LANDSNET

ANNUAL REPORT 2014

Contents

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Front cover: Landsnet is committed to ensuring a secure electricity supply for all. The front cover photo is from the theatre show Karítas and is courtesy of the National Theatre of Iceland.

Secure electricity supply for all in harmony with society

Statement by the Chairman and the President & CEO

Iceland occupies the unique position among nations of producing electricity almost entirely with clean, renewable energy sources. It is also one of the few countries with growth opportunities in this area. The majority of Icelanders support responsible utilisation of the country's energy sources to increase economic prosperity. Responsible utilisation and consensus thereon must, however, be underpinned by a comprehensive government policy.

Access to a secure electricity supply is essential for a good standard of living in a modern society. This was amply demonstrated by a recent outage in the Reykjanes region in the south-west of Iceland. Besides the usual impact on homes and businesses, including financial loss and discomfort, the outage severely disrupted telecommunications and caused disturbances in equipment at Keflavik International Airport and various public safety incidents. This showed the grid's vulnerability in a nutshell.

Problematic operating circumstances

Landsnet performed well on many fronts in 2014 despite difficult circumstances. Our activities have been affected significantly by continual heated debates over energy issues, which have held back sorely needed strengthening of the grid. The weather this year and last has been unfavourable for the electricity system, and the number of disturbances and shocks has risen. Against these odds, our employees achieved an adequate level of operational security through a combination of ingenuity and high-tech solutions. Nonetheless, the problems are clearly mounting as electricity use increases – problems that will not be solved without strengthening the grid. Recent analysis of security of supply during natural disasters carried out in connection with the seismic and volcanic activity at Mt Bárðarbunga also underscores the need for extensive grid strengthening.

Increased transmission through the grid coupled with system weaknesses led to a rise in energy losses and growing operational risk in 2014. Grid disturbances were up by almost one-third and the resultant outage minutes by 28% year-on-year. Our Wide Area Protection system split the grid into island operation 11 times in the year, with attendant discomfort and even losses for consumers. Inter-regional transmission exceeded security limits for nearly one-third of the year, or more than 102 days. Tellingly, overseas commentators have begun to call Iceland the "European champion" in the use of smart grid solutions such as wide-area protection and load management. A high-risk operation of this kind leads to inefficiencies for all our customers, threatens grid security and substantially increases the risk of outages.

Changes necessary

Many changes are needed to overcome the current situation. The government is working on two important changes to Landsnet's operating environment: (1) an amendment to the Electricity Act for new procedures to be used in the preparation of our Grid Plan and (2) a parliamentary resolution for the government to adopt a policy on undergrounding. Both are positive steps towards building a better consensus on our infrastructure projects in order to strengthen the grid.

To better promote a sustainable electricity system that uses energy sources in accordance with the public will, we are reviewing our policies and procedures to serve the following key aims:

- For all citizens to have access to electricity in the quantity and quality needed.
- To achieve broader consensus on our operations and for Landsnet to treat the environment responsibly.
- For Landsnet to promote a healthy investment environment for the electricity system and sustainable use of energy resources.
- For our operations to be efficient and cost-effective.
- For Landsnet to have a clear image, be honest in its relations and a progressive workplace for motivated employees.

Broad social consensus

Landsnet's role in the energy sector is not to be the driving force but to ensure equal treatment, equal access to the grid and security of supply, in addition to promoting healthy practices in electricity trading. This

role is a vital link in the electricity chain and must be carried out responsibly and steadfastly.

Our aim is to build the broadest possible social consensus on the future direction of electricity transmission and the development of the main grid. We have followed official procedures for the environmental impact assessment of infrastructure projects and of our Grid Plan, but unfortunately this has not produced the desired consensus. To keep abreast of the times, our current aim is to adopt new procedures with a sharper focus on corporate social responsibility, deeper consultation in the first stages of planned infrastructure projects and a formal consultation forum for stakeholders in larger projects. All analysis will be strengthened to find the best practicable solutions each time – solutions on which a social consensus can be reached.

Stable operating environment

A stable operating environment is a key requirement for activities of such importance as electricity transmission. The enactment of the 2011 Electricity Act aimed to strengthen our operating environment by determining our rate of return and thereby our revenue framework five years in advance at a time. At the start of 2015, however, a decision for the period 2011-2015 was not yet available, meaning major uncertainty for our revenue base.

The failure to ensure that government decisions on the allowed rate of return and the revenue cap are available at the time stipulated by law is extremely unfortunate. As a result, we are unable to react to circumstances through appropriate measures, including tariff changes at the start of each year. This can cause irregular tariff fluctuations, which is unacceptable for our customers.

Consensus must be forged on a stable foundation for Landsnet and its management to operate in a cost-effective manner for the benefit of all parties concerned.

A change at the helm and a 10-year anniversary

Having served as CEO & President of Landsnet from the company's inception, Þórður Guðmundsson stepped down at the turn of the year at his own request. We extend our sincere thanks to Þórður for a job well done and his strong leadership in steering the company through its early development, often in challenging circumstances.

Landsnet is marking a milestone in its history this year – a decade has passed since we began operations. In a sense, the company has come of age. Our good performance over the years has been achieved through the concerted efforts of our team of dedicated employees, to whom we extend thanks for their excellent work.

Geir A. Gunnlaugsson, Chairman of the Board

Guðmundur Ingi Ásmundsson, CEO & President

Key figures

	2010	2011	2012	2013	2014
System demand (Gwh)	16,165	16,287	16,652	17,108	17,116
Transmission losses (GWh)	331	324	339	378	361
Transmission losses as a ratio of consumption	2.0%	2.0%	2.0%	2.2%	2.1%
Operating revenue	12,846	11,903	12,344	13,874	14,350
Investing activities	1,338	830	2,211	6,408	3,851
Investing activities as a ratio of operating revenue	10.4%	7.0%	17.9%	46.2%	26.8%
Earnings before interest and taxes (EBIT)	6,341	5,440	5,306	6,568	6,174
EBIT as a ratio of operating revenue	49.4%	45.7%	43.0%	47.3%	43.0%
General operating costs*	2,401	2,550	3,187	3,209	3,445
General operating costs as a ratio of operating revenue	18.7%	21.4%	25.8%	23.1%	24.0%
Profit	3,563	840	801	2,183	3,762
Profit as a ratio of operating revenue	27.7%	7.1%	6.5%	15.7%	26.2%
Assets	70,513	74,679	74,873	77,608	81,859
Equity	11,622	12,462	13,263	15,446	19,208
Liabilities	58,891	62,217	61,610	62,162	62,651
Return on equity**	42.8%	7.2%	6.4%	16.5%	24.4%
Equity ratio***	16.5%	16.7%	17.7%	19.9%	23.5%
Length of overhead transmission lines (km)	3,054	3,055	3,055	3,061	3,066
Length of underground and sub-sea cables (km)	146	147	147	158	160
Full-time equivalent positions at year-end	95	94	106	114	113

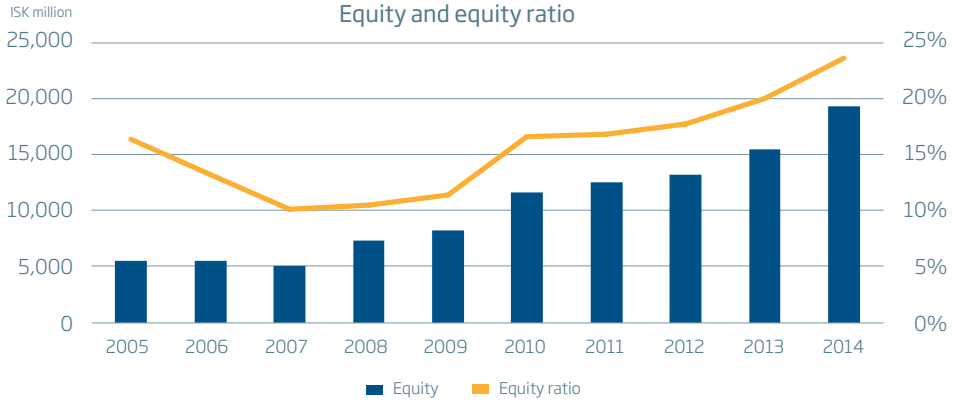
Amounts in ISK million

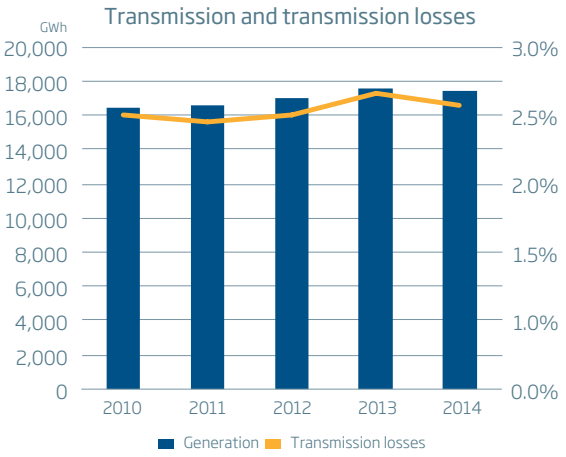
Calculation of key figures

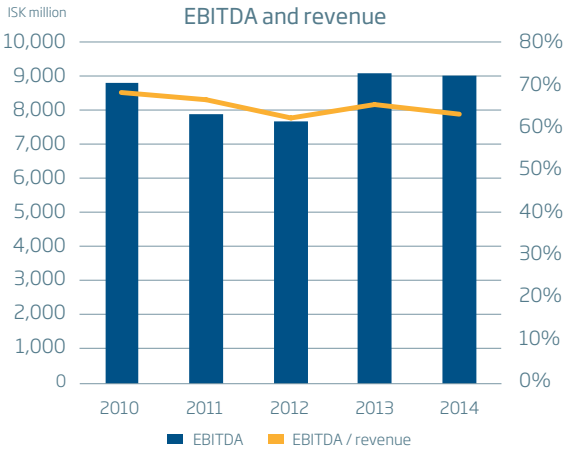
* General operating costs = operating expenses - depreciation and amortisation - ancillary services and losses

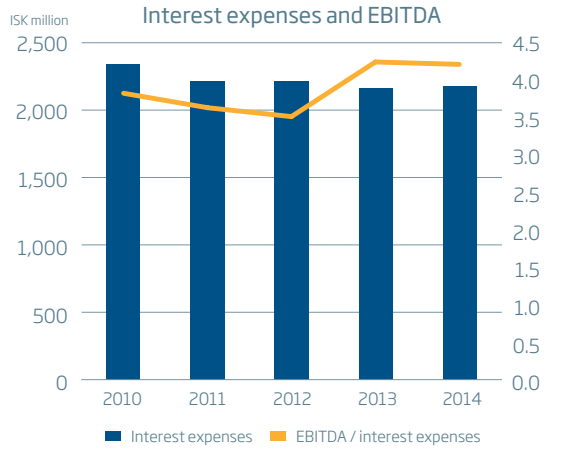
** Return on equity = profit/equity at beginning of year

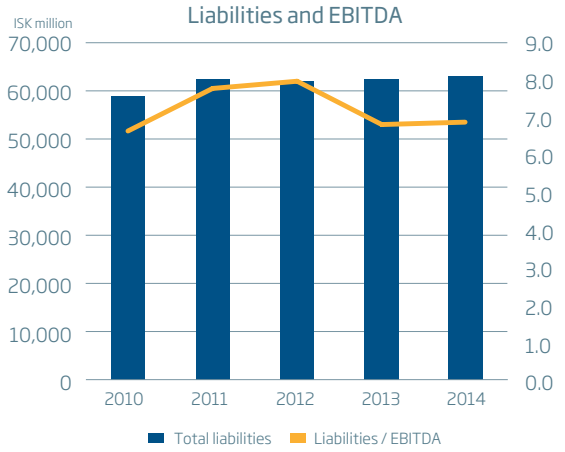
*** Equity ratio = equity/assets

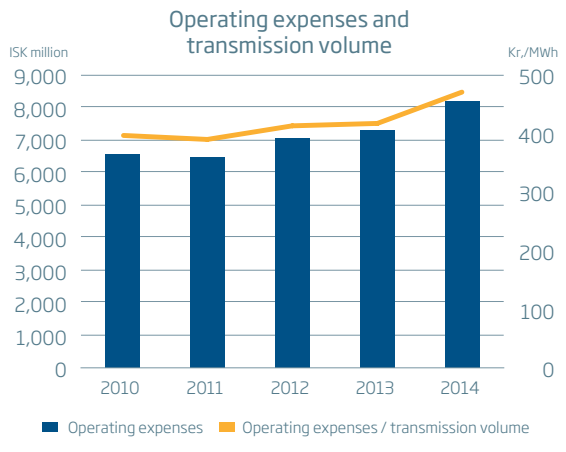


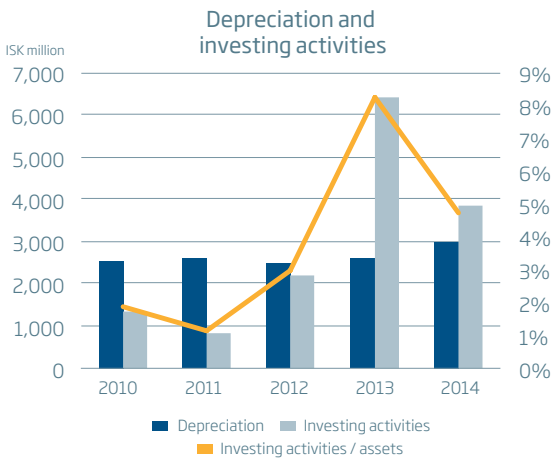

Transmission and transmission losses
GWh
20,000
18,000
16,000
14,000
12,000
10,000
8,000
6,000
4,000
2,000
0
3.0%
2.5%
2.0%
1.5%
1.0%
0.0%
2010
2011
2012
2013
2014
Generation
Transmission losses

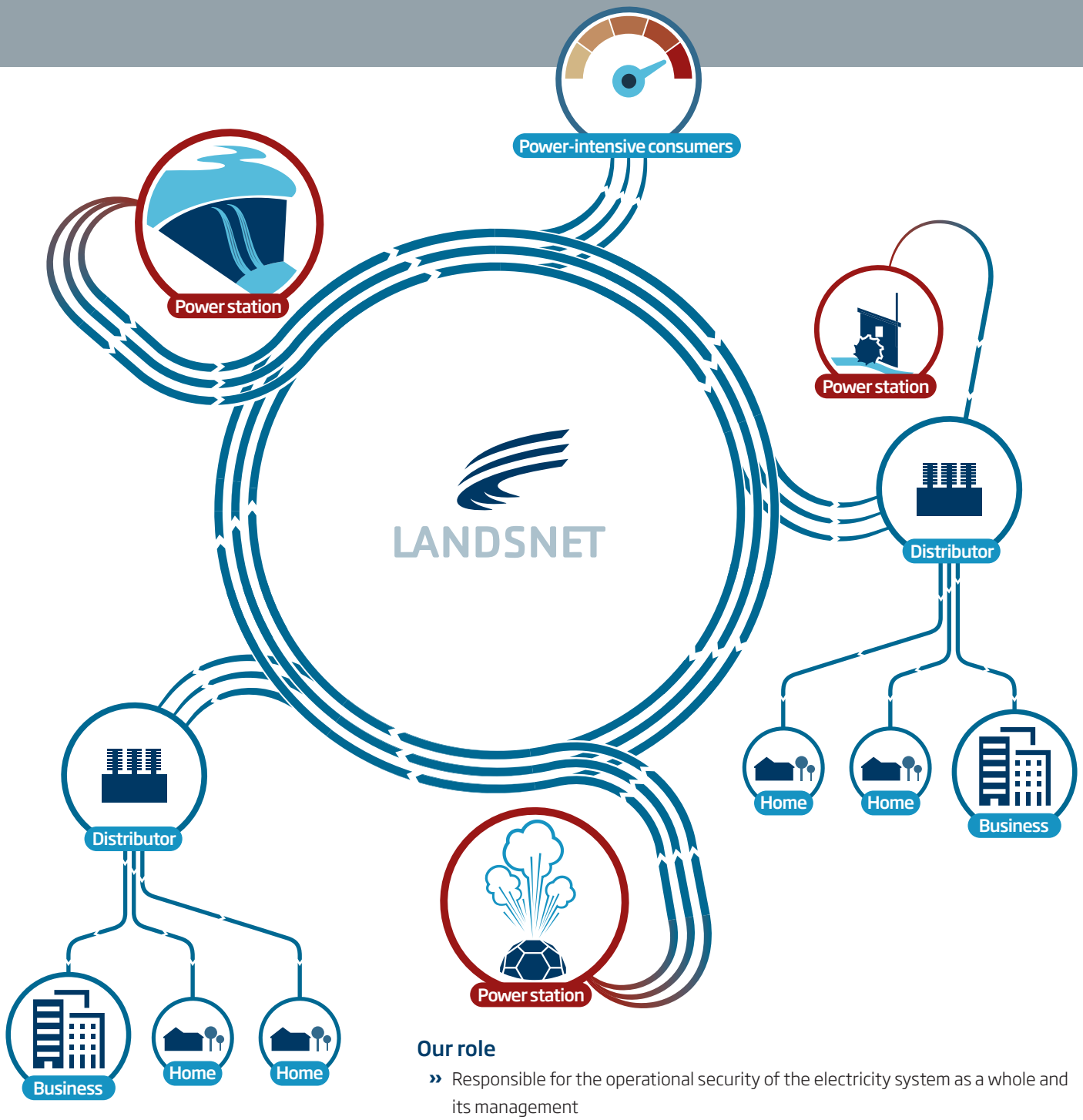

EBITDA and revenue
ISK million
10,000
9,000
8,000
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
80%
70%
60%
50%
40%
30%
20%
10%
0%
2010
2011
2012
2013
2014
EBITDA
EBITDA / revenue


Interest expenses and EBITDA
ISK million
2,500
2,000
1,500
1,000
500
0
4.5
4.0
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
2010
2011
2012
2013
2014
Interest expenses
EBITDA / interest expenses


Liabilities and EBITDA
ISK million
70,000
60,000
50,000
40,000
30,000
20,000
10,000
0
9.0
8.0
7.0
6.0
5.0
4.0
3.0
2.0
1.0
0.0
2010
2011
2012
2013
2014
Total liabilities
Liabilities / EBITDA


Operating expenses and transmission volume
ISK million
Kr./MWh
9,000
8,000
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
500
400
300
200
100
0
2010
2011
2012
2013
2014
Operating expenses
Operating expenses / transmission volume


Depreciation and investing activities
ISK million
7,000
6,000
5,000
4,000
3,000
2,000
1,000
0
9%
8%
7%
6%
5%
4%
3%
2%
1%
0%
2010
2011
2012
2013
2014
Depreciation
Investing activities
Investing activities / assets



Our role

- Responsible for the operational security of the electricity system as a whole and its management
- Balancing electricity supply and demand
- Maintaining the grid's capacities on a long-term basis and shaping the future grid
- Ensuring equal access to the grid and promoting an active electricity market

Landsnet – we transmit electricity

Landsnet hf is the owner and operator of Iceland's electricity transmission system – the grid. We began operations at the start of 2005 on the basis of the Electricity Act passed by the Icelandic parliament in the spring of 2003. The company operates under a concession arrangement and is subject to regulation by the National Energy Authority, which determines the revenue cap on which our tariff is based.

We are a responsible and cutting-edge service company with a strong team of professionals and a high level of community awareness. We aim to be at the global forefront in our industry.

Safety and work environment

We are committed to ensuring the highest level of safety in all our activities. To this end, we have established rules to promote a safe and healthy working environment reflecting respect for all those who carry out work for Landsnet at any given time.

In harmony with the environment

Landsnet is committed to treating Iceland's nature with respect, avoiding all unnecessary land disturbance and taking due account of the environment in all our activities. We constantly keep abreast of developments and progress in the design of transmission systems and strive to use the latest technologies where appropriate, whilst always minimising environmental impacts.

Landsnet's owners

Landsnet is a public limited company owned by Landsvirkjun, Iceland State Electricity (RARIK), Reykjavik Energy and the Westfjord Power Company.

Certified management systems

We are committed to maintaining high standards of professionalism and safety in all our activities. To these ends, we use international management standards.

ISO 9001:2008
quality management

OHSAS 18001:2007
safety management

ISO 14001:2004
environmental management

Iceland Construction Authority
Electrical safety management in accordance with the requirements of the Icelandic Construction Authority

Landsnet's Board of Directors

Our 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.

Executive Committee and core divisions

Landsnet's Executive Committee consists of Guðmundur Ingi Ásmundsson, who took over as President & CEO at the beginning of 2015, and Guðlaug Sigurðardóttir, CFO.

Mr Ásmundsson holds a degree in electrical engineering from the University of Iceland and a master's degree in electrical power engineering from the Technical University of Denmark. He was Deputy CEO of Landsnet from 2008, having previously served as Director of System Operations from the inception of the company at the start of 2005.

Ms Sigurðardóttir holds a degree in business administration from the University of Iceland. She joined Landsnet as Chief Financial Officer (CFO) in 2008, having previously held positions at KPMG Iceland, Meitillinn, the fisheries company VSV and the Municipality of Árborg.

Landsnet's core divisions

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 capabilities. It is responsible for forecasting future changes in the electricity market and providing effective solutions.

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. Grid Projects carries out this role.

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.

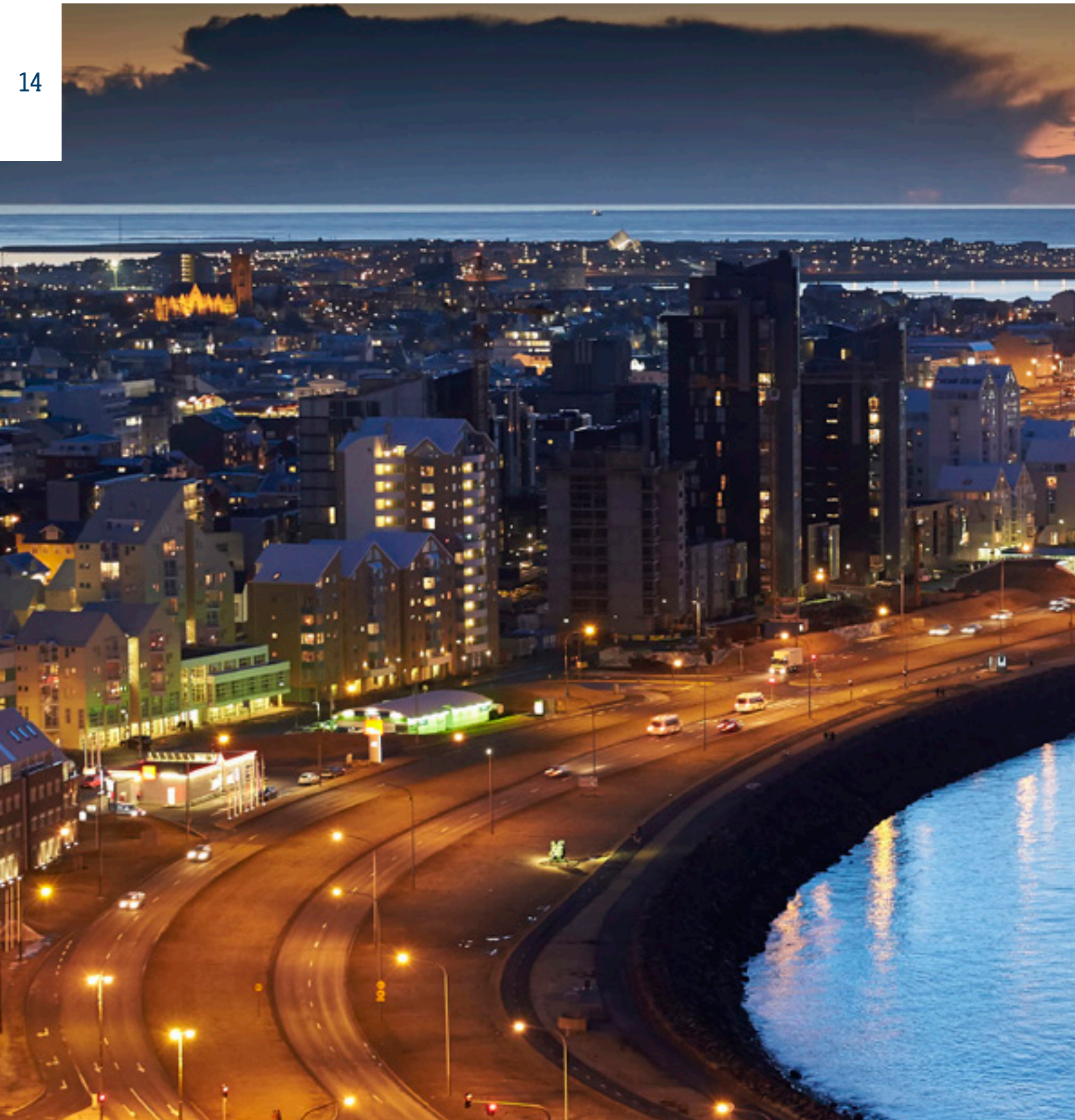
System Operation & Market controls the electricity system and co-ordinates operations in the grid and related units. This includes developing and operating protection equipment. The division also handles the development of market solutions, the drafting of terms and conditions relating to trade and operations,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

Senior management team

Landsnet's senior management team at the start of 2015

Íris Baldursdóttir, Head of System Operation & Market, Lúðvík B. Ögmundsson, Safety Manager, Einar S. Einarsson, Head of Markets and Services, Hildur B. Hrólfsdóttir, Quality and Environmental Manager, Nils Gústavsson, Head of Grid Projects, Guðlaug Sigurðardóttir, CFO, Guðmundur Ingi Ásmundsson, CEO, Sæmundur Valdimarsson, Head of IT, Elfa Hrönn Guðmundsdóttir, Human Resource Manager, Sverrir Jan Norðfjörð, Head of System Planning, Jórunn Gunnarsdóttir, VP – Corporate Office, and Guðlaugur Sigurgeirsson, Head of Operation & Maintenance (O&M).

Finance and operations



Landsnet performed well in 2014 and delivered a somewhat higher operating result than projected. Annual inflation for the year was only around 1%, which had a substantial positive effect on financial figures and thereby on the operating result as most of our funding is denominated in consumer price-indexed Icelandic krónur.

Under the Electricity Act, Landsnet's revenues are subject to a revenue cap. The 2011-2015 revenue cap was set by the National Energy Authority (NEA) in 2013 on the basis of a rate of return determined in 2012. Stakeholders then appealed the NEA's decision to the Appeals Committee on Electricity, which overturned it on 2 December 2013. The rationale for overturning the NEA's decision was that further reasoning was required to determine risk premiums and interest margins. Under the Appeals Committee's ruling, the NEA must issue a new decision on return criteria based on a new opinion delivered by an expert committee. That decision remains to be made, which means uncertainty over the revenue cap for the period.

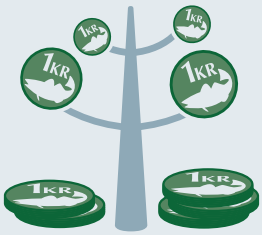
The repeated failure to issue NEA decisions on Landsnet's allowed rate of return and revenue cap at the time stipulated by law creates uncertainty for our operations. As a result, we are unable to react to the NEA's decisions with tariff changes before the start of

Highlights of the 2014 financial statements (ISKm):

Operating revenue

2013	2014
13,874	14,350

EBIT

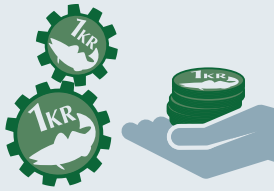


2013	2014
6,568	6,174

Profit

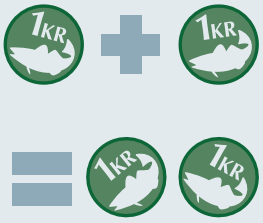
2013	2014
2,183	3,762

Cash flow from operating activities



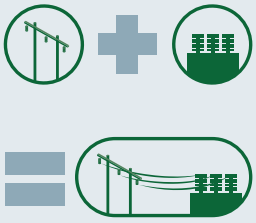
2013	2014
7,733	6,231

Total liquid assets



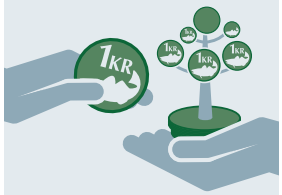
2013	2014
10,152	12,706

Total assets



2013	2014
77,608	81,859

Interest-bearing liabilities



2013	2014
55,088	54,647

Equity ratio

2013	2014
19.9%	23.5%

each revenue cap year, which would be the normal process. Frequent new and changed decisions also cause unexpected and irregular tariff fluctuations, which is unacceptable for our customers.

Investment in 2014 amounted to ISK 3,851 million, somewhat down year-on-year. Most of the year's infrastructure projects aimed to strengthen the current grid, although this could change in the near future as there are plans to connect new customers, both consumers and producers. Investment during the year was funded with cash on hand, which nonetheless increased significantly year-on-year. Repayments on our long-term loans are very low and not in normal sync with borrowings. The largest loan is a bullet loan maturing in 2020. A future vision for our funding is still being formulated, among other things with a view to balancing out the repayment curve.

Profit of nearly ISK 3.8 billion

According to the income statement, Landsnet generated a total profit of ISK 3,762 million in 2014, compared with a profit of ISK 2,183 million in 2013. Earnings before interest, taxes, depreciation and amortisation (EBITDA) were ISK 9,142 million, against ISK 9,166 million for 2013. The improved performance in 2014 is mainly due to low inflation, which was only around 1% on an annualised basis. Since the majority of our debt portfolio is denominated in ISK, the inflation trend has a significant effect on our operating result.

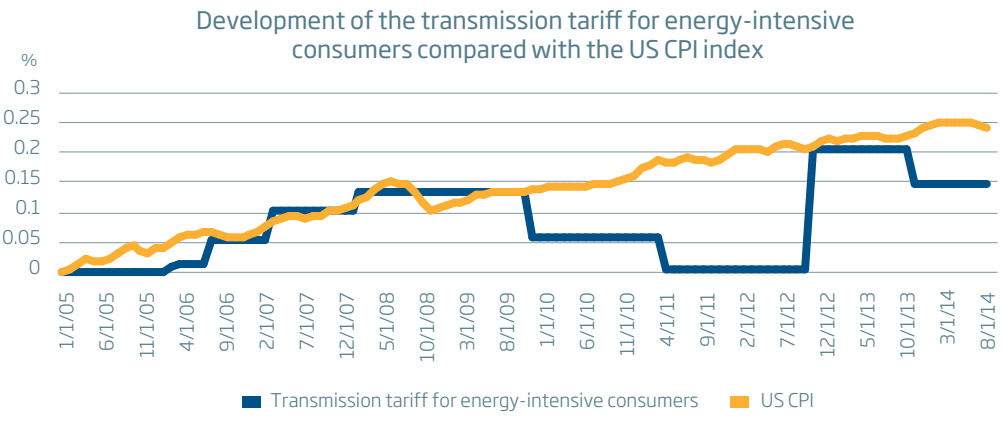
Operating revenue amounted to ISK 14,350 million. Transmission income accounted for ISK 14,277 million of this figure, up by ISK 509 million year-on-year, mostly driven by increased revenue from sales of ancillary services relating to transmission losses; this revenue source was up year-on-year as a result of higher electricity prices in the market.

Operating expenses before depreciation and amortisation were ISK 5,209 million, up by ISK 500 million or 11% year-on-year. Purchases of ancillary services and electricity because of transmission losses were up markedly year-on-year, which partly explains this increase in costs. Net financial expenses were ISK 1,519 million in 2014, compared with ISK 3,870 million in 2013, down 61% year-on-year. Indexation for the year amounted to ISK 511 million, against ISK 1,752 million in 2013, down by ISK 1,240 million. Exchange-rate movements were also positive, resulting in a gain of ISK 982 million for the year, compared with an ISK 328 million exchange rate loss in 2013. This gain was counteracted by lower capitalised interest, which was ISK 92 million, down from ISK 272 million in the year before.

Assets worth ISK 82 billion

Total assets stood at ISK 81,859 million at year-end 2014, as stated in the balance sheet, up from ISK 77,608 million a year earlier. Of this total, fixed assets accounted for ISK 66,780 million, compared with ISK 66,370 million at year-end 2013. Fixed assets in operation were ISK 63,771 million at year-end, compared with ISK 63,198 million at the end of 2013. New assets were brought into service during the year, including a substation at Ísafjörður and a reserve power station and substation at Bolungarvík in the West Fjords.

Long-term liabilities and obligations stood at ISK 58,496 million and short-term liabilities at ISK 4,155 million at year-end 2014. At the end of 2013, in comparison, long-term liabilities and obligations were ISK 58,564 million and short-term liabilities ISK 3,598 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 the ISK-denominated loan from the parent company, Landsvirkjun, until 2020. Loan repayments in 2014 are estimated at ISK 919 million, which is close to the amount repaid in 2013.


Development of the transmission tariff for energy-intensive consumers compared with the US CPI index
%
0.3
0.25
0.2
0.15
0.1
0.05
0
1/1/05
6/1/05
11/1/05
4/1/06
9/1/06
2/1/07
7/1/07
12/1/07
5/1/08
10/1/08
3/1/09
8/1/09
1/1/10
6/1/10
11/1/10
4/1/11
9/1/11
2/1/12
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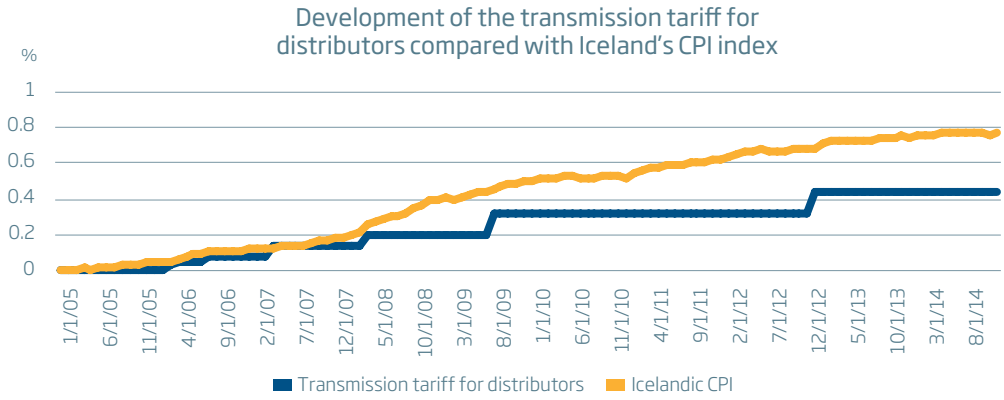
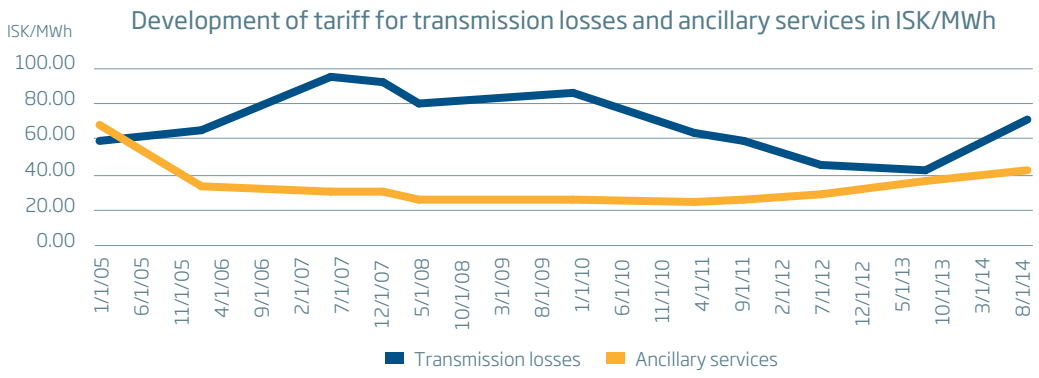
5/1/13
10/1/13
3/1/14
8/1/14
Transmission tariff for energy-intensive consumers
US CPI


Development of the transmission tariff for distributors compared with Iceland's CPI index
%
1
0.8
0.6
0.4
0.2
0
1/1/05
6/1/05
11/1/05
4/1/06
9/1/06
2/1/07
7/1/07
12/1/07
5/1/08
10/1/08
3/1/09
8/1/09
1/1/10
6/1/10
11/1/10
4/1/11
9/1/11
2/1/12
7/1/12
12/1/12
5/1/13
10/1/13
3/1/14
8/1/14
Transmission tariff for distributors
Icelandic CPI


Development of tariff for transmission losses and ancillary services in ISK/MWh
ISK/MWh
100.00
80.00
60.00
40.00
20.00
0.00
1/1/05
6/1/05
11/1/05
4/1/06
9/1/06
2/1/07
7/1/07
12/1/07
5/1/08
10/1/08
3/1/09
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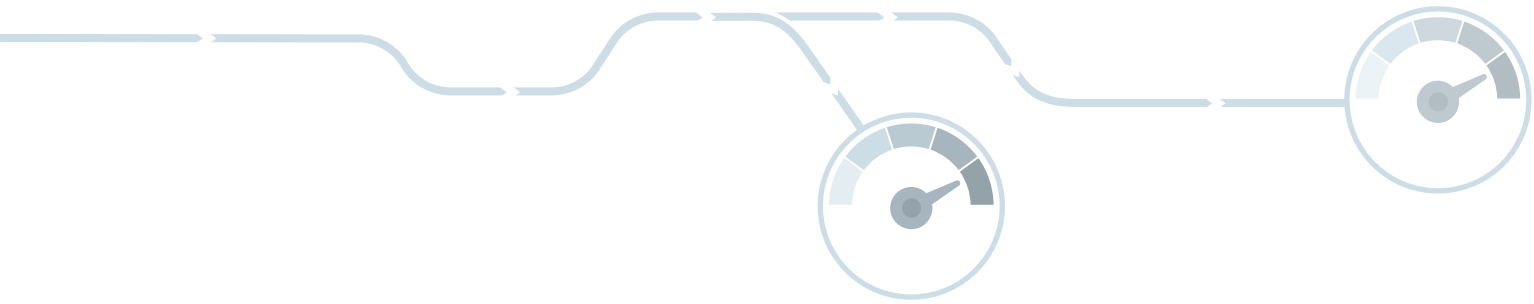
8/1/14
Transmission losses
Ancillary services



Equity at year-end 2014 stood at ISK 19,208 million, including share capital of ISK 5,903 million. By comparison, equity at the end of 2013 was ISK 15,446 million. The equity ratio was 23.5% at year-end 2014, up from 19.9% at the end of 2013.

Cash flow

Net cash from operating activities was ISK 6,231 million in 2014, compared with ISK 7,733 million in 2013. Cash outflows from investing activities for the year were ISK 3,851 million and financing activities amounted to ISK 907 million. Cash at year-end was ISK 12,235 million, up by ISK 2,317 million.

Long-term liabilities were 93% of total liabilities at the close of the year. Of interest-bearing debt, ISK-denominated loans accounted for 90% and CFH-denominated loans for 10%. No loan refinancing was required in 2014 as loan repayments and investments were 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) determines a revenue cap for Landsnet, which decides a tariff for its services in accordance with the cap. The revenue cap is based on historical operating expenses, depreciation of fixed assets and Landsnet's allowed rate of return, as decided by the NEA at the beginning of the revenue cap period and then reviewed annually.

The NEA issued three draft decisions in 2014 regarding Landsnet's required rate of return for 2011-2015. The Ministry of Industries proposed amendments to the Regulation on Weighted Average Cost of Capital, which were then retracted. The NEA also issued three decisions on revenue cap settlements for 2011, 2012 and 2013, subject to a final decision on return criteria for these years. More stable decision-making on the revenue cap and rate of return criteria is clearly required for Landsnet to be able to make long-term decisions on the grid's operation.

New tariff for transmission losses and ancillary services

On 1 January 2014, the tariff for ancillary services was increased by 16.2% and the tariff for transmission losses by 69.1%. The main reason was the rising market price of electricity, a continuing trend in the year.

Risk management and assessment

The objective of our risk management is to ensure operational continuity in any circumstances that may arise and to deliver an acceptable financial performance at any given time, with due regard to the underlying risks in our operations.

We worked on reviewing the company's total risk assessment during the year. The aim of this is to define and systematically map out the risks that can emerge in our activities, examine their possible impacts on operations and organise ways to minimise these. Among other things, the assessment covers operational risk, counterparty risk and financial risk.

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 as a whole, information systems, surveillance systems, management, the legal environment and contracts.

Counterparty risk is the risk of a counterparty to a financial or other agreement failing to meet its obligations thereunder.

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 as a result of 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 market risk, liquidity risk, exchange rate risk and indexation risk.

Market developments

We amended the Terms for Congestion Management (Terms C6) and the Terms for Delivering Electricity to Power-Intensive Users at Voltages below 132 kV (Terms B9). The amendments to the B9 Terms bring an important adjustment for power-intensive users at lower voltages, as these consumers will have a choice of connecting to the electricity system through a distribution system operator, subject to certain conditions being met. Both of these amended terms will take effect in the first half of 2015.

Landsnet is required by law to ensure the availability of sufficient spinning reserves[1] at any given time, to control frequency and voltage and ensure a minimum supply of regulating power[2] in the regulating power market. Long-term contracts with generating companies ensured the availability of 100 MW of spinning reserves in 2014.

Landsnet places an emphasis on increasing the range of bids in the regulating power market.[3] We continued experimenting with "telephone bids" and other special solutions in the regulating power market in an aim to stimulate competition and increase the number of suppliers. Agreements from the autumn of 2013 on guaranteed regulating power supply[4] remained in effect in 2014. Three tenderers submitted bids, following which a number of new generating units entered the regulating power market. The average price per guaranteed MWh during the period was ISK 336.

Our cost of transmission losses continued to increase year-on-year and was up by 65% on 2013. This is explained by increased transmission losses and a rising average tender price. The average price of electricity purchased by Landsnet to meet transmission losses rose by 47% year-on-year on the basis of a tender process held in the autumn of 2013. We ran a tender process in the autumn of 2014 to purchase electricity for transmission losses in 2015, which led to further increases from ISK 3,047/MWh to ISK 3,762/MWh, which represents a 23% average year-on-year rise.

We have in recent years been working to launch an Icelandic market for electricity trading, named ISBAS. The launch of a power trading 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.

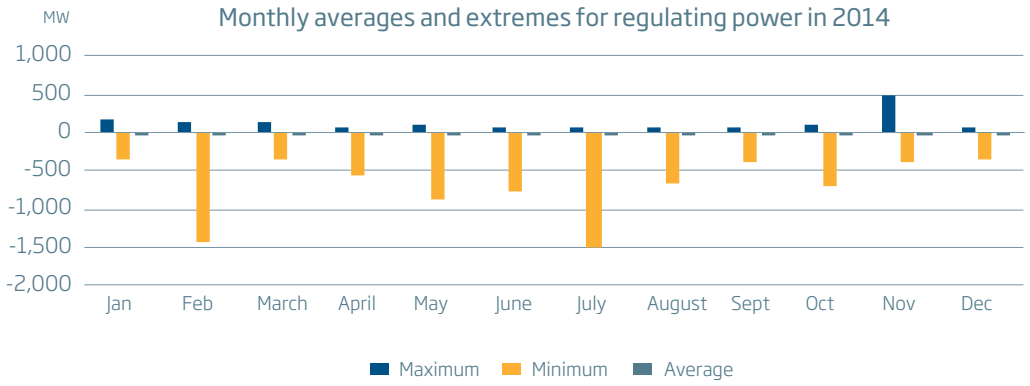
Guarantees of Origin

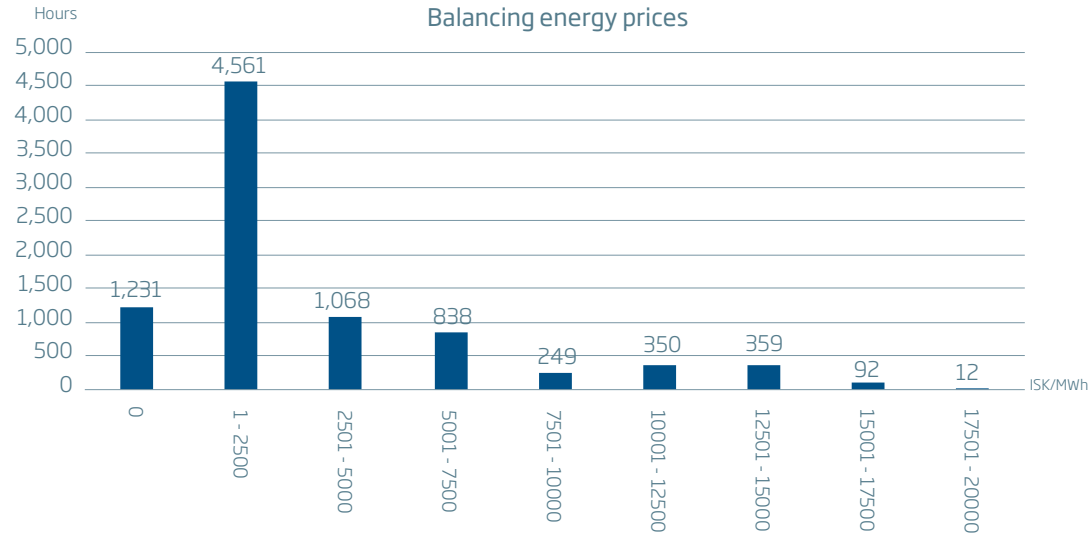
We have been issuing Guarantees of Origin of electricity (GOs) since 2012. The certificates serve as confirmation that certain electricity is generated using renewable energy sources, e.g. hydropower or geothermal. Our GOs issuance grew significantly between 2012 and 2013 but stabilised in 2014. The total number of certificates issued by the company was around 10 million in 2014, down from 13 million in the preceding year.

We have twice lowered the tariff since our issuance began, from the original price of ISK 7 per certificate to ISK 4.30 in October 2013 and ISK 3.60 in May 2014, which is roughly on par with the going rate in Europe.

Together with the Finnish registry system developer Grexel, we held a presentation during the year for sellers of GOs in Iceland. We have given presentations of GOs and their regulatory framework to interested buyers within the energy sector, and taken an active part in the Association of Issuing Bodies (AIB) ever since becoming an issuer.

1) Operating reserve ('back-up power') connected to the grid and immediately available.
2) The power procured by Landsnet to balance differences between forecast energy use and actual energy use in the electricity system as a whole.
3) Landsnet's procurement market for regulating power.
4) Guaranteed regulating power ensures a minimum supply in the regulating power market.





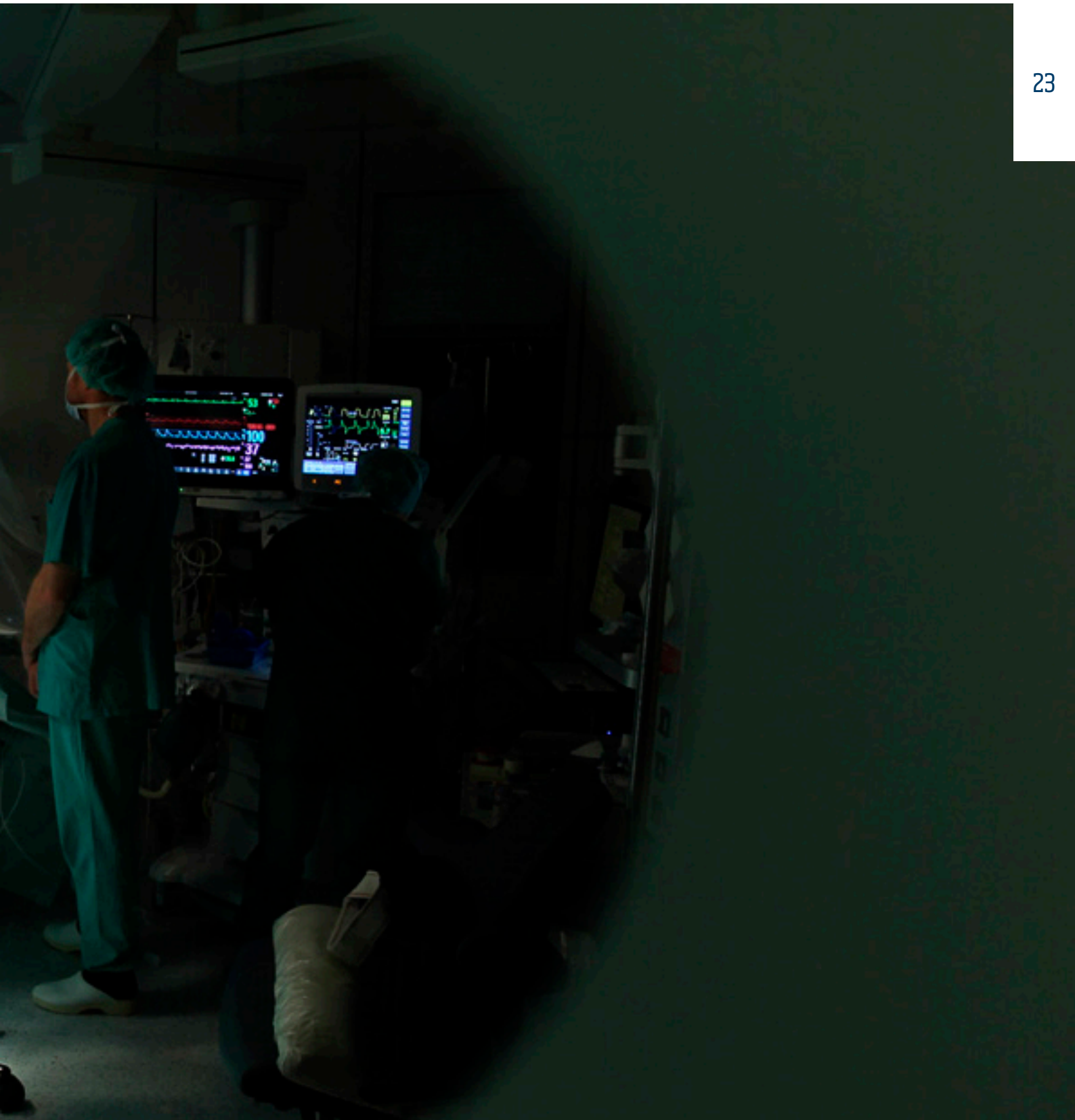
Purchasing and inventory control

We placed focus on reviewing our purchasing environment in 2014. This included tender documents, procurement processes and more emphasis on the use of negotiated procedures and FIDIC contract templates. The number of tender processes was far lower in 2014 than in the previous year, down from 15 to three, primarily because of postponed projects.

Inventory control was focused on changes to the storage system and the introduction of hand-held computers in our warehouse facility at Gylfaflöt, Reykjavík. Volcanic activity north of the Vatnajökull ice cap put its mark on our inventory control as we and suppliers worked to ensure fast access to reserve stock materials in case of damage to the electricity system due to an eruption.

A challenging and busy year

The year 2014 was both challenging and busy for our staff, who had to contend with emergency situations right from the first day of the year until the last to ensure electricity supply to our customers.



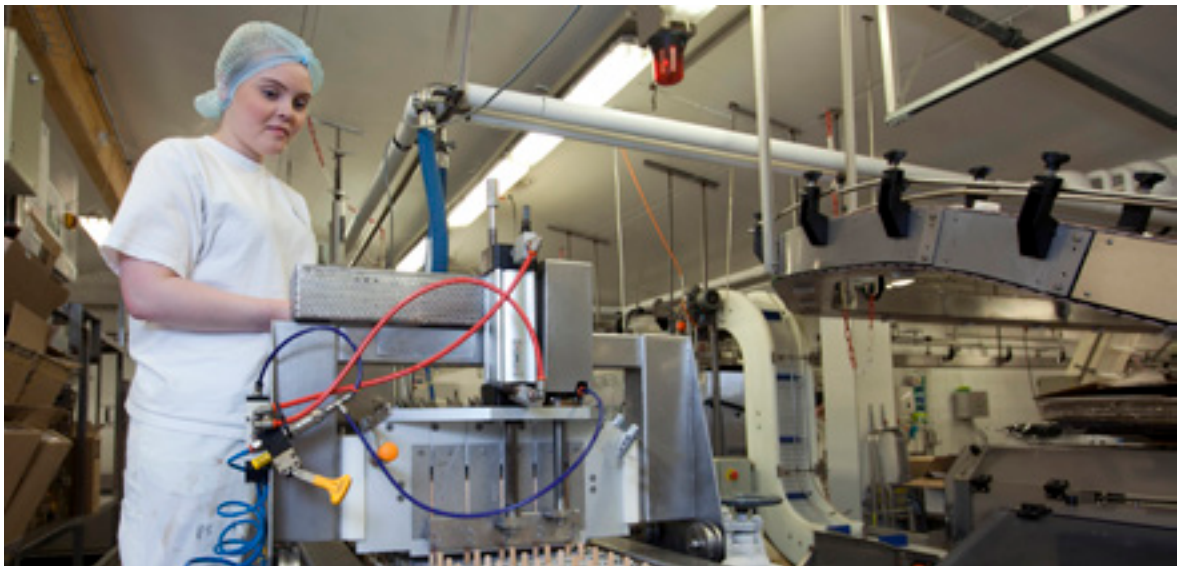
The year saw frequent disturbances and infrastructure damage in East Iceland due to persistent north-easterly winds, with heavy icing conditions and high wind speeds right from the beginning of the year into March. The conditions for carrying out repairs were very challenging, and our linesmen and other personnel performed no mean feat in getting the region's transmission infrastructure back up and running. In late winter, we had to deal with repeated disturbances in the West Fjords due to severe storms. Our staff were also in response mode against potential risks for the electricity system ever since news broke in August of major geologic activity in the northern part of the Vatnajökull ice cap.

We also worked on routine maintenance, grid development projects, new infrastructure projects and improvements to our Wide Area Protection systems. A large step was taken towards the end of the year when our reserve power station at Bolungarvík entered service together with smart grid controls, vastly improving operational security in the West Fjords. Another milestone was the completion of an environmental programme for our Grid Plan, subjecting it for the first time to a strategic environmental assessment. Subsequently, work began on assessing the environmental impact of building a transmission line across the Sprengisandur highland plateau, as the Grid Plan environmental report indicated that a connection over the interior highlands – bringing grid strengthening to the west and east – may be a viable option to achieve the strengthening of the main grid necessary in Landsnet's view.

Grid development

Like in previous years, we placed much emphasis on preparing strengthening of the main grid. This work is subject to much uncertainty and requires long preparation. Hence, we now endeavour to start the preparations earlier than was customary, in particular systems analysis, specific studies of weather conditions, option analysis, line routeing and planning-related work. Importance is attached to following statutory procedures to shorten the projects' preparation time once the final decision to build new infrastructure is made.

A draft scoping document for the environmental impact of a transmission line across the Sprengisandur highland plateau was presented in open meetings in northern and southern Iceland.



A strong transmission system is vital for Iceland's economy.

Grid Plan's strategic environmental assessment – increased focus on consultation

The Grid Plan provides a projection of necessary development of the grid and aims to ensure that Landsnet and government bodies have a full overview of the development needed to meet transmission demand.

This was the first year in which we subjected the Grid Plan to a strategic environmental assessment (SEA). We placed emphasis on sparking discussion and obtaining feedback on our infrastructure development plans as soon as possible in the process. The decision was made to use the process to present existing options, without selecting one over another at that stage, thereby enabling the collection of important information and providing more time to prepare important decisions. The Grid Plan scoping document was presented to all municipalities, statutory consultation bodies and key stakeholders. Anyone was permitted to comment, since the aim was to obtain as many views as possible on the Grid Plan's assessment process. Similarly, we presented a draft environmental report together with a Grid Plan draft proposal. Various comments received were used to inform the process. This was not possible where no particular option had as yet been selected over another, in which case the comments are applied to the subsequent Grid Plan now being drafted together with the SEA.

In our view, the Grid Plan's SEA meets all requirements of legislation, EU directives and applicable guidelines on SEAs. The main environmental impacts of different options are discussed in the environmental report, including overhead lines and underground cables, routeing and voltage levels. The report contains the information needed to make an informed decision on the various aspects of the Grid Plan. We hope that this new procedure will enable the consultation process for new projects to start sooner and to focus on the main options rather than individual projects, thereby enabling a better consensus on the grid's necessary future development.

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, work on solutions to transmission constraints in the main grid and an analysis of connection possibilities for a number of new power stations.

Preparations for a number of projects were completed in the year, many of which concern increased undergrounding at lower voltages than previously and renewal of old infrastructure. We prepared the connection of new customers at Helguvík and signed a transmission agreement with PCC BakkiSilicon hf, which is building a silicon metal plant at Bakki near the town of Húsavík in northern Iceland. This is the first agreement that we enter into for prospective industrial development at Bakki. The facility is scheduled to commence operations in 2017 under the agreement.

We took part in various public and community projects under government auspices, including consultation on amendments to the Electricity Act and committee work in relation to security of supply in the West Fjords and energy issues in the north-east of Iceland.

New infrastructure projects

Investment in the transmission system amounted to just under ISK 3.9 billion in 2014, somewhat down year-on-year. Most of the infrastructure projects worked on aimed primarily to strengthen the existing grid. There were relatively few grid expansions, but this could change in the near future with new connections of customers, both consumers and generators.

The construction of a new joint substation of Landsnet and the Westfjord Power Company and a Landsnet reserve power station at Bolungarvík was completed in the autumn of 2014. The finalisation of this project involved some of the most extensive testing ever undertaken by Landsnet, both of the power station itself and of the new smart grid system. The reserve power station ensures electricity supply to consumers when transmission to the West Fjords is curtailed, and the smart grid system shortens outages through increased automation and integrated intelligent protection systems. The power station and the smart grid system entered service at the end of November and have already proven their worth in disturbance management. An open day held at the power station in December was attended by almost 100 people, young

Landsnet's reserve power station at Bolungarvík.

and old, to mark this major milestone in the development of the West Fjords network.

The construction of a new substation of Landsnet and the Westfjord Power Company at Ísafjörður was completed in the summer of 2014. This substation marks an important step in the deployment of smart grid systems in the West Fjords. It formally entered service in September in the presence of the Minister of Industry and Commerce.

We have for years been preparing the construction of the Suðurnes Line 2, which will extend from the town of Hafnarfjörður in the Greater Reykjavík area to the Reykjanes peninsula and increase security of supply in the Suðurnes region. In May 2014, an application was submitted for a development permit from the four municipalities through which the line is proposed to be built, with construction expected to begin in late summer. At year-end 2014, only the Municipality of Reykjanesbær had issued a development permit. We now expect to start work on the line tracks and foundations for the Suðurnes Line 2 in the summer of 2015 and to complete the stringing in 2016.

In the spring of 2014, we entered into an agreement with United Silicon (USi) on transmission to a silicon metal plant to be constructed at Helguvík on the Reykjanes peninsula. Under the agreement, the connection should be installed by 1 February 2016. The project requires a new breaker at Fitjar, a 9km long 132 kV underground cable between Fitjar and Helguvík and a new substation at Helguvík. There will be three 132 kV breakers in the new substation and two transformers, one connected to the silicon metal plant and the other owned by the utility company HS Veitur. The contracts on the purchase of the underground cable and transformer for the silicon metal plant were concluded in 2014. The cable was purchased from the German company Nexans and will be installed in the summer of 2015. We are working on the design and preparation of its installation in close co-operation with Nexans, which will also carry out all connections.

The construction of our new substation at Akranes in west Iceland commenced in the year. The existing substation is both old and located in an area defined as residential in the local plan. The old substation building is owned by Reykjavik Energy (RE). Under a 2007 agreement between RE and the Municipality of Akranes, the new substation is to be built in the industrial district farther west. The construction is scheduled for completion in the second half of 2015 and the substation to be energised at the start of 2016.

The Selfoss Line 3, a new 25km long 66 kV underground cable, is planned between Selfoss and Þorlákshöfn in the south of Iceland to increase security of supply for the towns of Hveragerði, Þorlákshöfn and Selfoss. We worked on the design of the cable route, necessary changes in substations at Selfoss and Þorlákshöfn, planning and permitting. At the end of the year, we entered into an agreement with the Swedish cable producer NKT Cables AB on the purchase of an underground cable, whose installation is scheduled in 2015.

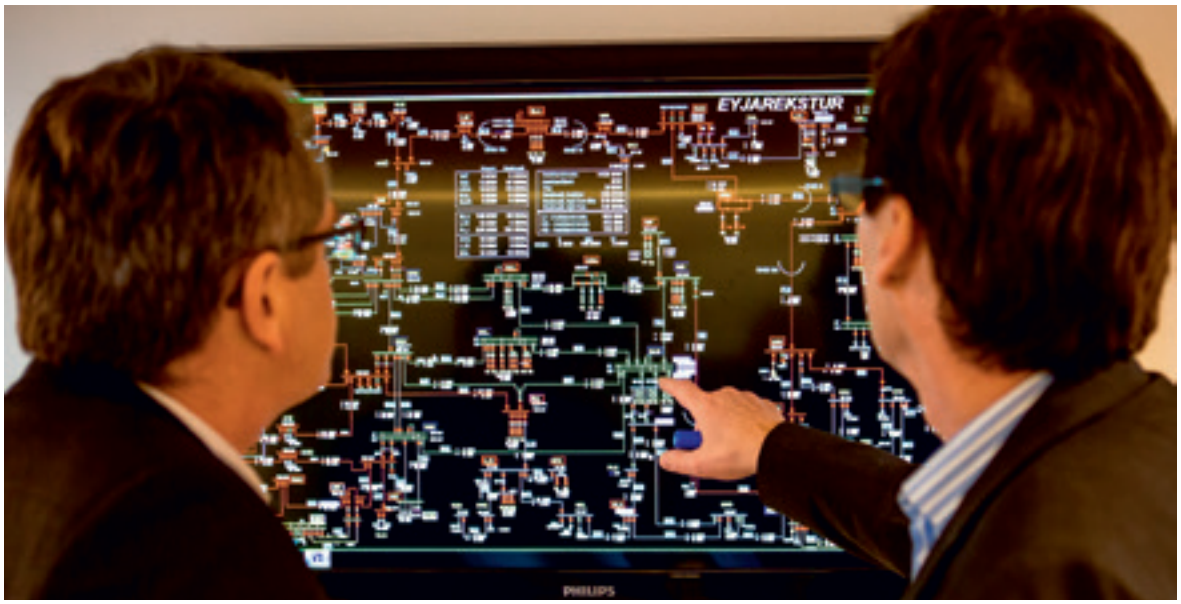
The Hella Line 2, which dates from 1948 and extends between the towns of Hella and Hvolsvöllur in southern Iceland, is among the grid's oldest lines and in need of renewal. We prepared a new 13km long 66 kV underground cable connection in the year to replace the current overhead line. We also entered into an agreement with NKT Cables AB on the purchase of the underground cable for the project, with installation scheduled in 2015.

The relocation of the Laxá Líne 1, a 66 kV overhead line in the Fnjóskadalur valley, was requested during the year to make way for a new road to the mouth of the Vaðlaheiði Tunnel. A 500m section of the line was undergrounded in the autumn. In October, the cable was energised and the overhead line demolished.

We received a new 220/132 kV, 100 MVA transformer for the Fljótsdalur substation from the Italian manufacturer Tamini in the spring of 2014. When it had entered service in the summer, one of the existing two transformers in the substation was sent to England for repairs.

The expansion of the Vatnshamrar substation was completed in early 2014. A 132/66 kV power transformer and two new breaker bays were added to

Landsnet and Norway's TSO, Statnett, have partnered to develop a new generation of transmission towers. The prototypes of two new tower designs are currently being built.



increase security of supply in West Iceland. Although the works were mostly completed before year-end 2013, site restoration and our acceptance tests were completed in March 2014.

At the beginning of 2014, transmission infrastructure for a new point of delivery was energised at Höfn in the south of Iceland. Various site restoration work, including on the cable trench, was completed in the autumn. An environmental audit of the project will be performed in the autumn of 2015 in accordance with our policy.

Prototypes of two new transmission towers being built

Landsnet is committed to innovation and R&D and spends considerable resources on such projects every year. As part of this, we are developing a new generation of transmission towers in collaboration with Norway's TSO, Statnett, with the assistance of Icelandic and foreign experts. A milestone was reached in 2014 when the decision was made to start building the prototypes of two of the tower designs. One of them has been named "the Bird" because its crossbar resembles the wing of a bird. The other is intended for use in a narrow line corridor. Both designs are tubular towers incorporating solutions never before used on transmission towers. The plan is to install the prototypes at selected sites in the spring of 2015, while continuing to develop more new tower designs.

Repairs and maintenance

Routine maintenance including periodic condition checking on transmission lines and substation maintenance projects began at the start of summer. We also prepared and completed more permanent repairs of transmission lines damaged earlier in the winter. Individual projects included improvements to the West Line, the finalisation of the strengthening of the Tálknafjörður Line, full repairs of transmission lines damaged earlier in the year in East Iceland and the relocation of the Prestbakki Line 1 because of coastal erosion at the Breiðamerkurlón glacial lagoon. A number of large-scale maintenance projects were

Árni Jón Elíasson, Project Manager at Landsnet, gives a presentation on a research project into the forecasting of icing events, at the 2014 Arctic Circle Assembly.

postponed until the autumn, so maintenance of lines and substation had to be carried out right until the end of the year.

We continued to develop forecasting models for ice build-up on transmission lines and expect to be able to use these to define load criteria and in day-to-day grid monitoring in the future. We gave a presentation of the status of the project at the Arctic Circle international assembly held in Reykjavík in early November, which was attended by 1,300 participants from 34 countries. In addition, we are currently analysing the implications of a possible sub-sea cable to Europe, such as the costs involved and the effects on transmission and generation in Iceland, the energy market and pricing.

Landsnet has long had basic research carried out on environmental factors that affect the grid's development and operation. This has built a unique database for decision-making on the grid's future development. We will continue such basic research and are mindful of the importance of its continuity.

Growing operational risk

The year's peak in power fed into the grid was recorded on 4 December at 2,253 MW, which is 0.8% higher than the previous year's peak. Total system demand in 2014 was 17,481 GWh, down 0.03% on the previous year. Transmission losses totalled 361 GWh, or 2.06% of generation, down by 3.38%.

The load on the grid increased further in 2014, which was reflected in heightened operational risk. The number of defined transmission cut-planes requiring constant monitoring had to be increased to nine (Figure 1). Owing to low reservoir water levels, high levels of inter-regional transmission were necessary. The resultant consumer curtailments and stability problems highlighted the transmission constraints in the current system.

The risk of an outage when a disturbance occurs is increased when the level of transmission through a cut-plane nears or exceeds security limits, as shown in Figure 2. The graph shows the transmission via six cut-planes for the entire year 2014 where the security limits are exceeded for a large portion of the time. Under such conditions, our Control Centre must require generators to change their generation plans, i.e. where in the country the electricity is produced, in addition to

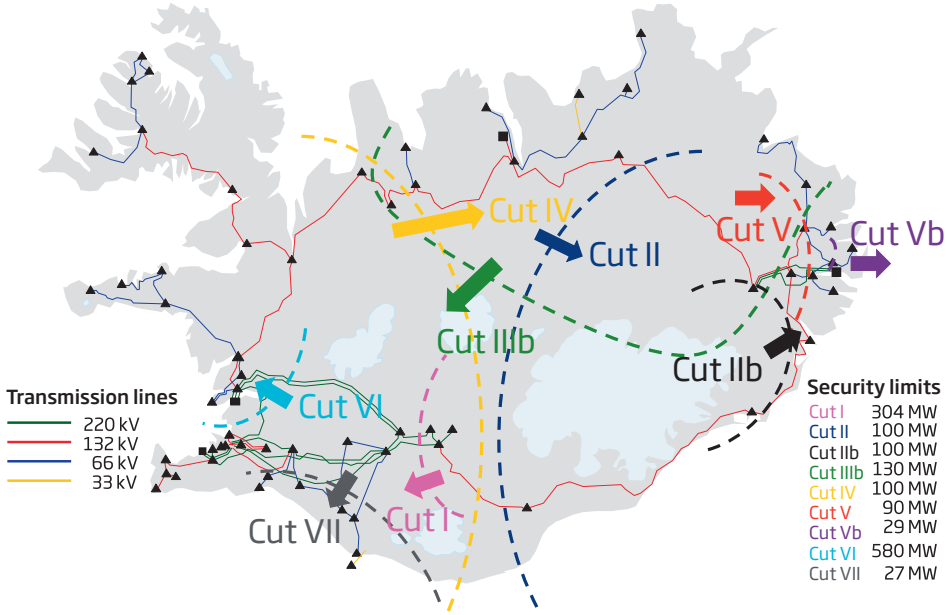


Figure 1. Defined transmission cut-planes and their security limits.

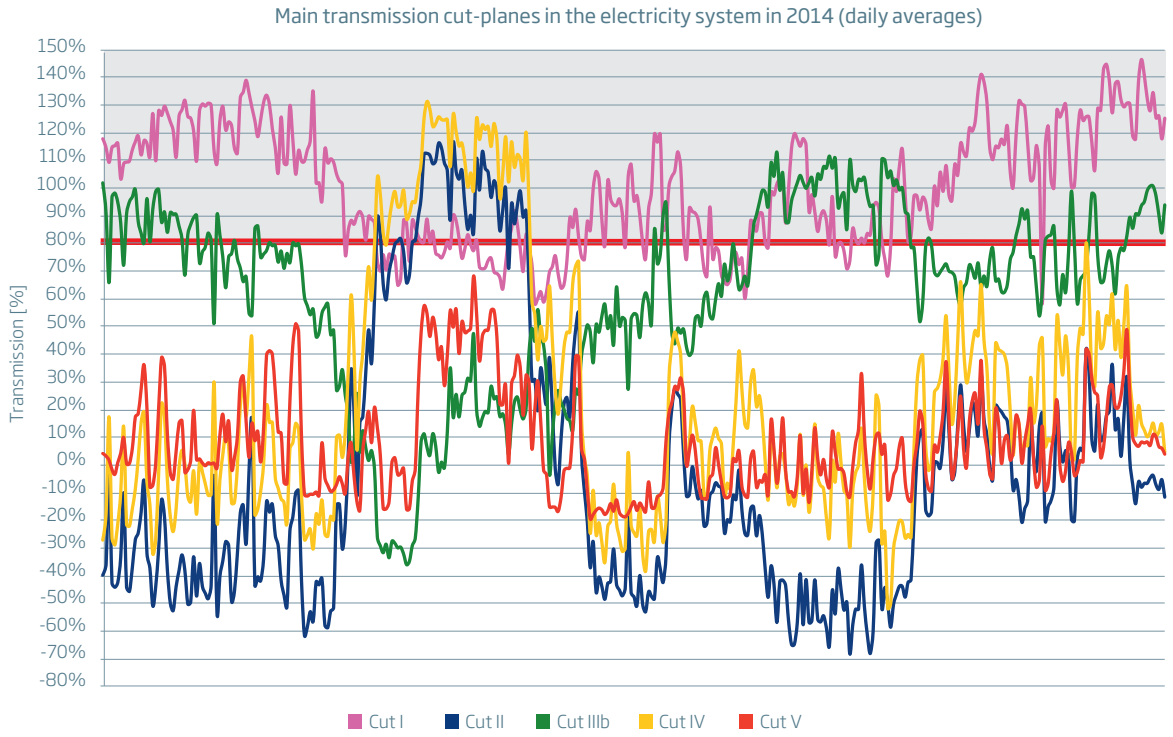


Figure 2. Daily transmission averages for six transmission cut-planes over the whole of 2014. The red line is a reference line used by our Control Centre to decide on measures to be taken if transmission levels exceed the line.

persistent curtailments in certain regions. High-risk operations of this kind bring with them inefficiencies for all those connected to the grid.

"European champion in Wide Area Protection"

In 2014, the inter-regional power flow exceeded security limits 28% of the time, or for a total of 2,456 hours. Energy transmitted at levels exceeding the limits totalled 294 GWh. Being so far in excess of the transmission cut planes' limits poses a threat to the system's stability. Because of grid disturbances, our Wide Area Protection systems divided the grid into two islands 11 times in 2014, resulting in inconvenience for consumers each time. Our co-operating partners in Europe have observed these stability problems with some interest and refer to Iceland as the "European champion in Wide Area Protection". We have devoted much work to improving our Wide Area Protection systems, with our experts in protection equipment extensively involved in the grid's operation.

Rise in the number of grid disturbances

The number of grid disturbances rose significantly year-on-year, from 52 in 2013 to 69 in 2014. The number of faults was also up from the previous year, from 54 in 2013 to 83 in 2014, which means that more than one fault occurred in some instances. The number of recorded disturbances in substations increased substantially, while the number of disturbances in transmission lines grew at a slower rate. Energy not supplied[1] as a result of grid disturbances totalled 748 MWh, which corresponds to 23 outage minutes.

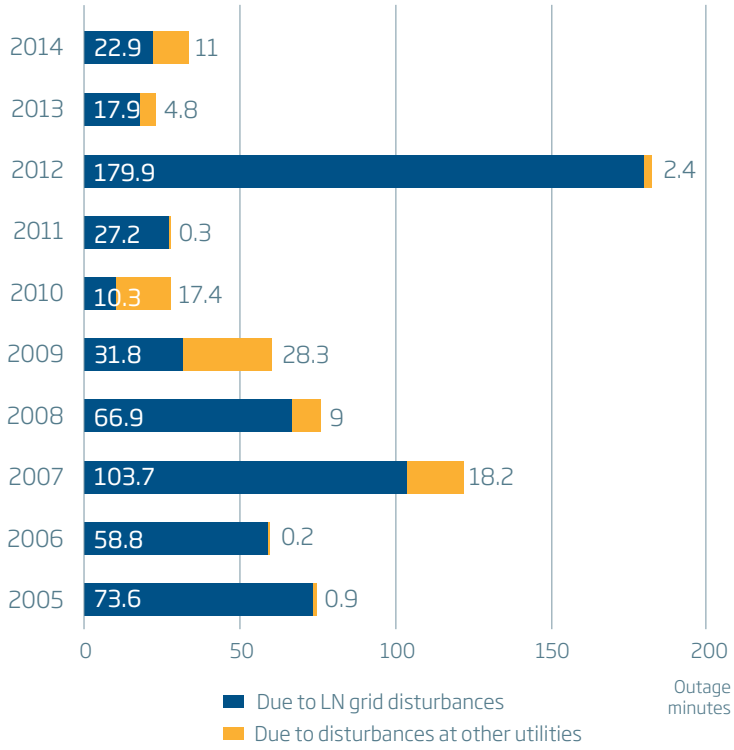
The main grid disturbances causing outages and curtailment of power supply to customers were as follows:

January 2014 was characterised by heavy precipitation, icing and wind load in East Iceland, which caused power disruptions. The Fljótsdalur Line 2 tripped[2] six times in the month owing to icing, but without causing non-supply of energy. The Vopnafjörður Line 1 tripped four times in the month and the Eskifjörður 1 and Fáskrúðsfjörður 1 Lines once each. Fault location and repairs were challenging because of impassable weather conditions and intense storms, so reserve power was used extensively in East Iceland during the month. Energy not supplied owing to these disturbances totalled 27 MWh.

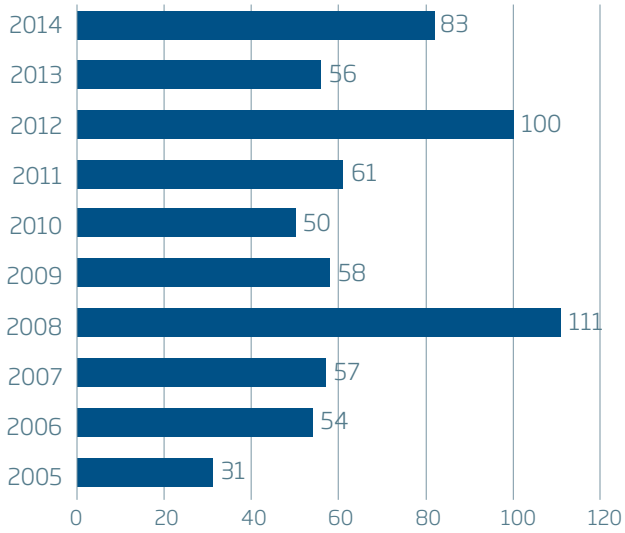
- On 13 January, the Fitjar Line 1 (MF1) tripped during work at the Fitjar substation. The town of Grindavík suffered an outage and all generating units at the Svartsengi Power Station and in the Reykjanes peninsula tripped. Energy not supplied was assessed at 20 MWh.
- On 15 January, the Kópasker Line 1 (KS1) tripped because of a manufacturing defect in the underground cable from the Þeistareykir Geothermal Power Plant. The cable had to be disconnected so that the line could be re-energised. Energy not supplied was 22 MWh.
- On 8 February, an extensive disturbance occurred in East Iceland. It started with the tripping of a 132 kV transformer at the Sigalda substation due to humidity in a connecting box, causing the grid to split into two islands.[3] Under-frequency in the system caused shedding of load for two consumers in the west island. A generating unit in East Iceland also tripped, resulting in extensive under-frequency in the east island, which in turn caused shedding of power-intensive consumer load. Restoring normal service proved challenging. Energy not supplied as a result was substantial at 218 MWh, as the power-intensive consumer load was offline for a long time.

1) Energy not supplied is electrical energy that could not be delivered to one or more consumers as a result of a fault in the electricity system, changes to it, maintenance work or transmission constraints.
2) Stopped transmitting electricity.
3) The temporary operation of two or more sections of the grid that have been disconnected from each other and are therefore asynchronous.

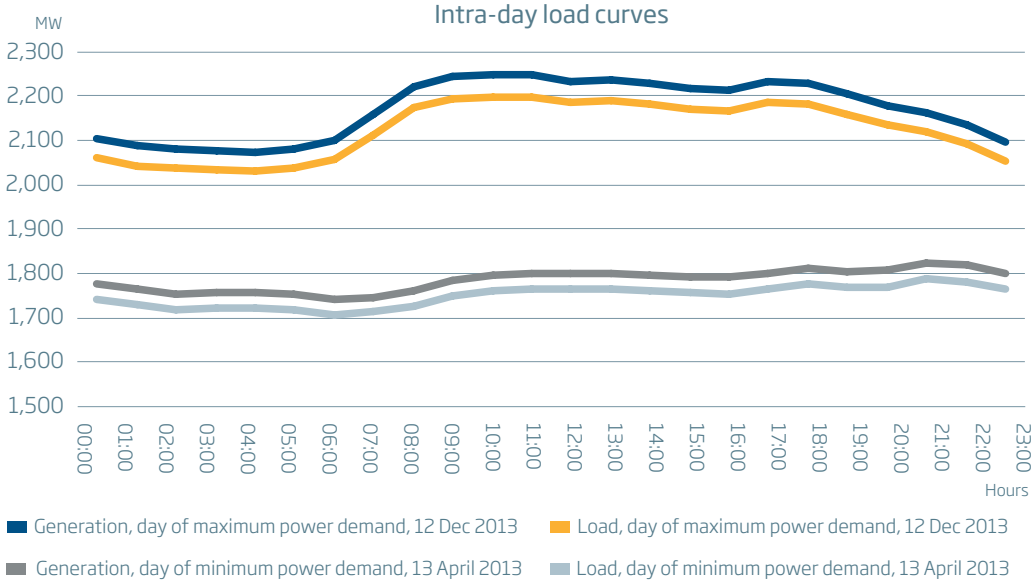
Outage minutes due to disturbances



Number of grid disturbances



Intra-day load curves



- On 12 February, icy weather conditions in the West Fjords caused the Mjólká Line 1 (MJ1) to trip. Re-energisation efforts being unsuccessful, reserve power was deployed. Shortly after completion of the repair on the MJ1 in the evening, the Breiðadalur Line 1 (BD1) tripped because of wind load and icing. The fault was located during the night but impassable conditions and bad weather delayed the repair's completion until four days later. Energy not supplied totalled 35 MWh.
- On 21 March, a fault occurred in a 66kV transformer at the Vatnshamrar substation. Efforts to activate reserve power were unsuccessful, resulting in an outage in the West Iceland regional network. Energy not supplied was assessed at 22 MWh.
- On 5-9 May, power-intensive consumer load was shed a number of times, resulting in the Wide Area Protection system splitting the grid into two islands. Our under-frequency protections also shed load to restore the frequency to 50 Hz. Energy not supplied as a result of these events was assessed at a total of 92 MWh.
- On 24 May, our under-frequency protections shed load after 105 MW of generating capacity tripped in the south-west of Iceland. Energy not supplied was assessed at 56 MWh.
- On 18 June, a disturbance occurred in relation to an upgrade of our Energy Management System (EMS). The Automatic Generation Control was sending incorrect values, resulting in significant under-frequency in the system and shedding of load. Energy not supplied was assessed at 320 MWh.
- On 3 August, power-intensive consumer load was shed unexpectedly, triggering under-frequency load shedding in Landsnet's system. Energy not supplied was assessed at 98 MWh.
- On 3 October, a thunderstorm hit southern Iceland and a lightning struck the Sigalda Line 4 (SI4) and the Prestbakki Line 1 (PB1). To prevent power fluctuations between areas, our Wide Area Protection system split the grid into two islands. Our under-frequency protections also shed load to restore normal frequency. Energy not supplied was assessed at 48 MWh.

We place a premium on using IT solutions in the best way possible to improve the grid's operational security and provide an efficient operating environment.

The Landsnet app enables users to keep their fingers on the grid's pulse and stay abreast of news and announcements.

IT ever more important

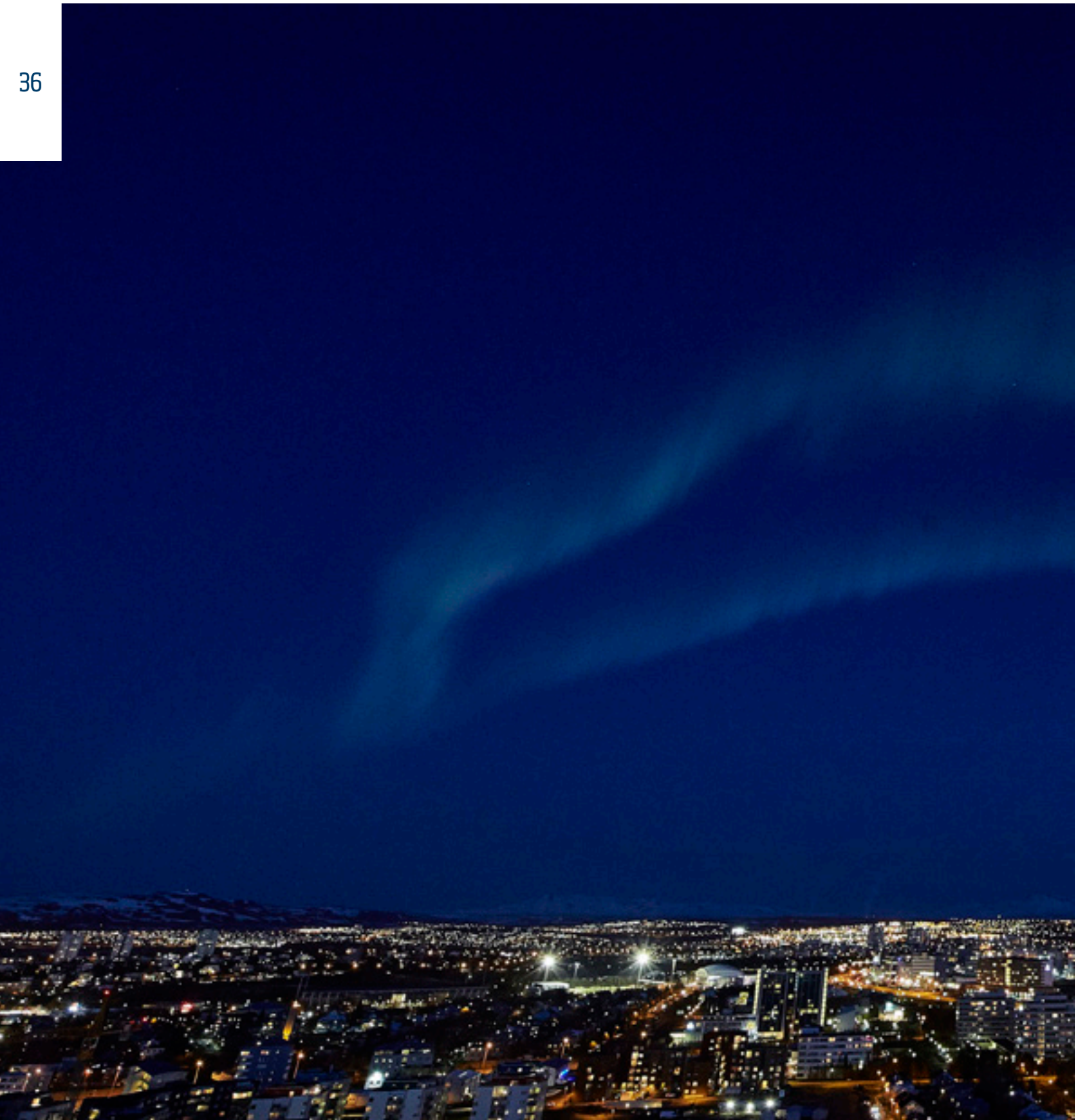
Landsnet relies on fast and secure telecommunications, effective information systems and well-trained IT specialists. We place a premium on technological solutions to enhance the grid's operational security and provide an efficient operating environment. We continued to deploy smart grid solutions, including the development of a system that detects unplanned load shedding and reacts immediately by adjusting the system's generating units in a way reducing the likelihood of shedding. We also worked on a solution designed to enable the system to shed curtailable load by using Tetra communications in areas lacking fully reliable communications.

Information and communication systems are exposed to a range of threats. Possible natural hazards due to geologic activity in Mt Bárðarbunga have called for contingency preparation and a review of communications links. Another potential threat that needs to be addressed is break-ins and attacks. To mitigate against these risks, our IT systems undergo regular security audits. We also partner with other European TSOs on IT-related issues, which in 2014 included a new joint project to measure the IT performance and costs of eight TSOs.

The Landsnet app

We made considerable changes to our e-services during the year. Our service web, Amper, and our scheduling system for planned works and service interruptions were upgraded. We completed the adoption of a new documentation and groupware system used in, among other things, co-operation projects with external parties. We also launched an app for Android and iOS to view grid transmissions, key figures from our operations and our latest news and announcements.

In harmony with the environment and society



Landsnet has a duty to ensure security of supply, protect consumer interests and support the strengthening of communities, value creation and the use of renewable energy sources. The grid plays an important role in achieving Iceland's environmental and climate targets. Green power generation is vital in this respect and investment in the grid better connects electricity generators to the market.

No serious environmental incidents occurred in our activities in 2014. We are committed to continual improvements in this respect, as reflected by our certification under the international environmental management standard ISO 14001. Care for the environment is part and parcel of our day-to-day activities.

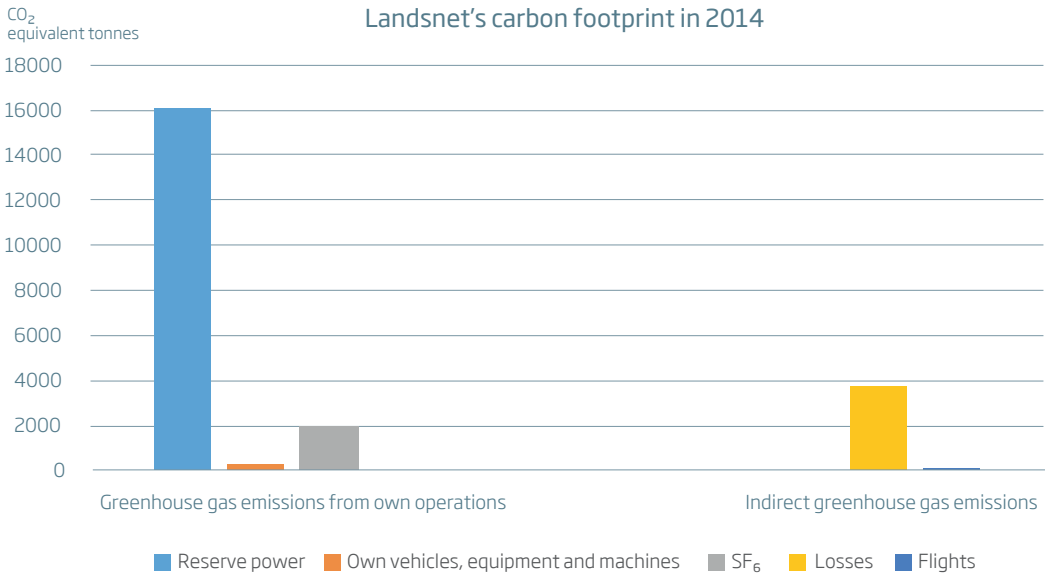
Environmental impact assessments and environmental audits

The environmental impact of our Grid Plan was assessed for the first time during the year in accordance with the Strategic Environmental Assessment Act. We also worked on the environmental impact assessment (EIA) of two new infrastructure projects, and sent a number of enquiries to government bodies about the requirement to carry out EIA.

As a statutory consultation body, Landsnet takes an active part in municipal planning. This aims to ensure that account is taken of the rights of way of transmission infrastructure and planned works on the grid.

Infrastructure projects have a range of environmental impacts, such as due to the manufacturing of system components, various soil disturbance, including line tracks, and the installation of underground cables and transmission towers. Other impact is more subjective, such as the visibility of structures, and therefore dependent on public consent. It should be noted that the visual impact of overhead lines is mostly reversible, and the simplest and most effective way of minimising their visibility is through line routeing.

Our tender documents for all Landsnet investment projects include stringent environmental requirements,



Direct and indirect greenhouse gas emissions from electricity transmission in 2014. The graph shows a breakdown of greenhouse gas emissions by different sources.

Activities	tonnes of CO_2 equivalents
Greenhouse gas emissions from own operations:	
Use of reserve power	16058
SF_6	1997
Own vehicles, equipment and machines:	
Petrol	36
Diesel	273
TOTAL:	**18364**
Indirect greenhouse gas emissions:	
Grid losses	3685
Domestic flights	50
TOTAL:	**3735**

Table 1. Greenhouse gas emissions from Landsnet's own operations:

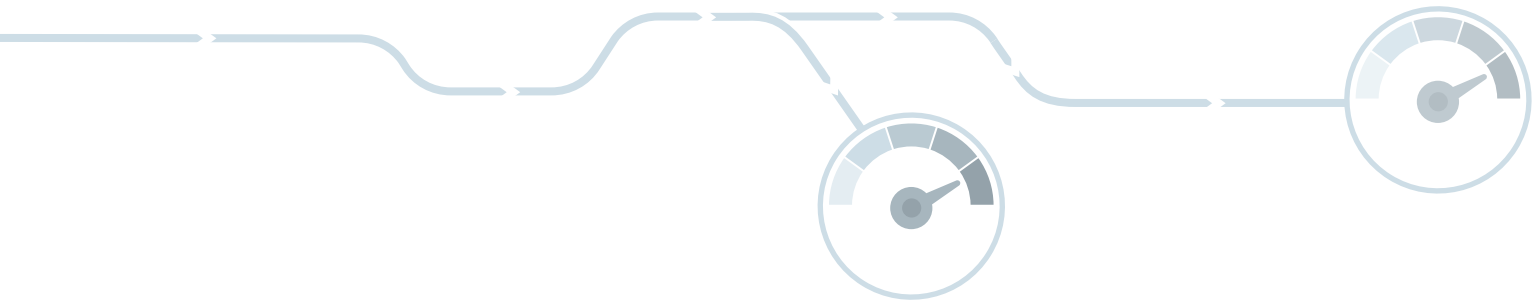
in which our project managers are well versed. During the works period, this and other aspects of the project are inspected, and upon completion of works our staff carry out an audit of the project's standard of finish from an environmental standpoint. Key stakeholders such as representatives of inspectorates, landowners and municipalities take part in this audit.

Environmental impact of day-to-day operations

Pollutant emissions from the grid's day-to-day operations are minor. They are mostly in the form of greenhouse gases. Only the most necessary chemicals are handled and stored in our substations. The chemicals in question are insulating media for electrical equipment and lead-acid batteries that ensure reserve power for substations. The insulating media are pure oil – which also cools the electrical equipment and is exempt from the labelling obligation under the Chemicals Act – and sulphur hexafluoride (SF_6), a very potent greenhouse gas.

Landsnet's carbon footprint and climate change

Our carbon footprint – direct greenhouse gas emissions excluding carbon sequestration through revegetation



– was 18,364 CO_2 equivalent tonnes in 2014. Our main challenges regarding greenhouse gas emissions concern the purchasing of reserve power and leakage of the insulating gas SF_6 from electrical equipment. These emissions account for more than 98% of our carbon footprint. Indirect greenhouse gas emissions are mostly due to power losses in the grid (Table 1).

Greenhouse gas emissions due to the purchasing of reserve power stem from the use of diesel-powered generators (backup generating stations) used in case of non-delivery of power owing to grid disturbances or maintenance. Improved security of supply is therefore the only way to cut the carbon footprint of reserve power. In recent years, we have made a major effort to minimise SF_6 emissions. A major milestone was passed with the construction of a new substation at Ísafjörður and the demolition of the old one, where we had been battling persistent gas leakage. This advantage of the demolition was partly offset by the discovery of a new leak in the Hrauneyjar substation, but nonetheless the leakage level was down to 0.34% of the total gas in the system in 2014, from 0.51% in 2013. This performance falls considerably short of the tightness requirements for new equipment (0.5%), so we will continue efforts to minimise all leakage of gas-filled electrical equipment through monitoring, maintenance and sound practices.

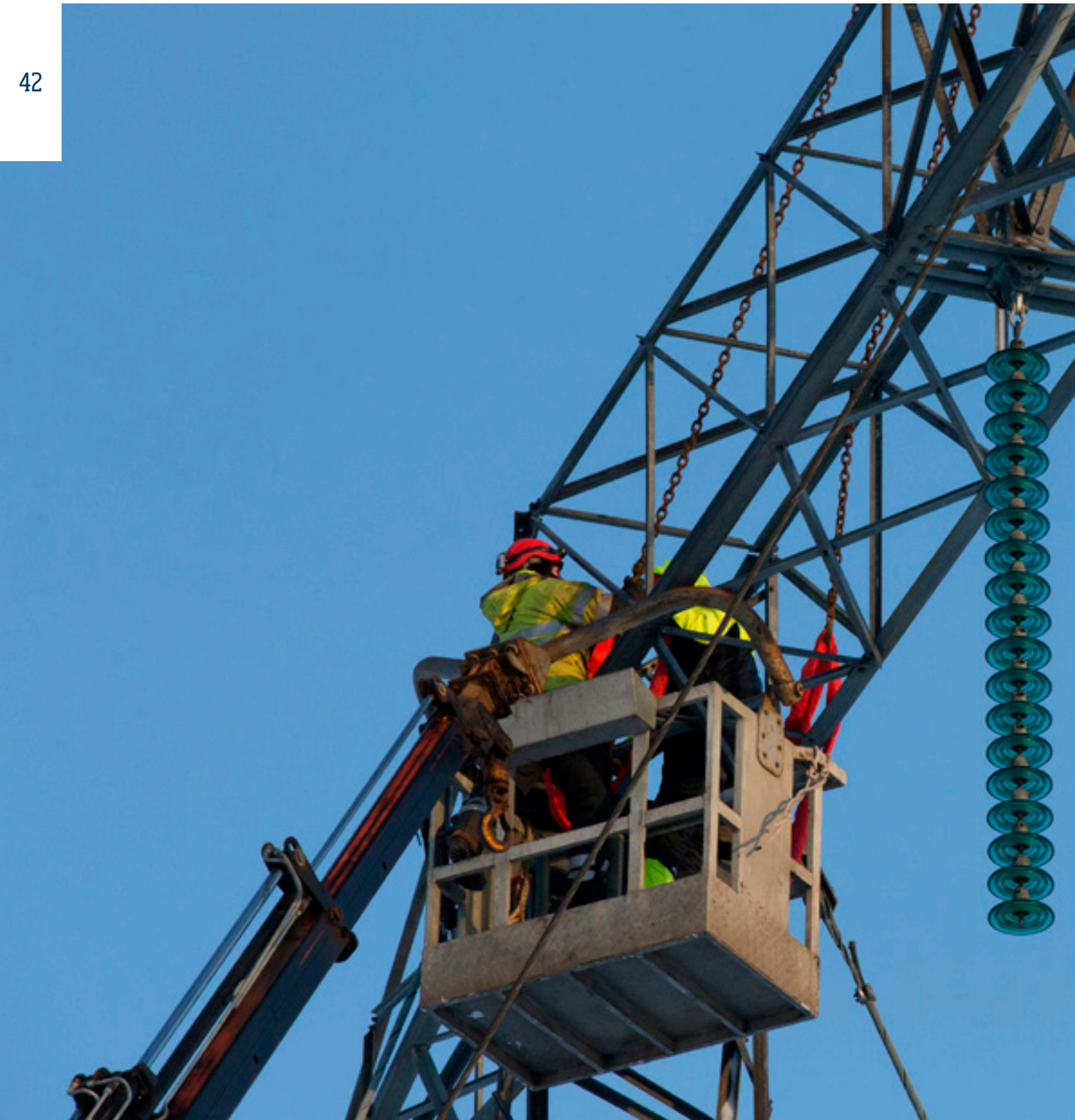
Our carbon footprint from power losses is due to the generation needed to make up energy lost in the grid. By far the largest driver of these losses is the increased role of geothermal power plants, which have a larger carbon footprint than hydroelectric ones. Cutting these losses to any significant degree is technically challenging under the current conditions because a large part of the grid is so heavily loaded. By raising the voltage of the system, however, the same amount of energy could be transmitted at a lower current, which would reduce losses because a lower current produces less wasted energy. To cut the carbon footprint of power losses, we would therefore need to rebuild the Inter-Regional Transmission Network and raise the voltage level.

Our emission calculations are based on empirical 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 megawatt hours 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 included in estimates of greenhouse gas emissions. International flights and the carbon footprint of grid infrastructure materials (e.g. steel, aluminium and concrete) are not included.

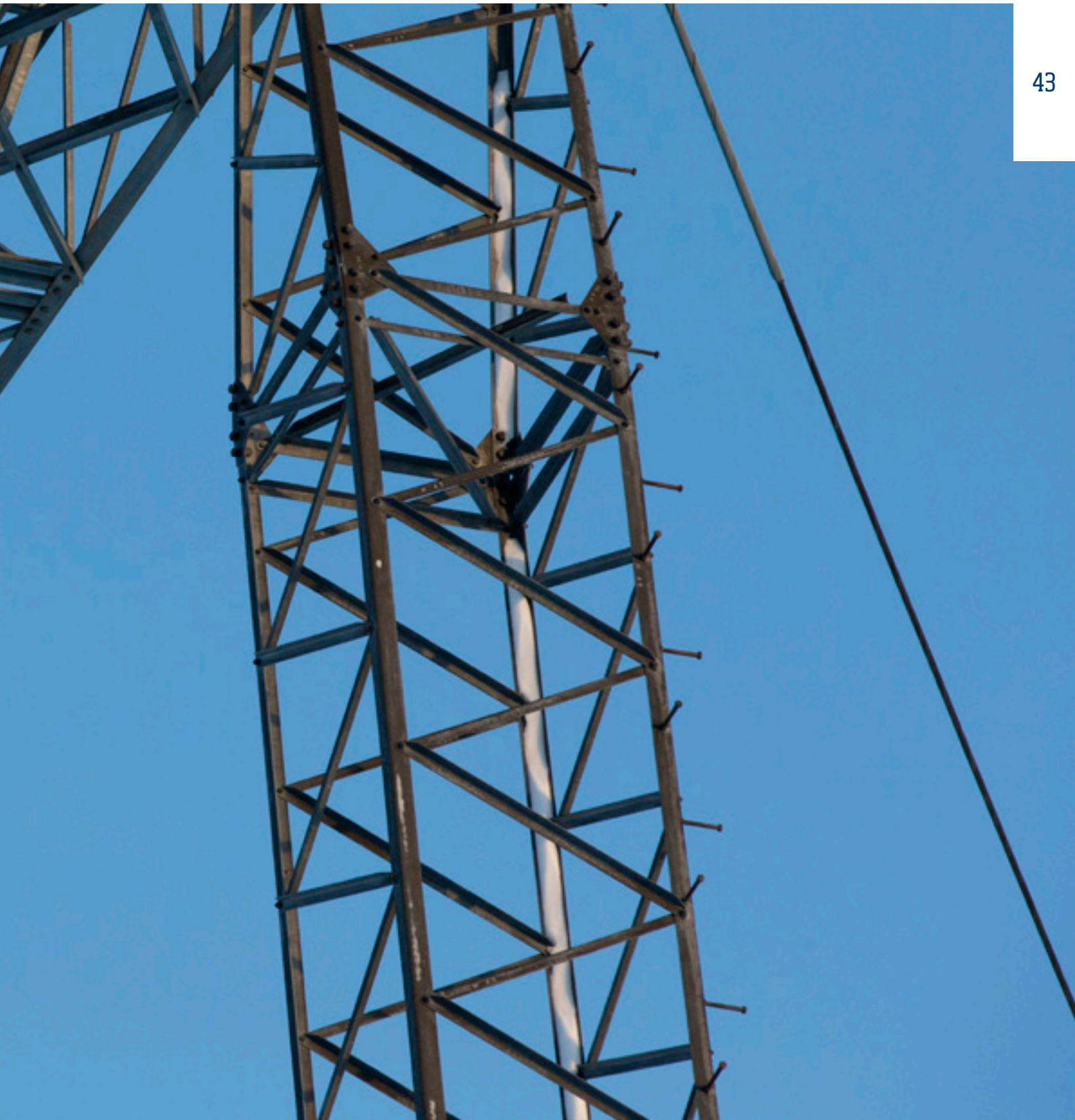
Favourable weather for soil conservation

Our co-operation with the Soil Conservation Service of Iceland on the revegetation of eroded land south of the Langjökull glacier and in the valley Víðidalur á Fjöllum continued as normal in the summer of 2014. We worked on the soil conservation of almost 160 hectares of land by distributing fertiliser and seeds. The weather was favourable for revegetation, warm and rainy.

Putting safety and security first



Landsnet has always put safety and security first. This includes personal safety and the grid's operational security, both of which are integral to our culture.



One accident is one too many. This philosophy is reflected in our zero-injury 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 had one lost-time injury[1] in 2014. Things turned out better than first thought and the event is considered a minor one.

Drop in injuries year-on-year

Despite the aforementioned injury, our Lost Time Injury Frequency Rate (LTIFR), was 0.68 at year-end 2014 based on 200,000 hours worked, compared with 2.07 in the previous year. This improvement was due to fewer accidents, an increase in the total number of hours worked at Landsnet and a targeted security training policy.

Our staff deserve praise for this performance, which far exceeds that of other companies with a similar operating environment. However, we must do better still to achieve a zero-injury workplace. 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 positive as more and better information will facilitate injury prevention.

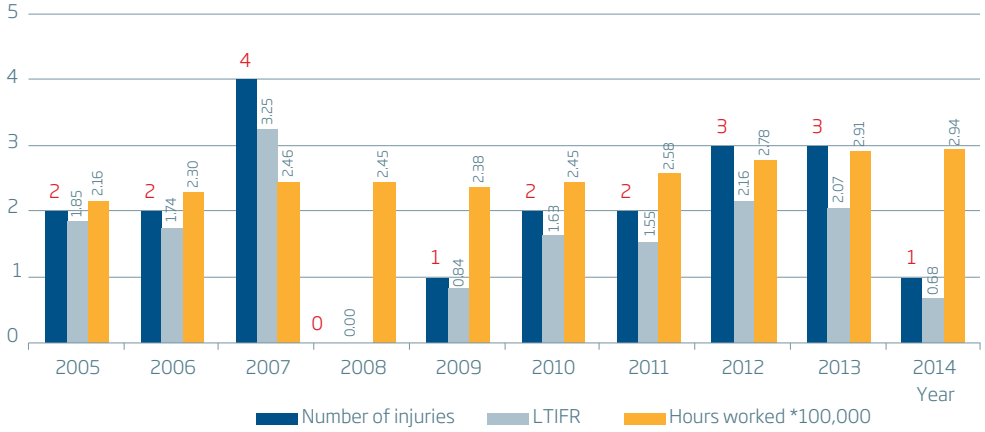
Safety manuals and standards

A cornerstone of our safety management is the Landsnet Safety Manual, which is under continual development. Other companies have shown an interest in using the manual's contents as a model for their own safety manuals, to which we have reacted positively as co-ordinated procedures are beneficial to all parties.

At the beginning of 2014, we issued the instructional manual *That's the Way We Do It* on safety procedures and arrangements at Landsnet premises. This publication provides certain criteria, including for the design of new structures and the co-ordination of safety practices, and has already proved very useful.

Over a year has now passed since we adopted the OHSAS 18001 safety standard. Its use has already

Landsnet's lost-time injury frequency rate per 200,000 hours worked



1) Accidents that lead to absence from work for more than one day from the day of the accident.

given good results by clearly sharpening our staff's safety awareness and delivering an improved safety performance. We have also had a positive experience with the certified electrical safety management system RÖSK, which we have been using for some time.

Landsnet Emergency Management

The Landsnet Emergency Management (LEM) team keeps a close watch over risks and hazards that may affect our activities, with numerous issues taken up for resolution, possible emergency scenarios discussed and solutions sought. LEM's activities were routine in the first half of 2014, but the second half of the year was very busy because of the geologic activity in the northern part of the Vatnajökull ice cap, the concern being that this could pose a serious risk to the grid. The preventive work we undertook provided, in effect, a big emergency management exercise, which was challenging for all management and other staff. However, it provided few surprises as our LEM team had simulated nearly the same scenario ten months earlier in an exercise in dealing with threats posed by geologic activity in Vatnajökull.

Increased participation in the Emergency Partnership

The Electricity System's Emergency Partnership (ESEP) is a co-operation forum for Landsnet, generators, distributors, power-intensive consumers and public bodies to deal with emergencies affecting power generation, transmission or distribution in Iceland. Its purpose is to provide assistance and co-ordinate action during emergencies. Participation in ESEP has been growing every year. Three ESEP meetings were held in 2014, with numerous experts giving presentations on the electricity system and its operation. One of the meetings was held at the request of the Ministry of Industries and Innovation to review the Vatnajökull situation and the preparedness of the ESEP partners.

NordBER

NordBER is the contingency planning and crisis management forum for Nordic TSO's and energy authorities. The participating countries share knowledge, provide cross-border assistance and hold joint emergency exercises. NordBER's activities are growing at a rapid rate. The Icelandic participants are Landsnet and the National Energy Authority. The activities are largely centred on three annual consultation meetings and special working groups that discuss specific issues. This co-operation has quite a long history, starting 18 years ago when the national energy authorities of four Nordic countries began co-operating on the operational security of electricity systems. A few years later, the Nordic Electricity Preparedness Forum was established. In 2006, these two forums merged under the NordBER banner.

Targeted HR development

We have devoted a concerted effort to developing our HR management and building a strong team of dedicated professionals that can take on future challenges. Importance is placed on training and knowledge, restructuring HR processes and providing more targeted and better information for management staff.

Our people are well-educated experts 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.

Our employees numbered 120 at year-end 2014, of which 80% were men and 20% women. Men comprised 67% of senior management and women 33%. We recruited nine new employees during the year. Increased staff turnover may be expected in the coming years due to age-related retirement.

Important to maintain expertise

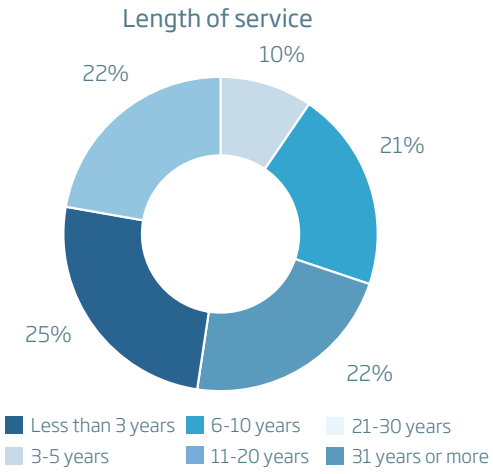
Around one in five of our staff is 60 or older, and in some of our departments a large proportion of the staff has entered the second half of their careers. Although we have stepped up recruitment of younger employees, training up highly specialised professionals takes time.

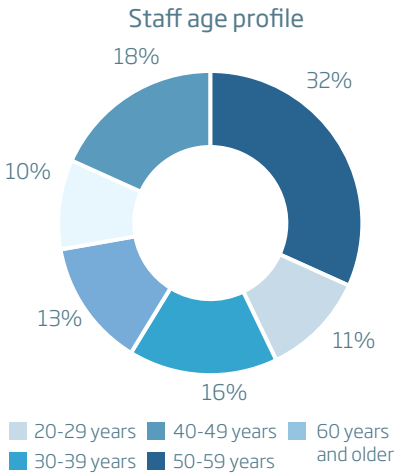
For grid maintenance and repairs, we continue to use the services of other energy companies and contractors. However, as their knowledge of the transmission system and related specialised tasks is on the decrease, Landsnet must increasingly maintain and build internal know-how to be able to perform these tasks without outside assistance.

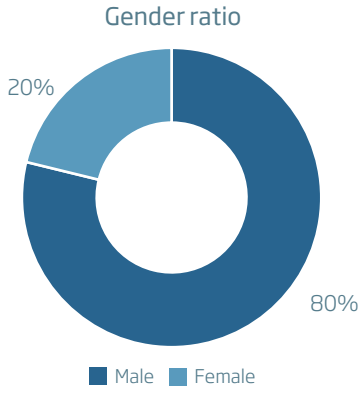
Active training and education

We place much emphasis on training and education for our staff, as reflected in our being one of eight nominees for the 2014 Excellence in Business Training Award.

We aim to foster continual improvement by ensuring in the best way possible that our employees have the capabilities and knowledge to tackle the tasks of the day and the company's future challenges. To this end,







It was a challenging and busy year for our staff, including this stalwart team manning our operations centre at Egilsstaðir, East Iceland.

we rely on needs analysis to prepare training programmes for individuals, groups and departments before issuing a Landsnet Academy Training Programme reflecting our specialised activities. Our employees have been generally satisfied with the diverse training opportunities afforded to them to enhance their professional and personal skills.

Summer jobs

We employed 43 upper secondary school students and 22 university students in summer jobs in 2014. Importance is attached to affording university students with opportunities to perform real-world tasks in their respective fields of study. We thereby aim to contribute more to society.

A spike in the sickness absence rate

Our people were in poorer health in 2014 than in previous years, as the sickness absence rate was up from 1.73% in 2013 to 2.49% in 2014. This fell short of our aim to be below 2%, despite the provision of preventive programmes including medical services for our staff.

The electricity system is Iceland's lifeline

Without electricity, our society would come to a standstill as so much is dependent on electrical power in one way or other. A strong grid is essential to ensuring power supply to all Icelanders and meeting security of supply requirements throughout the country. Industrial development in Iceland's south-west corner in the 1960s set in motion systematic grid development. Prior to that, the country was divided into a number of isolated systems – or "islands" – with inadequate operational security and higher costs for the economy.

Building infrastructure

The construction of the Regional Ring Network in 1972 to 1984 made a decisive difference for communities and economic development around Iceland. It also marked a huge step forward for the environment. Greenhouse effects were dramatically reduced when cleaner, domestic energy generated by hydropower or geothermal facilities replaced generating stations powered by imported diesel oil. Currently, however, the network's operation is affected by transmission constraints and instability that impede development around the country.

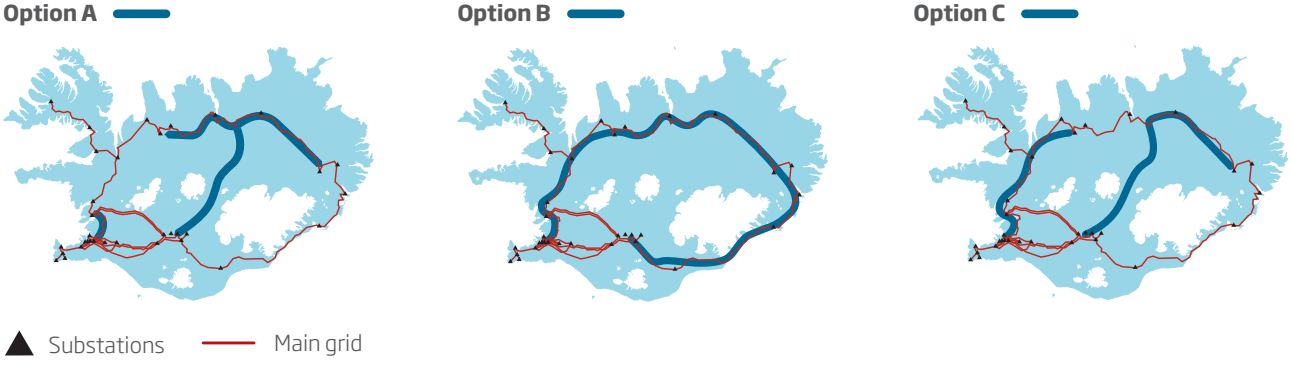
Unacceptable situation

Our dealing with this situation through high-tech solutions is yielding ever diminishing returns, making it very challenging to deal with large shocks. The grid is more and more frequently being divided into islands to protect it against shocks and minimise risk. The number of incidents causing damage to assets such as electrical equipment has risen markedly, co-ordinated operation of water reservoirs is problematic and business operations must often resort to being powered by oil, leading to increased pollution and costs. If nothing is done, the macroeconomic costs of grid bottlenecks will run in the billions of ISK every year.

A connection for the future

To strengthen the main grid – this lifeline for Iceland – and improve security of supply, we must look at the long-term overall picture. Our 2014-2023 Grid Plan sets out three possible ways of improving the connection of the power system's core, in the south, to the north of Iceland.

- Option A is a "T-solution" with a connection across the Sprengisandur highland plateau and grid strengthening to the east and west.
- Option B is the construction of a new Regional Ring Network around the country.
- Option C is a connection over the interior highlands and strengthening to the east and in the west of the country.



The transmission system in the south-west of Iceland is in robust shape, but improvements are needed elsewhere in the country. For large and small communities around Iceland to prosper, the grid must be able to transmit more energy, but so far the development of that capacity has failed to gain enough traction.

The grid

Iceland has only a single defined grid but a number of regional distribution networks. Landsnet owns and operates all bulk transmission lines in the country. Our 3,200km line network includes lines with voltages of 66 kV and higher and a number of 33 kV lines. The grid also includes all major substations in the country. The highest operating voltage in Iceland is 220 kV. A large part of the grid operates at 132 kV and some parts at 66 kV and 33 kV. Transmission lines in the south-west and east of Iceland were built as 420 kV lines but operate at 220 kV.

The grid receives electricity directly from power stations and transmits it to distributors and power-intensive users. All power stations with a capacity of 10 MW and higher must be connected to the grid, into which power is fed at 20 locations. The grid delivers the electricity to distributors at 59 locations around Iceland and to power-intensive users at six locations. Distributors then supply the power onwards to the consumer via their own distribution networks.

High-voltage undergrounding

We undertook an extensive research project in 2014 on the installation of 132 kV and 220 kV underground cables in Iceland. The aim was to identify the most cost-effective options for underground cable selection, installation and site restoration, with due account of transmission capacity, system conditions, reliability, the environment and costs. The results were presented in a full report in English and a short version in Icelandic. The key findings were:

- The maximum length of an underground cable across the Sprengisandur plateau is 50km because of the technical limits of the current electricity system.
- The price of high-voltage underground cables has come down considerably, by almost half for 220 kV cables whereas lower-voltage cables have decreased far less in price. The drop in prices is mainly driven by technological developments in manufacturing and greatly increased supply.
- The purchase price of an underground cable is 30-50% of the total capital cost of a 220 kV underground cable installation, but providing a general reference price is difficult. Each case needs to be examined on the basis of systemic circumstances, geological and geographical factors, access to the line route and other considerations.

The factors affecting the possible length of underground cables in the Icelandic electricity system include a low short-circuit power, or the strength of the system. The regional variability of the system's strength limits the possible inter-regional cable connections. For example, the electricity system in the north and east of Iceland is far weaker than in the south and south-west. This puts a limit on the possible length of the underground cable across the Sprengisandur plateau.

The thermal conductivity of soil in Iceland is generally lower than in neighbouring countries. The properties of the soil that surrounds underground cables in trenches and conducts heat from the cable have a significant effect on transmission capacity. The thermal conductivity of filler materials in Iceland is generally deemed to be half of that of Danish soil. As a result, the transmission capacity of a comparable underground cable is approximately 30% higher in Denmark than in Iceland, other things being equal.

Techniques and routeing

We studied the methods used in neighbouring countries at the forefront of cable installation and assessed whether techniques used in Iceland could be improved. In the vast majority of cases, however, conventional cable laying in an open trench was found to be the least costly option. Minimising environmental impact through effective routeing is important. On average, the width of the disturbance corridor is 8-14 metres for the installation of one 220 kV cable set. Restoring the ground surface is easy in sandy terrain, well vegetated heathland or cultivated land, whereas in forests and scrubland a treeless corridor must be left over the cable. In lava fields or where there is rock near the surface, the ground surface cannot be restored to its original condition. Holocene lava fields are protected under the Nature Conservation Act and lava fields are ill-suited to undergrounding, so there are good reasons to avoid undergrounding in lava fields as far as possible.

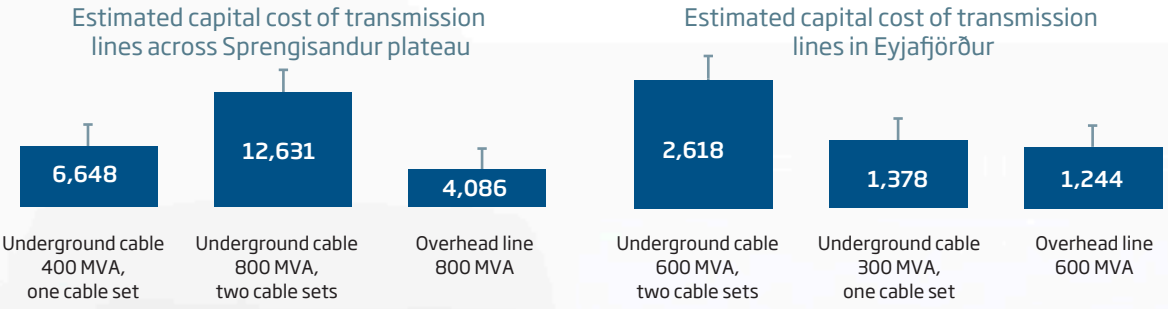
Analysis of undergrounding options

We specifically examined two undergrounding options across the Sprengisandur plateau and in the Eyjafjörður area, including cost estimates and a comparative estimate of the capital cost of an overhead line.

The total length of a line across the Sprengisandur would be 200km and the capital cost of a 50km underground cable with 400 megavolt-ampere (MVA) transmission capacity is estimated at over ISK 6.6

An undergrounding research project was undertaken in collaboration with experts from the Danish TSO, Energinet.dk (a global leader in undergrounding), StellaCable (a privately run consultancy firm specialising in high-voltage underground cables in Denmark), Reykjavik University and three of Iceland's largest engineering firms, Mannvit, Verkís and EFLA.

Experts from Energinet.dk, StellaCable, Reykjavik University, Mannvit, Verkís and EFLA in a work meeting with Landsnet staff.



Amounts in ISK million

billion. This cost is doubled when there are two cables with a combined capacity of 800 MVA. In comparison, the estimated capital cost of a 50km long, 800 MVA overhead line is ISK 4.1 billion.

The capital cost of two underground cables with a combined capacity of 600 MVA for the first 12km of the route between Akureyri and Krafla is about ISK 2.6 billion. The estimated capital cost of an overhead line with a capacity of 600 MVA, in comparison, is just over ISK 1.2 billion, although it would be about 40% longer than the underground route. The capital cost of one 300 MVA underground cable is comparable to that of installing an overhead line. Therefore, it could be advantageous to divide the undergrounding into steps by first laying one cable and then waiting with the other one for as long as this meets the transmission needs.

Number of undergrounding projects to rise

The number of undergrounding projects is expected to grow in the coming years. The experience from the above and other forthcoming projects will then come in useful. We will also continue our research in this field. We have already begun soil humidity measurements at selected sites where undergrounding is likely in the future.

A leader in smart grid solutions

Landsnet is among the world-leading TSOs in this field and has in co-operation with Icelandic and overseas partners been developing smart grid solutions to track the grid's condition in real time and react immediately to disturbances.

Smart grid deployment in the West Fjords

The addition of new substations at Ísafjörður and Bolungarvík coupled with vastly improved tele-communications enabled the deployment of a smart grid system in the northern West Fjords. We devoted much work to the design and testing of the built-in

Greatly increased operational security

Our latest smart grid milestone was the installation of a smart system in the northern West Fjords. It has dramatically increased security of supply in the region, proving its worth immediately when the first disturbance after the system's installation occurred in early December 2014.

"Smart grid" is an umbrella term for high-tech innovations in the generation, transmission and distribution of electricity. Smart grid solutions use communications, control and information technology to optimise security of supply and cost-efficiency.

smart grid capabilities of these new substations' protection equipment in the year, in addition to more routine testing when the substations were brought into service.

In the event of non-supply in the West Fjords due to faults or outages, the smart grid immediately starts up the new reserve power station at Bolungarvík and restores power shortly afterwards for general consumers at Ísafjörður, Bolungarvík and environs. It has cut outage times to just over a minute and a half from a previous reaction time of almost half an hour.

We are preparing further smart grid deployment in the West Fjords to continue to improve security of supply, since the region still lags the rest of the country considerably on this count.

Improved disturbance management

We are also working to deploy smart grid capabilities elsewhere around the country. These are mainly aimed to tackle transmission constraints and prevent extensive outages or systemic collapse over large geographical areas.

In recent years, we have been building a network of real-time, high-speed monitors called Phasor Measurement Units (PMUs) at key grid locations to detect events in the system before they cause tripping and to enable the mitigation of their impacts.

Testing of the use of these data in grid management has begun, the results of which are promising as we have managed to tighten our grip on disturbances and prevent extensive outages. Equipment has been installed in many system locations to shed curtailable consumer load (interruptible service) if such a signal is received from the PMU system when the system is split up because of lines tripping or when inter-regional power transmission changes significantly as load is shed or generating units trip.

When the equipment is activated, consumers connected to it are disconnected from the system to reduce load and then reconnected as stability is attained. This enables the prevention of a systemic collapse over large geographical areas. In turn, interconnection or system restoration takes a much shorter time and general consumers will not be aware of it.

The first step in building the PMU network was to install remote load shedding equipment at the premises of consumers with interruptible load in the north and east of Iceland. When tripping occurs in the Inter-Regional Transmission Network, or generation drops in the area, the equipment disconnects consumers from the grid. This reduces inter-regional transmission and the likelihood of a total division of the system. It also reduces the probability of under-frequency in the island remaining in operation. The equipment has time and again proved its worth by preventing systemic collapse in the north and east of Iceland.

More projects in the pipeline

Many other smart grid projects are in the experimental stages at Landsnet. In recent years, we have been forging closer co-operation with electricity generators and consumers on the grid's operation. This includes efforts to ensure a fast response to grid-related events and incidents, such as through the deployment of smart solutions. This co-operation has exceeded our expectations and is characterised by a general understanding of the issues.

In response mode for an eruption at Mt Bárðarbunga

Because of the seismic and volcanic activity at Mt Bárðarbunga, we reviewed all our contingency plans and communications and other equipment. Repair and spare stocks were replenished. As well as working closely with the Icelandic Civil Protection, the Icelandic Road and Coastal Administration and energy companies, we contacted contractors and other businesses that could provide assistance if additional personnel and equipment are needed.

The Nordic TSOs were immediately willing to provide any assistance required, such as repair materials, spare parts and personnel.

Five scenarios

Immediately after the Holuhraun eruption began, the main concern was that the electricity system would be damaged by catastrophic flooding in the north-east of the country. We therefore transported repair materials and reserve power stations to that region. The focus soon turned to other possible scenarios if an eruption were to occur at Mt Bárðarbunga, so our contingency plans now comprise five scenarios:

- A flood in the glacial river Jökulsá á Fjöllum
- A flood in the glacial river Skjálfandafljót
- A flood from under the Vatnajökull ice cap to the south onto the Skeiðarársandur outwash plain
- Flooding in the rivers Sveðja, Kaldakvísl, Tungnaá and Þjórsá
- Volcanic ash eruption

Ever since the announcement in late summer 2014 that volcanic activity was expected in the northern part of the Vatnajökull ice cap, our staff have been in response mode for possible damage to the electricity system due to flooding or ashfall.

The contingency plans for catastrophic flooding in the north and south of the country (scenarios 1-3) are designed to reconnect the Inter-Regional Transmission Network and other line infrastructure as soon as possible, as was done in reaction to the River Skeiðará glacial outburst flood in 1996. The same applies in the south-west (scenario 4) where flooding – at the heart of the power system – could be much more costly for Iceland's economy given all the generation and electricity infrastructure located there.

Preventive measures in the south-west

The main focus of the contingency work was soon directed at better analysing the possible consequences of catastrophic flooding in the Þjórsá and Tungnaá area and how best to ensure transmission from that area's power stations. The first flooding forecasts indicated a rather high level of vulnerability for transmission infrastructure, but later in-depth risk analysis based on 6,000 m^3/sec. showed that only one transmission tower in the area upriver from the Búrfell Power Station was at any serious risk from catastrophic flooding of that magnitude. This was a tower on the Sigalda Line 3 just east of the River Þjórsá riverbed at the Sultartangi Power Station. We proceeded to relocate this tower. In consultation with the Icelandic Civil Protection, we have taken various other preventive measures to shorten reaction times in case of catastrophic flooding in the area.

Clear rules necessary

The emergency exercise held by Landsnet and the Electricity System's Emergency Partnership (ESEP) in the autumn of 2013 revealed that catastrophic flooding in the south-west of the country following an eruption in the Vatnajökull ice cap could create conditions requiring measures to minimise potential macroeconomic losses due to long-term power rationing.

Landsnet therefore emphasises that contingency planning must provide a clear definition of the respective roles of electricity market participants in the event of an eruption at Mt Bárðarbunga or an equivalent natural catastrophic event – there must be no doubt about prioritisation in case extensive power curtailment or rationing is necessary.

Preparedness against a volcanic ash eruption

Our preparedness also covers a possible volcanic ash eruption at Mt Bárðarbunga (scenario 5). In this respect, we can build on the experience from the 2010 Eyjafjallajökull eruption and the 2011 Grímsvötn eruption. In such circumstances, it is important to remove ash off electrical and insulation equipment. We are looking to use powerful water or air pumps and are considering options to buy such equipment.

Transmission line network in 2014

Voltage [kV]	Line	KKS code	First year in service	Connected substations	Length [km]	Of which undergr. [km]
220	**Brennimelur Line 1**	BR1	1977	Geithals - Brennimelur	59	
	Búðarháls Line 1	BH1	2014	Búðarháls - HR1 (Langalda)	6	
	Búrfell Line 1	BU1	1969	Búrfell - Írafoss	61	
	Búrfell Line 2	BU2	1973	Búrfell - Kolviðarhóll	86	
	Búrfell Line 3 (partly built for 400 kV)	BU3	1992/1998	Búrfell - Hamranes	119	
	Fljótsdalur Line 3 (built for 400 kV)	FL3	2007	Fljótsdalur - Reyðarfjörður	49	
	Fljótsdalur Line 4 (built for 400 kV)	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 - Járnblendiv.	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 (built for 400 kV)	SU3	2006	Sultartangi - Brennimelur	119	
	Vatnsfell Line 1	VF1	2001	Vatnsfell - Sigalda	6	
				Total 220 kV	**859**	**0**
132	**Blanda Line 1**	BL1	1977/1991	Blanda - Laxárvatn	33	
	Blanda Line 2	BL2	1977/1991	Blanda - Varmahlíð	32	
	Eyvindará Line 1	EY1	1977	Hryggstekkur - Eyvindará	28	
	Fitjar Line 1	MF1	1991	Rauðimelur - Fitjar	7	
	Fljótsdalur Line 2 (line/underground cable)	FL2	1978	Fljótsdalur - Hryggstekkur	25	7
	Geiradalur Line 1	GE1	1980	Glerárskógar - Geiradalur	47	
	Glerárskógur Line 1	GL1	1983	Hrútatunga - Glerárskógar	34	
	Hafnarfjörður Line 1 (underground cable)	HF1	1989	Hamranes - Öldugata	4	4
	Höfn Line 1 (line/underground cable)	HA1	1987/2014	Hólar - Höfn	5	1.5
	Hnoðraholt Line 1 (line/underground cable)	AD7	1990	Hamranes - Hnoðraholt	7.5	2.2
	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	16
	Nesjavellir Line 2 (underground cable)	NE2	2010	Nesjavellir - Geithals	25	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	5
	Rauðimelur Line 1	RM1	2006	Reykjanes - Rauðimelur	15	
	Rauðavatn Line 1 (line/underground cable)	RV1	1953	Geithals - A12	3	1
	Sigalda Line 4	SI4	1984	Sigalda - Prestbakki	78	

Voltage [kV]	Line	KKS code	First year in service	Connected substations	Length [km]	Of which undergr. [km]
	Sog Line 2	SO2	1953	Írafoss - Geithals	44	
	Stuðlar Line 1 (underground cable)	SR1	2005	Hryggstekkur - Stuðlar	16	16
	Suðurnes Line 1	SN1	1991	Hamranes - Fitjar	31	
	Svartsengi Line 1	SM1	1991	Svartsengi - Rauðimelur	5	
	Teigarhorn Line 1	TE1	1981	Hryggstekkur - Teigarhorn	50	
	Vatnshamrar Line 1	VA1	1977	Vatnshamrar - Brennimelur	20	
				Total 132 kV	**1322.5**	**77.7**
66	**Akranes Line 1 (underground cable)**	AK1	1996	Brennimelur - Akranes	17	17
	Andakíll Line 1	AN1	1966	Andakílsvirkjun - Akranes	35	
	Bolungarvík Line 1 (line/underground cable)	BV1	1979/2014	Breiðidalur - Bolungarvík	17	0.7
	Bolungarvík Line 2 (underground cable)	BV2	2010/2014	Ísafjörður - Bolungarvík	15	15
	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 (line/underground cable)	HE1	1995	Flúðir - Hella	34	1
	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	1959/2014	Breiðidalur - Ísafjörður	13	1.1
	Kópasker Line 1	KS1	1983	Laxá - Kópasker	83	
	Lagarfoss Line 1 (line/underground cable)	LF1	1971	Lagarfoss - Eyvindará	23	6
	Laxá Line 1	LA1	1953	Laxá - Rangárvellir	58	
	Ljósafoss Line 1 (underground cable)	LJ1	2002	Ljósifoss - Írafoss	1	1
	Neskaupstaður Line 1 (line/underground cable)	NK1	1985	Eskifjörður - Neskaupstaður	18	1
	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 (line/underground cable)	SE1	1981	Ljósifoss - Selfoss	20	2
	Selfoss Line 2	SE2	1947	Selfoss - Hella	32	
	Seyðisfjörður Line 1	SF1	1996	Eyvindará - Seyðisfjörður	20	
	Steingrímsstöð Line 1 (line/undergr. cable)	ST1	2003	Steingrímsstöð - Ljósafoss	3	1
	Stuðlar Line 2 (line/underground cable)	SR2	1983	Stuðlar - Eskifjörður	18	1
	Tálknafjörður Line 1	TA1	1985	Mjólká - Keldeyri	45	
	Vatnshamrar Line 2	VA2	1974	Andakílsvirkjun - 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 (underground cable)	TR2	2013	Þeistareykir - KS1 (Höfuðreiðarmúli)	11	11
	Þorlákshöfn Line 1	TO1	1991	Hveragerði - Þorlákshöfn	19	
				Total 66 kV	**980**	**57.8**
33	**Húsavík Line 1**	HU1	1964	Laxá - Húsavík	26	
	Westman Islands Line 1 (sub-sea cable)	VM1	1962	Vestmannaeyjar - Rimakot	16	16
	Westman Islands Line 2 (sub-sea cable)	VM2	1978	Vestmannaeyjar - Rimakot	15	15
	Westman Islands Line 3 (sub-sea cable)	VM3	2013	Vestmannaeyjar - Rimakot	16	16
				Total 33 kV	**73**	**47**
				Total	**3234.5**	**182.5**

Substations in 2014

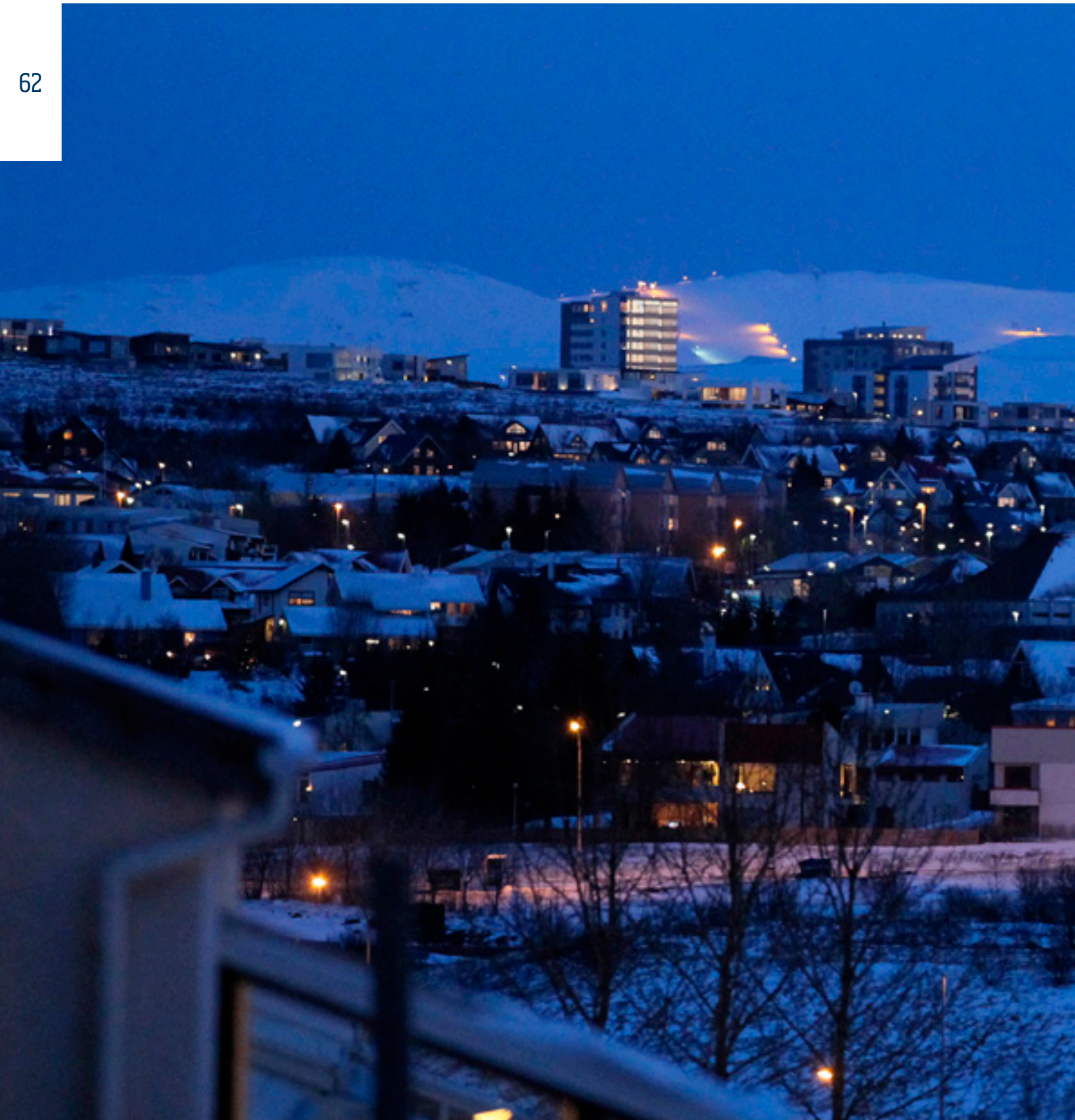
Substations	KKS code	Co-owner	Voltage [kV]	First year in service	No. of switchyard bays	Number of transformers
Substation 12	A12	OR	132	2006	1	1
Akranes	AKR	OR	66	1987	4	2
Andakíll	AND	OR	66	1974	3	1
Ásbrú	ASB		33	2011	6	2
Blanda	BLA	LV	132	1991	6	3
Bolungarvík	BOL	OV	66/11	2014	3/13	1
Breiðidalur	BRD	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	1981	3/7	1
Geiradalur	GED	OV	132/33/19	1983	3/1/4	1
Geithals	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	1982	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	1980	3/6	1
Hvolsvöllur	HVO	RA	66/11	1957	5/7	1
Höfn	HOF	RA	132/11	2014	-/9	1
Írafoss	IRA	LV	220/132/66/11	1953	2/7/-/7	5
Ísafjörður	ISA	OV	66/11	2014	4/-	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

Substations	KKS code	Co-owner	Voltage [kV]	First year in service	No. of switchyard bays	Number of transformers
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
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	1980	1/5/2	2
Sauðárkrókur	SAU	RA	66/33/11	1977	3/1/8	2
Selfoss	SEL	RA	66/11	2005	5/15	3
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	1989	1/6	1
Öldugata, Hafnarfjörður	OLD		132	1989	5	2

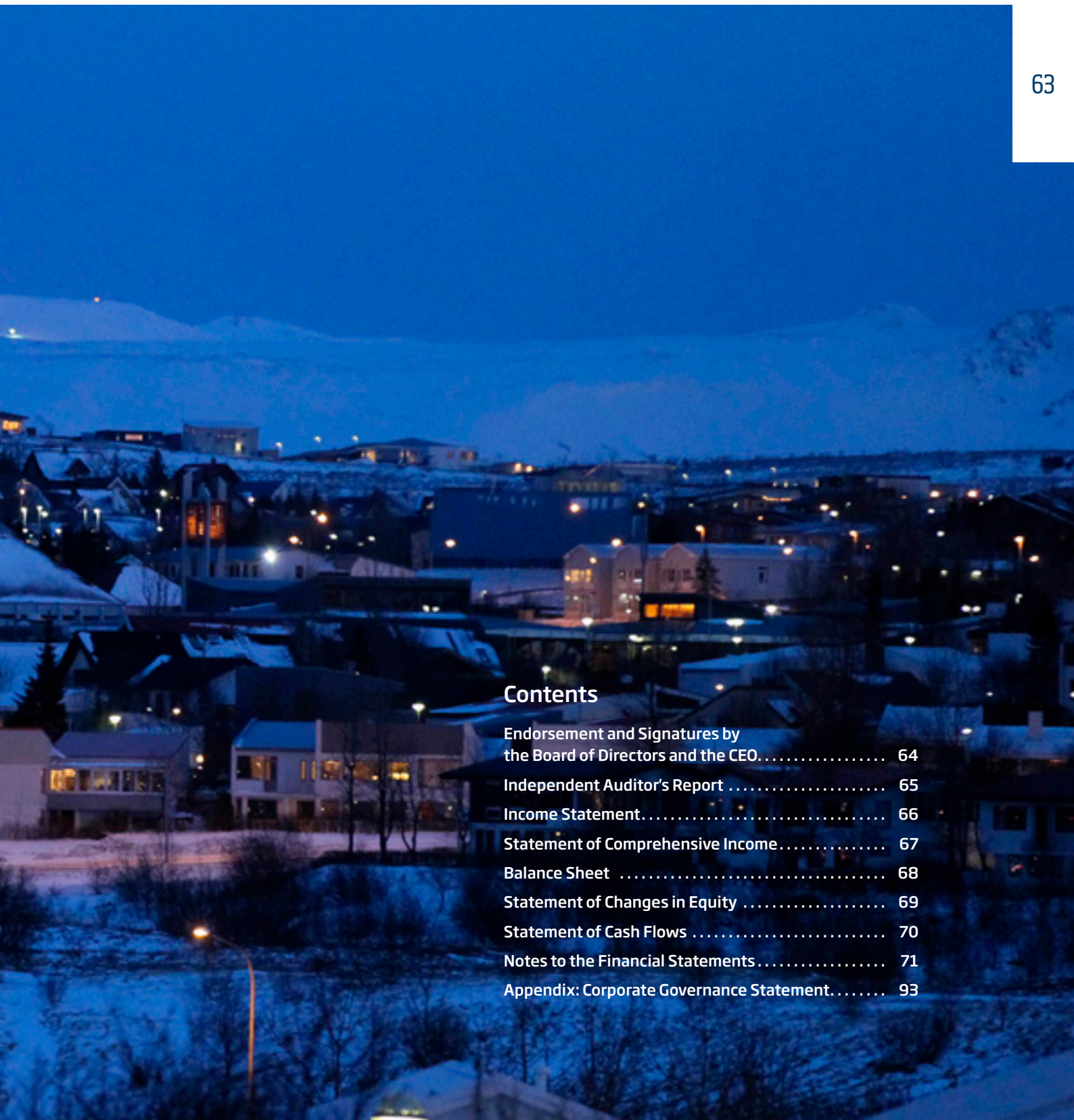
* RA=RARIK (Iceland State Electricity)
OV=Westfjord Power Company
HS=Sudurnes Regional Heating
LV=Landsvirkjun
OR=Reykjavík Energy

Energy terms/abbreviations

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



Financial Statements 2014



Contents

Endorsement by the Board of Directors and the CEO

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

Results of the year 2014

According to the income statement, profit and total profit for the year amounted to ISK 3.8 billion. According to the balance sheet, the Company's equity at year end amounted to ISK 19.2 billion, including share capital in the amount of ISK 5.9 billion. Average number of employees was 125.

Share capital at year end 2014 is divided between four shareholders as at the beginning of the year:

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

The Board of Directors proposes that no dividends be paid to shareholders in 2015 for the operating year 2014, in which context the Board makes reference to the annual financial statements regarding changes in equity.

Although the 2011 Electricity Act clearly stipulates that the Company's rate of return and thereby its revenue cap must be decided five years in advance, a decision on the revenue cap for 2011-2015 remains unavailable in early 2015. The National Energy Authority's most recent decision on the Company's rate of return, from 2 October 2012, was annulled by a ruling of the Appeals Committee on Electricity on 2 December 2013. Landsnet's tariff and thereby its revenue are based on a tariff approved on the basis of the Authority's aforesaid decision on the rate of return. In the event that the Authority's decision on the rate of return, and thereby on the revenue cap, proves to be substantially divergent from its previous decision, this can clearly have a significant impact on the Company's financial performance and balance sheet in 2015, and even over a longer period. For further information, reference is made to Note 31.

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 2014, its assets, liabilities and financial position as at 31 December 2014 and its cash flows for the financial year 2014.
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 2014 and confirmed them by means of their signatures.

Reykjavik, 19 February 2015

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, 2014, 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

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

Auditor's responsibility

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

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

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

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Landsnet hf. as at December 31, 2014, 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, 19 February 2015.

KPMG ehf.

Income Statement for the year 2014

	Notes	2014	2013
Operating revenue			
Transmission	5,6	14,227,404	13,717,748
Other income	7	123,002	156,534
		14,350,406	13,874,282
Operating expenses			
Energy procurement costs	8	1,763,886	1,499,804
Transmission costs	9,10	4,235,226	3,793,580
System operation	9,10	1,111,813	1,087,733
Other operating expenses	9,10	1,065,329	925,417
		8,176,254	7,306,534
Operating profit		6,174,152	6,567,748
Financial income		1,125,451	141,041
Financial expenses		(2,644,510)	(4,010,935)
Net financial expenses	11	(1,519,059)	(3,869,894)
Share in net earnings of associated company	16	38,303	25,055
Profit before income tax		4,693,396	2,722,909
Income tax	12,24	(931,155)	(539,511)
Profit		3,762,241	2,183,398
Earnings per share:			
Basic and diluted earnings per each ISK 1 share	22	0.64	0.37

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

Statement of Comprehensive Income for the year 2014

	Notes	2014	2013
Profit		3,762,241	2,183,398
Total items under total profit recognised among equity		0	0
Total profit of the year		3,762,241	2,183,398

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

Balance Sheet as at 31 December 2014

	Notes	2014	2013
Assets			
Fixed assets in operation	13	63,771,382	63,197,621
Projects under construction	13	809,211	1,086,550
Intangible assets	14	1,479,695	1,392,994
Investment in subsidiary	15	500	500
Investment in associates	16	707,209	668,906
Long-term note		11,643	23,286
Fixed assets		66,779,640	66,369,857
Inventories	17	549,804	519,313
Receivable from parent company	32	702,735	0
Trade and other receivables	18	1,121,663	567,397
Marketable securities	19	470,971	234,344
Cash and cash equivalents	20	12,234,663	9,917,204
Current assets		15,079,836	11,238,258
Total assets		81,859,476	77,608,115
Equity			
Share capital		5,902,733	5,902,733
Statutory reserve		227,774	0
Revaluation account		10,460,730	11,027,997
Retained earnings (accumulated deficit)		2,617,237	(1,484,497)
Equity	21	19,208,474	15,446,233
Liabilities			
Long term liabilities from parent company	23	44,692,176	44,235,700
Other interest bearing long-term liabilities	23	9,955,162	10,852,410
Deferred income tax liability	24	2,674,787	2,331,443
Deferred income	25	354,109	369,222
Provision due to site restoration	26	819,766	775,163
Long-term liabilities and obligations		58,496,000	58,563,938
Loans from parent company	23	1,463,420	1,936,526
Current maturities	23	919,008	914,607
Income tax payable	24	587,811	0
Trade and other payables	28	1,184,763	746,811
Short-term liabilities		4,155,002	3,597,944
Total liabilities		62,651,002	62,161,882
Total equity and liabilities		81,859,476	77,608,115

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

Statement of Changes in Equity for the year 2014

	Share capital	Statutory reserve	Revaluation account	(Accumulated deficit)/retained earnings	Total
Year 2013:					
Equity at 1 January 2013	5,902,733	0	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	0	11,027,997	(1,484,497)	15,446,233
Year 2014:					
Equity at 1 January 2014	5,902,733	0	11,027,997	(1,484,497)	15,446,233
Total comprehensive income				3,762,241	3,762,241
Transfer to statutory reserve		227,774		(227,774)	0
Depreciation on revaluation recognised under accumulated deficit			(567,267)	567,267	0
Equity at 31 December 2014	5,902,733	227,774	10,460,730	2,617,237	19,208,474

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

Statement of Cash Flows for the year 2014

	Notes	2014	2013
Cash flow from operating activities			
Operating profit		6,174,152	6,567,748
Adjustments for:			
Profit from sales of fixed assets		0	(865)
Depreciation and amortisation	10	2,967,730	2,597,921
Working capital from operation before financial items		9,141,882	9,164,804
Operating assets, (increase) decrease		(1,269,593)	791,449
Operating liabilities, increase (decrease)		194,992	(459,392)
Net Cash from operating activities before financial items		8,067,281	9,496,861
Interest income received		143,891	141,041
Interest expenses paid and foreign exchange difference		(1,980,531)	(1,904,633)
Net cash from operating activities		6,230,641	7,733,269
Cash flow from investing activities			
Investment in transmission infrastructures	13	(2,672,056)	(5,949,468)
Other investments	13	(936,078)	(461,312)
Proceeds from sale of property, plant and equipment		0	2,697
Repayments of long-term note		11,643	0
Marketable securities, change		(254,526)	0
Net cash to investment activities		(3,851,017)	(6,408,083)
Cash flow from financing activities			
Payments of long-term liabilities		(907,061)	(913,374)
Change in deferred income		0	88,500
Net cash to financing activities		(907,061)	(824,874)
Net increase in cash and cash equivalents		1,472,563	500,312
Effect of exchange rate changes on cash and cash equivalents		844,896	(892,880)
Cash and cash equivalents at 1 January		9,917,204	10,309,772
Cash and cash equivalents at 31 December	20	12,234,663	9,917,204

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 19 February 2015.

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. Landsnet revaluates part of fixed assets to fair value, as stated in note 13, just as they do with marketable securities, as stated in note 19. Other assets and liabilities are not recognised at fair value.

Trade and other receivables

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

Non-derivative financial liabilities

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

See accounting policies in note 35k

Transmission revenue consist of:	2014	2013
Energy transmission	12,184,594	12,277,156
Transmission losses and ancillary services	1,906,911	1,320,226
Service income	41,777	30,950
Input fees	94,122	89,416
Transmission revenue total	14,227,404	13,717,748

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:

	2014	2013
Energy transmission to power-intensive consumers	8,459,538	8,785,696
Energy transmission to distribution system operators	3,725,056	3,491,460
Energy transmission total	12,184,594	12,277,156

7. Other income

Other income consist of:

Income from work sold	53,057	74,501
Rental income	26,385	8,828
Income from guarantees of origin and certification	38,961	70,823
Sales profit from fixed assets	0	865
Other income	4,599	1,517
Other income total	123,002	156,534

8. Energy procurement costs

Energy procurement costs consist of:

Electricity purchases due to transmission losses	1,091,576	854,946
Purchase of ancillary services	672,310	644,858
Energy procurement costs total	1,763,886	1,499,804

9. Personnel expenses

See accounting policies in note 35i

Salaries and other personnel expenses consist of:

Salaries	1,248,163	1,182,882
Defined contribution plan payments	159,491	143,152
Defined benefit plan payments	7,281	8,178
Other payroll expenses	126,856	126,828
Capitalised salaries	(185,366)	(210,047)
Personnell expenses total	1,356,425	1,250,993

Personnel expenses are specified as follows:

Transmission costs	457,159	415,458
System operation	509,957	480,889
Other operating expenses	389,309	354,646
	1,356,425	1,250,993

Average number of employees	125	122
Full-time equivalent units at year-end	113	114

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

Remuneration of the Board of Directors	6,611	6,486
Remuneration and benefits of the CEO	17,015	15,440
Remuneration of two Excecutive Directors	45,966	41,621

9. Personnel expenses, contd.:

Changes in senior management were made at year-end 2014, in respect of which remuneration settlements were recognised in 2014.

10. Depreciation and amortisation

See accounting policies in notes 35c and 35d

Depreciation and amortisation are specified as follows:

	2014	2013
Depreciation of fixed assets in operation, see Note 13	2,737,096	2,509,721
Amortisation and impairment losses, see Note 14	230,634	88,200
Depreciation and amortisation recognised in the income statement	2,967,730	2,597,921

Depreciation and amortisation are allocated as follows to operating items:

Transmission costs	2,792,187	2,436,690
System operation	69,013	66,277
Other operating expenses	106,530	94,954
Depreciation and amortisation recognised in the income statement	2,967,730	2,597,921

11. Financial income and expenses

See accounting policies in note 35m

Financial income and expenses are specified as follows:

Interest income	116,685	129,748
Net gain in fair value of marketable securities	27,206	11,293
Exchange rate difference	981,560	0
Total financial income	1,125,451	141,041
Interest expenses	(2,181,395)	(2,161,747)
Indexation	(511,459)	(1,751,913)
Exchange rate difference	0	(328,397)
Change in present value of the provision due to site restoration	(43,698)	(40,856)
Capitalised interest expense due to projects under construction	92,042	271,978
Total financial expenses	(2,644,510)	(4,010,935)
Net financial expenses	(1,519,059)	(3,869,894)

Net financial expenses due to the construction of a transmission infrastructure amounting to ISK 92 million (2013: 272 million) is capitalised and has been reported as a reduction in financial expenses.

Capitalised financial expenses were 4.8% of capital tied in transmission structures under construction during the year (2013: 7.0%). This is the Company's average finance cost.

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	(343,344)	(539,511)
Income tax payable	(587,811)	0
Income tax recognised in the income statement	(931,155)	(539,511)
Change in deferred income tax liability is specified as follows:		
Change in temporary differences	(152,137)	120,199
Change in carry-forward losses	(191,207)	(659,710)
Change in deferred tax assets	(343,344)	(539,511)

12. Income tax, contd.:

		2014		2013
Reconciliation of effective tax rate				
Profit before income tax		4,693,396		2,722,909
Income tax according to the current tax rate	20.0%	(938,679)	20.0%	(544,582)
Effects of associates	(0.2%)	7,661	(0.2%)	5,011
Other	(0.0%)	(137)	0.0%	60
Effective tax rate	19.8%	(931,155)	19.8%	(539,511)

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. In the assessment of the Company's management, a revaluation of fixed assets in operation in 2014 is not necessary. The revaluation has been categorised as level 3 fair value.

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
Cost				
Balance at 1.1.2013	23,084,752	47,408,117	3,489,244	73,982,113
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	3,794,693	81,060,200
Additions	587,873	173,209	392,789	1,153,871
Transferred from projects under construction	2,051,466	105,521	0	2,156,987
Balance at 31.12.2014	29,788,369	50,395,207	4,187,482	84,371,058
Depreciation				
Balance at 1.1.2013	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 at 31.12.2013	5,571,973	11,232,250	1,058,356	17,862,579
Depreciation	926,411	1,613,287	197,398	2,737,096
Balance 31.12.2014	6,498,384	12,845,537	1,255,754	20,599,675
Carrying amount				
1.1.2013	18,310,392	37,709,026	2,605,997	58,625,415
31.12.2013	21,577,057	38,884,227	2,736,337	63,197,621
31.12.2014	23,289,985	37,549,670	2,931,728	63,771,382

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

Fixed assets in operation:

	Substations	Transmission lines	Other	Total
1.1.2013	15,794,313	25,733,557	2,605,997	44,133,867
31.12.2013	19,182,702	27,493,585	2,736,337	49,412,624
31.12.2014	21,021,349	26,742,393	2,931,728	50,695,470

Rateable value and insurance value

The rateable value of the Company's real property amounts to upwards of ISK 3.2 billion (2013: ISK 2.8 billion). Assessed value for the same property's fire insurance amounts to ISK 5.5 billion (2013: ISK 5.2 billion) and book value amounts to ISK 4.0 billion (2013: ISK 3.6 billion). The insurance value of the Company's assets amounts to ISK 53.5 billion (2013: ISK 47.5 billion), excluding transmission lines and cables, which are insured by an emergency insurance fund. The Company's emergency insurance amounts to ISK 113.1 billion (2013: ISK 109.9 billion).

Projects under construction:

	2014	2013
Balance at 1.1.	1,086,550	1,769,671
Additions	1,765,113	5,364,675
Transferred to fixed assets in operation	(2,156,987)	(6,097,094)
Transferred from intangible assets	114,535	49,298
Balance at 31.12.	809,211	1,086,550

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

	Capitalised development cost	Software	Total
Cost			
Balance at 1.1.2013	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
Additions	349,717	82,153	431,870
Transferred to projects under construction	(114,535)	0	(114,535)
Balance at 31.12.2014	1,786,604	509,652	2,296,256
Amortisation and impairment losses			
Balance at 1.1.2013	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
Amortisation and impairment losses	211,376	19,258	230,634
Balance at 31.12.2014	507,172	309,389	816,561
Carrying amount			
1.1.2013	1,261,624	114,606	1,376,230
31.12.2013	1,255,626	137,368	1,392,994
31.12.2014	1,279,432	200,263	1,479,695

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:

	2014		2013	
	Share	Carrying amount	Share	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:

	2014 Share in net earnings	2013 Share in net earnings	2014 Carrying amount	2013 Carrying amount
Orkufjarskipti hf. 50%	38,303	25,055	707,209	668,906

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 2014 nor for the year 2013.

18. Trade and other receivables

See accounting policies in note 35b

Trade and other receivables:

	2014	2013
Trade receivables	838,817	405,808
Other receivables	282,846	161,589
Trade and other receivables total	1,121,663	567,397

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.

Statutory reserve

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

Dividends

The Company paid no dividends in 2014 for the financial year 2013, nor in the year 2013 for the financial year 2012.

22. Earnings per share

See accounting policies in note 35o

	2014	2013
Basic and diluted earnings per share:		
Profit to shareholders	3,762,241	2,183,398
Weighted average number of ordinary shares at 31 December	5,902,733	5,902,733
Basic and diluted earnings per share	0.64	0.37

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.

	2014	2013
Long-term liabilities		
Indexed bond loan from parent company in ISK, fixed interest	44,692,176	44,235,700
Loan agreement in CHF, LIBOR + margin	5,639,308	6,436,052
Indexed bond loan in ISK, fixed interest	5,234,862	5,330,965
	55,566,346	56,002,717
Current maturities on long-term liabilities	(919,008)	(914,607)
Interest-bearing long-term liabilities total	54,647,338	55,088,110
Short-term liabilities		
Short-term loans from parent company specifies as follows:		
Accrued interest of long-term liabilities with parent company	1,463,420	1,448,473
Short-term loans from parent company total	1,463,420	1,448,473

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:

		2014		2013	
	Final maturity	Weighted avg. rate	Carrying amount	Weighted avg. rate	Carrying amount
Debt in CHF	2022	0.30%	5,639,308	0.31%	6,436,052
Debt in ISK:					
Indexed	2020 - 2034	4.30%	49,927,038	4.30%	49,566,665
Total interest-bearing loans and borrowings			55,566,346		56,002,717

23. Loans and borrowings, contd.:

Maturities by year of interest-bearing loans and borrowings:

	2014	2013
Year 2015/2014	919,008	914,607
Year 2016/2015	927,468	922,577
Year 2017/2016	936,356	930,950
Year 2018/2017	945,693	939,747
Year 2019/2018	955,504	948,989
Later	50,882,317	51,345,847
	55,566,346	56,002,717

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	2,331,443	1,791,932
Calculated income tax for the year	931,155	539,511
Income tax payable	(587,811)	0
Deferred tax liability at 31 December	2,674,787	2,331,443

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

Fixed assets in operation	2,604,009	2,609,784
Intangible assets	189,042	208,035
Other assets	20,913	
Provision due to site restoration	(163,953)	(155,033)
Other obligations	(84,206)	(86,162)
Unrealized exchange rate difference	108,982	(53,974)
Tax losses carried forward	0	(191,207)
Deferred tax liability at 31 December	2,674,787	2,331,443

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 369 millon (2013: 384 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 2014 amounted to ISK 15 million (2013: 12 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:

	2014	2013
Balance at 1.1.	775,163	734,307
Present value for the year reversed	43,699	40,856
Increase in provision	904	0
Balance at year-end	819,766	775,163

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 (2013: 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 7 million is expensed in relation thereto for 2014 (2013: 8 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:	2014	2013
Trade payables	847,191	419,108
Other payables	337,572	327,703
Trade and other payables total	1,184,763	746,811

29. Financial instruments

Overview

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

- Credit risk
- Liquidity risk
- Market risk

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

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

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

Credit risk

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

Trade and other receivables

The Company’s main customers are electricity generating companies, distribution system operators and power-intensive consumers. The Company's largest customers are also shareholders in the Company. Approximately 86% (2013: 87%) 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:

	2014	2013
Long-term note	23,286	34,929
Receivables from parent company	702,735	0
Trade and other receivables	1,110,020	555,754
Market securities	470,971	234,344
Cash and cash equivalents	12,234,663	9,917,204
Highest possible loss due to credit risk total	14,541,675	10,742,231

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. 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:

2014	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.	46,155,596	55,981,420	1,881,541	1,881,541	5,644,622	46,573,716
Long-term liabilities	10,874,170	13,942,350	1,205,789	1,202,673	3,374,244	8,159,644
Trade and other payables	1,184,763	1,184,763	1,184,763	0	0	0
	58,214,529	71,108,533	4,272,093	3,084,214	9,018,866	54,733,360
2013						
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

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 2014, 58.8% (2013: 62.7%) 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 Swiss Francs (CHF). The main currencies posing a foreign exchange risk are the USD and the Swiss Francs (CHF). In 2015, it is estimated that 64.4% 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
2014			
Cash and cash equivalent	7,177	8,476	10,509,162
Trade and other receivables	526	0	277,192
Other long-term liabilities	0	(5,639,308)	0
Trade and other payables	(80,814)	(5,569)	(3,788)
Net currency risk	(73,111)	(5,636,401)	10,782,566
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)	(6,506)	(15,680)
Net currency risk	(49,848)	(6,416,571)	8,819,701

	Av. exch. rate for the year		Year-end exch. rate	
	2014	2013	2014	2013
Currency risk				
EUR	154.86	162.38	154.27	158.50
CHF	127.50	131.91	128.29	129.19
USD	116.75	122.23	126.90	115.03

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 2013.

	2014	2013
EUR	5,849	3,988
CHF	450,912	513,326
USD	(862,605)	(705,576)

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 interest and fixed inflation-indexed interest. The majority of the Company's borrowings bear fixed inflation-indexed interest, cf. Note 23. At year end 2014, the proportion of liabilities with floating interest rates was 10% compared to 11% at year end 2013.

29. Financial instruments, contd.:

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

	Carrying amount 2014	2013
Financial instruments with floating interest rate		
Financial assets	12,728,920	10,186,477
Financial liabilities	(5,639,308)	(6,436,052)
	7,089,612	3,750,425
Financial instruments with fixed interest rate		
Financial liabilities	(49,927,038)	(49,566,665)

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 2013.

	Earnings 100bp increase	100bp decrease
31 December 2014		
Financial instruments with floating interest rates	43,360	(77,010)
Cash flow sensitivy (net)	43,360	(77,010)
31 December 2013		
Financial instruments with floating interest rates	26,061	(65,027)
Cash flow sensitivy (net)	26,061	(65,027)

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:

	2014		2013	
	Carrying amount	Fair value	Carrying amount	Fair value
Long-term liabilities from parent company	(44,692,176)	(47,580,197)	(44,235,700)	(49,842,048)
Other long-term liabilities	(10,874,170)	(11,907,963)	(11,767,017)	(13,115,500)
	(55,566,346)	(59,488,160)	(56,002,717)	(62,957,548)

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 2013.

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
2014				
Long-term note		11,643		11,643
Receivables from parent company		702,735		702,735
Trade and other receivables		1,121,663		1,121,663
Marketable securities	470,971			470,971
Cash and cash equivalents		12,234,663		12,234,663
	470,971	14,070,704	0	14,541,675
Loans from parent company			46,155,596	46,155,596
Other long-term liabilities			10,874,170	10,874,170
Trade and other payables		1,184,763		1,184,763
	0	1,184,763	57,029,766	58,214,529
2013				
Long-term note		23,286		23,286
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

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

Cash-flow sensitivity analysis for the Consumer Price Index

An increase in the Consumer Price Index of 100 basis points at the reporting date would have increased (decreased) equity and profit or loss after tax by the amounts stated below. If the Consumer Price Index had decreased by 100 basis points, the effect would have had the equal but opposite effect on profit or loss after tax. This analysis assumes that all other variables, in particular the exchange rates, remain constant. The analysis was performed in the same manner for the year 2013.

	Earnings	
	100bp increase	100bp decrease
31 December 2014		
Inflation-indexed financial instruments	(416,024)	416,024
Cash flow sensitivy (net)	(416,024)	416,024
31 December 2013		
Inflation-indexed financial instruments	(407,848)	407,848
Cash flow sensitivy (net)	(407,848)	407,848

29. Financial instruments, contd.:

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 2014 amounted to ISK 143 million (2013: ISK 166 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. 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 and no later than 1 August of each year the Authority must submit the updated revenue cap and the settlement for the preceding year, including reasoning for any changes. One of the main prerequisites for attaining the Electricity Act's objective of efficiency in Landsnet's operations, which is an aim of the revenue cap model, is that the rate of return be decided five years in advance.

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. Landsnet has three times appealed the Authority's decision on the settlement for that period to the Appeals Committee on Electricity, which in its ruling of 6 June 2014 overturned the Authority's decision for a third time and referred the case back to the Authority for a reassessment.

On 1 October 2012, the Authority issued a decision on the weighted average cost of capital, to be effective from 1 January 2011. The revenue cap for 2011-2015 was established by the Authority on 28 July 2013 on the basis of the aforesaid decision. Stakeholders appealed the Authority's 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 ruling, the Authority must issue a new decision on rate of return criteria based on a new opinion delivered by an expert committee. That decision remains to be made, which means uncertainty over the revenue cap for the period.

The repeated failure to issue the Authority's decisions on Landsnet's allowed rate of return and revenue cap at the time stipulated by law creates major uncertainty for the Company's operations. As a result, the Company is unable to react to the Authority's decisions with tariff changes before the start of each revenue cap year.

The settlement for 2010 is not in dispute, but uncertainty will remain regarding the revenue cap for 2011-2014 until the final decision on the weighted average cost of capital becomes available, which causes uncertainty about the Company's position.

31. Uncertainty, contd.:

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.

The anticipated decision of the Authority on the weighted average cost of capital, and thereby the revenue cap for 2011-2014, could change that result, as previously mentioned.

Distribution system operators

At year-end 2014, 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 on this matter is still pending, the level of the revenue cap for distribution system operators during this period remains unclear, with approximately ISK 1.5 billion in dispute. 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 Authority delivers a new decision. During the time that this matter has been unsettled, Landsnet has based its tariff on the Authority's decision, on which basis the repayment amount is currently estimated at ISK 0.3 billion.

The anticipated decision of the Authority on the weighted average cost of capital, and thereby the revenue cap for 2011-2014, could change that result, as previously mentioned.

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. 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 2006-2014 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 CEO and Managing Directors (Vice Presidents) of the Company receive a contribution to a defined benefit pension fund. They also receive a car allowance. Management's salaries are accounted for in Note 9.

32. Related parties, contd.:

Other transactions with related parties

	2014	2013
Sale of goods and services:		
Landsnet's parent company and its subsidiaries	7,428,440	6,656,405
Landsnet's other shareholders	4,900,660	4,765,500
Sale of goods and services to related parties total	12,329,100	11,421,905
Cost of goods and services:		
Landsnet's parent company and its subsidiaries	1,680,357	1,418,704
Landsnet's other shareholders	475,008	509,992
Cost of goods and services to related parties total	2,155,365	1,928,696

In addition the costs outlined above, the Company paid ISK 1,859 million (2013: ISK 1,802 million) in interest to its parent company.

Balance:

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

	2014		2013	
	Receivables	Payables	Receivables	Payables
Landsnet's parent company and its subsidiaries	702,735	0	0	(488,053)
Landsnet's other shareholders	543,582	0	398,764	(14,252)
	1,246,317	0	398,764	(502,305)

Other receivables and payables with related parties are as follows:

	2014	2013
Interest-bearing liabilities to parent company, see note 23	44,692,176	44,235,700
Accrued interest payable to parent company	1,463,420	1,448,473
	46,155,596	45,684,173

33. Financial ratios

The company's key financial ratios:

Financial performance:		
EBIT	6,174,152	6,567,748
EBITDA	9,141,882	9,165,669
Financial position:		
Current ratio – current assets/current liabilities	3.63	3.12
Equity ratio – equity/total assets	23.5%	19.9%
Return on equity	24.4%	16.5%

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 2014 was 13.6% (2013: 9.0%). 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.

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.

3. Significant accounting policies, contd.:

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.

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.

3. Significant accounting policies, contd.:

(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.

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.

3. Significant accounting policies, contd.:

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.

(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.

3. Significant accounting policies, contd.:

(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.

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.

3. Significant accounting policies, contd.:

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 2014 and that apply to its operations. The Company has not implemented standards, amendments thereto or interpretations entering into effect after year-end 2014 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 27 June 2013 and are available for inspection at the Company's head office.

Internal control and risk management

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

Corporate values and Code of Ethics

Landsnet's employees are obliged to abide by the Company's values in all their activities. Its corporate values are informed by its role and future vision and provide the foundation for the corporate culture for which the Company strives. Landsnet's values are: 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. She was chairman of the Federation of Icelandic Industries. Ms Björnsdóttir was at the same time chairman of Akkur SI. In addition, she was a member of the Executive Committee and a board member of the Confederation of Icelandic Employers. Her board memberships include Hagar hf, the Icelandic Data Protection Authority, the Association of Chartered Engineers in Iceland, the Seed Company Association in Iceland, University Council of Reykjavík University 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. Ms Björnsdóttir is boardmember of the software company Menn og mýs ehf., a boardmember in 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

The Board of Directors held 15 meetings in 2014. All of the meetings were attended by all Board members except for two meetings where one member was absent. Two meetings were attended by an Alternate Director.

Landsnet´s Executive Committee

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

Þórður Guðmundsson, former CEO & President, was 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. Mr Guðmundsson was CEO & President of Landsnet from 1 January 2005 until 31 December 2014.

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.

Guðlaug Sigurðardóttir, CFO is also a member of Lansdnet's Executive Committee

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
Svava Bjarnadóttir, Alternate Director of Landsnet's Board

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

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

The Audit Committee also makes proposals for improvements and deliberates on matters at the Board's request.

A total of 7 meetings were held in 2014, all of which were attended by all Committee members.

Remuneration Committee

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

The grid in 2014

LANDSNET

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