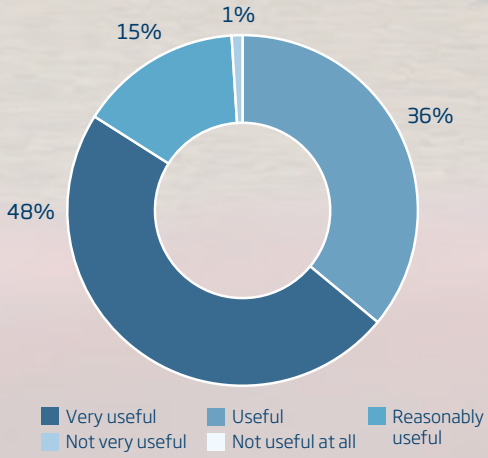
Courses for groups and divisions



How would you rate the course?



How useful do you think the course will be for your work?



“According to the income statement, Landsnet generated a total profit of ISK 2,183 million in 2013, up from ISK 801 million in 2012

Finance

Landsnet delivered a good financial performance in 2013, in line with plans. Our revenues are determined by a revenue cap under the Electricity Act. The 2011-2015 revenue cap was set during the year on the basis of profitability determined in 2012. At the end of the year, the Appeals Committee on Electricity overturned a profitability decision from 2012, creating uncertainty about part of our income base. Under the Electricity Act, Landsnet has a secure operating basis as regards regular activities and maintenance of the current grid. The risk facing the company is much rather that it is not provided with the revenue regime and capital structure necessary to take on new challenges and strengthen the current grid. A decision on Landsnet's allowable profitability must be made as soon as possible to ensure the company's operational stability.

A number of large investment projects were undertaken in 2013, with total investment of ISK 6,408 million. Most of these projects aimed to strengthen the grid. Investment in previous years had been much smaller, with grid maintenance and strengthening subsumed under larger projects. A new approach was taken last year given the importance of grid maintenance and strengthening under our statutory duties. Investment during the year was funded with cash on hand, which remains relatively unchanged year-on-year. Repayments on our long-term loans are low and not in normal sync with borrowings. A future vision for our funding is being formulated, among other things with a view to balancing out the repayment curve.

Income statement

According to the income statement, Landsnet generated a total profit of ISK 2,183 million in 2013, compared with a profit of ISK 801 million in 2012. Earnings before interest, taxes, depreciation and amortisation (EBITDA) were ISK 9,166 million, against ISK 7,773 million for 2012. The better year-on-year performance was mostly due to higher transmission revenues and lower cost of capital.

Operating revenue amounted to ISK 13,874 million. Transmission income accounted for ISK 12,277 million of this figure, up by ISK 1,360 million year-on-year, mostly due to an increase in the tariff for power-intensive consumers.

Operating expenses before depreciation and amortisation were ISK 4,709 million, up by ISK 137 million or 3% year-on-year. Net financial expenses were ISK 3,870 million in 2013, compared with ISK 4,339 million in 2012, down 10.8% year-on-year. Indexation for the year amounted to ISK 1,752 million, against ISK 2,079 million in 2012, down by ISK 327 million. Capitalised interest amounted to ISK 272 million in 2013, up by ISK 192 million. We incurred a net exchange rate loss, which was ISK 176 million higher than in 2012.

Highlights of the annual financial statements

ISK million

	2012	2013
Operating revenue	12,344	13,874
Earnings before interest and taxes (EBIT)	5,306	6,568
Profit	801	2,183
Cash flow from operating activities	5,808	7,733
Total liquid assets	10,561	10,152
Total assets	74,873	77,608
Interest-bearing liabilities	55,786	56,003
Equity ratio	17.7%	19.9%

Balance sheet

Total assets stood at ISK 77,608 million at year-end 2013, up from ISK 74,873 million a year earlier. Of this total, fixed assets accounted for ISK 66,370 million, compared with ISK 62,451 million at year-end 2012. Fixed assets in operation were ISK 63,198 million at year-end, compared with ISK 58,625 million at the end of 2012. New assets were brought into service during the year, including the sub-sea cable to the Westman Islands, the static VAR system at Klafastaðir, the substation at Búðarháls and voltage raising at Stuðlar in East Iceland.

Long-term liabilities and obligations stood at ISK 58,564 million and short-term liabilities at ISK 3,598 million at year-end 2013. At the end of 2012, in comparison, long-term liabilities and obligations were ISK 57,644 million and short-term liabilities ISK 3,966 million. No new loans were raised during the year and repayments are made on only a small part of our borrowings, as no payments are due on an ISK-denominated loan from the parent company, Landsvirkjun, until 2020. Loan repayments in 2014 are estimated at ISK 915 million, which is close to the amount repaid in 2013.

Equity at year-end 2013 stood at ISK 15,446 million, including share capital of ISK 5,903 million, as stated in the balance sheet. By comparison, equity at the end of 2012 was ISK 13,263 million. The equity ratio was 19.9% at year-end 2013, up from 17.7% at the end of 2012.

Cash flow

Net cash from operating activities was ISK 7,733 million in 2013, compared with ISK 5,808 million in 2012. Cash outflows from investing activities for the year were ISK 6,408 million and financing activities amounted to ISK 825 million. Cash at year-end 2013 was ISK 9,917 million, down by ISK 393 million year-on-year.

Long-term liabilities were 94% of total liabilities at the close of the year. Of interest-bearing debt, ISK-denominated loans now account for 89% and CFH-denominated loans for 11%. No loan refinancing will be required in 2013, as loan repayments and investments will be made with cash on hand.

Revenue cap and tariff

Landsnet operates on the basis of the Electricity Act No. 65/2003. Under Article 12 of the Act, the National Energy Authority (NEA) shall establish a revenue cap for Landsnet, which shall decide a tariff for its services in accordance therewith. The revenue cap is based on historical operating expenses, depreciation of fixed assets and Landsnet's allowable profitability as decided annually by the NEA. The profitability factor is accorded significant weight in deciding the revenue cap and is therefore of substantial importance.

On 1 October 2012, the NEA issued its decision on Landsnet's profitability based on weighted average cost of capital (WACC) for the period 2011-2015, and thereby the criteria for deciding the revenue cap, which was not set until mid-2013. On the basis of the required rate of return, we have made projections of the revenue cap and its effects on our tariffs for the said period. Under a regulation on profitability, the NEA is obliged to carry out an annual review of the transmission system operator's profitability. In April 2013, the NEA reviewed the profitability decision for 2014. This review produced substantially lower profitability results than for the period 2011-2013 and formed the basis for the 2011-2015 revenue cap.

The NEA's decision on the company's profitability for the 2011-2015 revenue cap period was appealed to the Appeals Committee on Electricity, which overturned the NEA's decision at year-end 2013 and required it to make a new one. Uncertainty about Landsnet's profitability parameters creates uncertainty in our operations. It is therefore important for decisions about the company's revenue cap and profitability to be on a firm footing to create the necessary stability with respect to charging for electricity transmission.

Transmission tariff for power-intensive consumers

In response to the imbalance that arose between the ISK-denominated revenue cap and our USD-denomin-

ated tariff as a result of the sharp depreciation of the ISK in 2008, we reduced the tariff for power-intensive consumers by 7% on 1 January 2010 and by 5% on 1 June 2011 to repay the debt that the imbalance produced. Under amendments to the Electricity Act, effective from 1 January 2011, the asset base underlying the revenue cap for power-intensive consumers was converted to USD at the exchange rate on 31 July 2007. This conversion of the asset base to USD affected the revenue cap and eliminated the rationale for the reductions from 2010 and 2011. On the basis of the said amendments, the tariff for power-intensive consumers was increased on 1 January 2013. Figure 1 shows how the tariff has developed since Landsnet's founding compared with the United States Consumer Price Index (US CPI), which the pricing of the asset base underlying our revenue cap follows. This comparison shows how the tariff developed in terms of USD purchasing power in the period. The tariff fluctuated considerably, with the collapse of the ISK as the key driver of the fluctuations, until the beginning of 2011 when the Act was amended. Since being converted to USD in the autumn of 2007, the tariff for power-intensive consumers has increased by 9.2%, compared with a 12.1% rise in the US CPI.

Transmission tariff for distributors

Despite changes in our external operating conditions, we had not changed the transmission tariff for distribution system operators since August 2009. We decided on the basis of law to raise the tariff by 9% on 1 January 2013. The NEA rejected this decision, which delayed its entry into effect, unamended from our proposals, until 1 July 2013. Figure 2 shows how the

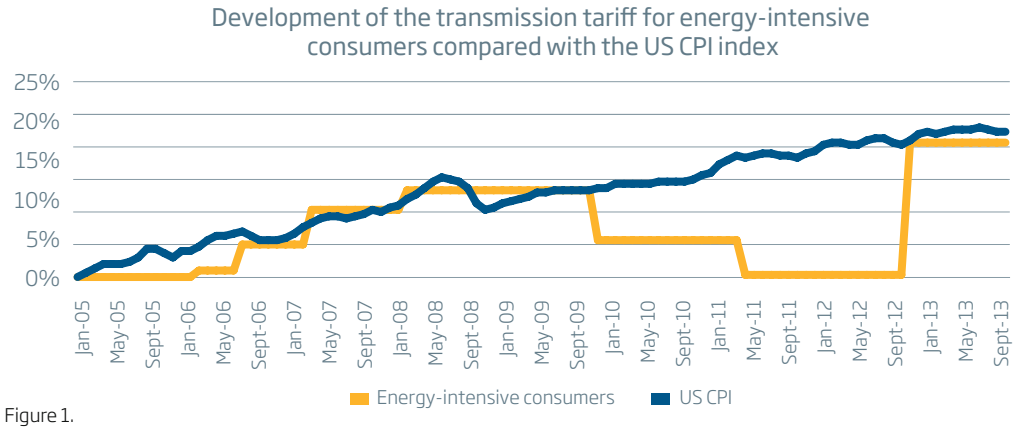


Figure 1.

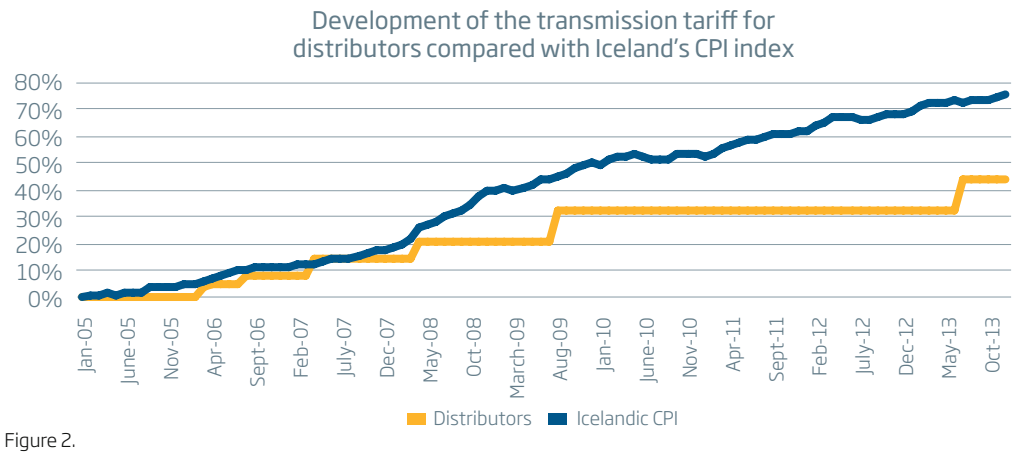


Figure 2.

tariff for distributors has developed since Landsnet's founding. Since 2009, the trend has been a sizeable real-value decrease in the tariff, as is clearly discernible from the graph. This trend reflects the rationalisation that has been achieved in our charging of distributors. The proportion of transmission costs to the total electricity costs of households and businesses has dropped markedly since Landsnet's founding, or from 12% to 9% at the beginning of 2013. These efficiency gains are largely due to grid expansion, profitable investment and mostly unchanged real operating costs despite the grid's expansion.

Tariff for ancillary services and transmission losses

Ancillary services are the services we provide to maintain operational security and balance between supply and demand of electricity at any given time. This includes spinning reserves[1)] for frequency control and disturbances, non-spinning reserves[2)] and instantaneous disturbance reserves[3)]. We must also provide guaranteed regulating power to operate a balancing energy market. To meet this statutory obligation, we purchase electricity, mainly from generating companies, and procure access to non-spinning reserves from distributors.

Under the Electricity Act, we must provide electricity to replace grid losses. From the outset, the arrangement of such purchases has been that the generators make offers to Landsnet for the purchase of electricity on the basis of a previous auction. We have entered into a one-year agreement on electricity purchasing for this purpose on the basis of such an auction.

Both types of purchasing are subject to regulation by the NEA to ensure that Landsnet does not set a higher tariff than is commensurate with the purchase price plus a 1.5% margin to cover administration costs. The tariff is identical for distributors and power-intensive consumers and published in ISK. Figure 3 shows how the tariff developed until year-end 2013. As can be seen, the relative proportions between the two types of charges has changed, as the cost of transmission losses decreased for a long period.

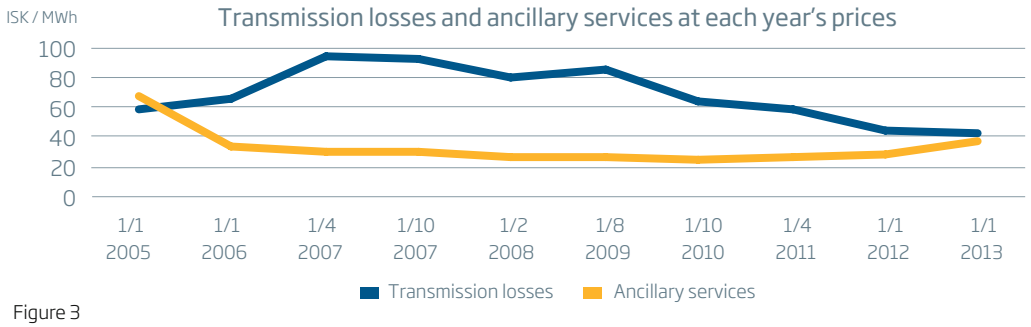
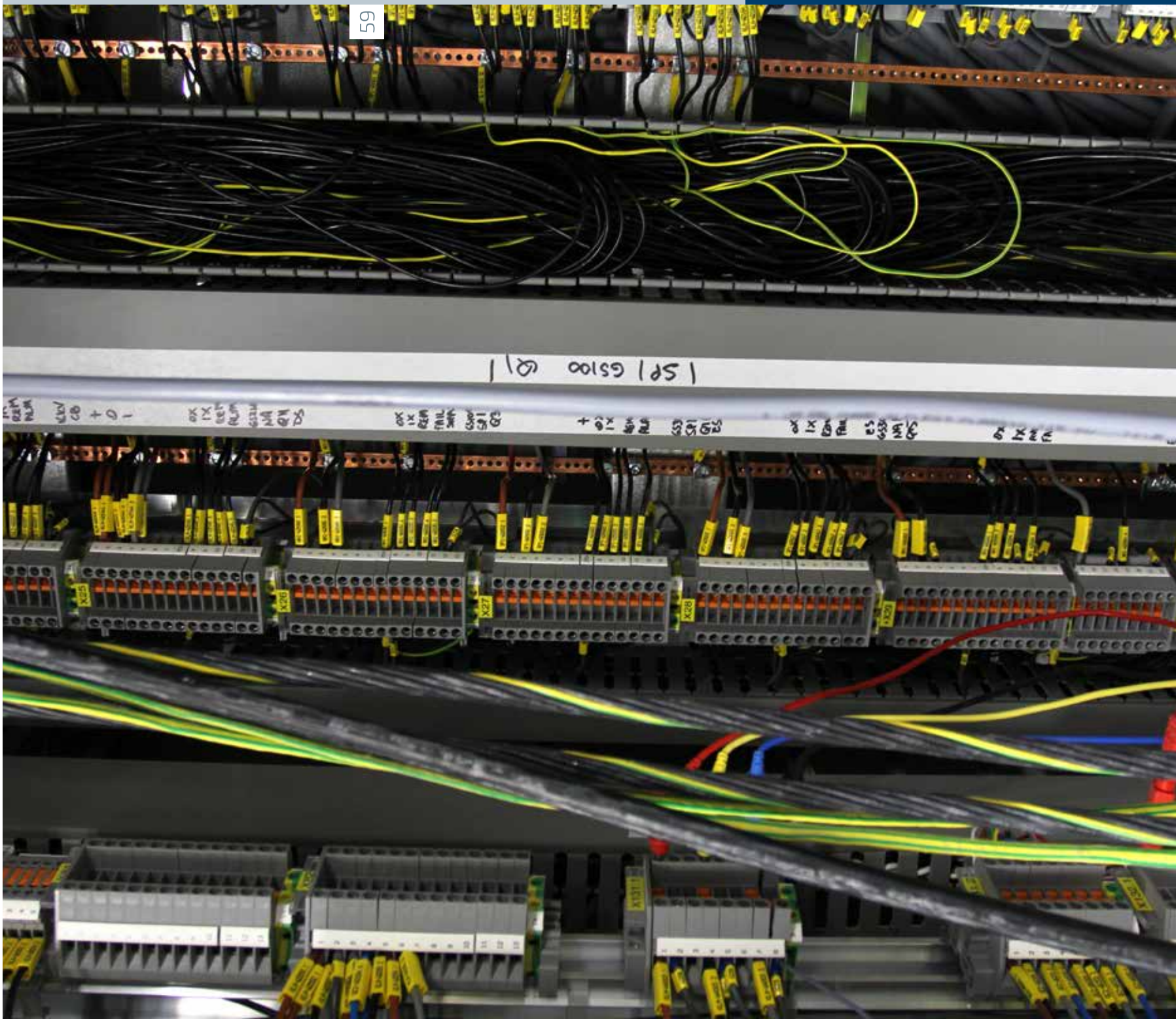


Figure 3

1) The reserve ('back-up') power already connected to the grid and immediately available.
2) Generating capacity that is not connected to the power system but can be brought online, connected to the system and fully utilised within a short time frame.
3) Reactive power activated either automatically or manually during a short deviation from normal operating conditions.



Ambitious design

A 3D image of Landsnet's substation at Bolungarvík currently under construction and an image of tubular transmission towers (p. 62) to be used near Hafnarfjörður town – examples of the ambitious design of new transmission infrastructure to mitigate visual impact.

Innovation and research

Landsnet has been increasing its focus on innovation and R&D and spends considerable resources on such projects every year. The key points of emphasis in our innovation programme are modern infrastructure design and increased use of high-tech solutions in every area. Examples of this include a new generation of transmission towers and substations developed in an extensive design innovation process at Landsnet, the GARPUR research project, smart grid solutions to increase transmission capacity and projects to analyse the cost and life cycle of underground cables. We are currently analysing the effects of a possible sub-sea cable to Europe, such as with respect to the costs involved, transmission and generation in Iceland and the effects on the energy market and pricing.

The new designs have already delivered benefits in the form of the new buildings at Klafastaðir and Búðarháls, in addition to substations currently under construction. Their design rationale aims for standardised, enclosed buildings to minimise initial and operating costs, increase operational security and mitigate environmental impacts.

New tower designs

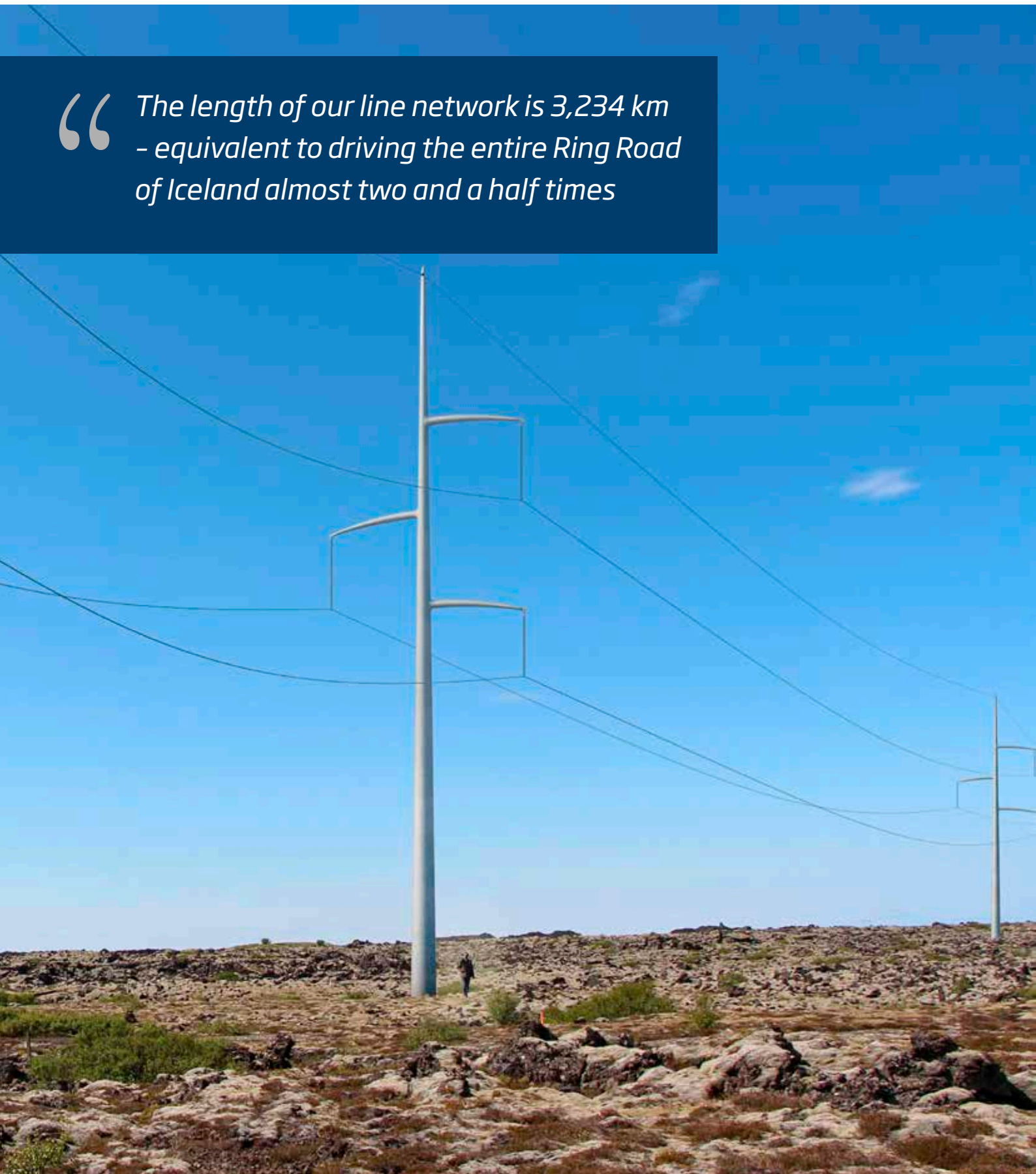
We continue to work on the design and development of new transmission towers in co-operation with the Norwegian TSO, Statnett, with the assistance of Icelandic and foreign experts. Of particular interest is the design and development of tubular towers (p. 62) to be used in narrow line corridors. This involves the development of technological solutions never before used in transmission towers.

Research project on underground cables

In light of the growing use of underground cables, we have launched a research project in partnership with the Danish TSO, Energinet.dk, StellaCable in Denmark and Reykjavik University to seek ways of reducing the cost of undergrounding, improving site restoration and reducing environmental impact.

This is a logical continuation of a previous research project on the life-cycle costs of overhead lines and underground cables, the results of which showed that life-cycle costs are completely dependent on specific circumstances, making it important to assess costs on a case-by-case basis.

“ The length of our line network is 3,234 km – equivalent to driving the entire Ring Road of Iceland almost two and a half times



Transmission line network in 2013

Voltage [kV]	Line name	KKS no.	First year in service	Connected substations	Length [km]
220	**Brennimelur Line 1**	BR1	1977	Geithals - Brennimelur	59
	Búðarháls Line 1	BH1	2013	Búðarháls - Langalda	6
	Búrfell Line 1	BU1	1969	Búrfell - Írafoss	61
	Búrfell Line 2	BU2	1973	Búrfell - Kolviðarhóll	86
	Búrfell Line 3	BU3	1992	Búrfell - Hamranes	119
	Fljótsdalur Line 3	FL3	2007	Fljótsdalur - Reyðarfjörður	49
	Fljótsdalur Line 4	FL4	2007	Fljótsdalur - Reyðarfjörður	53
	Hamranes Line 1	HN1	1969	Geithals - Hamranes	15
	Hamranes Line 2	HN2	1969	Geithals - Hamranes	15
	Hrauneyjafoss Line 1	HR1	1982	Hrauneyjafoss - Sultartangi	20
	ÍSAL Line 1	IS1	1969	Hamranes - ÍSAL	2
	ÍSAL Line 2	IS2	1969	Hamranes - ÍSAL	2
	Elkem Line 1	JA1	1978	Brennimelur - Elkem	5
	Kolviðarhóll Line 1	KH1	1973	Kolviðarhóll - Geithals	17
	Norðurál Line 1	NA1	1998	Brennimelur - Norðurál	4
	Norðurál Line 2	NA2	1998	Brennimelur - Norðurál	4
	Sigalda Line 2	SI2	1982	Sigalda - Hrauneyjafoss	9
	Sigalda Line 3	SI3	1975	Sigalda - Búrfell	37
	Sog Line 3	SO3	1969	Írafoss - Geithals	36
	Sultartangi Line 1	SU1	1982	Sultartangi - Brennimelur	122
	Sultartangi Line 2	SU2	1999	Sultartangi - Búrfell	13
	Sultartangi Line 3	SU3	2006	Sultartangi - Brennimelur	119
	Vatnsfell Line 1	VF1	2001	Vatnsfell - Sigalda	6
				Total 220 kV	**857**
132	**Substation 7 (line/underground cable)**	AD7	1990	Hamranes - Hnoðraholt	10
	Blanda Line 1	BL1	1977	Blanda - Laxárvatn	33
	Blanda Line 2	BL2	1977	Blanda - Varmahlíð	32
	Eyvindará Line 1	EY1	1977	Hryggstekkur - Eyvindará	28
	Fitjar Line 1	MF1	1991	Rauðimelur - Fitjar	7w
	Fljótsdalur Line 2 (line/underground cable)	FL2	1978	Fljótsdalur - Hryggstekkur	25
	Geiradalur Line 1	GE1	1980	Glerárskógar - Geiradalur	47
	Glerárskógar Line 1	GL1	1983	Hrútatunga - Glerárskógar	34
	Hafnarfjörður 1 (underground cable)	HF1	1989	Hamranes - Hafnarfjörður	4
	Hólar Line 1	HO1	1981	Teigarhorn - Hólar	75
	Hrútatunga Line 1	HT1	1976	Vatnshamrar - Hrútatunga	77
	Korpa Line 1	KO1	1974	Geithals - Korpa	6
	Krafla Line 1	KR1	1977	Krafla-Rangárvellir	82
	Krafla Line 2	KR2	1978	Krafla - Fljótsdalur	123
	Laxárvatn Line 1	LV1	1976	Hrútatunga - Laxárvatn	73
	Mjólká Line 1	MJ1	1981	Geiradalur - Mjólká	81
	Nesjavellir Line 1 (line/underground cable)	NE1	1998	Nesjavellir - Korpa	32
	Nesjavellir Line 2 (underground cable)	NE2	2010	Nesjavellir - Geithals	25
	Prestbakki Line 1	PB1	1984	Hólar- Prestbakki	171
	Rangárvellir Line 1	RA1	1974	Rangárvellir - Varmahlíð	88
	Rangárvellir Line 2 (underground cable)	RA2	2009	Rangárvellir - Krossanes	5
	Rauðamelur Line 1	RM1	2006	Reykjanes - Rauðimelur	15
	Rauðavatn Line 1 (line/underground cable)	RV1	1953	Geithals - A12	3
	Sigalda Line 4	SI4	1984	Sigalda - Prestbakki	78
	Sog Line 2	SO2	1953	Írafoss - Geithals	44

Voltage [kV]	Line name	KKS no.	First year in service	Connected substations	Length [km]
	Stuðlar Line 1 (underground cable)	SR1	2005	Hryggstekkur - Stuðlar	16
	Suðurnes Line 1	SN1	1991	Hamranes - Fitjar	31
	Svartsengi Line 1	SM1	1991	Svartsengi - Rauðimelur	5
	Teigarhorn Line 1	TE1	1981	Hyggstekkur - Teigarhorn	50
	Vatnshamrar Line 1	VA1	1977	Vatnshamrar - Brennimelur	20
				Total 132 kV	**1317**
66	**Akraneslína 1 (underground cable)**	AK1	1996	Brennimelur - Akranes	17
	Andakíll Line 1	AN1	1966	Andakíll - Akranes	35
	Bolungarvík Line 1	BV1	1979	Breiðidalur - Bolungarvík	17
	Bolungarvík Line 2 (underground cable)	BV2	2010	Ísafjörður - Bolungarvík	12
	Breiðadalur Line 1	BD1	1975	Mjólká - Breiðidalur	36
	Dalvík Line 1	DA1	1982	Rangárvellir - Dalvík	39
	Eskifjörður Line 1	ES1	2001	Eyvindará - Eskifjörður	29
	Fáskrúðsfjörður Line 1	FA1	1989	Stuðlar - Fáskrúðsfjörður	17
	Flúðir Line 1	FU1	1978	Búrfell - Flúðir	27
	Grundarfjörður Line 1	GF1	1985	Vogaskeið - Grundarfjörður	35
	Hella Line 1	HE1	1995	Flúðir - Hella	34
	Hella Line 2	HE2	1948	Hella - Hvolsvöllur	13
	Hveragerði Line 1	HG1	1982	Ljósifoss - Hveragerði	15
	Hvolsvöllur Line 1	HV1	1972	Búrfell - Hvolsvöllur	45
	Ísafjörður Line 1 (line/underground cable)	IF1	1959	Breiðidalur - Ísafjörður	15
	Kópasker Line 1	KS1	1983	Laxá - Kópasker	83
	Lagarfoss Line 1 (line/underground cable)	LF1	1971	Lagarfoss - Eyvindará	28
	Laxá Line 1	LA1	1953	Laxá - Rangárvellir	58
	Ljósafoss Line 1 (underground cable)	LJ1	2002	Ljósifoss - Írafoss	1
	Neskaupstaður Line 1	NK1	1985	Eskifjörður - Neskaupstaður	18
	Ólafsvík Line 1	OL1	1978	Vegamót - Ólafsvík	49
	Rimakot Line 1	RI1	1988	Hvolsvöllur - Rimakot	22
	Sauðárkrókur Line 1	SA1	1974	Varmahlíð - Sauðárkrókur	22
	Selfoss Line 1	SE1	1981	Ljósifoss - Selfoss	20
	Selfoss Line 2	SE2	1947	Selfoss - Hella	32
	Seyðisfjörður Line 1	SF1	1996	Eyvindará - Seyðisfjörður	20
	Steingrímsstöð Line 1 (line/underground cable)	ST1	2003	Steingrímsstöð - Ljósafoss	3
	Stuðlar Line 2	SR2	1983	Stuðlar - Eskifjörður	18
	Tálknafjörður Line 1	TA1	1985	Mjólká - Keldeyri	45
	Vatnshamrar Line 2	VA2	1974	Andakíll - Vatnshamrar	2
	Vegamót Line 1	VE1	1974	Vatnshamrar - Vegamót	64
	Vogaskeið Line 1	VS1	1974	Vegamót - Vogaskeið	25
	Vopnafjörður Line 1	VP1	1980	Lagarfoss - Vopnafjörður	58
	Þeistareykir Line 2	TR2	2013	Þeistareykir - Höfuðreyðarmúli	11
	Þorlákshöfn Line 1	TO1	1991	Hveragerði - Þorlákhöfn	19
				Total 66 kV	**987**
33	**Húsavík Line 1**	HU1	1964	Laxá - Húsavík	26
	Westman Islands Line 1 (sub-sea cable)	VM1	1978	Westman Islands - Rimakot	15
	Westman Islands Line 2 (sub-sea cable)	VM2	1966	Westman Islands - Rimakot	16
	Westman Islands Line 3 (sub-sea cable)	VM3	2013	Westman Islands - Rimakot	16
				Total 33 kV	**73**
				Total	**3234**

Substations in 2013

Substation name	KKS Code	Co-owner	Voltage [kV]	First year in service	Number of switch outputs	Number of transformers
Substation 12	A12	OR	132	2006	1	1
Akranes	AKR	OR	66	1987	4	2
Andakíll	AND	OR	66	1974	3	1
Ásbrú	ASB		33	2011	6	2
Bessastaðir	BES		132/33	2003	3/2/1	2
Blanda	BLA	LV	132	1991	6	3
Bolungarvík	BOL	OV	66/11	1977	2/6	1
Breiðidalur	BRD	OV	66/33/19/11	1959	4/2/2/1	1
Brennimelur	BRE	RA	220/132/66/11	1978	9/4/2/10	3
Búðarháls	BUD		220	2013	2	0
Búrfell	BUR		220/66	1999	10/4	3
Dalvík	DAL	RA	66/33/11	1981	2/3/8	1
Eskifjörður	ESK	RA	66/33/11	1993	5/-/7	2
Eyvindará	EYV	RA	132/66/33/11	1975	1/6/1/8	3
Fáskrúðsfjörður	FAS	RA	66/33/11	1998	3/1/5	2
Fitjar	FIT	HS	132	1990	4	2
Fljótsdalur	FLJ		220/132	2007	4/10	2
Flúðir	FLU	RA	66/11	1995	3/7	1
Geiradalur	GED	OV	132/33/19	1983	3/1/4	1
Geithális	GEH		220/132	1969	8/9/2	2
Glerárskógar	GLE	RA	132/19	1980	3/4	1
Grundarfjörður	GRU	RA	66/19	1987	1/6	1
Hamranes	HAM		220/132/11	1989	8/8/10	3
Hella	HLA	RA	66/11	1995	4/6	1
Hnoðraholt	HNO	OR	132	1990	4	2
Hólar	HOL	RA	132/19/11	1984	4/1/9	2
Hrauneyjafoss	HRA	LV	220	1981	6	3
Hrútatunga	HRU	RA	132/19	1980	4/5	1
Hryggstekkur	HRY	RA	132/66/11	1978	5/1/4	1
Húsavík	HUS	RA	33/11/6	1978	2/1/4	2
Hveragerði	HVE	RA	66/11	1983	3/6	1
Hvolsvöllur	HVO	RA	66/11	1995	5/7	1
Írafoss	IRA	LV	220/132/66/11	1953	2/7/-/7	5
Ísafjörður	ISA	OV	66/11	1959	4/9	2
Keldeyri	KEL	OV	66/33/11	1959	2/2/3	1
Klafastaðir	KLA		220/16	2013	1/4	1
Kolviðarhóll	KOL		220	2006	6	0
Korpa	KOR	OR	132/33/11	1976	7/6/-	3
Kópasker	KOP	RA	66/33/11	1980	1/3/5	3
Krafla	KRA	LV	132/11	1977	4/-	2
Lagarfoss	LAG	RA	66	2007	5	0
Laxá	LAX		66/33/11	1937	10/1/4	6
Laxárvatn	LAV	RA	132/33/11	1977	3/4/8	1
Lindarbrekka	LIN	RA	66/11	1985	1/4	1
Ljósafoss	LJO	LV	66/11	1937	6/7	2
Mjólká (lower)	MJO	OV	66/33/11	1980	2/1/-	1
Mjólká (upper)	MJO	OV	132/66	1980	2/2	1
Nesjavellir	NES	OR	132	1998	7	4
Neskaupstaður	NKS	RA	66/11	1994	2/7	2

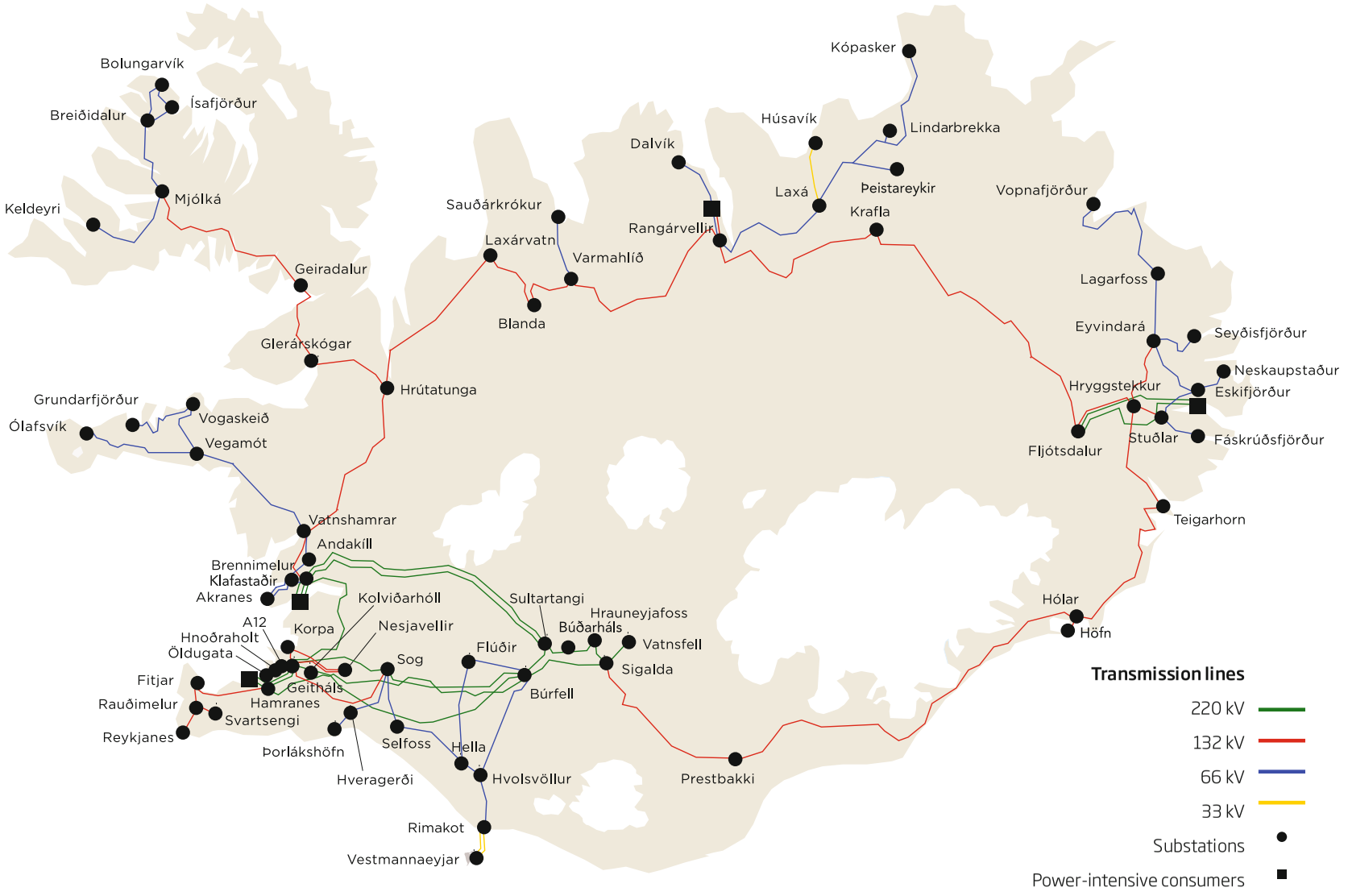
Substation name	KKS Code	Co-owner	Voltage [kV]	First year in service	Number of switch outputs	Number of transformers
Ólafsvík	OLA	RA	66/19	1980	1/5	1
Prestbakki	PRB	RA	132/19	1984	3/1	1
Rangárvellir	RAN	RA	132/66/11	1974	9/8/8	3
Rauðimelur	RAU		132	2006	3	0
Reykjanes	REY	HS	132	2006	1	0
Rimakot	RIM	RA	66/33/11	1990	1/5/2	2
Sauðárkrókur	SAU	RA	66/33/11	1977	3/1/8	2
Selfoss		SEL	RA	66/11	2005	5/153
Seyðisfjörður	SEY	RA	66/11	1957	1/9	1
Sigalda	SIG	LV	220/132	1977	4/1	1
Silfurstjarnan	SIL	RA	66/11	1992	1/3	1
Steingrímsstöð	STE	LV	66/11	1959	1/1	1
Stuðlar	STU	RA	132/66/11	1980	3/4/6	3
Sultartangi	SUL		220/11	1999	6/-	2
Svartsengi	SVA	HS	132	1997	4	2
Teigarhorn	TEH	RA	132/33/11	2005	3/2/-	1
Varmahlíð	VAR	RA	132/66/11	1977	3/1/5	1
Vatnsfell	VAF		220/11	2001	2	2
Vatnshamrar	VAT	RA	132/66/19	1976	3/5/6	3
Vegamót	VEG	RA	66/19	1975	4/4	1
Westman Islands	VEM	RA	33	2002	2	2
Vogaskeið	VOG	RA	66/19	1975	3/6	1
Vopnafjörður	VOP	RA	66/11	1982	1/6	1
Þeistareykir	THR		66	2013	1	1
Þorlákshöfn	TOR	RA	66/11	1991	1/6	1
Öldugata	OLD		132	1989	5	2

RA=RARIK (Iceland State Electricity), OV=Westfjord Power Company,
HS=Sudurnes Regional Heating LV=Landsvirkjun, OR=Reykjavík Energy

Energy terms/abbreviations

kV = kilovolt
kW = kilowatt
MW = megawatt = 1000 kW
kWh = kilowatt hour
MWh = megawatt hour = 1000 kWh
GWh = gigawatt hour = 1000 MWh

The grid in 2013



FINANCIAL STATEMENTS
2013

Contents

Endorsement by the Board of Directors and the CEO

Landsnet hf was established in August 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 2013

According to the income statement, profit and total profit for the year amounted to ISK 2.2 billion. According to the balance sheet, the Company's equity at year end amounted to ISK 15.4 billion, including share capital in the amount of ISK 5.9 billion. Average number of employees was 122.

Share capital at year end 2013 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%

Accumulated deficit amounts to ISK 1.5 billion at year end and therefore not permitted to pay dividend to shareholders.

Under the current Electricity Act, the National Energy Authority is charged with setting a revenue cap for Landsnet hf. Landnet and the National Energy Authority have been unable to agree on the settlement for the years 2006-2009. In addition, a decision is still pending on the profitability criteria for the years 2011, 2012 and 2013. This creates some uncertainty with regard to the Company's operating results and financial position at year end 2013. Note 31 provides a detailed account of the status of this issue.

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 Coporate Governance Statement, which is a appendix in the Financial Statements, provides further information.

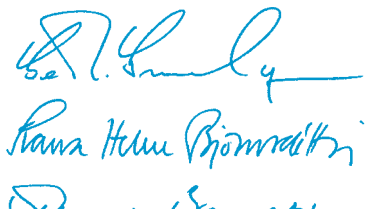
Statement of the Board of Directors and the CEO

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 2013, its assets, liabilities and financial position as at 31 December 2013 and its cash flows for the financial year 2013.
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 (see notes 29 and 31).

The Board of Directors and the CEO have today discussed the annual financial statements of Landsnet hf. for the year 2013 and confirmed them by means of their signatures.

Reykjavik, 12 February 2014

The Board of Directors:



CEO:

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, 2013, the statements of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the EU, and for such internal control as management determines 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, 2013, 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.

Report on the Board of Directors report

Pursuant to the legal requirement under Article 104, Paragraph 2 of the Icelandic Financial Statement Act No. 3/2006, we confirm that, to the best of our knowledge, the report of the Board of Directors accompanying the financial statements includes the information required by the Financial Statement Act if not disclosed elsewhere in the Financial Statements.

Reykjavik, 12 February 2014.

KPMG ehf.

Income Statement for the year 2013

	Notes	2013	2012
Operating revenue			
Transmission	5,6	13.717.748	12.228.758
Other income	7	156.534	115.704
		13.874.282	12.344.462
Operating expenses			
Energy procurement costs	8	1.499.804	1.383.844
Transmission costs	9,10	3.793.580	3.922.280
System operation	9,10	1.087.733	977.253
Other operating expenses	9,10	925.417	755.469
		7.306.534	7.038.846
Operating profit		6.567.748	5.305.616
Financial income		141.041	67.382
Financial expenses		(4.010.935)	(4.406.306)
Net financial expenses	11	(3.869.894)	(4.338.924)
Share in net earnings of associated company	16	25.055	18.580
Profit before income tax		2.722.909	985.272
Income tax	12,24	(539.511)	(184.319)
Profit		2.183.398	800.953
Earnings per share:			
Basic and diluted earnings per each ISK 1 share	22	0,37	0,14

Notes no. 1 to 35 are an integral part of these financial statements.

Statement of Comprehensive Income for the year 2013

	Notes	2013	2012
Profit		2.183.398	800.953
Total items under total profit recognised among equity		0	0
Total profit of the year		2.183.398	800.953

Notes no. 1 to 35 are an integral part of these financial statements.

Balance Sheet as at 31 December 2013

	Notes	2013	2012
Assets			
Fixed assets in operation	13	63.197.621	58.625.415
Projects under construction	13	1.086.550	1.769.671
Intangible assets	14	1.392.994	1.376.230
Investment in subsidiary	15	500	500
Investment in associates	16	668.906	643.851
Long-term note		23.286	34.929
Fixed assets		66.369.857	62.450.596
Inventories	17	519.313	522.301
Receivable from parent company	32	0	648.398
Trade and other receivables	18	567.397	690.778
Marketable securities	19	234.344	251.027
Cash and cash equivalents	20	9.917.204	10.309.772
Current assets		11.238.258	12.422.276
Total assets		77.608.115	74.872.872
Equity			
Share capital		5.902.733	5.902.733
Revaluation account		11.027.997	11.593.238
Accumulated deficit		(1.484.497)	(4.233.136)
Equity	21	15.446.233	13.262.835
Liabilities			
Long term liabilities from parent company	23	44.235.700	42.675.190
Other interest bearing long-term liabilities	23	10.852.410	12.141.815
Deferred income tax liability	24	2.331.443	1.791.932
Deferred income	25	369.222	300.678
Provision due to site restoration	26	775.163	734.307
Long-term liabilities and obligations		58.563.938	57.643.922
Loans from parent company	23	1.936.526	1.402.366
Current maturities	23	914.607	968.844
Trade and other payables	28	746.811	1.594.905
Short-term liabilities		3.597.944	3.966.115
Total liabilities		62.161.882	61.610.037
Total equity and liabilities		77.608.115	74.872.872

Notes no. 1 to 35 are an integral part of these financial statements.

Statement of Changes in Equity for the year 2013

	Share capital	Revaluation account	Accumulated deficit	Total
Year 2012:				
Equity at 1 January 2012	5.902.733	12.293.653	(5.734.504)	12.461.882
Total comprehensive income			800.953	800.953
Depreciation on revaluation recognised under accumulated deficit		(700.415)	700.415	0
Equity at 31 December 2012	5.902.733	11.593.238	(4.233.136)	13.262.835
Year 2013:				
Equity at 1 January 2013	5.902.733	11.593.238	(4.233.136)	13.262.835
Total comprehensive income			2.183.398	2.183.398
Depreciation on revaluation recognised under accumulated deficit		(565.241)	565.241	0
Equity at 31 December 2013	5.902.733	11.027.997	(1.484.497)	15.446.233

Notes no. 1 to 35 are an integral part of these financial statements.

Statement of Cash Flows for the year 2013

	Notes	2013	2012
Cash flow from operating activities			
Operating profit		6.567.748	5.305.616
Adjustments for:			
Profit from sales of fixed assets		(865)	(1.214)
Depreciation and amortisation	10	2.597.921	2.467.552
Working capital from operation before financial items		9.164.804	7.771.954
Operating assets, decrease (increase)		791.449	(128.552)
Operating liabilities, (decrease) increase		(459.392)	149.657
Net Cash from operating activities before financial items		9.496.861	7.793.059
Interest income received		141.041	49.839
Interest expenses paid and foreign exchange difference		(1.904.633)	(2.034.834)
Net cash from operating activities		7.733.269	5.808.064
Cash flow from investing activities			
Investment in transmission infrastructures	13	(6.040.219)	(2.001.415)
Other investments	13	(465.383)	(511.729)
Proceeds from sale of property, plant and equipment		2.697	82.609
Dividend from associated company		0	1.548
Change in unpaid construction costs, increase		94.822	217.580
Net cash to investment activities		(6.408.083)	(2.211.407)
Cash flow from financing activities			
Change in loans from parent company		0	(3.657.360)
Payments of long-term liabilities and provisions		(913.374)	(510.278)
Change in deferred income		88.500	178.520
Net cash to financing activities		(824.874)	(3.989.118)
Net increase (decrease) in cash and cash equivalents		500.312	(392.461)
Effect of exchange rate changes on cash and cash equivalents		(892.880)	459.317
Cash and cash equivalents at 1 January		10.309.772	10.242.916
Cash and cash equivalents at 31 December	20	9.917.204	10.309.772

Notes no. 1 to 35 are an integral part of these financial statements.

Notes to the Financial Statements

1. Reporting entity

Landsnet hf has its headquarters in Iceland and is domiciled at Gylfaflöt 9 in Reykjavik, Iceland. The Company is a subsidiary of Landsvirkjun, 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 12 February 2014.

Details of the Company's accounting policies are included in note 35.

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 35c - Fixed assets in operation
- Note 14 and 35d - Intangible assets
- Note 26 and 35j - Estimation of provision due to site restoration
- Note 24 and 35n - 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. Lansdnet revaluates part of fixed assets to fari 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 intest at the reporting date.

See accounting policies in note 35k

Transmission revenue consist of:	2013	2012
Energy transmission	12.277.156	10.916.642
Transmission losses and ancillary services	1.320.226	1.203.586
Service income	30.950	26.497
Input fees	89.416	82.033
Transmission revenue total	13.717.748	12.228.758

5. Revenue, contd.:

Landsnet's largest customers are also shareholders in the company. Further information on revenues from shareholders is provided in Note 32 on related parties.

6. Energy transmission

Energy transmission consist of:

	2013	2012
Energy transmission to power-intensive consumers	8.785.696	7.660.746
Energy transmission to distribution system operators	3.491.460	3.255.896
Energy transmission total	12.277.156	10.916.642

7. Other income

Other income consist of:

Income from work sold	74.501	61.924
Rental income	8.828	11.169
Income from guarantees of origin and certification	70.823	41.397
Sales profit from fixed assets	865	1.214
Other income	1.517	0
Other income total	156.534	115.704

8. Energy procurement costs

Energy procurement costs consist of:

Electricity purchases due to transmission losses	854.946	883.967
Purchase of ancillary services	644.858	499.877
Energy procurement costs total	1.499.804	1.383.844

9. Personnel expenses

See accounting policies in note 35i

Salaries and other personnel expenses consist of:

Salaries	1.182.882	1.042.459
Defined contribution plan payments	143.152	125.613
Defined benefit plan payments	8.178	11.909
Other payroll expenses	126.828	114.749
Capitalised salaries	(210.047)	(91.709)
Personnell expenses total	1.250.993	1.203.021

Personnel expenses are specified as follows:

Transmission costs	415.458	477.950
System operation	480.889	440.482
Other operating expenses	354.646	284.589
	1.250.993	1.203.021

Average number of employees	122	117
Full-time equivalent units at year-end	114	106

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

Remuneration of the Board of Directors	6.486	5.975
Remuneration and benefits of the CEO	15.440	13.225
Remuneration of two Excecutive Directors	41.621	34.688

10. Depreciation and amortisation

See accounting policies in notes 35c and 35d

Depreciation and amortisation are specified as follows:

	2013	2012
Depreciation of fixed assets in operation, see Note 13	2.509.721	2.427.328
Amortisation and impairment losses, see Note 14	88.200	40.224
Depreciation and amortisation recognised in the income statement	2.597.921	2.467.552

Depreciation and amortisation are allocated as follows to operating items:

Transmission costs	2.436.690	2.298.882
System operation	66.277	56.541
Other operating expenses	94.954	112.129
Depreciation and amortisation recognised in the income statement	2.597.921	2.467.552

11. Financial income and expenses

See accounting policies in note 35m

Financial income and expenses are specified as follows:

Interest income	129.748	40.318
Net gain in fair value of marketable securities	11.293	9.521
Gain on sale of shares in associate	0	17.543
Total financial income	141.041	67.382
Interest expenses	(2.161.747)	(2.216.696)
Indexation	(1.751.913)	(2.078.598)
Exchange rate difference	(328.397)	(152.823)
Change in present value of the provision due to site restoration	(40.856)	(38.226)
Capitalised interest expense due to projects under construction	271.978	80.037
Total financial expenses	(4.010.935)	(4.406.306)
Net financial expenses	(3.869.894)	(4.338.924)

Net financial expenses due to the construction of a transmission infrastructure amounting to ISK 272 million (2012: 80 million) is capitalised and has been reported as a reduction in financial expenses.

Capitalised financial expenses were 7.0% of capital tied in transmission structures under construction during the year (2012: 7.6%). This is the Company's average finance cost in the year 2013.

12. Income tax

See accounting policies in note 35n

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

Calculated income tax for the year	539.511	184.319
Income tax recognised in the income statement	539.511	184.319
Change in deferred income tax liability is specified as follows:		
Change in temporary differences	(120.199)	(308.482)
Change in carry-forward losses	659.710	492.801
Change in deferred tax assets	539.511	184.319

12. Income tax, contd.:

		2013		2012
Reconciliation of effective tax rate				
Profit before income tax		2.722.909		985.272
Income tax according to the current tax rate	20,0%	(544.582)	20,0%	(197.054)
Effects of associates	(0,2%)	5.011	(1,2%)	12.297
Other	0,0%	60	0,0%	438
Effective tax rate	19,8%	(539.511)	18,8%	(184.319)

13. Fixed assets in operation:

See accounting policies in note 35c

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. A revaluation was conducted on those assets in the year 2008. The revaluation was based on two methods. First, it was based on the estimated reconstruction cost of the transmission system, which was calculated by independent experts at the beginning of year and projected to year-end 2008. Second, the operating value was measured using a cash flow analysis. The valuation period was from 2009 to 2013, with the future operating value calculated thereafter. The year's revaluation was based on the operating value, the main premises of which were the Company's operating budgets for the years 2009-2013, a 30% equity ratio and that Landsnet's tariff for transmission to distributors would reflect price developments in Iceland while the tariff for industrial users would reflect price level changes in the United States. The estimation of weighted-average cost of capital (WACC) was based on comparable companies abroad. It is the opinion of the Company's management that nothing gives reason for a revaluation in the year 2013. The revaluation has been categorised as level 3 fair value.

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
Cost				
Balance at 1.1.2012	22.666.107	47.332.290	3.122.000	73.120.397
Additions	418.645	75.827	372.035	866.507
Sold and disposed of	0	0	(4.790)	(4.790)
Balance at 31.12.2012	23.084.752	47.408.117	3.489.245	73.982.114
Additions	500.107	175.437	311.121	986.665
Transferred from projects under construction	3.564.171	2.532.923	0	6.097.094
Sold and disposed of	0	0	(5.672)	(5.672)
Balance at 31.12.2013	27.149.030	50.116.477	3.794.694	81.060.201
Depreciation				
Balance at 1.1.2012	4.008.157	8.194.034	730.798	12.932.989
Depreciation	766.203	1.505.057	156.068	2.427.328
Sold and disposed of	0	0	(3.619)	(3.619)
Balance at 31.12.2012	4.774.360	9.699.091	883.247	15.356.698
Depreciation	797.613	1.533.159	178.949	2.509.721
Sold and disposed of	0	0	(3.840)	(3.840)
Balance 31.12.2013	5.571.973	11.232.250	1.058.356	17.862.579
Carrying amount				
1.1.2012	18.657.950	39.138.256	2.391.202	60.187.408
31.12.2012	18.310.392	37.709.026	2.605.998	58.625.415
31.12.2013	21.577.057	38.884.227	2.736.338	63.197.621

13. Fixed assets in operation, contd.:
Carrying amount without revaluation

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
1.1.2012	16.025.423	26.567.291	2.391.202	44.983.916
31.12.2012	15.794.313	25.733.557	2.605.998	44.133.868
31.12.2013	19.182.702	27.493.585	2.736.338	49.412.625

Rateable value and insurance value

The rateable value of the Company's real property amounts to upwards of ISK 2.8 billion (2012: ISK 2.7 billion). Assessed value for the same property's fire insurance amounts to ISK 5.2 billion (2012: ISK 5.2 billion) and book value amounts to ISK 3.6 billion (2012: ISK 3.7 billion). The insurance value of the Company's assets amounts to ISK 47.5 billion (2012: ISK 42.2 billion), excluding transmission lines and cables, which are insured by an emergency insurance fund. The Company's emergency insurance amounts to ISK 109.9 billion (2012: ISK 103.4 billion).

Projects under construction:

	2013	2012
Balance at 1.1.	1.769.671	276.275
Additions	5.364.675	1.506.943
Transferred to fixed assets in operation	(6.097.094)	0
Transferred from/to intangible assets	49.298	(8.075)
Sold and disposed of	0	(5.472)
Balance at 31.12.	1.086.550	1.769.671

14. Intangible assets:
See accounting policies in note 35d

	Capitalised development cost	Software	Total
Cost			
Balance at 1.1.2012	1.347.176	386.264	1.733.440
Additions	134.114	5.580	139.694
Transferred to projects under construction	8.075	0	8.075
Sold and disposed of	(7.252)	0	(7.252)
Balance at 31.12.2012	1.482.113	391.844	1.873.957
Additions	118.607	35.655	154.262
Transferred to projects under construction	(49.298)	0	(49.298)
Balance at 31.12.2013	1.551.422	427.499	1.978.921
Amortisation and impairment losses			
Balance at 1.1.2012	212.414	245.089	457.503
Amortisation and impairment losses	8.075	32.149	40.224
Balance at 31.12.2012	220.489	277.238	497.727
Amortisation and impairment losses	75.307	12.893	88.200
Balance at 31.12.2013	295.796	290.131	585.927
Carrying amount			
1.1.2012	1.134.762	141.175	1.275.937
31.12.2012	1.261.624	114.606	1.376.230
31.12.2013	1.255.626	137.368	1.392.994

14. Intangible assets, contd.:

Preparation 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 preparation cost is expensed as impairment.

15. Investment in subsidiary

See accounting policies in note 35e

The breakdown of investment in subsidiary is as follows:

	2013 Share	2013 Carrying amount	2012 Share	2012 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 35f

The breakdown of investment in associates is as follows:

	2013 Share in net earnings	2012 Share in net earnings	2013 Carrying amount	2012 Carrying amount
Orkufjarskipti hf. 50% / 50%	25.055	16.015	668.906	643.851
Netorka ehf. 0% / 0%	0	2.565	0	0
Total investment in other companies	25.055	18.580	668.906	643.851

17. Inventories

See accounting policies in note 35g

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 2013 nor for the year 2012.

18. Trade and other receivables

See accounting policies in note 35b

Trade and other receivables:

	2013	2012
Trade receivables	405.808	557.242
Other receivables	161.589	133.536
Trade and other receivables total	567.397	690.778

19. Marketable securities

See accounting policies in note 35b

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 35b

Cash and cash equivalents consist of instant-access bank deposits.

21. Equity

See accounting policies in note 35b

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.

21. Equity, contd.:

Revaluation account

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

Dividends

The Company paid no dividends in 2013 for the financial year 2012, nor in the year 2012 for the financial year 2011. Accumulated deficit amounts to ISK 1.5 billion at year end and therefore not permitted to pay dividend to shareholders.

22. Earnings per share

	2013	2012
See accounting policies in note 35o		
Basic and diluted earnings per share:		
Profit to shareholders	2.183.398	800.953
Weighted average number of ordinary shares at 31 December	5.902.733	5.902.733
Basic and diluted earnings per share	0,37	0,14

23. Interest-bearing loans and borrowings

See accounting policies in note 35b

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

	2013	2012
Long-term liabilities		
Indexed bond loan from parent company in ISK, fixed interest	44.235.700	42.675.190
Loan agreement in CHF, LIBOR + margin	6.436.052	7.830.765
Indexed bond loan in ISK, fixed interest	5.330.965	5.279.894
	56.002.717	55.785.849
Current maturities on long-term liabilities	(914.607)	(968.844)
	55.088.110	54.817.005
Short-term liabilities		
Short-term loans from parent company specifies as follows:		
Accrued interest of long-term liabilities with parent company	1.448.473	1.402.366
Short-term loans from parent company total	1.448.473	1.402.366

The bond loan from the parent company is an inflation-indexed bullet loan maturing in 2020 with interest payable once per year. Inflation-indexed bond loans from third parties consist of a 25-year superannuation loan maturing in 2034. The loan agreement denominated in Swiss francs (CFH) is a bond with equal installments and maturing in 2022.

Terms of interest-bearing loans and borrowings

Debts in foreign currencies:

		2013		2012	
	Final maturity	Weighted avg. rate	Carrying amount	Weighted avg. rate	Carrying amount
Debt in CHF	2022	0,31%	6.436.052	0,39%	7.830.765
Debt in ISK:					
Indexed	2020 - 2034	4,30%	49.566.665	4.30%	47.955.084
Total interest-bearing loans and borrowings			56.002.717		55.785.849

23. Loans and borrowings, contd.:

Maturities by year of interest-bearing loans and borrowings:

	2013	2012
Year 2014/2013	914.607	968.844
Year 2015/2014	922.577	976.162
Year 2016/2015	930.950	983.850
Year 2017/2016	939.747	991.928
Year 2018/2017	948.989	1.000.415
Later	51.345.847	50.864.650
	56.002.717	55.785.849

24. Deferred tax liability

See accounting policies in note 35n

The breakdown of deferred tax liability is as follows:

Deferred tax liability at 1 January	1.791.932	1.607.613
Calculated income tax for the year	539.511	184.319
Deferred tax liability at 31 December	2.331.443	1.791.932

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

Fixed assets in operation	2.609.784	2.756.995
Intangible assets	208.035	197.008
Provision due to site restoration	(155.033)	(146.861)
Other obligations	(86.162)	(137.342)
Unrealized exchange rate difference	(53.974)	(26.951)
Tax losses carried forward	(191.207)	(850.917)
Deferred tax liability at 31 December	2.331.443	1.791.932

The carry-forward taxable loss amounted to ISK 1.0 billion. The loss is utilisable against taxable income over ten years from when the loss is incurred. The management believes that the Company's operation over the next years will generate taxable income and that the accumulated carry-forward taxable loss will be fully utilised. Carry-forward taxable loss at year-end 2013 will be utilisable until the year 2018.

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 384 millon (2012: 308 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 2013 amounted to ISK 12 million (2012: 7 million).

26. Provision due to site restoration

See accounting policies in note 35j

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

	2013	2012
Balance at 1.1.	734.307	696.081
Present value for the year reversed	40.856	38.226
Balance at year-end	775.163	734.307

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 6.9% interest rate (2012: 6.9%), is reported under financial expenses, in addition to depreciation under operating expenses.

27. Pension fund obligation

See accounting policies in note 35i

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 8 million is expensed in relation thereto for 2013 (2012: 12 million), but the accrued benefit plan obligation is paid in full each year.

28. Trade and other payables

See accounting policies in note 35b

Trade and other payables are specified as follows:

	2013	2012
Trade payables	419.108	949.683
Other payables	327.703	645.222
Trade and other payables total	746.811	1.594.905

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 87% (2012: 89%) of the Company's transmission income derives from the Company's shareholders.

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:

	2013	2012
Long-term note	34.929	34.929
Receivables from parent company	0	648.398
Trade and other receivables	555.754	690.778
Market securities	234.344	251.027
Cash and cash equivalents	9.917.204	10.309.772
Highest possible loss due to credit risk total	10.742.231	11.934.904

29. Financial instruments, contd.:

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. As of its establishment, the Company has not incurred losses on accounts receivable. 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:

2013	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.	45.684.173	57.271.961	1.862.323	1.862.323	5.586.969	47.960.346
Long-term liabilities	11.767.017	15.144.891	1.239.031	1.225.321	3.698.011	8.982.528
Trade and other payables	1.234.864	1.234.864	1.234.864	0	0	0
	58.686.054	73.651.716	4.336.218	3.087.644	9.284.980	56.942.874
2012						
Long-term liabilities from parent comp.	44.077.556	56.474.945	1.796.625	1.796.625	5.389.876	47.491.819
Long-term liabilities	13.110.659	16.541.910	1.233.020	1.229.907	3.671.118	10.407.865
Trade and other payables	1.594.905	1.594.905	1.594.905	0	0	0
	58.783.120	74.611.760	4.624.550	3.026.532	9.060.994	57.899.684

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.

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 2013, 62.7% (2012: 65.8%) 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 Swedish krona (SEK). The main currencies posing a foreign exchange risk are the USD and the Swiss Francs (CHF). In 2014, it is estimated that 60.5% of the Company's total revenue will be in USD.

29. Financial instruments, contd.:

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
2013			
Cash and cash equivalent	10.991	25.987	8.541.356
Trade and other receivables	424	0	294.025
Other long-term liabilities	0	(6.436.052)	0
Trade and other payables	(61.263)	0	(15.680)
Net currency risk	(49.848)	(6.410.065)	8.819.701
2012			
Cash and cash equivalent	190.826	50.782	9.348.845
Trade and other receivables	0	0	255.691
Other long-term liabilities	0	(7.830.765)	0
Trade and other payables	(104.605)	0	(45.078)
Net currency risk	86.221	(7.779.983)	9.559.458

	Av. exch. rate for the year		Year-end exch. rate	
	2013	2012	2013	2012
Currency risk				
EUR	162,38	160,73	158,50	169,80
CHF	131,91	133,35	129,19	140,64
USD	122,23	125,05	115,03	128,74

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 2012.

	2013	2012
EUR	3.988	(6.898)
CHF	512.805	622.399
USD	(705.576)	(764.757)

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.

Interest rate risk

The Company´s interest rate risk arises from interest bearing assets and liabilities. The Company's borrowings bear both floating and fixed interest. The majority of the Company's borrowings bear fixed interest, cf. Note 23. At year end 2013, the proportion of liabilities with floating interest rates was 11% compared to 14% at year end 2012.

29. Financial instruments, contd.:

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

	Carrying amount 2013	2012
Financial instruments with floating interest rate		
Financial assets	10.186.477	10.595.728
Financial liabilities	(6.436.052)	(7.830.765)
	3.750.425	2.764.963
Financial instruments with fixed interest rate		
Financial liabilities	(49.566.665)	(47.955.084)

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 2012.

	Earnings 100bp increase	100bp decrease
31 December 2013		
Financial instruments with floating interest rates	26.061	(7.788)
Cash flow sensitivy (net)	26.061	(7.788)
31 December 2012		
Financial instruments with floating interest rates	22.610	(61.458)
Cash flow sensitivy (net)	22.610	(61.458)

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:

	2013		2012	
	Carrying amount	Fair value	Carrying amount	Fair value
Long-term liabilities from parent company	(44.235.700)	(49.842.048)	(42.675.190)	(49.613.500)
Other long-term liabilities	(11.767.017)	(13.115.500)	(13.110.659)	(14.398.193)
	(56.002.717)	(62.957.548)	(55.785.849)	(64.011.693)

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

Interest rate in valuation of fair value

Where applicable, expected contractual cash flow is discounted using the interest rate on government bonds plus a 0.4% margin on the reporting date. The same margin was used in discounting expected contractual cash flow in the year 2012.

29. Financial instruments, contd.:

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
2013				
Long-term note		23.286		23.286
Receivables from parent company		0		0
Trade and other receivables		567.397		567.397
Marketable securities	234.344			234.344
Cash and cash equivalents		9.917.204		9.917.204
	234.344	10.507.887	0	10.742.231
Loans from parent company		488.053	45.684.173	46.172.226
Other long-term liabilities			11.767.017	11.767.017
Trade and other payables		746.811		746.811
	0	1.234.864	57.451.190	58.686.054
2012				
Long-term note		34.929		34.929
Receivables from parent company		648.398		648.398
Trade and other receivables		690.778		690.778
Marketable securities	251.027			251.027
Cash and cash equivalents		10.309.772		10.309.772
	251.027	11.683.877	0	11.934.904
Loans from parent company			44.077.556	44.077.556
Other long-term liabilities			13.110.659	13.110.659
Trade and other payables		1.594.905		1.594.905
	0	1.594.905	57.188.215	58.783.120

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, while the majority of its revenue is USD-denominated

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 2013 amounted to ISK 166 million (2012: ISK 131 million).

31. Uncertainty

Under the Electricity Act No. 65/2003, the National Energy Authority shall set a revenue cap for Landsnet hf. in advance and for a specified period. The cap was initially set for a single year at a time, which applied for 2005 and 2006. In 2006, the revenue cap was for the first time set for a three-year period, 2007-2009, as prescribed by the then current Act. The 2010 revenue cap was not set by the Authority until August 2012, and then for only a single year owing to amendments to the Electricity Act that took effect in 2011.

Act No. 19/2011 introduced a number of amendments to the Electricity Act with respect to the revenue cap regime, which apply to the setting of the revenue cap as of 2011. The main changes were that the revenue cap period was lengthened from three to five years, profitability was to be based on weighted average cost of capital (WACC) instead of the yield on 5-year non-indexed government bonds, the asset base for power-intensive consumers was converted from ISK to USD and account was taken of investment in current assets. Under the current Electricity Act, a profitability limit must be determined separately for power-intensive consumers on the one hand and distribution system operators on the other hand. The revenue cap must be set no later than 15 September of the year prior to the year in which it takes effect.

On 1 October 2012, the National Energy Authority issued a decision on the weighted average cost of capital to be effective from 1 January 2011. Stakeholders appealed the decision to the Appeals Committee on Electricity, which overturned it on 2 December 2013. The rationale for overturning the Authority's decision was that further reasoning was required to determine risk premiums and interest margins. Under the Appeals Committee's decision, the Authority must issue a new decision on profitability criteria based on a new opinion delivered by an expert committee.

The revenue cap for 2011-2015 was established by the Authority on 28 July 2013 and was based on the aforesaid decision on profitability parameters, which has now been overturned.

Under the Electricity Act, the Authority must no later than 1 August of each year submit to the transmission system operator the updated revenue cap and the settlement for the preceding year, including reasoning for any changes. The Authority and Landsnet have been unable to agree on the settlement for the years 2006-2009 owing to different interpretations of the profitability criteria for distribution system operators; there is no disagreement about the revenue cap for power-intensive consumers.

Landsnet has twice appealed the Authority's decision regarding the settlement for the years 2006-2009 to the Appeals Committee on Electricity, which overturned both of the Authority's decisions and referred the case back to it for a reassessment. The Authority issued a third decision on the settlement for the said period on 20 December 2012, which has also been appealed. On 12 April 2012, the Authority issued a decision on the revenue cap settlement for 2010. This decision is not in dispute. The delays in effecting a settlement for the years 2006-2009 and 2011-2012 have caused some uncertainty with regard to the Company's performance measurement and financial position.

Power-intensive consumers

Between 2005 and August 2007, Landsnet's revenue and revenue cap for power-intensive consumers were denominated in ISK. In August 2007, after obtaining the National Energy Authority's approval, the tariff currency for power-intensive consumers was changed to USD, without changing the revenue cap accordingly.

Following the sharp ISK depreciation in 2008, Landsnet's USD-denominated revenue from power-intensive consumers increased substantially in ISK. The government authorities showed willingness to address the problem that this presented for the revenue cap regime and to amend legislation in order that the revenue cap for power-intensive consumers would be denominated in the same currency as the tariff. With Act No. 19/2011, amending the Electricity Act, the asset base from which profitability and depreciation are derived as determinants of the revenue cap for power-intensive consumers was converted to USD based on the exchange rate at 31 July 2007, thereby redressing the balance between the revenue cap and the tariff. Since 2011, Landsnet has accrued a credit balance vis-à-vis power-intensive consumers, and the Company estimates that obligations due to over-collected revenue in previous years have been settled in accordance with the provisions of law, whereas the Authority's revenue cap settlement remains pending.

Distribution system operators

At year-end 2013, a dispute remained to be resolved between Landsnet and the National Energy Authority regarding the profitability criteria used to determine the revenue cap for distribution system operators for the period 2006-2009 and the interpretation of a transitional provision of the Electricity Act on this matter. Since the final decision in this matter is still pending, the level of the revenue cap for distribution system operators during this period remains unclear. According to Landsnet's calculations, obligations resulting from over-collected revenue may amount to between ISK 0.1 billion and up to ISK 1.5 billion

31. Uncertainty, contd.:

In response to decisions by the National Energy Authority, Landsnet has initiated legal proceedings before the Reykjavík District Court to determine the interpretation of the said transitional provision, which applies to the period 2006-2009, but this case is pending until the Appeals Committee on Electricity delivers its decision.

Provisions of law concerning repayments

A transitional provision of Act No. 19/2011, amending the Electricity Act, provides that, in the event of the transmission system operator's over-collection of revenue for previous years, the Company shall set its tariff at a level ensuring that over-collected revenue does not exceed 10% of the revenue cap at year-end 2020. Over-collected revenue is not subject to interest calculation or inflation-indexation.

The provisions of the Act do not require Landsnet to deliver cash or other assets in repayment of over-collected revenue, nor to provide additional services without charge. Instead, the over-collection of revenue shall be corrected through general changes to the transmission tariff in the following years. Landsnet bases its tariff decisions on the revenue cap and the repayment provision.

On the basis of the provisions of law governing the repayment of over-collected revenue and the provisions of the International Financial Reporting Standards, no effects of revenue-cap-based settlements for 2006-2012 are recognised in the annual financial statements.

32. 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 Chief Executive Officer and Managing Directors (Vice Presidents) of the Company enjoy various benefits and a contribution to a defined benefit pension fund. Management's salaries are accounted for in Note 9.

Other transactions with related parties

	2013	2012
Sale of goods and services:		
Landsnet's parent company and its subsidiaries	6.656.405	6.747.318
Landsnet's other shareholders	4.765.500	4.390.775
Sale of goods and services to related parties total	11.421.905	11.138.093
Cost:		
Landsnet's parent company and its subsidiaries	1.418.704	1.130.216
Landsnet's other shareholders	509.992	665.616
Cost of goods and services to related parties total	1.928.696	1.795.832

In addition the costs outlined above, the Company paid ISK 1,802 million (2012: ISK 1,815 million) in interest to its parent company.

Balance:

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

	2013		2012	
	Receivables	Payables	Receivables	Payables
Landsnet's parent company and its subsidiaries	0	(488.053)	648.398	0
Landsnet's other shareholders	398.764	(14.252)	401.646	(53.624)
	398.764	(502.305)	1.050.044	(53.624)

Other receivables and payables with related parties are as follows:

	2013	2012
Interest-bearing liabilities to parent company, see note 23	44.235.700	42.675.190
Accrued interest payable to parent company	1.448.473	1.402.366
	45.684.173	44.077.556

33. Financial ratios

The company's key financial ratios:

Financial performance:		
EBIT	6.567.748	5.305.616
EBITDA	9.165.669	7.773.168
Financial position:		
Current ratio – current assets/current liabilities	3,12	3,13
Equity ratio – equity/total assets	19,9%	17,7%
Return on equity	16,5%	6,4%

The Company's revenue is determined under Article 12 of the Electricity Act and is based, inter alia, on a decision on profitability. The profitability parameters under the Act are determined on the basis of cost of capital in the market and a certain capital structure. The return on the calculated equity according to the revenue cap set for 2013 was just over 9%. The Company's equity ratio is somewhat lower than assumed in the profitability criteria, but its return on equity based on the revenue cap criteria is in line with the objectives on which the determined profitability is based.

34. 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 fari value at revaluation date in the year 2008.
- Financial assets at fair value through profit and loss are recognised at fair value.

35. Significant accounting policies

The following accounting methods have been consistently applied to all disclosed periods in the financial statements.

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

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.

3. Significant accounting policies, contd.:

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.

3. Significant 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.

The most recent revaluation of transmission lines and substations was carried out at year-end 2008.

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.

3. Significant 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. The Company has concluded agreements whereby the prospective buyers of electricity shall bear all expenses of the project if it is cancelled. Cost of capital attributable to developement costs is 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.

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.

3. Significant 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. Employee benefits

(i) Defined contribution plans

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

(ii) Defined benefit plans

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

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.

3. Significant 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 2013 and that apply to its operations. The Company has not implemented standards, amendments thereto or interpretations entering into effect after year-end 2013 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 March 2012. 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 31 March 2010 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: reliability, progress, economy and respect. These values are further defined as follows:

• Reliability. We show independence whilst maintaining due confidentiality and equal treatment of our customers. We show integrity and diligence in our behaviour and work methods.

• Progress. We take initiative, seek out opportunities and strive for continual improvement. We are creative and develop methods and solutions that stimulate competition. We pride ourselves on completing tasks and projects promptly and methodically.

• Economy. We maintain prudent stewardship of our funds and other resources and are guided by profitability targets.

• Respect. Our customers come first. We respect the natural environment and seek to minimise any undesirable effects of our operations. We respect our colleagues and their views and do not compromise on personal safety.

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.

Landsnet is committed to a strong community awareness. The Company's policies include that the development of the transmission system aims to deliver macroeconomic benefits and minimise any undesirable environmental impact of its operations. They also include that Landsnet honours its obligations and supports projects that are of relevance to its activities and benefit society.

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 on 30 July 1943 and lives in Reykjavík, Iceland. 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 served on government negotiating committees on power-intensive industry and on the board of the Marketing Office of the Ministry of Industry and the National Power Company in 1988-1997, including as chairman in 1989-1997. He 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 on 20 December 1960 and lives in Seltjarnarnes, Iceland. 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 and is an IRCA-certified lead auditor of corporate information security management systems based on international standards. She founded the information security company Stiki in 1992 and the subsidiary Stiki Ltd in the United Kingdom in 1996. Ms Björnsdóttir is now the Chairman of the Board of Stiki and a former CEO of Stiki and has worked as an IT and software engineering consultant on various projects for companies and organisations. She has served as a government supervisor on various projects. She has extensive experience in business management, international co-operation and export activities. Her board memberships include Hagar hf, the Icelandic Data Protection Authority, the Association of Chartered Engineers in Iceland, the Seed Company Association in Iceland and the Icelandic Society for Information Processing. She has sat on the Expert Panels of the Technology Development Fund and Research Fund of the Icelandic Centre for Research (RANNÍS). For several years she was Iceland's representative on the Council of European Professional Informatics Societies. She was elected chairman of the Federation of Icelandic Industries in March 2012. Ms Björnsdóttir is also chairman of Akkur SI. In addition, she is a board member of the Confederation of Icelandic Employers, the General Pension Fund, the Association of Small Investors, the Science and Technology Council and the High Tech and Seed Forum, a consultative forum between government and business. Ms Björnsdóttir has been a member of Landsnet´s Board of Directors from 31 March 2009.

Ómar Benediktsson, Director
Ómar Benediktsson was born on 22 October 1959 and lives in Reykjavík, Iceland. 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, including at Island Tours, Íslandsflug and Air Atlanta. He has sat on numerous boards and committees in these fields, including the Civil Aviation Board and the Icelandic Tourist Board, the Committee on Iceland's Future Policy on Tourism and as vice-chairman of Icelandair Group hf. Mr Benediktsson has been active in promoting Iceland as a tourist destination and has sat on a number of committees devoted to this end, including as chairman of the Icelandic Tourist Board Marketing Committee and chairman of Iceland Naturally, a co-operative marketing organisation. He founded the first Icelandic-owned specialised travel wholesaler offering trips to Iceland in Germany and later in other continental European countries. He sat on the preparatory committee for the founding of the Icelandic Travel Industry Association and on its nominations committee for the first few years. He has led the launch of a number of tourist industry companies, including Fosshótel. He was the first chairman of the Icelandic National Broadcasting Service after its conversion into a state-owned public limited company and sat on the boards of Blue Bird Cargo and Penninn for a number of years. Mr Benediktsson has long-standing experience in international business and relations. 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 been a member of Landsnet´s Board of Directors from 29 March 2012.

The Alternate Director is Svava Bjarnadóttir

A total of 15 meetings of the Board of Directors were held in 2013, which were attended by all Board members.

Landsnet´s Executive Committee

Þórður Guðmundsson, President & CEO, is a member of the Executive Committee.

Mr Guðmundsson was born on 2 October 1949 and lives in Garðabær, Iceland. He pursued studies at the Industrial Vocational School in Reykjavík, the Technical College of Iceland and the Norwegian University of Science and Technology, from which he graduated with an MSc degree in electrical engineering in 1978. He joined Landsvirkjun in 1978, starting as an engineer and later becoming chief engineer in the Operations department until appointed managing director of Operations in 1992. Following organisational changes in 1997, he became managing director of the Transmission division until appointed Landsnet's President & CEO on 1 January 2005.

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. The President & CEO is the chairman of the board of Landsnet ehf and a director of Samorka.

Other members of the Executive Committee are:
Guðmundur Ingi Ásmundsson, Deputy CEO
Guðlaug Sigurðardóttir, CFO

Audit Committee

The current Audit Committee of Landsnet hf was appointed on 10 November 2011 and consists of:
Ólafur Nilsson, accountant, Chairman
Geir A. Gunnlaugsson, Chairman of the Board of Landsnet hf
Ómar Benediktsson, Boardmember of Landsnet hf

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.
A total of 4 meetings were held in 2013, all of which were attended by all Committee members except for one meeting where one member was absent.

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.

LANDSNET

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