

# Farice hf.

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Financial Statements

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2009

Farice hf.  
Smáratorgi 3  
201 Kópavogur  
kt. 580902-2190

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# Farice hf.

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## Financial Statements

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2009

Approved on board meeting April 30, 2010

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# Independent Auditor's Report

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To the Board of Directors and Shareholders of Farice hf.

We have audited the accompanying financial statements of Farice hf., which comprise the endorsement and signatures of the board of directors and the CEO, the statement of financial position as at 31 December 2009, and the statement of comprehensive income, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes.

## Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards as adopted by the EU. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

## 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 policies 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 Farice hf. as at 31 December 2009, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by EU.

## Emphasis of matter

Without qualifying our opinion, we draw attention to the discussion in the endorsement by the board of directors and the CEO and the notes to the financial statements regarding the financial restructuring and financial position of the Group. The Group was in breach of some of its loan agreements at year-end 2009 and accordingly, those loans are classified as short term loans in the balance sheet. The management has been working on a restructuring plan and expect to finish negotiating with the creditors in the second quarter of 2010. If restructuring of the Group cannot be completed successfully then the Company will not be able to continue as a going concern and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business. The financial statements are however prepared on a going concern basis.

Reykjavík, 30 April 2010.

KPMG hf.



Sign'vinn H. Sveinsson

# The Board of Directors' and CEO's Report

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The Financial Statements for the year 2009 comprise the financial statements of Farice hf. The Financial Statements are prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union (EU) and additional Icelandic disclosure requirements.

According to the Statement of Income, the Company's operating revenue amounted to EUR 4,7 million in the year 2009 (2008: EUR 6,7 million), and the loss of the year amounted to EUR 2,8 million (2008: EUR1,7 million). According to the statement of financial position, the Company's assets amounted to EUR 31,5 million at year end 2009 (at year end 2008: 35,4million). Equity amounted to EUR 5,8 million at the end of 2009 (at year end 2008: 8,6 million), or 18,5% of total assets (at year end 2008: 24,3%).

The number of shareholders in the Company and its subsidiary at year end 2009 were 7, the same as at year end 2008. Two shareholders had a holding interest of more than 10% in the Company; Eignarhaldsfélagið Farice ehf 79,9% and Telefonverkið P/F 19,9%.

In November 2009 the parent company, Eignarhaldsfélagið Farice ehf (E-Farice), signed agreements with a financial consulting company to undertake certain work to manage a financial restructuring process for Farice and E-Farice. The plan entails standstill agreements signed with the creditors of the Company and its parent, for the postponement of financial payments. This work is expected to be finished in the second quarter of 2010.

The management of the Company believes it is taking all the necessary measures to support the sustainability and growth of the Company's business. Accordingly they continue to adopt the going concern basis in preparing the annual report and financial statements. If restructuring of the Company cannot be completed successfully then the Company will not be able to continue as a going concern and therefore it may be unable to realize its assets and discharge its liabilities in the normal course of business.

Applicable legal provisions do not permit payment of dividend for the financial year 2009. The Board of Directors refers to the financial statement regarding appropriation of the loss for the period.

## **Statement of the Board of Directors and the CEO**

According to the Board of Director's best knowledge, these Financial Statements comply with IFRS as adopted by the EU, on Annual Accounts and give a true and fair view of the Company's assets and liabilities, financial position as at 31 December 2009, operating performance and the cashflow for the year ended 31 December 2009 as well as describing the principal risks and uncertainty factors faced by the company. The report of the Board of Directors provides a clear overview of developments and achievements in the company's operations and its situation.

The Board of Directors and CEO of Farice hf hereby confirm the Financial Statements of Farice hf for the year 2009 with their signatures.

Kópavogur, 30 April, 2010

**Board of directors**



Stefán Pétursson

Kristian R. Davidsen

Bjarni A. Bjarnason

Friðrik Friðriksson



Karl Alvarsson



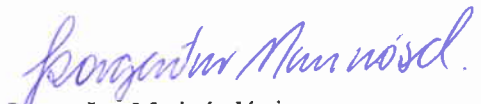
Hrönn Sveinsdóttir



Páll Ásgrímsson



Páll Erland



Þorgerður Marinósdóttir

**Chief Executive Officer**



Guðmundur Gunnarsson

# Statement of comprehensive income

For the year ended 31 December 2009

	Notes	2009	2008
Operating revenue .....	3	4.694.848	6.693.881
Operating expenses .....		(3.074.240)	(2.251.425)
Administrative expenses .....		(378.353)	(756.260)
Depreciation .....	8	(2.682.369)	(3.251.467)
<b>Operating profit</b>		<b>(1.440.114)</b>	<b>434.729</b>
Financial income .....	5	1.894	45.475
Financial expenses .....	5	(970.120)	(1.906.888)
Net loss before tax .....		(2.408.340)	(1.426.684)
Income tax .....	6	(385.082)	(270.848)
<b>Total comprehensive income for the period</b>		<b>(2.793.422)</b>	<b>(1.697.532)</b>
Basic net loss per share .....	7	(0,20)	(0,12)

During the years of 2009 and 2008 no items were recognised among other comprehensive income

The notes on pages 10-22 are an integral part of these financial statements

# Balance Sheet

Assets	Notes	31.12.2009	31.12.2008
<b>Non-current assets</b>			
Point of Presence .....	8	210.475	237.956
Backhaul .....	8	3.611.507	4.293.658
Cable stations .....	8	514.255	547.244
Farice 1 .....	8	24.181.241	25.908.468
Common items .....	8	447.161	646.162
Deferred tax asset .....	12	0	385.082
Prepaid lease .....		224.971	269.952
		<u>29.189.610</u>	<u>32.288.522</u>
<b>Current assets</b>			
Accounts receivable .....		116.073	132.631
Related parties receivable (E-Farice) .....		2.122.275	2.262.431
Other receivables .....		79.497	295.084
Bank deposits and cash .....		13.700	402.372
		<u>2.331.545</u>	<u>3.092.518</u>
<b>Total assets</b>		<u><u>31.521.155</u></u>	<u><u>35.381.040</u></u>

The notes on pages 10-22 are an integral part of these financial statements

## December 31, 2009

<b>Equity and liabilities</b>	<b>Notes</b>	<b>31.12.2009</b>	<b>31.12.2008</b>
<b>Equity</b>			
Share capital .....		13.689.662	13.689.662
Loss carry-forward .....		(7.868.932)	(5.075.510)
<b>Total equity</b>		<u>5.820.730</u>	<u>8.614.152</u>
<b>Non-current liabilities</b>			
Non-current liabilities .....	10	0	20.679.999
		<u>0</u>	<u>20.679.999</u>
<b>Current liabilities</b>			
Current and due maturities .....	10	23.652.083	4.286.667
Accounts payable .....		677.328	611.262
Interest rate swaps .....	14	1.017.499	733.261
Other liabilities .....		353.515	455.699
		<u>25.700.425</u>	<u>6.086.889</u>
<b>Total liabilities</b>		<u>25.700.425</u>	<u>26.766.888</u>
<b>Total equity and liabilities</b>		<u>31.521.155</u>	<u>35.381.040</u>

The notes on pages 10-22 are an integral part of these financial statements



## Statement of changes in Equity for the year ended December 31, 2009

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	Share capital	Loss carry-forward	Total equity
Balance at January 1, 2008.....	13.689.662	(3.377.978)	10.311.684
Net loss for the year.....		<u>(1.697.532)</u>	<u>(1.697.532)</u>
Balance at January 1, 2009.....	13.689.662	(5.075.510)	8.614.152
Net loss for the year.....	0	<u>(2.793.422)</u>	<u>(2.793.422)</u>
Balance at December 31, 2009.....	<u>13.689.662</u>	<u>(7.868.932)</u>	<u>5.820.730</u>

The notes on pages 10-21 are an integral part of these financial statements

# Statement of Cash Flows for the year 2009

For the year ended 31 December

	2009	2008
<b>Cash flows from operating activities</b>		
Profit (loss) for the period .....	(2.793.422)	(1.697.532)
Adjustments for :		
Depreciation .....	2.682.369	3.259.893
Changes in current assets and liabilities .....	185.666	(211.893)
Net finance cost .....	968.226	1.861.413
Income tax expense .....	385.082	270.848
<b>Cash generated from operating activities</b>	<u>1.427.921</u>	<u>3.482.729</u>
Interest paid .....	(649.977)	(1.141.684)
Income tax paid .....	0	0
<b>Net cash from operating activities</b>	<u>777.944</u>	<u>2.341.045</u>
<b>Investing activities</b>		
Investment in fixed assets .....	(13.520)	(58.988)
Related parties .....	140.156	
Disposal of assets .....	0	26.379
	<u>126.636</u>	<u>(32.609)</u>
<b>Financing activities</b>		
Long-term liabilities repaid .....	<u>(1.314.583)</u>	<u>(2.200.000)</u>
Increase (decrease) in cash and cash equivalents .....	(410.003)	108.436
Effects of foreign exchange adjustments .....	21.331	48.170
Cash and cash equivalents at beginning of the year .....	<u>402.372</u>	<u>245.766</u>
Cash and cash equivalents at end of the year .....	<u>13.700</u>	<u>402.372</u>

The notes on pages 10-22 are an integral part of these financial statements

# Notes to Financial Statements

## 1. General information

Farice hf. is a limited company incorporated in Iceland. Farice is the communications link for the nations of Iceland and the Faroe Islands. The Company's mission is to assure continuous and secure connectivity for enterprise, governments, and the citizens of Iceland. Farice hf is a subsidiary of Eignarhaldsfélagið Farice ehf. which owns 79,9% of shares in Farice hf. Daily activities are run by the management of Eignarhaldsfélagið Farice ehf.

The company has operations in Iceland, the Faroe Islands and the United Kingdom. The income originates in Iceland and the Faroe Islands while the operating expenses originate in all three countries.

### Adoption of new and revised standards

#### Standards and interpretations effective in the current period

The Consolidated Financial Statements are presented in accordance with the new and revised standards (IFRS / IAS) and new interpretations (IFRIC), applicable in the year 2008. These standards and interpretations are:

IFRS 2 (revised 2008) -	Share-based Payment (effective for accounting periods beginning on or after 1 January 2009);
IFRS 7 (revised 2008)	Financial instruments: Disclosures (effective for accounting periods beginning on or after 1 January 2009);
IFRS 8 -	Operating segments: (effective for accounting periods beginning on or after 1 January 2009);
IAS 1 - (revised 2008)	Presentation of Financial Statements (effective for accounting periods beginning on or after 1 January 2009);
IAS 23 (revised 2008) -	Borrowing Costs (effective for accounting periods beginning on or after 1 January 2009);
IAS 32 (revised 2008) -	Financial Instruments: Presentation (effective for accounting periods beginning on or after 1 January 2009);

Minor changes to various standards as a result of the IASB's annual improvement measures (2008). Most changes take effect for periods beginning 1 January 2009 or later.

IFRIC 13 -	Customer Loyalty Programs (effective for accounting periods beginning on or after 1 July 2008);
IFRIC 15 -	Agreements for the Construction of Real Estate (effective for accounting periods beginning on or after 1 January 2009);
IFRIC 16 -	Hedges of a Net Investment in a Foreign Operation (effective for accounting periods beginning on or after 1 October 2008);

The amendments to IFRS 2 - Share-based Payment clarify the definition of vesting conditions and the accounting treatment of cancellations by the counterparty to a share-based payment arrangement.

The amendments to IFRS 7 - Financial Instruments: Disclosures expand the disclosures required in respect of fair value measurements recognised in the Balance Sheet. For the purpose of these expanded disclosures, a three-level hierarchy has been introduced. The amendments also require enhanced liquidity risk disclosures.

According to IFRS 8 - Operating Segments an entity shall disclose information to enable users of its financial statements to evaluate the nature and financial effects of the business activities in which it engages and the economic environments in which it operates. IFRS 8 supersedes IAS 14 - Segment Reporting from date of application.

The text of IAS 1 - Presentation of Financial Statements has been substantially rewritten, with many changes in terminology. The most significant effects of the amendments is the introduction of a statement of comprehensive income for the presentation of 'other comprehensive income' or non-owner movements (e.g. gains and losses on revaluation of property, plant and equipment) separately for the statement of changes of equity. All items of income and expense (including those recognised outside of profit and loss must be presented either in a single statement of comprehensive income or in two statements, a separate income statement and a statement of comprehensive income.

# Notes to Financial Statements

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The amendments to IAS 23 - Borrowing costs eliminate the option available under the previous version of the Standard to recognise all borrowing costs immediately as an expense. To the extent that borrowing costs relate to the acquisition, construction or production of a qualifying asset, the revised standard requires that they be capitalised as part of the cost of that asset. All other borrowing costs should be expensed as incurred.

The amendments to IAS 32 - Financial Instruments: Presentation address the classification of puttable financial instruments and obligations arising only on liquidation.

IFRIC 13 - Customer Loyalty Programmes. This interpretation addresses the accounting by entities that provide their customers with incentives to buy goods or services by providing award credits as part of a sales transaction. IFRIC 13 requires the entity that grants the awards to account for the sales transaction that gives rise to the award credits as a 'multiple-element revenue transaction' and to allocate the fair value of the consideration received or receivable between the award credits granted and the other components of the revenue transaction. Common examples are airline and hotel loyalty schemes.

IFRIC 15 - Agreements for the Construction of Real Estate. The interpretation addresses the accounting for revenue and associated expenses by entities that undertake the construction of real estate directly or through subcontractors. IFRIC 15 addresses two (related) issues, determining whether an agreement for the construction of real estate is within the scope of IAS 11 - Construction Contracts or IAS 18 - Revenue, and when revenue from the construction of real estate should be recognised.

IFRIC 16 - Hedges of a Net Investment in a Foreign Operation. The interpretation clarifies three main issues, the first issue is that the presentation currency does not create an exposure to which an entity may apply hedge accounting. Consequently, a parent entity may designate as a hedged risk only the foreign exchange differences arising from a difference between its own functional currency and that of its foreign operation. The second issue is that the hedging instrument(s) may be held by any entity or entities within the group except for the entity being hedged as long as the designation and effectiveness requirements for a hedge of a net investment are satisfied. The third issue is that when a foreign operation is disposed of, IAS 39 must be applied to determine the amount that needs to be reclassified to profit or loss from the foreign currency translation reserve in respect of the hedging instrument, while IAS 21 must be applied in respect of the hedged item.

## Standards and interpretations in issue not yet adopted

Following is an overview of new or revised standards and interpretations that are not yet effective:

IFRS 1 (revised 2008) -	First-time adoption of International Financial Reporting Standards (effective for accounting periods beginning on or after 1 July 2009);
IFRS 2 (revised 2008) -	Share-based Payment (effective for accounting periods beginning on or after 1 January 2010);
IFRS 3 (revised 2008) -	Business combinations (effective for accounting periods beginning on or after 1 July 2009);
IFRS 9 -	Financial Instruments: Classification and Measurement (effective for accounting periods beginning on or after 1 January 2013);
IAS 24 (revised 2009) -	Related Party Disclosures (effective for accounting periods beginning on or after 1 January 2011);
IAS 27 (revised 2008) -	Consolidated and separate Financial Statements (effective for accounting periods beginning on or after 1 July 2009);
IAS 32 (revised 2009) -	Financial Instruments: Presentation (effective for accounting periods beginning on or after 1 February 2009);
IAS 39 (revised 2008) -	Financial Instruments: Recognition and measurement (effective for accounting periods beginning on or after 1 July 2009);
IFRIC 14 (revised 2009) -	IAS 19 - The limit on a Defined Benefit Asset, Minimum Funding Requirements and their Interaction (effective for accounting periods beginning on or after 1 January 2011);

# Notes to Financial Statements

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## Adoption of new and revised standards (continued)

IFRIC 17 -	Distributions of Non-cash Assets to Owners (effective for accounting periods beginning on or after 1 July 2009);
IFRIC 18 -	Transfers of Assets from Customers (effective for accounting periods beginning on or after 1 July 2009);
IFRIC 19 -	Extinguishing Financial Liabilities with Equity Instruments (effective for accounting periods beginning on or after 1 July 2010);

Revised IAS 1 will have the impact that all items of income and expense (including those recognised outside of profit or loss) must be presented either in a single statement as a statement of comprehensive income; or in two statements as a separate income statement and a statement of comprehensive income.

Revised IAS 23 eliminates the previously available option to expense all borrowing costs when incurred. This revision will not have any impact on these Financial Statements because it has always been the Company's accounting policy to capitalise borrowing costs incurred on qualifying assets.

Revised IFRS 3 states that all acquisition-related costs are to be recognised as period expenses. Implementation may also mean a change in accounting for the recognition of goodwill related to the minority share of the purchased companies, step acquisitions and partial disposal of shares in subsidiaries.

It is the management's assessment that the adoption of those new and revised standards and interpretations will have no material impact on the Financial Statements. The above new or revised standards and interpretations have not yet been approved by the EU.

## 2. Significant accounting policies

### Statement of compliance

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

### Basis of preparation

The Consolidated Financial Statements are prepared under the historical cost basis except for certain financial instruments. These Financial Statements are presented in euros which is the functional currency of the Company.

The principal accounting policies adopted are set out below.

### Basis of consolidation

The Consolidated Financial Statements incorporate the financial statements of the Company and enterprises controlled by the Company (its subsidiaries). Control is achieved where the Company has the power to govern the financial and operating policies of an investee enterprise so as to obtain benefits from its activities.

All intra-group transactions, balances, income and expenses are eliminated in full on consolidation.

Minority interests in the net assets of consolidated subsidiaries are identified separately from the Company's equity therein. Minority interests consist of the amount of those interests at the date of the original business combination and the minority's share of changes in equity since the date of the combination. Losses applicable to the minority in excess of the minority's interest in the subsidiary's equity are allocated against the interests of the Company except to the extent that the minority has a binding obligation and is able to make an additional investment to cover the losses.

### Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable and represents amounts receivable for goods and services provided in the normal course of business, net of discounts, VAT and other sales related taxes.

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate

# Notes to Financial Statements

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applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

Dividend income from investments is recognised when the shareholders' rights to receive payment have been established.

## Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised as assets of the Company at their fair value at the inception of the lease or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance charges and reduction of the lease obligation so as to achieve a constant rate of interest on the remaining balance of the liability. Finance charges are charged directly to profit or loss, unless they are directly attributable to qualifying assets, in which case they are capitalised in accordance with the Company's general policy on borrowing costs. Contingent rentals are recognised as expenses in the periods in which they are incurred.

## Foreign currencies

Transactions in currencies other than euros are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are recognised in profit or loss in the period in which they arise.

## Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, which are assets that necessarily take a substantial period of time to get ready for their intended use or sale, are added to the cost of those assets, until such time as the assets are substantially ready for their intended use or sale.

All other borrowing costs are recognised in profit or loss in the period in which they are incurred.

## Taxation

The tax expense represents the sum of the tax currently payable and deferred tax.

The income tax currently payable is based on taxable profit for the year. Taxable profit differs from net profit as reported in the income statement because it excludes items of income or expense that are taxable or deductible in other periods and it further excludes items that are never taxable or deductible. The consolidated liability for current tax is calculated using tax rates that have been enacted or substantively enacted by the balance sheet date.

Deferred tax is the tax expected to be payable or recoverable on differences between the carrying amount of assets and liabilities in the financial statements and the corresponding tax bases used in the computation of taxable profit, and is accounted for using the balance sheet liability method. Deferred tax liabilities are generally recognised for all taxable temporary differences and deferred tax assets are recognised to the extent that it is probable that taxable profits will be available against which deductible temporary differences can be utilised. Such assets and liabilities are not recognised if the temporary difference arises from goodwill or from the initial recognition (other than in a business combination) of other assets and liabilities in a transaction that affects neither the tax profit nor the accounting profit. Deferred tax assets and liabilities are offset when they relate to income taxes levied by the same taxation authority and the Company's intends to settle its current tax assets and liabilities on a net basis.

The carrying amount of deferred tax assets is reviewed at each balance sheet date and reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow all or part of the asset to be recovered.

# Notes to Financial Statements

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Deferred tax is calculated at the tax rates for each country that are expected to apply in the period when the liability is settled or the asset is realized. Deferred tax is charged or credited in the income statement, except when it relates to items charged or credited directly to equity, in which case the deferred tax is also dealt with in equity.

## 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 shares outstanding during the period, adjusted for own shares held. Diluted EPS is determined by adjusting the profit or loss attributable to ordinary shareholders and the weighted average number of ordinary shares outstanding, adjusted for own shares held, for the effects of all dilutive potential ordinary shares, which comprise convertible notes and share options granted to employees.

## Property, plant and equipment

Property, plant and equipment are recognised as an asset when it is probable that future economic benefits associated with the asset will flow to the company and the cost of the asset can be measured in a reliable manner. Property, plant and equipment are stated at cost less accumulated depreciation and impairment losses. Cost includes professional fees and, for qualifying assets, borrowing costs capitalised in accordance with the Company's accounting policy.

Depreciation is charged so as to write off the cost or valuation of assets, other than properties under construction, over their estimated useful lives, using the straight-line method.

Assets held under finance leases are depreciated over their expected useful lives on the same basis as owned assets or, where shorter, the term of the relevant lease.

The gain or loss arising on the disposal or retirement of an item of property, plant and equipment is determined as the difference between the sales proceeds and the carrying amount of the asset and is recognised in profit or loss.

## Impairment of tangible assets

At each balance sheet date, the company reviews the carrying amounts of its tangible assets to determine whether there is any indication that those assets have suffered an impairment loss. If any such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss (if any). Where it is not possible to estimate the recoverable amount of an individual asset, the Company estimates the recoverable amount of the cash-generating unit to which the asset belongs.

Recoverable amount is the greater of net selling price and value in use. 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.

If the recoverable amount of an asset is estimated to be less than its carrying amount, the carrying amount of the asset is reduced to its recoverable amount. Impairment losses are recognised as an expense immediately.

Where an impairment loss subsequently reverses, the carrying amount of the asset is increased to the revised estimate of its recoverable amount, but so that the increased carrying amount does not exceed the carrying amount that would have been determined had no impairment loss been recognised for the asset in prior years. A reversal of an impairment loss is recognised as income immediately, unless the relevant asset is carried at a revalued amount, in which case the reversal of the impairment loss is treated as a revaluation increase.

## Financial assets

Accounts receivable and other receivables are valued at nominal value less any impairment losses.

Financial assets are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted.

# Notes to Financial Statements

## Financial liabilities

### Long-term liabilities

Long-term liabilities are valued at amortised cost less payments made and the remaining nominal balance is adjusted by exchange rate or index, if applicable. Interest expense is accrued on a periodical basis, based on the principal outstanding and at the interest rate applicable.

### Accounts payable and other liabilities

Accounts payable and other liabilities are valued at fair value.

## 3. Operating revenue

Net sales are specified as follows:

	31.12.2009	31.12.2008
Lease of bandwidth - Farice 1 .....	4.694.848	6.576.529
Other income .....	0	117.352
	<u>4.694.848</u>	<u>6.693.881</u>

## 4. Salaries

Salaries and salary-related expenses paid by the Company are specified as follows:

	31.12.2009	31.12.2008
Salaries.....	136.568	286.120
Pension fund.....	14.912	34.213
Salary-related expenses .....	18.762	38.380
Other employee expenses.....	(311)	2.429
	<u>169.931</u>	<u>361.142</u>
Average number of positions.....	1,5	1,3

## 5. Financial income / (expenses)

	31.12.2009	31.12.2008
Interest income.....	1.894	45.475
	<u>1.894</u>	<u>45.475</u>
Interest expenses and borrowing costs.....	(649.789)	(1.397.114)
Exchange rate differences.....	(36.091)	223.487
Fair value changes of interest rate swaps.....	(284.240)	(733.261)
	<u>(970.120)</u>	<u>(1.906.888)</u>



# Notes to Financial Statements

## 6. Income tax

Income tax is specified as follows:

	2009		2008	
	Amount	%	Amount	%
Deferred tax (expenses) / revenue .....	(385.082)		(270.848)	
	(385.082)		(270.848)	
Net loss before tax .....	(2.408.340)		(1.426.684)	
Tax at the rate of 15% .....	361.251	-15%	214.003	15%
Effect of different tax rates of other jurisdictions .....	443	0%	10.760	-1%
Change in tax rate .....	96.906	-4%	(99.121)	7%
Exchange differences .....	(103.218)	4%	(396.490)	28%
Effect of write-down of deferred tax asset .....	(740.464)	31%		0%
Income tax according to income statement .....	(385.082)	16%	(270.848)	19%

In December 2009 the Icelandic Parliament approved to increase the income tax rate from 15% to 18% as of 1 January 2010. The effect on the Income Statement due to changes in tax rates amount to 96.906.

A deferred tax asset has not been recognised in respect of tax losses on the operation in 2009 due to uncertainty of when the tax loss can be utilized against future profits. Tax assets recognised in previous years have been impaired for the same reason.

## 7. Earnings per share

The calculation of Earnings per share is based on the following data:

	31.12.2009	31.12.2008
Net loss for the year .....	(2.793.422)	(1.697.532)
Total average number of shares including potential shares .....	13.689.662	13.689.662
Basic and diluted net loss per share .....	(0,20)	(0,12)

## Notes to Financial Statements

### 8. Property, plant and equipment

	Point of presence	Backhaul	Cable stations	Farice 1	Common Items
<b>Cost</b>					
At January 1, 2008 .....	365.669	6.838.953	993.609	34.544.546	4.411.748
Additions .....					58.988
Disposals .....					(40.161)
At January 1, 2009 .....	365.669	6.838.953	993.609	34.544.546	4.430.575
Additions .....	5.952		12.287		
Disposals .....					(4.719)
At December 31, 2009 .....	371.621	6.838.953	1.005.896	34.544.546	4.425.856
<b>Accumulated depreciation</b>					
At January 1, 2008 .....	94.548	1.863.144	356.940	6.908.851	3.070.270
Charge for the year .....	33.165	682.151	89.425	1.727.227	719.499
Disposals .....					(5.356)
At January 1, 2009 .....	127.713	2.545.295	446.365	8.636.078	3.784.413
Charge for the year .....	33.433	682.151	45.276	1.727.227	194.282
At December 31, 2009 .....	161.146	3.227.446	491.641	10.363.305	3.978.695
<b>Carrying Amount</b>					
At December 31, 2009 .....	210.475	3.611.507	514.255	24.181.241	447.161
At January 1, 2009 .....	237.956	4.293.658	547.244	25.908.468	646.163

The following useful lives are used in the calculation of depreciation.

Point of Presence (PoP) .....	10 years
Backhaul .....	10 years
Cable stations .....	20 years
Farice 1 .....	20 years
Common items .....	5-10 years

### 9. Share capital

Common stock is as follows:

	Shares	Ratio	Nominal value
Total share capital at period-end .....	13.689.662	100,0%	13.689.662
Own shares.....	0	0,0%	0
	13.689.662	100,0%	13.689.662

Each share of one euro carries one vote. No dividends were paid during the year

# Notes to Financial Statements

## 10. Long-term liabilities

Terms and conditions of outstanding loans were as follows in original terms of loan facilities

	Currency	Nominal interest rate	Year of maturity	31.12.2009	31.12.2008
Secured bank loan .....	EUR	Libor+0,18-1,5	2011-2015	23.652.083	24.966.666
				<u>23.652.083</u>	<u>24.966.666</u>
Current and overdue maturities .....				(23.652.083)	(4.286.667)
Loans from credit institutions .....				<u>0</u>	<u>20.679.999</u>

Aggregated annual maturities are as follows:

Current and overdue maturities .....	23.652.083	4.286.667
Installments 2011/2010 .....	0	5.640.000
Installments 2012/2011 .....	0	6.815.000
Installments 2013/2012 .....	0	2.350.000
Installments 2014/2013 .....	0	2.350.000
Installments 2015/2014 .....	0	2.350.000
Installments later.....	0	1.175.000
	<u>23.652.083</u>	<u>24.966.667</u>

Guarantees on longterm liabilities:

	31.12.2009	Guarantor
Secured bank loans A-term.....	9.400.000	Icelandic State
Secured bank loans B-term.....	9.400.000	Skipti hf
Secured bank loans C-term.....	4.700.000	Foroya Tele
Secured bank loans D-term.....	152.083	
	<u>23.652.083</u>	

The Bank loans are also guaranteed with 1st. ranking securities in the Farice cable, landing stations and accounts receivables.

According to IAS1, when an entity breaches a provision of a long-term loan arrangement on or before the end of the reporting period with the effect that the liability becomes payable on demand, it classifies the liability as current, even if the lender agreed, after the reporting period and before the authorisation of the financial statements for issue, not to demand payment as a consequence of the breach.

The terms of a loan facilities include various provisions that limits certain actions by the company without prior consulting with the lender. In addition the loan facilities include certain financial covenants.

At the end of 2009, the Company was in breach of some of its loan agreements and therefore the full amount of the relevant loans can be called in. Accordingly, these loans are classified as short term loans in the balance sheet. Failure to reach an agreement on new terms with the Company's creditors will result in insolvency.

The mother Company has been working on a restructuring plan for the Company and its subsidiary. The plan entails standstill agreements signed with the creditors of the Company and its subsidiary, for the postponement of financial payments. This work is expected to be finished in the second quarter of 2010. The management is confident that the restructuring plan will be completed successfully, securing the future operations of the company.

# Notes to Financial Statements

## 11. Interest rate swaps

In the year 2004 the Company entered into Interest Rate Swap Agreements with Landsbanki Íslands hf. and Glitnir hf. In the year end the contracts' estimated fair value is negative by EUR 1,0 million and the principal amounting to EUR 23,5 million. In October 2008, the Icelandic Financial Supervisory Authority (the "FSA") used powers granted by the Icelandic Parliament, to take control of the Banks. Substantial part of the Banks' assets and operations were transferred to new banks. The transfer of assets from the Banks to the New Banks included all long term loan agreements. However, as a general rule, no derivative contracts were transferred from the Banks to the New Banks, including Interest Rate Swap Agreements. In November 2008, the District Court of Reykjavik granted the Banks a moratorium. The legal position of the agreements is uncertain and therefore the final treatment of the Interest Rate Swap Agreements is subject to uncertainty.

## 12. Deferred tax

Deferred tax assets and liabilities are attributable to the following:

There is no deferred income tax liability credited in the balance sheet due to taxation loss carry forward, even though income tax liability is related to some individual items of the balance sheet. The following are the major deferred tax liabilities and assets.

2009	Assets	Liabilities	Net
Non-current assets.....		1.178.131	(1.178.131)
Interest rate swaps.....	183.150		183.150
Exchange rate difference of losses.....	(27.460)		(27.460)
Tax loss carry forwards.....	1.859.309		1.859.309
Impairment of tax asset.....	(836.868)		(836.868)
Tax assets liabilities.....	<u>1.178.131</u>	<u>1.178.131</u>	<u>0</u>
2008	Assets	Liabilities	Net
Non-current assets.....		1.198.682	(1.198.682)
Interest rate swaps.....	109.989		109.989
Exchange rate difference of losses.....	(396.490)		(396.490)
Tax loss carry forwards.....	1.870.266		1.870.266
Tax assets liabilities.....	<u>1.583.765</u>	<u>1.198.682</u>	<u>385.082</u>

At balance sheet date the Company has unused tax losses available for offset against future profits as follows:

Available for the year 2012 .....	15.718
Available for the year 2013 .....	1.340.348
Available for the year 2014 .....	2.536.371
Available for the year 2015 .....	2.410.874
Available for the year 2016 .....	353.147
Available for the year 2017 .....	459.043
Available for the year 2018 .....	633.208
Available for the year 2019 .....	2.393.573
	<u>10.142.282</u>

# Notes to Financial Statements

## 13. Financial risk Categories of financial instruments

Financial assets	31.12.2009	31.12.2008
Bank deposits and cash .....	13.700	402.372
Loans and receivables .....	2.317.845	2.690.146
<b>Financial liabilities</b>	<b>31.12.2009</b>	<b>31.12.2008</b>
Other financial liabilities at amortised cost .....	25.700.425	26.766.888

### Financial risk management objectives

The Company's management monitors and manages the financial risks relating to the operations of the Company. These risks include market risk (including currency risk, interest rate risk and price risk), credit risk and liquidity risk. The Company seeks to minimise the effects of these risks for example by using derivative financial instruments to hedge these risk exposures. The Company does not enter into or trade financial instruments, including derivative financial instruments, for speculative purposes.

### Interest rate risk

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 floating rate interest bearing financial instruments and has entered into a variety of interest rate swaps to hedge its exposure to interest rate fluctuations. The interest rate swaps are not active at year end.

### Sensitivity analysis

In the analysis below the effects of 50 and 100 basis points decrease on P/L and equity are demonstrated. The sensitivity analysis below have been determined based on the exposure to interest rates at the balance sheet date. The analyses 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 basis points, are held constant. The sensitivity analysis does not take into account tax effects. A positive number below indicates an increase in profit and other equity. An increase in basis points would have an opposite impact on income statement and equity.

	31.12.2009		31.12.2008	
	50 bps.	100 bps.	50 bps.	100 bps.
Effects on P/L and equity .....	(100.463)	(200.926)	(122.821)	(245.643)

# Notes to Financial Statements

## Foreign currency risk

Foreign 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.

Foreign currency risk 31.12 2009	Assets	Liabilities	Net balance
GBP .....	84.920	9.477	75.443
ISK .....	3.420	32.047	-28.627
DKK .....	234	114.952	-114.718
USD .....	873	0	873
Foreign currency risk 31.12 2008	Assets	Liabilities	Net balance
GBP .....	434.693	55.810	378.883
ISK .....	10.059	150.722	-140.663
DKK .....	61.676	99.879	-38.203
USD .....	4.302	0	4.302

## Sensitivity analysis

The table below shows what effects 5% and 10% increase of the relevant foreign currency rate 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. The sensitivity analysis does not take into account tax effects. 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.

Effects on P/L and equity	31.12.2009		31.12.2008	
	5%	10%	5%	10%
GBP .....	3.772	7.544	18.944	37.888
ISK .....	(1.431)	(2.863)	(7.033)	(14.066)
DKK .....	(5.736)	(11.472)	(1.910)	(3.820)
USD .....	44	87	215	430

## Credit risk

Credit risk is the risk of a financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Company's receivables from customers and investments securities

Maximum credit risk:

	Carrying amounts	
	31.12.2009	31.12.2008
Accounts receivables .....	116.073	132.631
Related parties receivables .....	2.122.275	2.262.431
Other receivables .....	79.497	295.084
Cash and cash equivalents .....	13.700	402.372
	<u>2.331.545</u>	<u>3.092.518</u>

No write-downs were recognised during the year of 2009.

# Notes to Financial Statements

## Liquidity risk management

Liabilities 31.12.2009	Carrying amount	Contractual cash flows	Within one year	2011	2012+
Non-interest bearing .....	2.048.342	2.048.342	2.048.342	0	0
Floating interest rates .....	23.652.083	24.279.380	8.910.089	6.943.929	8.425.362
	<u>25.700.425</u>	<u>26.327.722</u>	<u>10.958.431</u>	<u>6.943.929</u>	<u>8.425.362</u>
Assets 31.12.2009					
Non-interest bearing .....	2.317.845	2.317.845	2.317.845	0	0
Floating interest rates .....	13.700	13.700	13.700	0	0
	<u>2.331.545</u>	<u>2.331.545</u>	<u>2.331.545</u>	<u>0</u>	<u>0</u>
Net balance 31.12 2009	<u>(23.368.880)</u>	<u>(23.996.177)</u>	<u>(8.626.886)</u>	<u>(6.943.929)</u>	<u>(8.425.362)</u>
Liabilities 31.12 2008	Total	Contractual cash flows	Within one year	2010	2011+
Non-interest bearing .....	1.800.222	1.800.222	1.800.222	0	0
Floating interest rates .....	24.966.666	26.206.887	4.513.285	5.927.523	15.766.079
	<u>26.766.888</u>	<u>28.007.109</u>	<u>6.313.507</u>	<u>5.927.523</u>	<u>15.766.079</u>
Assets 31.12 2008					
Non-interest bearing .....	2.690.146	2.690.146	2.690.146	0	0
Floating interest rates .....	402.372	402.372	402.372	0	0
	<u>3.092.518</u>	<u>3.092.518</u>	<u>3.092.518</u>	<u>0</u>	<u>0</u>
Net balance 31.12 2008	<u>(23.674.370)</u>	<u>(24.914.591)</u>	<u>(3.220.989)</u>	<u>(5.927.523)</u>	<u>(15.766.079)</u>

## 14. Approval of Financial Statements

The Financial Statements were approved by the Board of Directors and authorised for issue on 30 April, 2010.