

Farice ehf.
Financial Statements 2018

Farice ehf.
Smáratorgi 3
201 Kópavogur

Reg. no. 511203-2950

Contents

	Page
Report of the Board of Directors and the CEO	3
Independent Auditors' Report	5
Statement of Comprehensive Income	8
Statement of Financial Position	9
Statement of Changes in Equity	10
Statement of Cash Flows	11
Notes	12
Appendix:	
Non-financial Reporting	27

Report of the Board of Directors and the CEO

Farice ehf. was established in 2003 as a transmission and data service provider. The Company plays an important role in Iceland's infrastructure for the greater public good and economic life in Iceland. The Company operates two submarine cables FARICE-1 and DANICE between Iceland and Europe and connects Iceland to the world with backhaul agreements to other networks in major connecting points in Europe such as London, Amsterdam and Copenhagen.

Operations in the year 2018

The Company is delivering Operating Profit for the fifth year in a row. According to the Statement of Comprehensive Income the operating revenue amounted to EUR 14,6 million and the EBITDA EUR 8 million. Depreciation was EUR 7,1 million and operating profit EUR 933 thousand. According to the Statement of Financial Position the Company's assets amounted to EUR 70,9 million and the equity amounted to EUR 27,9 million, an equity ratio of 39,3%. The Financial Statements are prepared in accordance with International Financial Reporting Standards. Applicable legal provisions do not permit payment of dividend and equity is used to cover the loss of the year which amounted to EUR 334 thousand.

At 31 December 2018 management reviewed whether there was an indication of impairment of the Company's operating assets and concluded there was no indication of impairment. In April 2019 the Company has the option to pay off its issued bonds and the Board of Directors is considering that option. For further information regarding loans and borrowings we refer to Note 15 in the Financial Statements.

Share capital

The three shareholders in Farice ehf. are Arion Bank (ID 581008-0150) with 38,35%, the Icelandic State (ID 540269-5459) with 27,06%, Landsvirkjun, The National Power Company (ID 420269-1299) with 33,16% and 1,43% belongs to the Company itself.

Corporate governance and non-financial reporting

The Board is practicing good corporate governance based on provisions of law, the company's Articles of Association and guidelines in KPMG's handbook on corporate governance. The purpose of these rules is to ensure transparency and internal control and increase risk awareness. The Board consists of five members and two alternative members and the board hires the CEO. Internal audit and control systems are limited due to the fact that few people work for the Company. Three members, whereof two are independent, form the audit committee that follows in detail the closing of the Financial Statements. The risk assessment mainly relates to an action plan if a disruption happens to the submarine cables.

The Board refers to appendix to this financial statements regarding other non-financial information about social matters, respect for the environment, employees, human rights, anti-corruption and bribery. Information about the financial risk management can be found in note 16.

Statement by the Board of Directors and the CEO

According to the Board of Directors' best knowledge, the Financial Statements comply with International Financial Reporting Standards as adopted by the EU and give a true and fair view of the Company's assets and liabilities, financial position as at 31 December 2018, operating performance and the cash flow for the year ended 31 December 2018 as well as describing the principal risk and uncertainty factors faced by the company. The report of the Board of Directors provides a clear overview of the development and achievements in the company's operations and its situation.

Report of the Board of Directors and the CEO, Contd.:

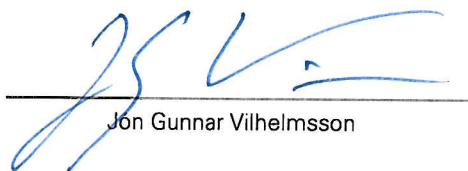
The Board of Directors and CEO of Farice ehf., hereby confirm the Financial Statements of Farice ehf., for the year 2018 with their signatures.

Kópavogur, 8 February 2019

The Board of Directors of Farice ehf.



Martha Eiríksdóttir, Chairman




Jón Gunnar Vilhelmsson



Kristín Guðmundsdóttir




Sölvi Sölvason



Ríkarður Ríkarðsson

Chief Executive Officer



Ómar Benediktsson

Independent Auditor's Report

To the Board of Directors and Shareholders of Farice ehf.

Report on the Audit of the Financial Statements

Opinion

We have audited the financial statements of Farice ehf. ("the Company"), which comprise the statement of financial position as at December 31, 2018, the statement of comprehensive income, changes in equity and cash flows for the year then ended, and notes, comprising significant accounting policies and other explanatory information.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as at December 31, 2018, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union and additional Icelandic disclosure requirement in accordance with Icelandic Financial Statement Act no. 3/2006.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Financial Statements* section of our report. We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code) together with the ethical requirements that are relevant to our audit of financial statements in Iceland and we have fulfilled our other ethical responsibilities in accordance with these requirements and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key audit matters

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

Key audit matter	How the matter was addressed in the audit
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Impairment test of operating assets

Impairment test is performed annually in order to determine if carrying amount of the company's operating assets is greater than its estimated recoverable amount. As explained in note 11 is the test is based on management's assumptions about future growth of revenues, operating margin, and weighted average cost of capital. The impairment test is based on a five year forecast but with fixed income and margin for the period thereafter. The expected recoverable amount of operating assets is key audit matter in our audit due to the inherent uncertainty involved in forecasting and discounting future cash flows which are the basis of the impairment test.

We obtained the annual impairment test performed by management and critically evaluated the model and assumptions used by management in their calculations.

Our audit work included following procedures:

- Management forecasts were agreed with the forecasts presented to the Board and compared with historic amounts and growth rates.
- Assessing the reasonableness of key assumptions in the valuation model such as historic forecasts, long-term growth rates and EBIDTA. Forecasts from prior periods were also compared to actual results to test accuracy.
- Assessing the reasonableness of inputs used for the calculation of weighted cost of capital with comparason to current finance costs and market conditions.
- The model used for the impairment test was reviewed and validated.
- Review of the notes to the financial statements to confirm that applicable information regarding the impairment test of the operating assets were provided.

Independent Auditor's Report , cont.:

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

The Board of Directors and CEO are responsible for the preparation and fair presentation of the financial statements in accordance with IFRSs as adopted by the European Union and additional Icelandic disclosure requirement in accordance with Icelandic Financial Statement Act no. 3/2006, and for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

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

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

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

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

Independent Auditor's Report , cont.:

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

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

Report on Other Legal and Regulatory Requirements

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 and CEO accompanying the financial statements includes the information required by the Financial Statement Act if not disclosed elsewhere in the financial statements.

The engagement partner on the audit resulting in this independent auditor's report is Árni Claessen.

Reykjavík, 8 February 2019

KPMG ehf.



Statement of Comprehensive Income for the year ended 31 December 2018

	Notes	2018	2017
Sale of bandwidth	4.	11.047.605	11.238.988
Income from Public Service Contract	5	3.582.866	3.811.744
		<u>14.630.471</u>	<u>15.050.732</u>
Operating expenses	6	5.721.596	6.113.298
Administrative expenses	7	913.914	950.710
		<u>6.635.509</u>	<u>7.064.008</u>
Profit before depreciation and finance items		7.994.962	7.986.724
Depreciation	11	(7.061.484)	(7.052.929)
Operating profit		933.478	933.795
Interest income		25.222	20.706
Interest and indexation expenses	10	(3.816.590)	(3.381.065)
Exchange rate differences		2.524.145	2.079.720
Net finance cost		<u>(1.267.222)</u>	<u>(1.280.639)</u>
Total comprehensive loss for the year		<u>(333.744)</u>	<u>(346.844)</u>

Notes on pages 12 to 26 are an integral part of these financial statements.

Statement of Financial Position 31 December 2018

	Notes	31.12.2018	31.12.2017
Assets			
Operating assets	11	66.252.817	73.099.711
Prepaid expenses	12	1.368.559	1.457.811
Non-current assets		<u>67.621.376</u>	<u>74.557.522</u>
Trade receivables		187.853	458.278
Other receivables		317.140	689.963
Cash and cash equivalents		2.797.733	143.289
Current assets		<u>3.302.726</u>	<u>1.291.530</u>
Total assets		<u><u>70.924.102</u></u>	<u><u>75.849.052</u></u>
Equity			
Share capital	14	59.615.031	59.615.031
Accumulated deficit		(31.739.126)	(31.405.382)
Total equity		<u>27.875.905</u>	<u>28.209.649</u>
Liabilities			
Loans and borrowings	15	38.669.395	41.665.718
Deferred income		0	1.500.000
Non-current liabilities		<u>38.669.395</u>	<u>43.165.718</u>
Loans and borrowings	15	1.695.237	1.869.687
Trade payables		437.699	348.913
Other liabilities and deferred income		2.245.866	2.255.085
Current liabilities		<u>4.378.802</u>	<u>4.473.685</u>
Total liabilities		<u>43.048.197</u>	<u>47.639.403</u>
Total equity and liabilities		<u><u>70.924.102</u></u>	<u><u>75.849.052</u></u>

Notes on pages 12 to 26 are an integral part of these financial statements.

Statement of Changes in Equity for the year ended 31 December 2018

	Notes	Share capital	Accumulated deficit	Total equity
2018				
Equity as at 1 January 2018		59.615.031	(31.405.382)	28.209.649
Total comprehensive loss for the year			(333.744)	(333.744)
Equity as at 31 December 2018	14	<u>59.615.031</u>	<u>(31.739.126)</u>	<u>27.875.905</u>
2017				
Equity as at 1 January 2017		59.615.031	(31.058.538)	28.556.493
Total comprehensive loss for the year			(346.844)	(346.844)
Equity as at 31 December 2017	14	<u>59.615.031</u>	<u>(31.405.382)</u>	<u>28.209.649</u>

Notes on pages 12 to 26 are an integral part of these financial statements.

Statement of Cash Flows for the year ended 31 December 2018

	Notes	2018	2017
Cash flow from operating activities			
Loss for the year		(333.744)	(346.844)
Adjustments for:			
Depreciation	11	7.061.484	7.052.929
Net finance cost		1.267.222	1.280.639
		<u>7.994.962</u>	<u>7.986.724</u>
Changes in current assets and liabilities		(631.382)	(2.079.034)
Cash generated from operating activities before interest		<u>7.363.580</u>	<u>5.907.690</u>
Interest received		25.222	20.706
Interest paid		(2.506.360)	(2.631.875)
Net cash from operating activities		<u>4.882.442</u>	<u>3.296.521</u>
Cash flows from investing activities			
Acquisition of property and equipment	11	(214.590)	0
Net cash used in investing activities		<u>(214.590)</u>	<u>0</u>
Cash flows from financing activities			
Repayment of long-term loans		(1.893.643)	(3.733.611)
Net cash used in financing activities		<u>(1.893.643)</u>	<u>(3.733.611)</u>
Net decrease in cash and cash equivalents		2.774.209	(437.090)
Cash and cash equivalents at 1 January		143.289	599.365
Effect of exchange rate fluctuations on cash held		(119.765)	(18.986)
Cash and cash equivalents at 31 December		<u>2.797.733</u>	<u>143.289</u>

Notes on pages 12 to 26 are an integral part of these financial statements.

Notes

1. Reporting entity

Farice ehf. is a limited liability company domiciled in Iceland. The Company's registered office address is Smáratorg 3, Kópavogur, Iceland. The principal activities of the Company are to insure safe telecommunications between Iceland and its neighbour countries by submarine cables.

The company has operations in Iceland, the Faroe Islands, Denmark and the United Kingdom. The income and expenses originate in Iceland and neighbouring countries.

2. Basis of preparation

A. Statement of compliance

The Company's financial statements are prepared according to International Financial Reporting Standards (IFRS) as adopted by the EU and additional Icelandic disclosure requirement in accordance with the Icelandic financial statement act no. 3/2006.

These financial statements were authorized for issue by the Board of Directors on 8 February 2019.

B. Going concern

Management has evaluated whether the Company is a going concern. It is the opinion of the management that the Company's ability to meet its obligations in the foreseeable future has been ensured. Therefore, the financial statements are presented based on the assumption that the Company is a going concern.

C. Basis of measurement

The financial statements have been prepared on the historical cost basis.

D. Presentation and functional currency

These financial statements are presented in euro (EUR), which is the Company's functional currency.

E. Use of estimates and judgements

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

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

Information about critical judgements in applying accounting policies that have the most significant effect on the amounts recognized in the financial statements is included in the following notes:

- Note 11 - operating assets

Information about assumptions and estimates that have a significant risk of resulting in a material adjustment within the next financial year are included in the following notes:

- Note 11 - key assumptions used in discounted cash flow projections

Notes, contd.:

3. Changes in significant accounting policies

The Company has initially applied IFRS 15 (see A) and IFRS 9 (see B) from 1 January 2018.

A. IFRS 15 Revenue from Contracts with customers

IFRS 15 established a comprehensive framework for determining whether, how much and when revenue is recognised and replaces IAS 18 and IAS 11. The standard introduces a new model for revenue recognition which is based on transfer of control of goods and services while prior model was based on transfer of risk and rewards. Determining the timing of the transfer of control - at a point in time or over time - requires judgement. The management's analysis of the impact of IFRS 15 revealed that implementation of the new standard does not change the company's revenue recognition and have no impact on the company's balance sheet at 1 January 2018.

B. IFRS 9 Financial Instruments

IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 largely retains the existing requirements in IAS 39 for the classification and measurement of financial liabilities. However, it eliminates previous IAS 39 categories for financial assets of held to maturity, loans and receivables and available for sale. Under IFRS 9, on initial recognition, financial assets are classified and measured as: amortised cost, FVOCI and FVTPL. The new classification and measurement approach for financial assets is generally based on the business model in which financial assets are managed and their cash flow characteristics. The adoption of IFRS 9 has not a significant impact on the Company's accounting policies related to financial assets or financial liabilities.

4. Sale of bandwidth

The Company generates revenues by providing data services between Iceland, the Faroe Islands, UK and mainland Europe via submarine cable system. Revenues from the sale of bandwidth is recognized in profit and loss based on recorded measurement of delivery during the period. Contract with customers are usually made for at minimum two years period. The payment terms range from 15 - 30 days. Prepaid revenues are deferred and recognized in income statement based on delivery over the lifetime of the contract.

Four customers account for 70% of the revenues from sale of bandwidth of the Company (2017: 57%). 64% of the revenue from sold bandwidth comes from the domestic market (2017: 54%).

5. Public service contract

In April 2012 The Company and The Telecommunications Fund entered into a Public Service Contract concerning electronic communication connectivity between Iceland and Europe. The purpose of the contract is that the parties acknowledge that submarine electronic communications cables, providing international connectivity to the territory of Iceland are part of an essential infrastructure. The parties furthermore acknowledge that Farice is the only undertaking in possession of submarine cables connecting Iceland and other parts of Europe. Since the contract was signed in 2012 the Company has received annual public service payments in the range of EUR 2,1 - 3,8 million.

This contract expired at the end of 2018 but was replaced with a new one year contract with the Telecommunications Fund. According to the new contract will Farice be compensated for a seabed research carried out in 2019 for a possible optic fibre cable between Iceland and Europe. The total reserach cost is estimated to be EUR 1,9 million. The contract also guarantees additional funding if revenue is not sufficient to cover the cost of operating the public service. However, based on the current operation and financial position of the Company the management does not expect additional funding from the Telecommunications Fund for that matter.

Notes, contd.:

6. Operating expenses	2018	2017
Backhaul	2.719.835	2.979.026
Cable stations and submarine cable maintenance support	1.409.588	1.445.283
Other operating expenses	1.592.173	1.688.989
Total operating expenses	5.721.596	6.113.298
7. Administrative expenses	2018	2017
Salaries and salary-related expenses	653.108	667.408
Office rent	96.241	100.510
Auditing and accounting support	46.008	44.271
Other administrative expenses	118.557	138.521
Total administrative expenses	913.914	950.710
8. Fee to auditors	2018	2017
Audit of financial statements	27.533	25.324
Review of interim financial statements	7.300	8.250
Other services	9.136	10.266
	43.969	43.840
9. Salaries and salary-related expenses are specified as follows:		
Salaries	783.697	842.350
Contributions to pension funds	106.850	101.521
Other salary related expenses	114.081	110.194
Total salaries and other salary related expenses	1.004.628	1.054.065
Administrative expenses	653.108	667.408
Operating expenses	351.520	386.657
Total salaries and other salary related expenses	1.004.628	1.054.065
Number of employees in full time equivalent units	7	7
Salaries and salary-related expenses to the Board of Directors	81.734	78.566
Salaries and salary-related expenses to the CEO	182.885	219.411
10. Finance income and finance expenses		
Interest- and indexation expenses are specified as follows:		
Interest expenses and borrowing costs	2.470.637	2.592.882
Indexation charge	1.345.953	788.183
Total finance expenses	3.816.590	3.381.065

Notes, contd.:

11. Operating assets

Operating assets, their impairment and depreciation is specified as follows:

	PoP/			Common	
	Backhaul/CS	Farice	Danice	Items	Total
Total value					
Total cost 1.1.2017	18.450.959	46.950.412	82.622.979	4.427.583	152.451.933
Total cost 31.12.2017	18.450.959	46.950.412	82.622.979	4.427.583	152.451.933
Additions during the year	0	0	214.590	0	214.590
Total cost 31.12.2018	18.450.959	46.950.412	82.837.569	4.427.583	152.666.523
Depreciation and impairment					
Depreciated 1.1.2017	11.772.734	29.398.363	26.700.613	4.427.583	72.299.293
Depreciation for the year	513.053	2.699.471	3.840.405	0	7.052.929
Depreciated 31.12.2017	12.285.787	32.097.834	30.541.018	4.427.583	79.352.222
Depreciation for the year	489.712	2.699.471	3.872.301	0	7.061.484
Depreciated 31.12.2018	12.775.499	34.797.305	34.413.319	4.427.583	86.413.706
Carrying amount					
Carrying amount 1.1.2017	6.678.225	17.552.049	55.922.366	0	80.152.640
Carrying amount 31.12.2017	6.165.172	14.852.578	52.081.961	0	73.099.711
Carrying amount 31.12.2018	5.675.460	12.153.107	48.424.250	0	66.252.817

Insurance value of the Company's assets amounted to EUR 13,0 million.

At year end, the Company's operating assets were tested for impairment. The test was based on evaluation of the Company's operating value, based on management's assumptions, mainly with respect to future growth in revenue, operating margin and weighted average cost of capital. In the evaluation a five year forecast was used, but a fixed income increase and margin was assumed in the period thereafter. The conclusions of the impairment test did not lead to an impairment loss. Nevertheless if future operation will not be in line with budgets there is a possibility that an impairment loss will be recognised. The value of the operating assets was estimated to be significantly higher than their carrying amount and no impairment was required.

12. Prepaid expenses

The prepaid expenses are a state guarantee fee paid in 2010 for the secured bond issue.

13. Deferred tax asset

A deferred tax asset is not recognised in the balance sheet due to the uncertainty of utilisation of the deferred carryforward tax loss. Carry forward losses may be utilised for 10 years from when it is incurred.

Deferred tax asset is as follows at the year end:	31.12.2018	31.12.2017
Property and equipment	(2.933.221)	(3.740.187)
Trade receivables	0	(4.583)
Deferred foreign exchange difference	(1.199.471)	(232.204)
Tax loss carryforward	23.818.878	23.866.932
Impairment of tax asset	(19.686.186)	(19.889.958)
	<u>0</u>	<u>0</u>

Notes, contd.:

13. Deferred tax asset, contd.:

At year-end 2018 the Company has unused tax losses available for offset against future profits as follows:

Available until the year 2019	24.132.448
Available until the year 2020	13.210.465
Available until the year 2021	13.662.769
Available until the year 2022	6.608.028
Available until the year 2023	7.734.017
Available until the year 2024	8.699.532
Available until the year 2025	11.027.959
Available until the year 2026	20.089.149
Available until the year 2027	9.983.558
Available until the year 2028	1.413.021
Unused tax losses total	<u>116.560.946</u>

14. Equity

Share capital

Total share capital is EUR 60,5 million where nominal value of A-class shares is EUR 54,3 million and B-class shares 6,2 million. The nominal value of A-class treasury shares is EUR 862.335 and the nominal value of outstanding shares therefore amounts to EUR 59,6 million. Owners of the ordinary A-class shares are entitled to 55% of dividend payments and one vote per share at general meetings. Owners of the B-class shares are entitled to 45% of dividend payments and 6 votes per share at general meetings of the company.

15. Loans and borrowings

This note provides information about the contractual terms of the Company's interest-bearing loans and borrowings, which are measured at amortized cost. For more information about the Company's exposure to interest rate, foreign currency and liquidity risk, see note 16.

	2018				2017	
	Curr.	Year of maturity	Interest rate	Carrying amount	Interest rate	Carrying amount
Secured bond issue.....	ISK	2034	5,5% + indexed	40.364.632	5,5% + indexed	43.321.827
Secured loan.....	EUR	2018	Euribor + 4,5%	0	Euribor + 4,5%	213.578
				<u>40.364.632</u>		<u>43.535.405</u>
Current maturities.....				(1.695.237)		(1.869.687)
Total long term liabilities.....				<u>38.669.395</u>		<u>41.665.718</u>

Maturities are specified as follows over the next years:

	31.12.2018	31.12.2017
Year 2019/2018.....	1.695.237	1.869.687
Year 2020/2019.....	1.791.560	1.750.250
Year 2021/2020.....	1.893.254	1.849.641
Year 2022/2021.....	2.000.618	1.954.573
Year 2023/2022.....	2.113.968	2.065.356
Year 2024/2023.....	2.233.638	2.182.315
Subsequent.....	28.636.357	31.863.583
	<u>40.364.632</u>	<u>43.535.405</u>

Guarantees on long-term liabilities:

	Guarantor/Guarantee	31.12.2018
Secured bond issue, indexed.....	Icelandic State	40.364.632
		<u>40.364.632</u>

Notes, contd.:

15. Loans and borrowings, contd.:

The Icelandic State has a 1st ranking security in the Danice cable system as collateral against its guarantee of the secured bond.

The company complies with all covenants in loan agreements at year-end.

The Company has the option to fully repay the issued bonds on 15 April 2019 with 5% settlement fee on indexed principle amount at the payment date.

Reconciliation between the opening balance and closing balance for liabilities arising from financing activities:

	2018	2017
Balance 1. January 2018.....	43.535.405	48.659.021
Repayment of long-term loans.....	(1.893.643)	(3.733.611)
Currency fluctuations and indexations.....	(1.277.130)	(1.390.005)
Balance 31. December 2018.....	40.364.632	43.535.405

16. Financial risk management

Overview

The following risks arise from the Company's 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 the management of capital.

Financial risk management objectives

The Company's management monitors and manages the financial risks relating to the operations of the Company. These risks primarily include credit risks and liquidity risk and is being closely followed by the management. The Company does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

Credit risk

Credit risk is the risk of financial loss to the Company if a customer fails to meet its contractual obligations. Over 85% of the revenue is coming from long standing customers and the company has never had to write off considerable receivables. There is no provision in place for impairment of receivables.

The Company's maximum possible loss due to financial assets with inherent credit risk is their carrying amount, which is specified as follows at year end:

	2018	2017
Trade receivables.....	187.853	458.278
Other short term receivables.....	317.140	689.963
Cash and cash equivalents.....	2.797.733	143.289
	3.302.726	1.291.530

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company's objective is to always have sufficient liquidity to meet its payment obligations as they become due.

Notes, contd.:

16. Financial risk management, contd.:

Liquidity risk, contd.:

The following table shows the remaining contractual maturities at the end of the reporting period of financial liabilities and financial assets, including estimated interest payments:

Year end 2018	Carrying amount	Contractual cash flows	0 - 12 months	1 - 2 years	More than 2 years
Trade and other payables.....	1.183.565	1.183.565	1.183.565		
Long-term loans.....	40.364.632	74.743.800	3.927.007	4.028.163	66.788.630
	<u>41.548.197</u>	<u>75.927.365</u>	<u>5.110.572</u>	<u>4.028.163</u>	<u>66.788.630</u>
Trade receivables.....	187.853	187.853	187.853		
Other receivables.....	317.140	317.140	317.140		
Cash and cash equivalents.....	2.797.733	2.797.733	2.797.733		
	<u>3.302.726</u>	<u>3.302.726</u>	<u>3.302.726</u>	<u>0</u>	<u>0</u>
Net balance 31.12.2018.....	38.245.471	72.624.639	1.807.846	4.028.163	66.788.630
Year end 2017					
Trade and other payables.....	1.103.998	1.103.998	1.103.998		
Long-term loans.....	43.535.405	83.491.970	4.269.063	4.155.145	75.067.762
	<u>44.639.403</u>	<u>84.595.968</u>	<u>5.373.061</u>	<u>4.155.145</u>	<u>75.067.762</u>
Trade receivables.....	458.278	458.278	458.278		
Other receivables.....	689.963	689.963	689.963		
Cash and cash equivalents.....	143.289	143.289	143.289		
	<u>1.291.530</u>	<u>1.291.530</u>	<u>1.291.530</u>	<u>0</u>	<u>0</u>
Net balance 31.12.2017.....	43.347.873	83.304.438	4.081.531	4.155.145	75.067.762

Market risk

Market risk is the risk that changes in market prices, such as foreign exchange rates and interest rates will affect the income of the Company or the value of its holdings of financial instruments.

Currency risk

Currency risk exposure does arise when there is a difference between assets and liabilities denominated in foreign currency. The majority of the Company's assets and liabilities are denominated in EUR and ISK.

The Company's exposure to currency risk is specified as follows at year end:

Year 2018	Assets	Liabilities	Net exposure
USD	86.558	62.400	24.158
DKK	319	128.254 (	127.935)
ISK	1.178.364	41.302.231 (	40.123.867)
GBP	88.490	55.326	33.164
Net exposure	<u>1.353.731</u>	<u>41.548.211 (</u>	<u>40.194.480)</u>

Notes, contd.:

16. Financial risk management, contd.:

Year 2017	Assets	Liabilities	Net exposure
JPY	74.300	0	74.300
DKK	6.405	73.882 (	67.477)
ISK	567.905	44.234.436 (	43.666.531)
GBP	85.044	52.707	32.337
Net exposure	733.654	44.361.025 (	43.627.371)

The following exchange rates applied during the year:

	Average exchange rate		End of year exchange rate	
	2018	2017	2018	2017
USD	1,18	1,13	1,18	1,20
ISK	127,7	120,9	128,1	125,4
GBP	0,88	0,88	0,89	0,89
DKK	7,45	7,44	7,45	7,44

Market risk

Sensitivity analysis

The table below shows what effects 5% and 10% strengthening of the relevant foreign currency rates against the EUR would have on P/L and equity. The foreign currency assets and liabilities in the sensitivity analysis are mainly foreign currency borrowings and foreign currency bank balances. The analysis is prepared assuming the amount outstanding at the balance sheet date was outstanding for the whole year. The analysis assumes that all variables other than the relevant foreign currency rate are held constant. A positive number below indicates an increase in profit and other equity. A decrease of the relevant foreign currency rate against the EUR would have an opposite impact on P/L and equity.

	31.12.2018		31.12.2017	
	5%	10%	5%	10%
USD.....	967	1.933	2.972	5.944
ISK..... (	1.604.955) (	3.209.909) (	1.746.661) (	3.493.322)
DKK..... (	5.118) (	10.235) (	2.699) (	5.398)
GBP.....	1.327	2.653	1.294	2.587

Interest rate risk

The Company is exposed to cash flow interest rate risk due to changes in interest rates of floating rate financial liabilities. As stated before, the Company endeavours to ensure it always has sufficient liquidity to meet its liabilities as they become due.

Interest rate risk is the risk that fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company has both fixed and floating rate interest bearing financial instruments.

Notes, contd.:

16. Financial risk management, contd.:

Exposure to interest rate risk

Interest-bearing financial assets and liabilities are as follows at the year end:

	2018	2017
Financial instruments with floating interest rate		
Financial assets.....	2.797.733	143.289
Financial liabilities.....	(40.364.632)	(43.535.405)
	(37.566.899)	(43.392.116)

Fair value sensitivity analysis for fixed interest rate instruments

Financial instruments with fixed interest rates are not measured at fair value. Therefore, a change in interest rates at the reporting date would not affect profit and loss or equity.

Cash flow sensitivity analysis for floating interest rate instruments

An increase or decrease in interest rates of 100 basis points at the reporting date would have increased (decreased) profit or loss after tax by following amounts. This analysis is based on that all other variables, in particular foreign currency rates, remain constant. The analysis was performed on the same basis for the year 2017.

	Effect on profit or loss	
	100 bp increase	100 bp decrease
2018		
Financial assets.....	22.382	(22.382)
Financial liabilities.....	(322.917)	322.917
	(300.535)	300.535
2017		
Financial assets.....	1.146	(1.146)
Financial liabilities.....	(348.283)	348.283
	(347.137)	347.137

Fair value

Fair value versus carrying amounts

The carrying amount of financial assets and non interest bearing liabilities is equal to their fair value. Comparison of fair value of interest bearing liabilities, together with the carrying amounts shown in the statement of financial position, is as follows:

	2018		2017	
	Carrying amount	Fair value	Carrying amount	Fair value
Interest bearing liabilities.....	40.364.632	46.495.192	43.535.405	44.596.158
	40.364.632	46.495.192	43.535.405	44.596.158

Interest rates used for determining fair value

The interest rates used to discount estimated cash flows, where applicable, are based on the government yield curve at the reporting date in the case of ISK denominated debt. For other debt the discount rates are based on interbank rates. All discount rates include a 2,2% credit spread (2017:2,5%) which is based on last transaction of Farice Bond (EFAR 09 1) in October 2018.

17. Related parties

The Company's related parties are shareholders, Board members, the CEO, and close family members of the aforementioned parties. No related parties purchased service from the company in 2018 and 2017 and the company did not buy any goods or service from related parties in 2018 and 2017.

The Company has a public service agreement with the Telecommunication Fund that belongs to one shareholder. Further information on the public service agreement can be found in note 5.

Notes, contd.:

18. Capital management

The Board's policy is to maintain a strong capital base to sustain future developments of the business.

The Company's Board of Directors seeks to maintain a balance between the higher returns that might be possible with higher levels of borrowings and the advantages and security afforded by a sound capital position. The equity ratio was 39% at year end 2018 (2017: 37%).

There were no changes in the Company's approach to capital management during the year and the Company is not obliged to comply with external rules on minimum equity other than those related to covenants in its loan agreements.

19. Operating leases

At 31 December, the future minimum lease payments under non-cancellable leases were payable as follows.

	2018	2017
Less than one year.....	283.268	307.328
Between one and five years.....	844.348	844.348
More than five years.....	323.820	607.070
	<u>1.451.436</u>	<u>1.758.746</u>

20. Significant accounting policies

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

A. Foreign currencies

Transactions in foreign currencies

Transactions in foreign currencies are translated to the functional currency of the Company at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the year. Foreign currency differences arising on translation are recognized in profit or loss. Non-monetary items that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction.

B. Revenues from contracts with customers

The Company has initially applied IFRS 15 from 1 January 2018. Information about the Company's accounting policies relating to contracts with customers is provided in Notes 4 and 5.

C. Employee benefits

Defined contribution plans

A defined contribution plan is a post-employment benefit plan under which an entity pays fixed contributions into a separate entity and will have no legal or constructive obligation to pay further amounts. Obligations for contributions to defined contribution pension plans are recognized as an employee benefit expense in profit or loss in the periods during which services are rendered by employees. Prepaid contributions are recognized as an asset to the extent that a cash refund or a reduction in future payments is available.

Notes, contd.:

D. Finance income and finance expenses

Interest income is recognised in the income statement as it accrues based on effective interest.

Finance expenses comprise interest expenses on borrowings and inflation indexation. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognised in the income statement using the effective interest method.

Foreign currency gains and losses on financial assets and financial liabilities are reported on a net basis as either finance income or finance cost depending on whether foreign currency movements are in a net gain or net loss position.

E. Income tax

Income tax expense comprises current and deferred tax. Income tax is recognised in profit or loss except to the extent that it relates to operating items recognised directly in equity or in other comprehensive income, in which case the income tax is recognised together with those items.

Current tax is the income tax estimated to be payable or receivable next year in respect of the taxable income or loss for the year, based on the tax rate at the reporting date, in addition to adjustments to tax payable in respect of previous years, if any.

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts 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 temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority.

A deferred tax asset is recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. 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 realized.

F. Operating assets

(i) Recognition and measurement

Items of operating assets are measured at cost less accumulated depreciation and accumulated impairment losses.

Cost includes expenditure that is 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 assets to a working condition for their intended use and capitalized borrowing costs. Purchased software that is integral to the functionality of the related equipment is capitalized as part of that equipment.

When operating assets consist of parts which have different useful lives, the parts are separated and depreciated based on the useful life of each part.

The gain on sale of operating assets, which is the difference between their sale proceeds and carrying amount, is recognised in the income statement among other operating income and the loss on sale among administrative expenses.

Notes, contd.:

F. Operating assets, contd.:

(ii) Subsequent costs

Costs of replacing single components of property and equipment is capitalised when it is considered likely that the benefits associated with the asset will flow to the Company and the costs can be measured reliably. The carrying amount of the replaced component is expensed. All other costs are expensed in the income statement as they are incurred.

(iii) Depreciation

Depreciation is calculated based on the depreciable amount, which is the cost less estimated residual value. Depreciation is calculated on a straight line basis over the estimated useful lives of each component of property and equipment. Leased assets are depreciated over the shorter of the lease term and their useful lives unless it is reasonably certain that the Company will obtain ownership by the end of the lease term. Estimated useful lives are specified as follows:

Point of Presence (PoP).....	10 years
Backhaul.....	10 years
Cable stations.....	20 years
Wet section.....	20 years
Common items.....	5 - 10 years

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

G. Financial instruments

(i) Recognition and initial measurement

Trade receivables and debt securities issued are initially recognised when they are originated. All other financial assets and financial liabilities are initially recognised when the Company becomes a party to the contractual provisions of the instrument.

A financial asset (unless it is a trade receivable without a significant financing component) or financial liability is initially measured at fair value plus, for an item not at FVTPL, transaction costs that are directly attributable to its acquisition or issue. A trade receivable without a significant financing component is initially measured at the transaction price.

(ii) Classification and subsequent measurement

Financial assets

On initial recognition, a financial asset is classified as measured at: amortised cost; FVOCI – debt investment; FVOCI – equity investment; or FVTPL.

Financial assets are not reclassified subsequent to their initial recognition unless the Company changes its business model for managing financial assets, in which case all affected financial assets are reclassified on the first day of the first reporting period following the change in the business model.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

All financial assets of the Company are measured at amortised cost.

Notes, contd.:

G. Financial instruments, contd.:

Financial assets at amortised cost

These assets are subsequently measured at amortised cost using the effective interest method. The amortised cost is reduced by impairment losses. Interest income, foreign exchange gains and losses and impairment are recognised in profit or loss. Any gain or loss on derecognition is recognised in profit or loss.

Financial liabilities

Financial liabilities are classified as measured at amortised cost using the effective interest method. Interest expense and foreign exchange gains and losses are recognised in profit or loss. Any gain or loss on derecognition is also recognised in profit or loss.

(iii) Derecognition

Financial assets

The Company derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

The Company enters into transactions whereby it transfers assets recognised in its statement of financial position, but retains either all or substantially all of the risks and rewards of the transferred assets. In these cases, the transferred assets are not derecognised.

Financial liabilities

The Company derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire. The Company derecognises a financial liability when its terms are modified and the cash flows of the modified liability are substantially different, in which case a new financial liability based on the modified terms is recognised at fair value.

On derecognition of a financial liability, the difference between the carrying amount extinguished and the consideration paid (including any non-cash assets transferred or liabilities assumed) is recognised in profit or loss.

iv. Offsetting

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

v. Cash and cash equivalents

Cash and cash equivalents comprise cash balances and call deposits with maturities of three months or less from the acquisition date that are subject to an insignificant risk of changes in their fair value, and are used by the Company in the management of its short-term commitments.

H. Share capital

(ii) Ordinary shares

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity, net of any tax effects.

Notes, contd.:

I. Impairment

(i) Financial assets

The Company recognises loss allowances for ECLs on financial assets measured at amortised cost. Loss allowances for trade receivables and contract assets are always measured at an amount equal to lifetime ECLs.

When determining whether the credit risk of a financial asset has increased significantly since initial recognition and when estimating ECLs, the Company considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Company's historical experience and informed credit assessment and including forward-looking information.

The Company assumes that the credit risk on a financial asset has increased significantly if it is more than 90 days past due. The credit risk related to financial assets is very low as the Company has never incurred significant impairment losses on financial assets.

(i) Financial assets

The maximum period considered when estimating ECLs is the maximum contractual period over which the Company is exposed to credit risk.

ECLs are a probability-weighted estimate of credit losses. Credit losses are measured as the present value of all cash shortfalls (i.e. the difference between the cash flows due to the entity in accordance with the contract and the cash flows that the Company expects to receive). ECLs are discounted at the effective interest rate of the financial asset.

(ii) Non-financial assets

At each reporting date, the Company reviews the carrying amounts of its non-financial assets to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Operating assets are tested annually for impairment.

J. Leases

(i) Determining whether an arrangement contains a lease

At inception of an arrangement, the Company determines whether the arrangement is or contains a lease.

At inception or on reassessment of an arrangement that contains a lease, the Company separates payments and other consideration required by the arrangement into those for the lease and those for other elements on the basis of their relative fair values. If the Company concludes for a finance lease that it is impracticable to separate the payments reliably, then an asset and a liability are recognised at an amount equal to the fair value of the underlying asset; subsequently, the liability is reduced as payments are made and an imputed finance cost on the liability is recognised using the Company's incremental borrowing rate.

Assets held under other leases are classified as operating leases and are not recognised in the statement of financial position.

(ii) Lease payments

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

Minimum lease payments made under finance leases are apportioned between the finance expense and the reduction of the outstanding liability. The finance expense is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability.

K. Fair value measurement

'Fair value' is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Company has access at that date. The fair value of a liability reflects its non-performance risk.

L. Segment reporting

An operating segment is a component of the Company that engages in business activities from which it may earn revenues and incur expenses, including revenues and expenses that relate to transactions with any of the Company's other components. All operating segments' operating results are reviewed regularly by the Company's management to make decisions about resources to be allocated to the segment and assess its performance, and for which discrete financial information is available. The Company's management considers the Company to have one segment.

21. Standards issued but not yet effective

A number of new standards, amendments to standards and interpretations are effective for annual periods beginning after 1 January 2019, and have not been applied in preparing these financial statements. Of those standards that are not yet effective, IFRS 16 is expected to have impact on the Company's financial statements in the period of initial application.

IFRS 16 Leases

The Company is required to adopt IFRS 16 Leases from 1 January 2019. IFRS 16 introduces a single, on-balance sheet lease accounting model for lessees. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are recognition exemptions for short-term leases and leases of low-value items. Lessor accounting remains similar to the current standard – i.e. lessors continue to classify leases as finance or operating leases.

Based on the information currently available, the Company estimates that it will recognise additional lease liabilities of EUR 1,4 million as at 1 January 2019. The company plans to apply IFRS 16 initially on 1 January 2019, using the modified retrospective approach. Therefore, the cumulative effect of adopting IFRS 16 will be recognised as an adjustment to the opening balance of retained earnings at 1 January 2019, with no restatement of comparative information.

Non Financial Reporting

Society

Farice plays an important role in Icelandic society by being the only Icelandic company providing telecommunication and transmission services to other countries. Our ambition is to continue to provide seamless services for the greater public good and economic life in Iceland. Protected service on our network delivered 100% availability in 2018 as in previous years. Single and unprotected routes availability taking into account faults and maintenance was 99.39% to 100%. The most significant threat to our network is cable damage on our submarine cables and therefore we have an agreement with a repair ship to be on standby.

Environment

Even though no formal policy is in place regarding the environment, Farice respects the environment and is committed to treating the environment with respect. Farice supports environmental protection and initiatives conceived to increase environmental responsibility. We are dedicated to minimising our environmental impact by using sustainable energy and other means available to us. One such particular example is that when the submarine cables Farice-1 and Danice were laid extensive seabed research was performed with the aim to reduce potential impact on the environment and fishing grounds. Our experience gained since has reinforced our confidence that this work was performed using best professional practices.

This year the company intends to undertake thorough seabed research for a possible third cable based on the same principles as before. Moreover, we expect this cable would be ploughed into the seabed and buried terrestrially using techniques which cause minimal disruption to the environment.

Employees

Farice has few employees and considering the importance of the company to Icelandic society it is of great importance to employ and retain competent employees. To achieve this, we offer a safe and healthy work environment and encourage as well as enable our employees to develop themselves through team work and training courses. We emphasise equal opportunities and non-discrimination. The company promotes open communication and a sustainable balance between work and personal life. We actively seek opportunities to improve our workplace gender balance and other features that can make it more likely to attract and retain the qualified human resources we depend on.

Human Rights, Anti-corruption and bribery

As stated before, Farice has few employees. There are no formal policies in place regarding human rights, anti-corruption and bribery. However, we view rights to life, liberty, equality, fair trial, freedom from slavery and torture, and freedom of thought and expression to be inherent in Farice's values.

Human rights violations or harassments are not tolerated. We emphasise equal opportunities and non-discrimination and have performed accordingly throughout our history.

Farice's policy is to conduct its business in an honest and ethical manner. We are committed to comply with relevant anti-bribery and anti-corruption legislation as well as following global standards regarding prevention of corruption and bribery.