Orkuveita Reykjavíkur

Consolidated
Financial Statements 2019

*These Financial statements are translated from the original which is in Icelandic. Should there be discrepancies between the two versions, the Icelandic version will take priority over the translated version.

Orkuveita Reykjavíkur
Bæjarháls 1
110 Reykjavík

reg no. 551298-3029

Contents

Endorsement by the Board of Directors and the CEO

Orkuveita Reykjavíkur is a partnership that complies with the Icelandic law no.136/2013 on the founding of the partnership Orkuveita Reykjavíkur. The Group provides services through its subsidiaries that operate power plants, distribute electricity, hot water and cold water, operates the sewage systems in its service area as well as a fiber optic system in its service area.

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS´s) as adopted by the European Union and the additional requirements set out in the local rules and regulations regarding financial statements of companies with listed bonds. The financial consolidated statements comprise the financial statements of Orkuveita Reykjavikur and its subsidiaries.

Profit of operations of the Group for the year was ISK 6.916 million (2018: ISK 5.978 million). Comprehensive income for the year was ISK 22.972 million (2018: ISK 18.844 million). According to the statement of financial position the Group's assets were ISK 369.884 million at the end of the year (31.12.2018: ISK 340.089 million). Book value of equity at the end of the year was ISK 182.299 million (31.12.2018: ISK 160.827 million), resulting in equity ratio of 49,3% (31.12.2018: 47,3%).

At the beginning of the year and at the end of the period the Company´s shareholders were the following three municipalities:

	Share
Reykjavíkurborg	93,539%
Akraneskaupstaður	5,528%
Borgarbyggð	0,933%

The Board of Directors will propose at the 2020 Annual General Meeting that dividend amounting to ISK 1.750 million will be paid for the operational year 2019, and refers to the Consolidated Financial Statements regarding appropriation of the profit for the year and changes in Shareholders' equity.

Changes in the Group

On January 1, 2019, Orka náttúrunnar ohf.'s operations were divided into two companies, on the one hand, Orka náttúrunnar ohf., which has the functional currency of the ISK and, on the other, ON Power ohf., which has the functional currency of the US dollar.

Orka náttúrunnar's activities include the production of electricity and hot water in Andakílsárvirkun and Nesjavallavirkjun, the purchase and sale of electricity for households and companies in the general and wholesale markets, the operation of geothermal exhibitions, street lighting and charging stations.

ON Power's activities include the production of electricity and hot water in Hellisheiðarvirkun, the purchase and sale of electricity in the wholesale market, the sale of electricity to foreign users in foreign currency, as well as the operation and development of the geothermal garden.

In December 2019, a subsidiary, Carbfix ohf., was established, which aims to promote the further development and expansion of the Carbfix carbon sequestration process with the aim of reducing greenhouse gas emissions and combating climate change.

Corporate governance

The Board maintains and seeks to improve good corporate governance. Corporate governance is directed by law no. 136/2013, collective ownership contract, owners' policy and the Board's operating procedure. The procedures also take into account the company´s moral guidelines, Guidelines on corporate governance, which were issued by the Icelandic Chamber of Commerce, Nasdaq OMX Iceland ehf. and SA - Business Iceland and a handbook for board members, issued by KPMG. Subsidiaries have their separate company agreements and their Board´s procedures. These documents can be found on the Company´s website, www.or.is. The Board of Orkuveita Reykjavíkur has appointed a Compensation committee and has nominated a representative in Reykjavík City´s Audit committee.

The principal operations of Orkuveita Reykjavíkur (OR) are governed by Act no.136/2013. The corporate governance of OR should ensure professionalism, efficiency, cost effectiveness, transparency and responsible management. The partnership agreement and ownership policy can be viewed on OR's website www.or.is. Moreover, the Board of Directors of OR and the boards of directors of the subsidiaries in the Group have established precise working rules and a code of conduct, which can also be found on the company's website.

The Board of directors

In accordance with the law on undertakings, the Board of Directors of OR comprises six members, five elected by the City Council of Reykjavik and one elected by the town council of Akranes. Borgarbyggd has an observer on the board. The City Council of Reykjavik elects a chairperson and vice-chairperson to the board from a group of members of the City Council of Reykjavik. The Board of Directors is responsible for the finances and operations of OR. The board of Directors appoints two committees; The Audit Committee and The Compensation Committee.

In conjunction with the annual accounts, OR publishes the Annual Report 2019, which includes a more detailed description of OR's governance practices. The report can be found on the URL arsskyrsla2019.or.is

Information on the Company´s risk management can be found in notes 28-32 to the financial statements.

Non-financial information

In parallel with this annual accounts, Orkuveita Reykjavíkur issues its annual report 2019. The report is integrated and prepared in accordance with the guidelines from Nasdaq OMX Nordic. It outlines governance, environmental issues, human rights and social affairs, as required by Act no. 3/2006 on annual accounts. The report also outlines the business model of the OR Group, the main business processes and stakeholders in the operation. It describes OR´s human rights policy and how OR tracks fraud and bribery. There are also reports from the Chairman and CEO. In the Appendix with the Financial Statements p. 63 discloses more non-financial information.

In light of the Covid-19 virus it is evident that the epidemic will influence the Icelandic economy and the world at large. OR conducts stress tests on a regular basis which assumes currency depreciation, reduction of aluminium prices and increased inflation. Cash position is currently strong and today total cash amounts to about 21.4bn ISK. Furthermore, the company has access to credit lines amounting to ISK 7bn throughout 2020. The company is strong and operateable and is well capable to handle shocks in the foreseeable future.

The report is endorsed by independent financial, environmental, social and administrative experts, as well as the directors of Orkuveita Reykjavíkur and the CEO.

Statement by the Board of Directors

According to the best knowledge of the Board of Directors and the CEO of Orkuveita Reykjavíkur, the consolidated financial statements are in accordance with IFRS´s as they have been approved by EU and the additional requirements set out in the local rules and regulations regarding Financial statements of companies with listed bonds. It is the opinion of the Board of Directors and the CEO that the Financial Statements give a fair view of the Group’s assets, liabilities and financial position 31 December 2019 and the Group´s operating return and changes in cash and cash equivalents in the year 2019. The Financial Statements also describe the main risk factors and uncertainties faced by the Group.

The Board of Directors and the CEO of Orkuveita Reykjavíkur hereby confirm the Group's consolidated financial statements for the year 2019.

Reykjavík, 12 March 2020.

The Board of Directors:

Brynhildur Davíðsdóttir
Sigríður Rut Júlíusdóttir
Gylfi Magnússon
Eyþór Laxdal Arnalds
Hildur Björnsdóttir
Valgarður Lyngdal Jónsson

CEO:
Bjarni Bjarnason

INDEPENDENT AUDITOR´S REPORT

To the Board of Directors and Owners of Orkuveitu Reykjavíkur.

Opinion on the Consolidated Financial Statement

Opinion

We have audited the accompanying Consolidated Financial Statements of Orkuveitan Reykjavíkur. (hereafter the Group) for the year 2019. The Consolidated Financial Statements comprise the Statement by the Board of Directors and CEO, the Statement of Income, the Statement of Financial Position, the Statement of Comprehensive Income, the Statement of Cash Flows, the Changes in Equity, a summary of significant accounting policies and other explanatory information.

In our opinion, the Consolidated Financial Statements present fairly, in all material respects, the consolidated results of operations of the Group. for the year 2019, its consolidated financial position as at December 31, 2018, and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU and the Financial Statements Act.

In accordance with the provisions of Article 104, paragraph 2 of the Icelandic Financial Statements Act No. 3/2006, we confirm that the Statement by the Board of Directors and CEO accompanying the Consolidated Financial Statements includes at least the information required by the Financial Statements Act if not disclosed elsewhere in the Consolidated Financial Statements.

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 Consolidated Financial Statements section of our Report. We are independent of the Group in accordance with the Code of Ethics for Professional Accountants in Iceland, and we have fulfilled all ethical requirements therein. 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 judgement, were of most significance in our audit of the Consolidated Financial Statements for the year 2019. These matters were addressed in the context of our audit of the Consolidated Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

In our opinion the following matters were key audit matters:

Explanation of Key Audit Matter	Responses to Key Audit Matter
Mat framleiðslu- og veitukerfis See note 39 (d) on significant accounting policies and note 13 on property, plant and equipment. We have defined the valuation of production and distribution systems as a key audit matter in our audit. The Group's production and distribution systems are carried at revalued amount. An assessment is made of the changes in construction costs of similar types of assets and both cost and accumulated depreciation are revalued accordingly. The Group performs impairment tests on the reporting date and recognises impairment loss if value in use is lower than book value of an asset. Revalued amount will also not be higher than value in use.	As part of our audit, we reviewed the Group's methodology for valuing the production and distribution systems and its consistency with international financial reporting standards. We reviewed the Group's processes for the revaluation and impairment tests. We also reviewed the functionality of models used in the assessments. We evaluated management assumptions by comparing to public information where applicable. Where assumptions are not based on public information, we made our own evaluation on management assumptions. We used the work of a valuation specialist to assist in this evaluation.

The assumptions used for revaluation and impairment tests are based on management assessments and are partly subjective. With production and distribution systems being a significant part of the consolidated financial statements, any change in assumptions can have significant effect on the income statement and balance sheet of the Group. Our work both included estimates of the revaluation assessments and the impairment tests of the production and distribution systems.

Revenue recognition

See note 39 (j) on significant accounting policies and note 4 on operation and revenue recognition of Group's components.

Revenue from sale and distribution of electricity and hot water is recognised based on measurements into the systems, taking into account energy losses occurring in the distribution systems. Differences between the actual amounts that go into the systems, minus losses and invoiced usage, leads to a period correction.

Due to the fact that income recognition at the end of the year is based on management estimates, there is uncertainty regarding revenue recognition relating to revenue cut-off and existence. For that reason, we focus specifically on revenue cutoff in our audit, as well as performing other audit procedures relating to revenue recognition.

In our audit of revenues, we have assessed controls relating to revenues in the Group. We have also tested certain controls relating to revenue recognition. We have reviewed and evaluated the IT control environment in the Group, including review of how access to finance and accounting related IT systems is controlled.

We have used substantive testing methods where we have for example reviewed reconciliations between accounting systems and subsystems and received third party confirmation of energy usage, turnover and outstanding balances at year-end from specific customers. We have also reviewed deposits after year-end where balance confirmations from customers were not available.

We have also performed substantive tests where we have compared our expectations to actual revenue recognition in the Group.

Valuation of embedded derivatives

See note 29 (c) on significant accounting policies, note 18 on embedded derivatives in electricity sales contracts and note 33 on fair value hierarchy.

Because prices of specific electricity sales contracts with large counterparties are tied to aluminium prices, the Group recognises embedded derivatives on the balance sheet. As electricity and aluminium prices are generally not closely related, financial reporting standards require the risk relating to this relationship to be evaluated specifically.

The embedded derivatives are considered to be third level financial items, where estimates are based on management assumptions and unobservable inputs. Because of the vulnerability of the estimate, any change in assumptions can have significant effect on the income statement and balance sheet of the Group. For these reasons, we assume there is significant risk related to embedded derivatives and have therefore defined them as a key audit matter.

In our audit, we reviewed the Group's pricing methodology and consistency with international financial reporting standards.

We reviewed the Group's process for analysing and assessing assumptions used in the valuation, as well as reviewing valuation models used. We recalculated derivative valuations based on information we collected.

We used the work of a valuation specialist to assist with this review.

Independent auditor's report, contd.

Other Information

The Board of Directors and the CEO are responsible for all information presented by the Group, both the Consolidated Financial Statements as well as other information. The other information comprises the information included in the Annual Report, but does not include the Consolidated Financial Statements and our Auditor's Report thereon. Our opinion on the Consolidated Financial Statements does not cover the information in the Annual Report or other documents issued by the Group, and we do not express any form of assurance on the information in those documents thereon. In connection with our audit of the Consolidated Financial Statements, our responsibility is to read the other information identified above when it becomes available and, in doing so, consider whether the other information is materially inconsistent with the Consolidated Financial Statements, our knowledge obtained in the audit, or otherwise appears to be materially misstated. If we conclude that there are material misstatements or inconsistencies therein, we are required to communicate the matter to the Board of Directors and take appropriate action depending on the severity of the misstatement.

The Board of Directors and CEO's Responsibilities for the Consolidated Financial Statements

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

In preparing the Consolidated Financial Statements, the Board of Directors and CEO are responsible for assessing the Group'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 the Board of Directors and CEO either intend to liquidate the Group or to cease operations, or have no realistic alternative but to do so.

The Board of Directors and the Audit Committee are responsible for overseeing the Group's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated Financial Statements

Our objectives are to obtain reasonable assurance about whether the Consolidated 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 Consolidated Financial Statements.

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

- Identify and assess the risks of material misstatement of the Consolidated 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 Group´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 exist related to events or conditions that may cast significant doubt on the Group'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 Consolidated 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 Group to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the Consolidated Financial Statements, including the disclosures, and whether the Consolidated Financial Statements represent the underlying transactions and events in a manner that achieves fair presentation

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the Consolidated Financial Statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

We communicated with the Board of Directors and the 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 identified during our audit. Our Audit Report, which has been provided to the Board of Directors and the Audit Committee, reports these matters and is in accordance with this report.

We have not provided the Group with any services that are prohibited according to laws on auditors. We have provided the Board of Directors and the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and communicated 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 determined those matters that were of most significance in the audit of the Consolidated Financial Statements of the current year and are therefore the key audit matters. We describe these matters in our Auditor's Report unless law or regulations 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.

We were elected auditors for the Group in the Group's annual general meeting on April 4th, 2019 and this is therefore the second continuous fiscal year where we are the Group's auditors.

On behalf of Grant Thornton endurskoðun ehf.
Reykjavík, 12. mars 2020

Davíð Arnar Einarsson

Davíð Arnar Einarsson, State Authorized Public Accountant

J. Sturla Jónsson

J. Sturla Jónsson, State Authorized Public Accountant

Income Statement 2019

	Notes	2019	2018
Operating revenue	5	46.569.730	45.594.861
Profit from sale of assets		396	321.354
Operating revenues, total		46.570.126	45.916.215
Energy purchase and distribution		(5.658.834)	(6.106.174)
Salaries and salary related expenses	8	(6.871.986)	(6.146.613)
Salary related expenses - defined contribution pension expenses		0	(31.875)
Other operating expenses		(5.867.087)	(5.014.837)
Operating expenses, total		(18.397.906)	(17.299.499)
EBITDA		28.172.219	28.616.715
Depreciation and amortisation	10	(12.121.294)	(10.270.945)
Results from operating activities, EBIT		16.050.925	18.345.771
Interest income		416.293	380.992
Interest expenses		(7.194.532)	(6.911.403)
Other income (expenses) on financial assets and liabilities		(2.019.003)	(7.222.848)
Total financial income and expenses	11	(8.797.242)	(13.753.258)
Share in (loss) profit of associated companies	16	(544)	6.033
Profit before income tax		7.253.139	4.598.545
Income tax	12	(336.769)	1.379.848
Profit for the year		6.916.370	5.978.394

The notes on pages 14 to 62 are an integral part of these Consolidated Financial Statements.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 9 Amounts are in ISK thousand

Statement of Comprehensive Income 2019

	Notes	2019	2018
Profit for the year		6.916.370	5.978.394
Other comprehensive income			
Items moved to equity that will not be moved later to the income statement			
Revaluation reserve, increase	13	14.922.393	8.389.138
Income tax effect of revaluation	20	(2.102.110)	(1.677.828)
		12.820.283	6.711.310
Items moved to equity that could be moved later to the income statement			
Changes in fair value for financial assets at fair value through OCI	17	1.364.646	251.808
Translation difference	24	1.870.938	5.902.197
		3.235.584	6.154.005
Other comprehensive income, after taxes		16.055.867	12.865.315
Total comprehensive income for the year		22.972.237	18.843.708

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Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 10 Amounts are in ISK thousand

Statement of Financial Position
31 December 2019

	Notes	31.12.2019	31.12.2018
Assets			
Property, plant and equipment	13	328.956.132	303.582.858
Intangible assets	14	2.498.099	1.999.523
Right-of-use assets	15	2.488.863	0
Investments in associated companies	16	73.753	67.296
Investments in other companies	17	5.216.267	3.859.015
Hedge contracts	19	229.072	295.670
Deferred tax assets	20	4.879.759	3.819.233
Total non-current assets		344.341.945	313.623.595
Inventories	21	1.195.475	1.019.807
Trade receivables	22	4.915.008	5.482.511
Hedge contracts	19	388.451	946.717
Other receivables	22	368.978	496.986
Prepaid expenses		184.464	307.939
Deposits and marketable securities	23	9.833.014	7.223.231
Cash and cash equivalents	23	8.657.025	10.988.087
Total current assets		25.542.415	26.465.279
Total assets		369.884.360	340.088.874
Equity			
Revaluation reserve		93.186.474	83.821.060
Equity reserve		48.585.813	42.972.671
Fair value reserve		4.760.587	3.395.941
Translation reserve		2.411.820	540.882
Retained earnings		33.354.772	30.096.679
Total equity	24	182.299.466	160.827.232
Liabilities			
Loans and borrowings	25	138.955.006	133.577.622
Lease liabilities		2.355.873	0
Pension liability	26	723.084	682.404
Embedded derivatives in electricity sales contracts	18	5.307.027	4.270.604
Hedge contracts	19	613.778	777.053
Deferred tax liabilities	20	14.679.794	12.813.107
Total non-current liabilities		162.634.563	152.120.791
Accounts payable		2.926.455	3.125.135
Loans and borrowings	25	15.064.107	17.706.249
Lease liabilities	15	153.878	0
Embedded derivatives in electricity sales contracts	18	1.372.302	1.046.265
Hedge contracts	19	317.233	548.022
Deferred revenue		149.735	162.980
Current tax liability	12	1.693.071	1.497.031
Other current liabilities	27	3.273.550	3.055.169
Total current liabilities		24.950.331	27.140.851
Total liabilities		187.584.894	179.261.642
Total equity and liabilities		369.884.360	340.088.874

The notes on pages 14 to 62 are an integral part of these Consolidated Financial Statements.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 11 Amounts are in ISK thousand

Statement of Changes in Equity for the year 2019

	Revaluation reserve	Equity reserve	Fair value reserve	Translation reserve	Retained earnings	Total equity
The year 2019						
Equity at 1 January 2019	83.821.060	42.972.671	3.395.941	540.882	30.096.679	160.827.232
Adjusted positon 1.1	(21.564)				21.564	0
Revaluation, increase	14.922.393					14.922.393
Income tax effect of revaluation	(2.102.110)					(2.102.110)
Changes in fair value for financial assets at fair value through OCI			1.364.646			1.364.646
Translation difference				1.870.938		1.870.938
Profit for the year					6.916.370	6.916.370
Total comprehensive income	12.820.283	0	1.364.646	1.870.938	6.916.370	22.972.234
Depreciation transferred to retained earnings	(3.433.305)				3.433.305	0
Share in profit of subsidiaries and associates transf. to equity reserve		8.622.182			(8.622.182)	0
Dividends paid					(1.500.000)	(1.500.000)
Equity at 31 December 2019	93.208.038	51.594.853	4.760.587	2.411.820	30.324.171	182.299.466
The year 2018						
Equity at 1 January 2018	80.349.640	16.805.347	3.144.133	(5.361.315)	48.295.719	143.233.524
Revaluation, increase	8.389.138					8.389.138
Income tax effect of revaluation	(1.677.828)					(1.677.828)
Changes in fair value for financial assets at fair value through OCI			251.808			251.808
Translation difference				5.902.197		5.902.197
Profit for the year					5.978.394	5.978.394
Total comprehensive income	6.711.310	0	251.808	5.902.197	5.978.394	18.843.708
Depreciation transferred to retained earnings	(3.239.891)				3.239.891	0
Share in profit of subsidiaries and associates transf. to equity reserve		26.167.324			(26.167.324)	0
Divident paid					(1.250.000)	(1.250.000)
Equity at 30 September 2018	83.821.060	42.972.671	3.395.941	540.882	30.096.679	160.827.232

The notes on pages 14 to 62 are an integral part of these Consolidated Financial Statements.

Amounts are in ISK thousand

Statement of Cash Flows for the year 2019

	Notes	2019	2018
Cash flows from operating activities			
Profit for the year		6.916.370	5.978.394
Adjusted for:			
Financial income and expenses	11	8.797.242	13.753.258
Share in P/L of associates	16	544	(6.033)
Income tax	12	336.769	(1.379.848)
Depreciation and amortisation	10	12.121.294	10.270.945
Profit from sale of property, plants and equipment		(396)	(321.354)
Pension liability, change		42.980	76.843
Working capital from operation before interest and taxes		28.214.803	28.372.204
Inventories, increase		(175.668)	(82.481)
Current assets, decrease (increase)		895.581	(557.459)
Current liabilities, increase (decrease)		58.929	(240.761)
Cash generated from operations before interests and taxes		28.993.646	27.491.503
Received interest income		337.231	397.918
Paid interest expenses		(5.372.708)	(4.805.897)
Dividend received		55.713	33.831
Payments due to other financial income and expenses		327.848	(580.996)
Paid taxes		(1.477.262)	(1.482.446)
Net cash from operating activities		22.864.467	21.053.913
Cash flows from investing activities			
Acquisition of property, plant and equipment	13	(18.537.372)	(15.325.095)
Acquisition of intangible assets	14	(772.281)	(545.692)
Proceeds from sale of property, plant and equipment		9.713	431.473
Acquisition of associated companies		(7.000)	0
Proceeds from sale of other companies		12.472	0
Change in deposits		500.000	1.000.000
Change in marketable securities		(2.286.016)	(1.747.623)
Other financial assets		0	3.903.336
Net cash used in investing activities		(21.080.484)	(12.283.601)
Cash flows from financing activities			
Proceeds from new borrowings	25	16.966.850	20.562.335
Repayment of borrowings	25	(19.145.055)	(22.072.703)
Payments of currency hedges		(484.429)	(1.657.785)
Dividends paid	24	(1.500.000)	(1.250.000)
Current liabilities, change	25	(144.238)	0
Net cash used in financing activities		(4.306.872)	(4.418.153)
(Decrease) increase in cash and cash equivalents		(2.522.888)	4.352.159
Cash and cash equivalents at year beginning		10.988.087	6.254.983
Effect of currency fluctuations on cash and cash equivalents		191.827	380.945
Cash and cash equivalents at the end of the year	23	8.657.025	10.988.087
Investments and financing without payment effects:			
Acquisition of property, plant and equipment		(65.139)	(448.539)
Current liabilities, change		65.139	448.539
Other information:			
Working capital from operation	37	21.683.679	24.337.015

The notes on pages 14 to 62 are an integral part of these Consolidated Financial Statements.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 13 Amounts are in ISK thousand

Notes

1. Reporting entity

Orkuveita Reykjavíkur "OR" is a partnership that complies with the Icelandic law no. 136/2013 on Orkuveita Reykjavíkur. OR's headquarters are at Bæjarháls 1 in Reykjavik. OR's condenced consolidated interim financial statements include the interim financial statements of the parent company and its subsidiaries, (together referred to as "the Group") and a share in associated companies.

The Group provides services through its subsidiaries that operate power plants, distribute electricity, hot water and cold water, operates the sewage systems in its service area as well as a fiber optic system in its service area.

2. Basis of preparation

a. *Statement of compliance*

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and the additional requirements set out in the local rules and regulations regarding financial statements of companies with listed bonds.

The consolidated interim financial statements were approved by the Board of Directors on 12 March 2020.

Significant accounting policies for the Group are described in note 39.

b. *Functional and presentation currency*

The consolidated interim financial statements are presented in Icelandic kronas, which is the Company's functional currency. All financial information has been rounded to the nearest thousand unless otherwise stated.

c. *Basis of measurement*

The consolidated interim financial statements have been prepared on the historical cost basis except for a part of property, plant and equipment have been revalued at fair value, derivative agreement, embedded derivatives in electricity sales contracts, assets held for sale and other financial assets and liabilities are stated at fair value. The methods used to measure fair values are discussed further in note 39.

d. *Use of estimates and judgements*

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

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

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

- note 13 - Property, plant and equipment (revaluation of the distribution- and production system and valuation of impairment.)
- note 17 - Investments in other companies (presumptions made when calculating fair value of assets classified as assets held for sale.)
- note 18 - Embedded derivatives in electricity sales contracts (presumptions when calculating fair value)
- note 19 - Other financial assets and other financial liabilities (presumptions when calculating fair value)
- note 20 - Deferred tax assets and liabilities (valuation of future taxable profits against carry forward tax losses)
- note 29 - Market risk

3. Change in significant accounting policies

The financial statements are prepared using the same accounting policies as in the preparation of the consolidated financial statements for 2018, with the exception of the changes described below.

IFRS 16 Leases

The Group has initially adopted IFRS 16 Leases from 1 January 2019. A number of other new standards are effective from 1 January 2019 but they do not have a material effect on the Group's financial statements.

The Group has applied IFRS 16 by recording right-of-use asset and lease liabilities at 1 January 2019. The comparative information presented for 2018 has not been restated – i.e. it is presented, as previously reported, under IAS 17 and related interpretations. The details of the changes in accounting policies are disclosed below. IFRS 16 disclosure requirements has generally not been applied to comparative information.

Definition of a lease
Previously, the Group determined at contract inception whether an arrangement was or contained a lease under IFRIC 4 *Determining Whether an Arrangement contains a Lease* . The Group now assesses whether a contract is or contains a lease based on the new definition of a lease, as detailed in note 39 t.

On transition to IFRS 16, the Group elected to apply the practical expedient to grandfather the assessment of which transactions are leases. It applied IFRS 16 only to contracts that were previously identified as leases. Contracts that were not identified as leases under IAS 17 and IFRIC 4 were not reassessed. Therefore, the definition of a lease under IFRS 16 has been applied only to contracts entered into or changed on or after 1 January 2019.

As a lessee
The Group is recording right-of-use assets and lease liabilities for properties lease contracts in which it is a lessee. As a lessee, the Group previously classified leases as operating or finance leases based on its assessment of whether the lease transferred substantially all of the risks and rewards of ownership. Under IFRS 16, the Group recognises right-of-use assets and lease liabilities for most leases – i.e. these leases are on-balance sheet.

At inception or on reassessment of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease and non-lease component on the basis of their relative stand-alone prices. However, for leases of properties in which it is a lessee, the Group has elected not to separate non-lease components and will instead account for the lease and non-lease components as a single lease component.

Lease agreements classicied as operating lease according to IAS 17

At transition to IFRS 16 lease liabilities were measured at the present value of the remaining lease payments, discounted at the Group's incremental borrowing rate as at 1 January 2019. Right-of-use assets are measured at an amount equal to the lease liability, adjusted by the amount of any prepaid or accrued lease payments. On the date of implementation of IFRS 16 The Group assessed the impairment of right-of-use assets and concluded that there was no evidence of impairment.

3. Change in significant accounting policies, cont.:

Lease agreements classicied as operating lease according to IAS 17, cont.:

The Group applied the exemption not to recognise right-of-use assets and liabilities for leases with less than 12 months of lease term as well as excluding a direct initial starting cost. The Group has elected not to recognise right-of-use assets and lease liabilities for some leases of low-value assets. The Group has applied judgement to determine the lease term for some lease contracts in which it is a lessee that include renewal options. The assessment of whether the Group is reasonably certain to exercise such options impacts the lease term

The Group as a lessor

The accounting policies applicable to the Group as lessors are not different from those applicable to IAS 17.

Impact on transition during the year

On transition to IFRS 16, the Group recognised in balance sheet right-of-use assets equal to lease liabilities on 1 January 2019. As a result of initially applying IFRS 16, in relation to the leases the Group has recognised depreciation and interest costs, instead of operating leases expense. The impact on transition at 1 January 2019 and the year 2019 is summarised below:

Impacts on transition on balance sheet:	**1 January to 31 December**	**1 January 2019**	**31 December 2019**
Right-of-use assets		2.571.612	2.488.863
Lease liabilities		2.571.612	2.509.752
Income tax payable		0	(7.854)
Equity		0	(13.035)
Impacts on transition on income statement:			
Depreciation	110.805		
Interest cost	72.006		
Reversal of operating leases expense	(161.923)		
Income tax	(7.854)		
Total impact on income statement for the year 2019	13.035		

When measuring lease liabilities for leases that were classified as operating leases, the Group discounted lease payments using its incremental borrowing rate at 1 January 2019. The weighted-average rate applied is 3,08%.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 16 Amounts are in ISK thousand

3. Change in significant accounting policies, cont.:

Impact on transition during the year, cont.:

If the standard would not have been implemented on 1 January 2019 then the EBITDA for the year 2019 would have been ISK 162 million lower and profit for the period ISK 13 million higher. The impact on year 2019 is summarised below:

Income statements	**1 January to 31 December**	**Impact of new standard**	**1.1.2019**
Operating income	46.570.126	0	46.570.126
Operating expenses	(18.589.419)	161.923	(18.427.497)
EBITDA	27.980.706	161.923	28.142.629
Depreciation and impairment	(12.010.602)	(110.805)	(12.121.407)
Results from operating activities, EBIT	15.970.105	51.118	16.021.222
Financial income and expenses	(8.694.884)	(72.006)	(8.766.890)
Share in profit of associated companies	(544)	0	(544)
Profit before income tax	7.274.677	(20.889)	7.253.788
Income tax	(351.946)	7.854	(344.092)
Profit for the period	6.922.731	(13.035)	6.909.697

The impact on transition to IFRS 16 on Group's balance sheet 1 January 2019 is summarised below:

Balance sheet	**31.12.2018**	**new standard**	**1.1.2019**
Right-of-use assets	0	2.571.612	2.571.612
Total assets	313.623.595	2.571.612	316.195.207
Equity	160.827.232	0	160.827.232
Non-current lease liabilities	0	2.421.297	2.421.297
Current lease liabilites	0	150.315	150.315
Total liabilites	179.261.642	2.571.612	181.833.254
Total equity and liabilites	340.088.874	2.571.612	342.660.486

The effect of IFRS 16 on segment information and EBIDTA is in note 6. For more information on accounting policies in accordance with IFRS 16 and IAS 17, see note 39 t.

Statements of Orkuveita Reykjavíkur 31 December 2019 17 Amounts are in ISK thousand

4. Operation and revenue recognition of Group's components

The following provides information about the operation of Group's components. Breakdown of revenue for different operations is given in note 5 and income by segment in note 6.

	Products and services	Nature, timing of revenue recognition and payments terms
a.	Electricity	ON Power ohf. and Orka náttúrunnar ohf. generate electricity and sell electricity and Utilities distribute electricity according to law no. 65/2003. Revenue from the sale and distribution of electricity is recognised in the income statement according to measured delivery to customer over the period plus a fixed fee. The rate for the distribution of electricity has a revenue cap set by the National Energy Authority in accordance with laws on energy number 65/2003. Upon connection of new users to distribution systems of electricity and upon renewal of connection an initial fee is charged. The initial fee is intended to cover cost of new distribution systems and their renewal. Connection fee is recognised in the income statement upon delivery of the service. Trade receivables from the sale and distribution of electricity generally have a 30 day grace period. Some contracts with certain customers may have different payment arrangements but that is an exception.
b.	Hot water	ON Power, Orka náttúrunnar and Utilities generate harness hot water and Utilities distribute harness hot water. Revenue from the sale and distribution of harness hot water is recognised in the income statement according to measured delivery to customer over the period plus a fixed fee. Upon connection of new users to distribution systems of harness hot water or upon renewal of connection an initial fee is charged. The initial fee is intended to cover cost of new distribution systems and their renewal. Connection fee is recognised in the income statement upon delivery of the service. Trade receivables from the sale and distribution of harness hot water generally have a 30 day grace period. Some contracts with certain customers may have different payment arrangements but that is an exception.
c.	Cold water	OR Water and Sewage collects and distributes cold water from reservoirs. Revenue from the sale of cold water is based on the size of properties plus a fixed fee which is recorded over the period in the income statement. The legal limitation on the upper limit of the rate is 0,5% of the real estate value. In addition revenue is stated for cold water according to measurement from specific industries. Upon connection of new users to distribution systems of cold water and upon renewal of connection an initial fee is charged. The initial fee is intended to cover cost of new distribution systems and their renewal. Connection fee is recognised in the income statement upon delivery of the service. Trade receivables from the sale of cold water generally have a 30 day grace period. Some contracts with certain customers may have different payment arrangements but that is an exception. Billing for cold water and sewage is done in the first 9 months of the year but income is distributed evenly over the year.
d.	Sewer system	OR Water and Sewage runs the sewer system. Revenue is based on the size of properties plus a fixed fee which is recorded over the period in the income statement. The legal limitation on the upper limit of the rate is 0,5% of the real estate rateable value. Upon connection of new users to sewage system and upon renewal of connection an initial fee is charged. The initial fee is intended to cover cost of new sewer systems and their renewal. Connection fee is recognised in the income statement upon delivery of the service. Trade receivables from the sewer system generally have a 30 day grace period. Some contracts with certain customers may have different payment arrangements but that is an exception. Billing for cold water and sewage is done in the first 9 months of the year but income is distributed evenly over the year.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 18 Amounts are in ISK thousand

4. Operation and revenue recognition of Group's components, contd.

Products and services	Nature, timing of revenue recognition and payments terms
e. Other revenues	Gagnaveita Reykjavíkur operates fiber optics data system. Revenue from fiber optics data system is recognised in the income statement upon delivery of the goods and service. This is a competitive practice that is supervised by The Post and Telecom Administration. Orkuveita Reykjavíkur the parent company operates rental of housing and equipment, incidental sale of specialist consultancy services and more. Rental income is recorded as income in the income statement linearly over the lease term and other revenue is recognised upon delivery of goods or services. Trade recevables from other revenues generally have a 30 day grace period.

5. Revenues from sales of goods and services

The Group's income from sales of goods and services is specified as follows:

	2019	2018
Electricity	19.383.914	19.248.507
Hot water	12.789.501	12.630.589
Cold water	2.890.309	3.172.786
Sewer system	5.594.225	5.299.106
Other revenues	5.911.782	5.243.872
Revenues from sales of goods and services total	46.569.730	45.594.861

6. Segment reporting

Business divisions and sectors

The Group's service area is mainly in the Reykjavík city area, but it also extends to the southern and western parts of Iceland. The Group is divided into three separate divisions: production and Sales, Utilities and Other Operation.

Energy sale and production generate electricity and harness hot water from the power plants, sells electricity to wholesale and retail customers as well as the new construction and operation of street lighting.

The subsidiaries **Utilities** and **OR Water and Sewage** distribute electricity, harnessing hot water from low-temperature fields and the geothermal plants and distribute it for space heating. It also collects and distributes cold water from reservoirs and runs a sewerage system.

Other operations cover the fiber optic system, rental of housing and equipment, incidental sale of specialist consultancy services and more.

The Group is income taxed and collects value added tax, except for operations regarding cold water and sewer but they are regulated by law no. 33/2004 concerning cold water suppliers of municipalities and law no. 9/2009 concerning the operations of sewer. The provision of hot water supply is subject to law no. 58/1967, concerning earnings from hot water. The distribution of electricity is subject to law no. 65/2003, which stipulates revenue caps that are decided by the National Energy Authority.

Statements of Orkuveita Reykjavíkur 31 December 2019 19 Amounts are in ISK thousand

6. Segment reporting, contd.

Sector	Official obligations
Hot water	Minister approves utility rates not subject to the open market. These take effect upon publication in the Ministerial Gazette.
Electricity, distribution	Price rates are subject to authorisation from The National Energy Authority. Rates are officially published.
Electricity, production	Energy sales are subject to the open market, electricity rate changes are therefore not subject to government approval.
Cold water	The legal limitation on the upper limit of the rate is 0,5% of the real estate value. Rates are officially published in the Law and Ministerial Gazette.
Sewer system	The Rates for the sewer system shall cover all costs. Rates are officially published in the Ministerial Gazette.
Fiber-optic data system	This is a competitive practice that is supervised by The Post and Telecom Administration.

Customers that have significant effect on the Group's revenues

One customer of Energy sale and production has significant effect on the Group's revenues in the year 2019. The Group´s revenues from this customer represents approximately ISK 5.903 million or 12,7% of total revenues. (2018: ISK 6.144 million, or 11,3% of total revenue).

6. Segment reporting

Segment information is presented by the Group's internal reporting. Business segments presented are *Utilities,* that represent licensed operations in hot and cold water, distribution of electricity and sewage*,* Energy sale and production, representing the competitive operations in producing and sale of electricity and hot water and *Other Operation,* that represents the activities of the parent company and the fiber optic operations. The parent company's main activities is providing service to subsidiaries, rental of housing and equipment, incidental sale of specialist consultancy services and more. Reykjavik fiber network represents the fiber optic operations. Segment reporting is conducted by using the same accounting principle as the group uses and is described in note 39 with the consolidated financial statements for the year ended 31 December 2019.

Business segments - divisions

The year 2019	**Utilities**	**Energy sale and production**	**Other Operation**	**Adjust-ments**	**IFRS 16***	**Total**
External revenue	28.888.456	14.179.522	3.502.147	0		46.570.126
Inter-segment revenue	4.014.286	4.726.898	8.343.194	(17.084.378)		(0)
Total segment revenue	32.902.742	18.906.420	11.845.341	(17.084.378)		46.570.126
Segment operation expenses	(17.941.848)	(8.274.973)	(9.427.386)	17.084.378	161.923	(18.397.907)
Segment profit EBITDA	14.960.894	10.631.448	2.417.955	0	161.923	28.172.219
Depreciation and amortisation	(5.430.576)	(4.946.765)	(1.633.149)	0	(110.805)	(12.121.294)
Segment results, EBIT	9.530.318	5.684.683	784.807	0	51.118	16.050.925
Financial income and expenses	(3.043.492)	(2.630.320)	(1.688.965)	(1.362.459)	(72.006)	(8.797.242)
Share in (loss) profit of associated companies	0	0	(544)	0		(544)
Income tax	(732.959)	(602.751)	478.803	512.285	7.854	(336.769)
Profit (loss) for the year	5.753.866	2.451.612	(425.899)	(850.175)	(13.035)	6.916.370
The year 2018						
External revenue	28.547.607	14.362.387	3.006.220	0		45.916.215
Inter-segment revenue	3.271.509	4.571.879	7.471.011	(15.314.399)		(0)
Total segment revenue	31.819.116	18.934.266	10.477.231	(15.314.399)		45.916.215
Segment operation expenses	(16.091.802)	(8.201.064)	(8.321.032)	15.314.399		(17.299.499)
Segment profit EBITDA	15.727.314	10.733.202	2.156.199	0		28.616.715
Depreciation and amortisation	(5.284.361)	(3.610.586)	(1.375.998)	0		(10.270.945)
Segment results, EBIT	10.442.953	7.122.616	780.202	0		18.345.771
Financial income and expenses	(3.376.721)	(907.649)	(1.927.908)	(7.540.981)		(13.753.258)
Share in profit of associated companies	0	0	6.033	0		6.033
Income tax	(850.526)	(1.060.552)	491.518	2.799.409		1.379.848
Profit (loss) for the year	6.215.706	5.154.415	(650.155)	(4.741.572)		5.978.394

* Segment reporting as used by management does not take into account the guidance of IFRS 16

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 21 Amounts are in ISK thousand

6. Segment reporting, contd.

Business segments - divisions, contd.

	Utilities	Energy sale and production	Other Operation	Adjust-ments	IFRS 16	Total
Balance sheet (31.12.2019)						
Property, plant and equipment and intangible assets	166.763.273	131.123.708	33.567.250	0		331.454.232
Right-of-use assets	0	0	0		2.488.863	2.488.863
Other assets	17.485.349	10.956.734	158.713.621	(151.214.439)		35.941.265
						369.884.360
Loans and borrowings	62.611.008	57.530.973	154.019.113	(120.141.981)		154.019.113
Lease liabilities	0	0	0		2.509.752	2.509.752
Other liabilities	12.867.235	13.439.264	31.663.896	(26.914.498)		31.055.897
						187.584.762
Investments						
Property, plant and equipment and intangible assets	9.959.235	4.867.051	4.548.507	0		19.374.792
Balance sheet (31.12.2018)						
Property, plant and equipment and intangible assets	152.659.606	122.261.566	30.661.209	0		305.582.381
Other assets	17.305.051	7.786.039	159.058.806	(149.643.402)		34.506.493
						340.088.874
Loans and borrowings	62.300.634	58.219.127	155.477.198	(124.713.088)		151.283.870
Other liabilities	11.189.885	8.310.387	30.092.174	(21.614.674)		27.977.771
						179.261.642
Investments						
Property, plant and equipment and intangible assets	6.948.654	4.694.831	4.716.621	0		16.360.107

Amounts are in ISK thousand

Notes

7. Analysis of geothermal power plant operation

Return analysis of production of electricity and hot water, cf. Article 41, paragraph 5 of law no. 65/2003:

	Electricity 2019	Hot water 2019	Electricity 2018	Hot water 2018
Geothermal power plant				
Revenue	9.745.898	3.972.998	8.937.101	3.907.206
Operating expenses	(2.260.428)	(985.692)	(2.115.614)	(905.204)
Depreciation and amortisation	(3.405.497)	(1.492.114)	(2.689.919)	(899.497)
Profit before financial expenses	4.079.973	1.495.191	4.131.568	2.102.505
Return on investment	4,3%	4,8%	5,1%	8,8%

The power plants at Hellisheiði and Nesjavellir are mixed production plants, where both hot water and energy are produced.
The cost allocation is based on Orka náttúrunnar and ON Power´s methods, that the National Energy Authority "NEA" has not approved. NEA is obligated to set new cost allocation rules after having disapproved the companies proposal, NEA has not yet carried this out. Until NEA sets new rules for cost allocation, the return of the sectors are reported using Orka náttúrunnar and ON Power's methods.

8. Salaries and salary related expenses

	2019	2018
Salaries and salary related expenses are specified as follows:		
Salaries	6.531.982	5.825.605
Defined contribution pension expenses	866.243	780.361
Defined contribution pension expenses paid to Bru Pension Fund	0	31.875
Defined benefit pension expenses	73.843	104.576
Other salary related expenses	597.684	551.389
Total salaries and salary related expenses	8.069.752	7.293.806
Salaries and salary related expenses are stated in the financial statements as follows:		
Expensed in the income statement	6.871.986	6.178.487
Capitalised on projects	1.197.767	1.115.319
Total salaries and salary related expenses	8.069.752	7.293.806
Number of employees:		
Number of annual working units	602	558
Management's salaries and benefits for the parent company and subsidiaries are specified as follows:		
Salaries to the Board of Directors of the Parent Company	19.274	16.202
Salaries of the CEO of the Parent Company 1)	31.634	36.105
Salaries of three Managing Directors of the Parent Company	86.220	70.696
Salaries to the Board of Directors of three subsidiaries	14.915	28.384
Salaries of three Managing Directors of subsidiaries	80.889	80.448
Termination expenses, pension expenses included 2)	0	18.077
	232.932	249.911

1) There were two CEO of the Parent Company for two months in the year 2018 due to internal inspection of workplace culture of Orkuveita Reykjavíkur.

2) The manager of Orka náttúrunnar ohf. left his position at year-end 2018. Salaries and salary related expenses were all expensed in P/L upon his departure.

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 23 Amounts are in ISK thousand

Notes

9. Auditors fee

Audit of financial statements and review of interim financial statements	19.056	24.007
Other services	1.375	9.714
Total auditors fee	20.431	33.721

10. Depreciation, amortisation and impairment

	2019	2018
Depreciation, amortisation and impairment is specified as follows:		
Depreciation of property, plant and equipment cf. note 13	11.736.785	10.117.272
Depreciation of Right-of-use assets	110.805	0
Amortisation of intangible assets, cf. note 14	273.704	153.673
Depreciation, amortisation and impairment expensed in income statement	12.232.099	10.270.945

11. Financial income and expenses

	2019	2018
Financial income and expenses are specified as follows:		
Interest income	416.149	380.992
Interest expense and paid indexation	(4.738.400)	(4.313.317)
Indexation	(1.779.693)	(1.881.751)
Guarantee fee to owners 1)	(676.439)	(716.334)
Total interest expenses	(7.194.532)	(6.911.403)
Fair value changes of embedded derivatives in electricity sales contracts	(1.362.459)	(7.540.981)
Fair value changes of assets available for sale	5.078	15
Fair value changes of financial assets and financial liabilities through P/L	586.648	(186.784)
Fair value changes of hedge contracts	(230.800)	2.777.686
Hedge contracts	(122.306)	(2.318.375)
Foreign exchange difference	(950.877)	9.760
Dividends	55.713	35.831
Total of other income (expenses) on financial assets and liabilities	(2.019.003)	(7.222.848)
Total financial income and expenses	(8.797.386)	(13.753.258)

1) The Group paid a guarantee fee to current and former owners of the company for guarantees they have made on the Groups loans and borrowings according to a decision made on the annual meeting of Orkuveita Reykjavikur in 2005. The fee on yearly basis for its licensed operations is 0,89% (2018: 0,91%) and 0,60% (2018: 0,58%) regarding loans due for operations in the open market. The guarantee fee is calculated on total loans quarterly. The guarantee fee amounted to ISK 676 million in the year 2019 (2018: ISK 716 million) and is accounted for among interest expenses.

Fair value changes through P/L

Generally accepted valuation methods are used to determine the fair value of certain financial assets and financial liabilities, further discussed in note 39 with the financial statements of the Group for the year 2019. Change in fair value that is recognized in the income statement amounts to ISK 1.002 million expense in the year 2019 (2018: expense ISK 4.950 million). Fair value changes on financial assets and liabilities defined at level 3 amounts to ISK 5 million expense in the year 2019 (2018: expense ISK 7.728 million).

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 24 Amounts are in ISK thousand

Notes

12. Income tax

The Group's companies are tax liable according with Article 2 of law no. 90/2003 on income tax. The part of the Group's operation concerning operation of cold water supply and sewer is though exempt from income tax.

The parent Company´s tax rate is 37,6%, other taxable subsidiaries have a 20% tax rate.

Income tax recognised in the income statement is specified as follows:	2019	2018
Current income tax	1.693.071	1.497.031
Change in deferred income tax	(1.356.302)	(2.876.879)
Income tax recognised through P/L	336.769	(1.379.848)

Reconciliation of effective tax rate:		2019		2018
Profit before income tax		7.253.139		4.598.545
Income tax according to tax ratio of parent	37,6%	2.727.424	37,6%	1.729.053
Effect of tax rates of subsidiaries	(17,3%)	(1.256.754)	(41,1%)	(1.889.989)
Effect of valuation of impairment of deferred tax losses	(0,4%)	(26.082)	0,3%	12.158
Non-taxable operation of water supply and sewer	(14,6%)	(1.059.885)	(23,0%)	(1.057.168)
Effect of different functional currencies in the Group	0,01%	940	(1,4%)	(63.864)
Effect of adjustments of operating revenue 1.1.			(2,6%)	(118.581)
Other items	(0,67%)	(48.874)	0,2%	8.542
Effective income tax	4,6%	336.769	(30,0%)	(1.379.848)

Income tax recognised in other comprehensive income

Deferred tax

Due to income and expenses moved direct to equity	2019	2018
Tax effect of revaluation	2.102.110	1.677.828
Deferred tax, total	2.102.110	1.677.828

Statements of Orkuveita Reykjavíkur 31 December 2019 25 Amounts are in ISK thousand

13. Property, plant and equipment

The year 2019	Production system	Utility system	Other real estates	Other equipment	Total
Cost or deemed cost					
Balance at year beginning	260.440.447	305.542.948	8.254.030	3.296.922	577.534.348
Additions during the year	7.892.160	9.945.634	333.211	431.505	18.602.511
Translation difference	4.144.473	0	0	0	4.144.473
Sold or disposed of	0	0	0	(30.352)	(30.352)
Revaluation, increase	14.344.647	18.450.743	1.227		32.796.617
Balance at year end	286.821.727	333.939.325	8.588.468	3.698.076	633.047.596
Depreciation					
Balance at year beginning	107.220.489	164.524.931	546.567	1.659.502	273.951.489
Reclassification of assets					0
Depreciated during the year	6.077.989	5.068.983	139.577	450.236	11.736.785
Translation difference	550.001	0	0	0	550.001
Sold or disposed of	0	0	0	(21.035)	(21.035)
Revaluation, increase	7.062.411	10.811.309	504	0	17.874.224
Balance at year end	120.910.890	180.405.224	686.648	2.088.703	304.091.464
Carrying amounts					
At 1.1. 2019	153.219.958	141.018.017	7.707.463	1.637.421	303.582.858
At 31.12. 2019	165.910.837	153.534.101	7.901.820	1.609.374	328.956.132

The year 2018	Production system	Utility system	Other real estates	Other equipment	Total
Cost or deemed cost					
Balance at year beginning	225.610.766	296.836.009	7.915.813	2.675.184	533.037.772
Reclassification of assets	2.361	3.566	(5.927)	0	0
Additions during the year	6.110.808	8.709.948	342.907	650.751	15.814.415
Translation difference	17.169.416	0	1.237	38.578	17.209.231
Sold or disposed of	(671.371)	(6.576)	0	(67.591)	(745.537)
Revaluation, increase	12.218.466	0	0	0	12.218.466
Balance at year end	260.440.447	305.542.948	8.254.030	3.296.922	577.534.348
Depreciation					
Balance at year beginning	93.588.728	159.664.516	401.597	1.386.244	255.041.084
Reclassification of assets	98	24	(121)	0	0
Depreciated during the year	4.802.256	4.860.392	144.609	310.016	10.117.272
Translation difference	5.586.849	0	483	3.125	5.590.457
Sold or disposed of	(586.769)	0	0	(39.883)	(626.651)
Revaluation, increase	3.829.329	0	0	0	3.829.329
Balance at year end	107.220.489	164.524.931	546.567	1.659.502	273.951.489
Carrying amounts					
At 1.1. 2018	132.022.038	137.171.493	7.514.216	1.288.940	277.996.688
At 31.12. 2018	153.219.958	141.018.017	7.707.463	1.637.421	303.582.858
Thereof assets under construction at year end	2.234	0	0	0	2.234

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 26 Amounts are in ISK thousand

13. Property, plant and equipment, contd.

Revaluation

When revaluating, the relevant asset groups are measured at fair value. The aforementioned revaluation is recognised in a revaluation reserve among equity taken into account effects of deferred income tax as further explained in note 39 d. The revaluation is carried out by experts within the Group.

Revaluation was carried out for production system in hot and cold water and for hot and cold water, sewage and electricity for the distribution systems at end of september 2019 as part of regular revaluation of the assets of the Group. The revaluation led to an increase in book value of assets amounting to ISK 14.841 million.

Revaluation was last conducted according to the following table:

	Date of Revaluation
Production systems	
Hot water	30.9.2019
Cold water	30.9.2019
Electricity	31.12.2018
Distribution systems	
Hot water	30.9.2019
Cold water	30.9.2019
Sewage	30.9.2019
Electricity	30.9.2019
Fiber-optic cable system	31.12.2015

The fair value of these assets is determined on the basis of the depreciated replacement cost. This consists in that an assessment is made on changes in the construction cost of comparable assets and both cost and accumulated depreciations are revaluated in accordance with those changes. The calculation is based on official information and actual statistics from the Group's books on value changes of cost of items and takes into account an estimate on the weight of each cost item in the total cost of construction of comparable assets. Cost items and their proportional weight were determined by experts within the Group. The impairment test of assets is also taken into consideration and revaluation is not recognised beyond the expected future cash flow of the assets. Distribution systems for hot water, cold water, sewage and electricity are licensed operations and subject to official revenue targets that are based mostly on changes in the construction cost index. This is taken into consideration when revaluating these systems. Revaluation is classified as level 3 of the hierarchy of fair value, further explained in note 33.

Information on revalued assets at year end

31.12.2019	Production system	Distribution system	Total
Revalued carrying amount	165.910.837	153.534.101	319.444.939
Thereof effect of revaluation	(51.331.512)	(57.341.666)	(108.673.177)
Carrying amount before effect of revaluation	114.579.326	96.192.436	210.771.762
31.12.2018			
Revalued carrying amount	153.219.958	141.018.017	294.237.974
Thereof effect of revaluation	(43.898.515)	(51.501.690)	(95.400.205)
Carrying amount before effect of revaluation	109.321.443	89.516.327	198.837.769

Statements of Orkuveita Reykjavíkur 31 December 2019 27 Amounts are in ISK thousand

13. Property, plant and equipment, contd.

Impairment tests

Impairment tests were performed at the end of September 2019 for distribution systems and at year end for production systems and power plants in order to confirm both carrying amounts of assets and main assets under construction would meet estimated future cash flows of these assets. The impairment tests are carried out for every sector in the utilities and production systems.

The recoverable amount of each sector was evaluated based on value in use. The value in use was determined by discounting the expected future cash flows at the continued use in each sector. Cash flows were based on the future cash flow of the next five years. In assessing value in use, management make the plan for business development, based on both internal and external information.

The following criteria was used in assessing the value in use:

	Year 2019				
	Distribution system				Prod. systems
	Hot water	Electricity	Cold water	Sewage	Power plants
Revenue CAGR 2020-2024	1,3%	1,7%	4,7%	0,9%	1,1%
CAGR w.r.t. to price changes	0,6%	0,7%	0,7%	0,7%	0,0%-6,54%
EBITDA CARG 2019-2023	2,3%	3,1%	6,4%	0,7%	-1,4%
WACC	4,0%	4,0%	4,3%	4,1%	4,22%-7,83%

	Year 2018				
	Distribution system				Prod. systems
	Hot water	Electricity	Cold water	Sewage	Power plants
Revenue CAGR 2019-2023	0,4%	0,5%	1,8%	1,7%	1,2%
CAGR w.r.t. to price changes	1,5%	1,0%	0,8%	0,8%	0%-7,7%
EBITDA CARG 2019-2023	0,4%	-1,3%	1,9%	1,8%	1,2%
WACC	4,7%	4,6%	5,3%	4,9%	4,4%-8,8%

Impairment for distribution system for Utilities or Power plants is unlikely because of considerable additional value. However the test for electricity in power plants is sensitive to changes in key assumptions. If the required rate of ROCE increased by 0,25 percentage points, and other criteria are kept unchanged the calculated impairment in electricity for power plants would be ISK 2,7 billion. If the projected EBITDA is 5% lower during the planning period and other terms are unchanged, calculated impairment would be ISK 10,4 billion.

Rateable value and insurance value

The rateable value of the Group's assets measured in the rateable value assessment amounted to ISK 32.849 million at year end 2019 (2018: ISK 30.988 million). The fire insurance value of the company's assets amounted to ISK 45.023 million at the same time (2018: ISK 42.798 million). Among those assets are real estates capitalised among production and distribution systems. The insurance value of the Group's assets amounted to ISK 397.366 million at year end 2019 (2018: ISK 379.097 million).

Obligations

The Group has entered into contracts and placed purchase orders with suppliers and developers concerning work on production and distribution systems. The balance of these contracts and purchase orders at year end is estimated at ISK 2.628 million (2018: ISK 3.054 million).

Statements of Orkuveita Reykjavíkur 31 December 2019 28 Amounts are in ISK thousand

14. Intangible assets

Intangible assets are specified as follows:

The year 2019	Heating rights	Software	Total
Cost			
Balance at year beginning	1.427.031	2.248.007	3.675.038
Additions during the year	0	772.281	772.281
Balance at end of the year	1.427.031	3.020.288	4.447.319
Amortisation			
Balance at year beginning	457.768	1.217.747	1.675.515
Amortisation during the year	0	273.704	273.704
Balance at end of the year	457.768	1.491.451	1.949.219
Carrying amounts			
At 1.1. 2019	969.263	1.030.260	1.999.523
At 31.12. 2019	969.263	1.528.837	2.498.100
The year 2018			
Cost			
Balance at year beginning	1.427.031	1.702.315	3.129.346
Additions during the year	0	545.692	545.692
Balance at year end	1.427.031	2.248.007	3.675.038
Amortisation			
Balance at year beginning	457.768	1.064.073	1.521.842
Amortisation during the year	0	153.673	153.673
Balance at year end	457.768	1.217.747	1.675.515
Carrying amounts			
At 1.1. 2018	969.263	638.242	1.607.504
At 31.12. 2018	969.263	1.030.260	1.999.523

15. Lease agreements

Significant accounting policies are described in note 39t.

The Group rents office space and land. These leases are for long periods of time, but usually with the possibility of renewal at the end of the lease. Some leases include additional lease payments that are based on a change in certain indices. The Group may not enter into sublease agreements for certain leases.

The Group has elected not to recognise right-of-use assets and lease liabilities for some leases of low-value assets. The Group charges lease payments for these leases on a straight-line basis during the lease term.

Statements of Orkuveita Reykjavíkur 31 December 2019 29 Amounts are in ISK thousand

Notes

15. Lease agreements, cont.:

Right-of-use assets 1.1.2019	2.571.612
Additions during the year	9.248
Indexation	18.808
Depreciation of the year	(110.805)
Right-of-use assets 31.12.2019	2.488.863

Amounts in Profit and Loss Account:	**2019**
Right-of-use assets, depreciation	110.805

Changes in lease liabilities in the year are specified as follows:

Lease liabilities 1 January 2019	2.571.612
Current portion on lease liabilities	(89.916)
New lese liabilities	9.248
Indexation	18.808
Lease liabilities 31 December 2019	2.509.752

Repayment of lease liabilities is as follows:

The year 2020	153.878
The year 2021	154.846
The year 2022	128.195
The year 2023	101.544
The year 2024	101.570
Later	1.869.719
Total lease liabilites, including next year's repayment	2.509.752

Income statement:

Interest expenses:	72.006

Statement of Cash Flows:

Interest rate of rent payments (presented in cash flow statement in line "Paid interest")	17.684
The installment element of the lease payments (presented in a cash flow statement in the line "Payments of rent liabilities")	144.238

Most of the Group's leasing contracts for real estate include extension permits that the Group may use up to one year before the end of an unenforceable lease period. At the beginning of the lease, the Group assesses whether it is considered likely that it will utilize extensions. If there are significant changes in circumstances that are within the control of the Group, it will reassess whether the extension rights will be used.

Statements of Orkuveita Reykjavíkur 31 December 2019 30 Amounts are in ISK thousand

Notes

16. Investments in associated companies

	2019		2018	
	Share	Carrying amount	Share	Carrying amount
Íslensk Nýorka ehf.	29,88%	27.378	28,95%	22.968
Netorka hf.	38,41%	40.347	38,41%	38.286
Orkuskólinn REYST hf.	45,00%	6.027	45,00%	6.043
Total		73.753		67.296

The Group's share in the profit of its associated companies amounted to ISK 544 million in 2019 (2018: profit of ISK 6,0 million). During the year, the share capital increase in Íslenskri Nýorku ehf. in the amount of ISK 7

17. Investments in other companies

Investments in other companies are specified as follows:	Share	2019	2018
Landsnet hf. 1)	6,8%	5.160.587	3.795.941
Other shares in companies		55.680	63.074
Other shares in companies, total		5.216.267	3.859.015

Fair value of financial assets available for sale is based on generally accepted valuation methods performed by independent experts and internal experts. Fair value change of Landsnet hf. amounted to ISK 1.365 million in 2019 (2018: ISK 252 million) and the increase was transferred to a fair value reserve among equity. See further discussion in note 33.

1) According to provisions in the Energy laws no. 65/2003 only current owners of shares in Landsnet are allowed to assign their shares to other owners of Landsnet and are not allowed to sell their shares to other parties.

18. Embedded derivatives in electricity sales contracts

	2019	2018
Fair value of embedded derivatives at the beginning of the year	(5.316.869)	2.224.111
Fair value changes during the year	(1.362.459)	(7.540.981)
Fair value of embedded derivatives at year-end asset/(liability)	(6.679.328)	(5.316.869)

The allocation of embedded derivatives in electricity sales contracts is specified as follows:

	2019	2018
Non-current embedded derivatives asset/(liability)	(5.307.027)	(4.270.604)
Current embedded derivatives, asset/(liability)	(1.372.302)	(1.046.265)
Total embedded derivatives at year-end	(6.679.329)	(5.316.869)

Further discussion regarding embedded derivatives can be found in note 29 c.

19. Other financial assets and financial liabilities

Financial assets at fair value through profit or loss:	2019	2018
Non-current assets		
Hedge contracts	229.072	295.670
Current assets		
Hedge contracts	388.451	946.717
Non current liabilities		
Hedge contracts	(613.778)	(777.053)
Current liabilities		
Hedge contracts	(317.233)	(548.022)

Hedge contracts are measured by discounted future cash flow and market observable data is used in the price determination.

Statements of Orkuveita Reykjavíkur 31 December 2019 31 Amounts are in ISK thousand

20. Deferred tax assets and liabilities

Deferred tax assets and liabilities is specified as follows:

2019	**Tax assets**	**Tax liabilities**	**Net amount**
Deferred tax assets/liabilities at the beginning of the year	3.819.233	(12.813.107)	(8.993.875)
Exchange difference on current tax liability	0		0
Calculated income tax for the year	1.048.204	(1.384.973)	(336.769)
Current tax liability	12.322	1.680.749	1.693.071
Tax effect on the revaluation account	0	(2.085.755)	(2.085.755)
Other changes	0	(76.707)	(76.707)
Deferred tax assets/(liabilities) at end of the year	4.879.759	(14.679.794)	(9.800.035)

2018	**Tax assets**	**Tax liabilities**	**Net amount**
Deferred tax assets/liabilities at the beginning of the year	1.265.410	(11.080.041)	(9.814.631)
Calculated income tax for the year	2.553.822	(1.173.974)	1.379.848
Current tax liability	0	1.497.031	1.497.031
Tax effect on the revaluation account	0	(1.677.828)	(1.677.828)
Other changes	0	(378.295)	(378.295)
Deferred tax assets/(liabilities) at end of the year	3.819.233	(12.813.107)	(8.993.875)

Deferred tax assets and liabilities are attributable to the following:

	31.12.2019		**31.12.2018**	
	Tax assets	**Tax liabilities**	**Tax assets**	**Tax liabilities**
Property, plant and equipment	732.841	(14.849.805)	671.767	(12.856.236)
Embedded derivatives	2.511.428	0	1.999.143	0
Other items	824.656	81.249	1.148.323	(49.672)
Effect of carry forward taxable loss	810.835	113.468	0	556.849
Effect of write-down of taxable loss	0	(24.706)	0	(464.047)
Deferred tax assets/liabilities at year end	4.879.759	(14.679.794)	3.819.233	(12.813.107)

Carry forward taxable loss

Based on current tax law, a carry forwards taxable loss can be used against taxable profit within 10 years from when it was incurred. Carry forwards taxable loss at year end can be used as follows:

	2019	**2018**
Carry forward taxable loss for the year 2009, usable until year 2019	123.530	250.515
Carry forward taxable loss for the year 2016, usable until year 2026	205.368	205.368
Carry forward taxable loss for the year 2017, usable until year 2027	238.443	238.443
Carry forward taxable loss for the year 2018, usable until year 2028	41.429	50.176
Carry forward taxable loss for the year 2019, usable until year 2029	2.115.047	0
Carry forwards taxable loss at year end	608.771	744.503
Carry forward taxable loss for the year 2009, write-down	123.530	250.515
Total write-down of taxable loss	123.530	250.515

Management has evaluated the utilization of income tax losses and made plans for taxable profit for the next years. Deferred tax assets due to the taxable loss carried forward is recognized to the extent that it is believed to be useful. Loss carried forward in the amount of ISK 124 million is not capitalised at the end of 2019.

Statements of Orkuveita Reykjavíkur 31 December 2019 32 Amounts are in ISK thousand

21. Inventories

	2019	2018
Inventory of materials	1.195.475	1.019.807

The Group's material inventories consist of material for maintenance, renewal and construction of the Group's production and distribution systems. A part of the inventories is defined as safety inventories, i.e. inventories that are necessary to have on hand in case of malfunction or maintenance even though their turnover is low. The value of inventories is estimated regularly. Inventories for renewal and new constructions are accounted for among property, plant and equipment as part of building cost of assets under construction.

22. Receivables

Trade receivables is specified as follows at year end:	2019	2018
Trade receivables, industrial consumers	730.191	805.832
Trade receivables, retail	4.284.565	4.801.943
Trade receivables, total	5.014.756	5.607.774
Allowance for doubtful accounts	(99.749)	(125.264)
	4.915.008	5.482.511
Other current receivables are specified as follows at year end:		
Capital income tax	172.085	149.369
Accrued interest income	131.247	92.034
Receivables from employees	2.754	4.533
Other receivables	62.892	251.050
	368.978	496.986

23. Cash and cash equivalents, deposits and marketable securities

Cash and cash equivalents and deposits at year end are specified as follows:	2019	2018
Bank deposits, available from three to twelve months	2.500.000	3.000.000
Marketable securities	7.333.014	7.223.231
	9.833.014	10.223.231
Bank balances available within three months	8.657.025	10.988.087

24. Equity

Equity ratio of the Group at year end 2019 is 49,3% (2018: 47,3%). Return on equity was positive by 4,1% in the year 2019 (2018: positive by 4,0%).

Revaluation reserve

Revaluation reserve comprises of increase in the value of properties, plant and equipment after taking tax effects into account. Depreciation of the revaluated price are expensed in the income statement and transferred at the same time from the revaluation reserve account to retained earnings.

Translation reserve

The translation reserve comprises all foreign currency differences arising from the translation of financial statements of operations with other functional currency than ISK.

Fair value reserve

Fair value reserve comprises change of the value of assets categorised as available for sale after taking tax effects into account.

Equity reserve

According tothe Financial Statements Act no. 3/2006, share in profit of subsidiaries and associates, which exceeds the dividends received or the dividend decided of retained earnings, is accounted for on a restricted reserve account among equity.

Development reserve

According to the law no. 3/2006 companies that capitalize developmental cost should account for the same amount on a restricted reserve account among equity.

Retained earnings

Dividend in the amount of ISK 1.500 million was paid to the owners of the parent Company in the year 2019. (2018: ISK 1.250 million).

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 33 Amounts are in ISK thousand

25. Loans and borrowings

Interest bearing loans are recorded using the method of amortised cost. Further information on the Group's exposure to interest rate, foreign currency and liquidity risk, see note 29. Loans and borrowings are detailed as follows:

Non-current liabilities	**31.12.2019**	**31.12.2018**
Bank loans	94.785.840	98.040.070
Subordinated loan from owners of the Company	10.489.126	11.650.874
Bond issuance	48.744.147	41.592.927
	154.019.113	151.283.870
Current portion on non-current liabilities	(15.064.107)	(17.706.248)
	138.955.006	133.577.622
Current liabilities		
Current portion on non-current liabilities	15.064.107	17.706.248
Total interest bearing loans and borrowings	154.019.113	151.283.870

Terms of interest-bearing loans and borrowings

Liabilities in foreign currencies:		**31.12.2019**		**31.12.2018**	
	Date of maturity	**Average interest rate**	**Carrying amount**	**Average interest rate**	**Carrying amount**
Liabilities in CHF	5.10.2027	0,00%	9.255.023	-0,04%	10.149.953
Liabilities in EUR	19.12.2027	0,68%	20.397.149	0,94%	26.861.257
Liabilities in USD	19.11.2033	3,20%	31.642.746	3,76%	33.585.771
Liabilities in JPY	10.5.2027	0,01%	3.801.448	0,02%	4.542.820
Liabilities in GBP	26.2.2024	1,80%	1.825.255	1,91%	2.037.939
Liabilities in SEK	5.10.2027	0,04%	2.613.969	0,00%	3.054.356
			69.535.590		80.232.096
Liabilities in Icelandic kronas:					
Indexed	9.5.2046	3,51%	71.488.523	3,72%	61.526.774
Non-indexed	5.4.2035	4,93%	12.995.000	5,83%	9.525.000
			84.483.523		71.051.774
Total interest-bearing loans and borrowings			154.019.113		151.283.870

Repayment on non-current liabilities are specified as follows on the next years:

31.12.2019

The year 2020	15.064.107
The year 2021	15.492.569
The year 2022	14.770.524
The year 2023	15.553.737
The year 2024	14.507.819
Later	78.630.358
Total non-current liabilities, including next year's repayment	154.019.113

31.12.2018

The year 2019	17.706.248
The year 2020	14.430.015
The year 2021	13.731.679
The year 2022	17.106.717
The year 2023	14.836.186
Later	73.473.025
Total non-current liabilities, including next year's repayment	151.283.870

Consolidated Financial Statements of Orkuveita Reykjavíkur 31 December 2019 34 Amounts are in ISK thousand

25. Loans and borrowings, contd.,

Changes in loans and borrowings in the year are specified as follows:	2019	2018
Movements with payment effects		
Total interest bearing loans and borrowings 1. January	151.283.870	144.478.770
New borrowings	16.966.850	20.562.335
Repayment of borrowings	(19.145.055)	(22.072.703)
Movements without payment effects		
Currency fluctuation	2.955.842	6.407.046
Indexation	1.957.605	1.880.659
New borrowings	0	27.763
Total interest bearing loans and borrowings 31. December	154.019.113	151.283.870

Guarantees and pledges

The owners of the parent company are responsible, pro rata, for 54% of all liabilities and obligations. The Group has not pledged its assets as guarantee for its liabilities.

Covenants

Loans for the amount of ISK 64.490 million have certain covenants that regard repayment time as a proportion of EBITDA and as interests as a proportion of EBITDA as well as reviewing that budgets are within set limits (31.12.2018: ISK 50.365 million). Management regularly evaluate the covenants and in their view there is not risk of them being breached. At the end of the year the Group measured up to all financial covenants of loan agreements.

26. Retirement benefit obligation

The Group has retirement benefit obligation due to benefits of current and former employees in pension benefit plans.

The Group's accrued retirement benefit obligation amounted to ISK 753 million at year end 2019, discounted based on 2% interests and taken into account the share in the net asset of the pension fund (2018: ISK 710 million). The Group updates the obligation according to an assessment from an actuary each year when that assessment is available. Premises for life expectancy are in accordance with provisions of Regulation no. 391/1998 on obligatory insurance of pension benefits and operation of pension funds. The estimated increase in the obligation in the year is based on general increase in salaries taken into account interests. The increase of the obligation during the year is expensed in the income statement among salaries and salary related expenses. The part of the obligation that is estimated to be payable in the year 2019 is recognised among current liabilities.

	2019	2018
Retirement benefit obligation at the beginning of the year	710.104	633.261
Contribution due to pension payments during the year	(30.863)	(27.733)
Increase in the pension fund obligation during the year	73.843	104.576
Retirement benefit obligation at year end	753.084	710.104
Non-current component of retirement benefit obligation	723.084	682.404
Current component of retirement benefit obligation	30.000	27.700
Retirement benefit obligation at year end	753.084	710.104

Statements of Orkuveita Reykjavíkur 31 December 2019 35 Amounts are in ISK thousand

27. Current liabilities

Other current liabilities is specified as follows:	2019	2018
Unpaid taxes	311.208	276.179
Unpaid salaries and salary related items	1.436.757	1.252.189
Accrued interest expenses	746.025	715.955
Current component of retirement benefit obligation	30.000	27.700
Derivative contracts in default, see note 38	740.000	740.000
Other liabilities	9.561	43.146
Total current liabilities	3.273.550	3.055.169

28. Risk management and financial instruments

The risk policy was updated and approved by the Board of Directors of OR at the end of year 2019. The Board´s policy is that in all of the Group´s operations, risks are to be considered and by that implementing efficient decision making and governance. The risk policy explains the overview and main targets of the Board in this matter. The risk policy also defines the main risk factors, measurement indicators, objectives and risk limits in the daily risk management. One of the main foundation in the risk policy is to define the risk factors which are of relevance, measure their impact and define acceptable limits when controlling them.

Decision making and control on the execution of the risk management is in the hands of a risk council. The risk council consists of the CEO, CFO, Head of risk management, Head of treasury, planning and analysis and Deputy to the CFO. It overviews for instance:
• that suitable methods are used to recognise and measure risk
• that risk monitoring systems are in place and efficient
• that the risk policy of the Board is complied with in the operations of the Group
The Risk management department oversees and controls risk. The objective of the department is to monitor, analyse and control the financial risks of the Group.
Financial risk is divided into:
• Market risk, further discussed in note 29
• Liquidity risk, further discussed in note 30
• Credit risk, further discussed in note 31
• Operational risk, further discussed in note 32

29. Market risk

Market risk is the risk that changes in the exchange rate of foreign currencies, aluminium price, interests and other price changes will affect the Group's income or the value of its financial instruments. With regards to the current Balance Sheet, market risk is mainly due to changes in interest, exchange rates, CPI and aluminium price but risk regarding portfolio assets such as shares in companies and bonds is minimal. The risk that weighs the most in the Group is divided into:

a. Currency risk due to assets and liabilities in the balance sheet and cash flow in foreign currencies.
b. Interest rate risk due to loans and contracts made by the Group
c. Risk due to changes in the world market price of aluminium.

Statements of Orkuveita Reykjavíkur 31 December 2019 36 Amounts are in ISK thousand

29. Market risk, contd.

a. *Currency risk*

Currency risk is the risk of changes in exchange rates having a negative effect on the Group's income. Currency risk is measured in the difference between assets and liabilities in each currency where taken into consideration all assets, liabilities and derivatives. The Risk Management department is permitted to use forward contracts and currency swaps to mitigate risk due to currency fluctuations. Limits on the minimum/maximum currency imbalance is cash flows for the next 5 financial years have been approved.

The Group is exposed to currency risk on sales, purchases and borrowings. Main currency exposures are in Euro (EUR), Swiss Francs (CHF), United States dollar (USD) and Icelandic kronas (ISK).

Approx. 45,1% of the Group's interest bearing loans are in foreign currencies. The Group has entered into long term electricity sales contracts in foreign currency (USD). The expected future revenues from these contracts on the accounting date amount to approx. ISK 71.489 million (2018: ISK 77.787 million). That amount is based on the future price of aluminium on LME (London Metal Exchange) and expectations of price development of aluminium for the next 25 years according to, an independent evaluation party CRU, as available on the accounting date.

	2019	2018	31.12.2019	31.12.2018
	Average exchange rate		Exchange rate at year end	
CHF	123,460	110,723	125,140	118,230
EUR	137,300	127,730	135,830	133,230
USD	122,650	108,382	121,100	116,330
JPY	1,126	0,980	1,116	1,057
GBP	156,490	144,350	159,420	148,330
SEK	12,968	12,455	12,994	13,020
TWI	180,974	166,714	179,696	174,073

Statements of Orkuveita Reykjavíkur 31 December 2019 37 Amounts are in ISK thousand

29. Market risk, contd.

b. *Interest rate risk*

Interest rate risk is the risk of changes in interest rates having a negative effect on the Group's income. The Group is exposed to interest rate risk due to interest bearing assets, liabilities and financial instruments measured at fair value. The Group´s liabilities both have fixed and variable interest rates, majority being subject to variable interest rates. The risk management department monitors that interest rate risk is within preset limits and has permission to control interest rate risk with derivatives for the next 5 financial years within approved limits. On the accounting date hedges covered 83% of loans, taking into account hedges, with fixed interest rates 1 year ahead.

Interest-bearing financial assets and liabilities are specified as follows:

	31.12.2019	31.12.2018
Fixed rate instruments		
Financial liabilities	(83.755.223)	(72.302.467)
Variable rate instruments		
Financial liabilities	(70.263.891)	(78.981.404)
Financial instruments at fair value		
Bonds	0	0
Marketable securities	7.333.014	4.223.231
Hedge contracts	(313.489)	(82.688)
	7.019.526	4.140.543

The following table shows the calculated effect of changes in interest on one year cash flows and on the value of financial instruments measured at fair value, taken into account the effect of taxes. The analysis was done in the same way for the year 2018.

Sensitivity analysis on interest	**Cash flow sensitivity analysis**		**Fair value sensitivity analysis**	
31.12.2019	**100 p increase**	**100 p decrease**	**100 p increase**	**100 p decrease**
Embedded derivatives	0	0	155.587	(163.786)
Investments in other companies	0	0	(1.072.618)	1.898.285
Hedge contracts	86.143	(86.143)	262.074	(271.255)
Interest bearing liabilities	(251.305)	251.305	0	0
	(165.162)	165.162	(654.957)	1.463.244
31.12.2018	**100 p increase**	**100 p decrease**	**100 p increase**	**100 p decrease**
Embedded derivatives	0	0	108.615	(110.398)
Other financial assets	0	0	0	0
Investments in other companies	0	0	(1.285.264)	2.077.616
Hedge contracts	134.727	(134.727)	649.920	(275.457)
Interest bearing liabilities	(505.481)	505.481	0	0
	(370.754)	370.754	(526.729)	1.691.761

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 40 Amounts are in ISK thousand

29. Market risk, contd.

c. *Aluminium risk*

Aluminium risk is the risk that changes in the price of aluminium has a negative impact on the income of the Group.

Two electricity sales contracts are in place at the accounting date. One is with Landsvirkjun with regards of Norðurál, one is with Norðurál in regards of the aluminium plant at Grundartangi and Orkuveita Reykjavíkur and Norðurál have also made an electricity sales contract due to sale of electricity to a pending aluminium plant in Helguvík, where delivery of electricity has begun partly with delivery to Grundartangi. These electricity sales contracts are denominated in USD and the price of the electricity is connected to the market price of aluminium. Income of electricity contracts that is effected by price of aluminium is 12,7% of total revenue in the reporting year 2019 (2018: 14,4%).

To reduce risk due to aluminium prices the Group has entered into derivative contracts to reduce the fluctuation of income affected by aluminium prices. The risk management department has permission to hedge this risk within approved limits for the nest 5 financial years. At the accounting date hedges amounted to 52% of expected income affected by aluminium price until 31 December 2020 (31.12 2018: 50%).

Embedded derivatives in electricity sales contracts

The aforementioned electricity sales contracts include embedded derivatives as income thereon is subject to changes in the future world market price of aluminium. In accordance with provisions of International standards on financial instruments, the fair value of embedded derivatives for Grundartangi has been measured and recognised in the financial statements and partly for the contracts with Helguvík.

As the market value of the embedded derivatives is not available their fair value has been measured with generally accepted evaluation methods. The expected net present value of the cash flow of a contract on the accounting date has been measured, based on the future price of aluminium on LME (London Metal Exchange) on the accounting date and expectations of price development of aluminium for the next 25 years according to the assessment of CRU, an independent evaluation party, as available on the accounting date. From the expected net present value of cash flow of the contract on the accounting date the expected net present value based on premises on aluminium price on the initial date of the contract is deducted. The difference is the fair value change of the derivative. The valuation is based on the premises that the derivative has no value at the initial date of the contract.

Embedded derivatives of the electricity sales contracts recognised in the financial statements are capitalised in the balance sheet at fair value at the accounting date and fair value changes during the year are recognised in the income statement among income on financial assets and liabilities.

29. Market risk, contd.

c. *Aluminium risk, contd.*

In the following table shows the calculated effect on financial instruments measured at fair value due to change in aluminium price, taking tax effect into account.

Sensitivity analysis on the price of aluminium

31.12.2019	**Sensitivity of Fair value**	
	10% decrease	**10% increase**
Embedded derivatives	(3.925.777)	3.925.777
Aluminium hedges	206.704	(203.968)
Total	(3.719.073)	3.721.809

31.12.2018	**Sensitivity of Fair value**	
	10% decrease	**10% increase**
Embedded derivatives	(4.437.550)	4.437.550
Aluminium hedges	192.401	(164.179)
Total	(4.245.149)	4.273.371

d. *Other market risk*

Other market risk such as interest spread and risk in shares in other companies is limited as investments in such securities is an insubstantial part of the Group's operation with the exception of liquity management. The value of the financial assets tied up in funds or in asset management is subject to changes in the market, e.g. due to price changes in the bond- and equity markets. For further information, see note 30.

30. Liquidity risk

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due.

The Group's cash and cash equivalents at end of the year amounted to ISK 8.657 million and deposits available in three to twelve months amounting to ISK 2.500 million as well as marketable securities amounting to ISK 7.333 million. Therefore the Group owned ISK 18.490 million in bank deposits. Furthermore, the Group had unused loan authorisations and a open credit line to the total amount of approx. ISK 9.600 million. The Group had thus in total ensured capital at year-end to the amount of approx. ISK 28.090 million. The corresponding amount at year end 2018 amounted to ISK 29.211 million.

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 42 Amounts are in ISK thousand

30. Liquidity risk, contd.

Contractual payments due to financial liabilities, including estimated interest payments, are specified as follows:

31.12.2019

	Carrying amount	Contractual cash flows	Less than 1 year	After 1 - 2 years	After 2 - 5 years	More than 5 years
Non-derivative financial instruments						
Trade receivables	4.915.008	4.915.008	4.915.008	0	0	0
Other receivables	368.978	368.978	368.978	0	0	0
Deposits	2.500.000	2.500.000	2.500.000	0	0	0
Marketable securities	7.333.014	7.333.014	7.333.014	0	0	0
Cash and cash equivalents	8.657.025	8.657.025	8.657.025	0	0	0
Interest-bearing liabilities	(154.019.113)	(189.602.397)	(21.567.633)	(18.900.312)	(53.088.328)	(96.046.124)
Accounts payable	(2.926.455)	(2.926.455)	(2.926.455)	0	0	0
Other liabilities	(3.273.550)	(3.273.550)	(3.273.550)	0	0	0
	(136.445.093)	(172.028.377)	(3.993.613)	(18.900.312)	(53.088.328)	(96.046.124)
Derivative financial instruments, net financial assets and financial liabilities						
Embedded derivatives	(6.679.329)	71.488.870	6.174.299	6.432.786	21.097.067	37.784.717
Hedge contracts	(313.489)	(53.800)	181.726	(154.582)	(80.944)	0
	(6.992.817)	71.435.070	6.356.026	6.278.204	21.016.124	37.784.717

31.12.2018

	Carrying amount	Contractual cash flows	Less than 1 year	After 1 - 2 years	After 2 - 5 years	More than 5 years
Non-derivative financial instruments						
Trade receivables	5.482.511	5.482.511	5.482.511	0	0	0
Other receivables	496.986	496.986	496.986	0	0	0
Deposits	3.000.000	3.000.000	3.000.000	0	0	
Marketable securities	4.223.231	4.223.231	4.223.231	0	0	0
Cash and cash equivalents	10.988.087	10.988.087	10.988.087	0	0	0
Interest-bearing liabilities	(151.283.870)	(184.148.522)	(18.170.439)	(18.162.051)	(55.108.120)	(92.707.911)
Accounts payable	(3.125.135)	(3.125.135)	(3.125.135)	0	0	0
Other liabilities	(3.055.169)	(3.055.169)	(3.055.169)	0	0	0
	(133.273.359)	(166.138.011)	(159.928)	(18.162.051)	(55.108.120)	(92.707.911)
Derivative financial instruments, net financial assets and financial liabilities						
Embedded derivatives	(5.316.869)	77.787.143	6.091.027	6.358.703	20.320.407	45.017.005
Hedge contracts	(82.688)	653.808	374.216	193.424	86.168	0
	(5.399.558)	78.440.950	6.465.243	6.552.127	20.406.575	45.017.005

If non-current loans are refinanced in order to prolong the loan terms, it can be assumed that the distribution of the repayments will be different from the above.

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 43 Amounts are in ISK thousand

31. Credit risk

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk is mainly due to whole sale electricity contracts and derivatives that the Group has entered into for hedging purposes. Possible losses due to unpaid receivables are insubstantial and have limited effect on the Group's return. The Group disregards the financing factors of receivables that are expected to be collected within a year according to authorization in IFRS 15.

When entering into contracts it shall be insured, as possible, that the counterparty is trustworthy and settlement with large counterparties shall be looked into regularly as well as their credit rating.

The carrying amount of financial assets represents the maximum credit exposure, which is specified as follows:

	31.12.2019	31.12.2018
Trade receivables	4.915.008	5.482.511
Other current receivables	368.978	496.986
Hedge contracts	617.523	1.242.387
Deposits	2.500.000	0
Marketable securities	7.333.014	7.223.231
Cash and cash equivalents	8.657.025	10.988.087
Total	24.391.547	25.433.202

Financial assets as stated above are categorised at amortised cost or at fair value throught P/L. Their categorisation can be seen in note 34.

The maximum exposure to credit risk for trade receivables at the reporting date by type of customer was:

Trade receivables, industrial consumers	730.191	805.832
Trade receivable, retail	4.184.817	4.676.679
	4.915.008	5.482.511

Impairment of accounts receivables

The year 2019	Gross balance	Impairment	Book value
Not past due receivables	4.579.258	65.388	4.513.870
Past due, 1 to 30 days	241.703	4.911	236.792
Past due, 31 to 90 days	95.264	5.572	89.692
Past due, 91 days and older	98.531	23.877	74.653
Total	5.014.756	99.749	4.915.008

The year 2018	Gross balance	Impairment	Book value
Not past due receivables	5.007.040	64.764	4.942.277
Past due, 1 to 30 days	433.045	8.821	424.225
Past due, 31 to 90 days	89.879	9.563	80.316
Past due, 91 days and older	77.809	42.116	35.693
Total	5.607.774	125.264	5.482.511

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 44 Amounts are in ISK thousand

31. Credit risk, contd.

Changes in impairment of accounts receivables is specified as follows:	2019	2018
Balance at year beginning	125.264	123.651
Receivables written off	55.162	31.085
Impairment	(80.677)	(29.473)
Balance at year end	99.749	125.264

Allowance due to receivables is valuated at each reporting date by management. Collectability is valuated both in general using historic evidence and economic conditions and also specifically for receivables that are in default. Allowance is only deemed necessary for trade receivables.

Receivables due to sewage and cold water have statutory lien in properties and therefore allowance is not considered for those claims.

The Customer Services department governs the collection of receivables and supplies customers with information regarding claims. Collection is done in a well defined process where among other things, consistency in procedures is maintained as much as possible.

Impairment of accounts receivables is among other operating expenses in P/L.

32. *Operational risk*

Operational risk is the risk of negative impact on income as the result of natural disasters, weather, sabotage, terrorism, riots, war, poisoning, pollution, breakdowns, fires, accidents, inadequate information systems, administrative error, inadequate controls, prosecutions, fraud and human error. The risk management department assesses operational risk and monitors known operational risks of the Group and measures on a regular basis, if possible.

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 45 Amounts are in ISK thousand

33. *Fair value*

Comparison of fair value versus carrying amounts

The carrying amounts of financial assets and financial liabilities is equal to their fair value with the exception that interest bearing loans are stated at amortised cost. The fair values of interest bearing liabilities, together with the carrying amounts are specified as follows:

	31.12.2019		31.12.2018	
	Carrying amount	Fair value	Carrying amount	Fair value
Interest-bearing liabilities	154.019.113	160.699.452	151.283.870	153.218.591

The fair value of interest bearing liabilities is calculated based on present value of future principal and interest cash flows, discounted at the interest rate plus appropriate interest rate risk premium at the reporting date. The fair value of interest bearing liabilities is defined at Level 2.

Interest rates used for determining fair value

Where applicable, the interest yield curve at the reporting date is used in discounting estimated cash flow. The interests are specified as follows:

	31.12.2019	31.12.2018
Embedded derivatives in electr. sales contr.	6,84% til 7,21%	3,72% to 5,83%
Hedge contracts	-0,4% til 1,9%	-0,7% to 2,8%
Interest bearing liabilities	1,23% til 6,01%	1,19% to 7,94%

Fair value hierarchy

The table below analysis financial instruments carried at fair value, by valuation method. The different levels have been defined as follows:

Level 1: Quoted prices (unadjusted) in active markets for identical assets and liabilities.

Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e., as prices) or indirectly (i.e., derived from prices).

Level 3: Inputs for the asset or liability that are not based on observable market data (unobservable inputs). Valuation of shares in other companies is prepared by specialists within the company and other specialists and based on the results and official data on future earnings and investments in underlying assets.

31.12.2019	**Level 1**	**Level 2**	**Level 3**	**Total**
Shares in companies	0	0	5.216.267	5.216.267
Embedded derivatives in sales contracts	0	0	(6.679.329)	(6.679.329)
Hedge contracts	0	(313.489)	0	(313.489)
Marketable securities	7.333.014	0	0	7.333.014
	7.333.014	(313.489)	(1.463.062)	5.556.464
31.12.2018				
Shares in companies	0	0	3.859.015	3.859.015
Embedded derivatives in sales contracts	0	0	(5.316.869)	(5.316.869)
Other financial assets/liabilities	0	(82.688)	0	(82.688)
Marketable securities	4.223.231	0	0	4.223.231
	4.223.231	(82.688)	(1.457.854)	2.682.689

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 46 Amounts are in ISK thousand

33. Fair value, contd.

Changes in assets and liabilities defined at level 3 is specifed as follows:	**2019**	**2018**
Balance at year beginning	(1.457.854)	9.921.423
Sold/redemption	0	(3.903.481)
Valuation changes	(5.207)	(7.475.796)
Balance at year end	(1.463.062)	(1.457.854)

Embedded derivatives in electric sales contracts that have more than ten years duration is classified under level 3 due to the fact that the forward market for aluminium only reaches maximum of ten years.

Fair value measurement

A part of the Group´s financial assets and financial liabilities are measured at fair value. Fair value of these assets and liabilities are determined by market data or price in recent transactions if that is available. Otherwise, accepted valuation methods are used. Further information on fair value calculations can be found in the discussion of the relevant assets and liabilities in notes 17, 18 and 19.

34. Overview of financial instruments

Financial assets and financial liabilities are specified in the following financial groups:

	31.12.2019			**31.12.2018**		
	Amortised cost	**Financial asset/ financial liability at fair value through P/L**	**Financial asset/ financial liability at fair value through OCI**	**Amortised cost**	**Financial asset/ financial liability at fair value through P/L**	**Financial asset/ financial liability at fair value through OCI**
Shares in other companies			5.216.267			3.859.015
Embedd. contr.		(6.679.329)			(5.316.869)	
Bonds		0				
Hedge contr.		617.522			1.242.387	
Trade receivabl.	4.915.008			5.482.511		
Other receivabl.	368.978			496.986		
Prepaid exp.	184.464			307.939		
Bank deposits and marketable securities	2.500.000	7.333.014		3.000.000	4.223.231	
Cash	8.657.025			10.988.087		
Interest-bearing liabilities	(154.019.113)			(151.283.870)		
Hedge contr.		(931.011)			(1.325.075)	
Account payabl.	(2.926.455)			(3.125.135)		
Deferred rev.	(149.735)			(162.980)		
Other current liabilities	(3.273.550)			(3.055.169)		
	(143.743.379)	340.197	5.216.267	(137.351.631)	(1.176.326)	3.859.015

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 47 Amounts are in ISK thousand

35. Related parties

Definition of related parties

Reykjavik city, institutions and companies ruled by the city, associated companies, Board members, Directors and key management are considered as the Group's related parties. Spouses of the before mentioned and financially dependent children are also considered as related parties as well as companies owned by or directed by those in question.

Transactions with related parties

The parties mentioned here above have had transactions with the Group within the last year. Terms and conditions of these transactions were equivalent with transactions with unrelated parties.

The following gives an overview of the transactions with related parties during the last two years as well as a statement of receivables and payables. Transactions and positions with subsidiaries are eliminated in the financial statement, therefore that information is not provided. This information does not include sale of conventional household supplies to the related parties.

Sale to related parties:	**2019**	**2018**
Reykjavik City	2.224.274	1.749.885
Institutions and companies controlled by Reykjavik City	594.091	572.562
Associates	170	0
	2.818.535	2.322.448
Purchases from related parties:		
Reykjavik City	66.682	138.016
Institutions and companies controlled by Reykjavik City	11.471	11.273
Associates	58.230	54.136
	136.383	203.425
Receivables for related parties:		
Reykjavik City	184.011	142.723
Institutions and companies controlled by Reykjavik City	65.356	43.122
	249.366	185.845
Payables for related parties:		
Reykjavik City	168.214	352.786
Institutions and companies controlled by Reykjavik City	771	1.373
Associates	7.000	418
	175.985	354.577

Interest bearing loans from owners of the parent Company:		
Reykjavik City	9.811.423	10.898.111
Akranes town	579.839	644.060
Borgarbyggð, municipality	97.864	108.703
	10.489.126	11.650.874
Interest expense on loans from owners of the parent Company:		
Reykjavik City	93.334	1.102.730
Akranes town	5.516	64.930
Borgarbyggð, municipality	931	10.959
	99.781	1.178.619

Guarantee fee to owners

Orkuveita Reykjavíkur paid a guarantee fee to Reykjavík City and other owners of the company for guarantees they have granted on the Groups loans and borrowings. For further information regarding amounts and the guarantee fee, see note 11. Management´s salaries and benefits are listed in note 8.

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 48 Amounts are in ISK thousand

Notes

36. Group entities

Subsidiaries	Main operation	Share 31.12.2019	Share 31.12.2018
Gagnaveita Reykjavíkur ehf.	Data transfer	100,0%	100,0%
OR Eignir ohf.	Holding company	100,0%	100,0%
Veitur ohf.	Distribution of electricity and hot water	100,0%	100,0%
Orka náttúrunnar ohf.	Sale of electricity	100,0%	0,0%
ON Power ohf.	Sale of electricity	100,0%	100,0%
OR vatns- og fráveita sf.	Cold water and sewage	100,0%	100,0%
Reykjavík Energy Invest ehf.	Investments	100,0%	100,0%
Úlfljótsvatn frítímabyggð ehf.	Preparation company	100,0%	100,0%
Carbfix ohf.	Consulting, researches and innovation	100,0%	0,0%
Foss faseignafélag slhf.	Operation of real estate	0,0%	100,0%

In December 2018, the decision was made to wind-up Foss fasteignafélag slhf. and allocate its assets to the parent company, Orkuveita Reykjavíkur. A Winding-up Committee was elected at the shareholders‘ meeting and certified by the Annual Accounts Register in January 2019. The winding-up was completed in the fourth quarter of 2019.

On January 1, 2019, Orka náttúrunnar ohf.'s operations were divided into two companies, on the one hand, Orka náttúrunnar ohf., which has the functional currency of the ISK and, on the other, ON Power ohf., which has the functional currency of the US dollar.

In December 2019, a subsidiary, Carbfix ohf., was established, which aims to promote the further development and expansion of the Carbfix carbon sequestration process with the aim of reducing greenhouse gas emissions and combating climate change.

37. Statement of cash flows

Working capital from operation is specified as follows:	2019	2018
Profit for the year	6.916.370	5.978.394
Operating items that do not affect cash flow:		
Depreciation	12.121.294	10.270.945
Profit from sale of assets	(396)	(321.354)
Profit from sale of investments in other companies	(5.078)	(15)
Share in profit (loss) of associated companies	544	(6.033)
Pension liability change	42.980	76.843
Write-down of bonds	0	186.784
Currency fluctuation and indexation	2.826.334	2.172.907
Embedded derivatives in electricity contracts	850.175	4.705.572
Deferred tax liability	(222.486)	1.539.651
Hedge contracts	29.395	411.130
Fair value changes	(586.648)	(350.886)
Effects of currency fluctuation on cash and cash equivalents	(199.140)	(374.249)
Other items	(89.665)	47.327
Working capital from operation	21.683.679	24.337.015

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 49 Amounts are in ISK thousand

38. Other matters

Derivative contracts in default

Among other current liabilities are derivative contracts accounted for that are in default. The contracts have not been settled and Orkuveita Reykjavíkur has recently been sued regarding the claims. Great uncertainties is on how to settle them. In previous periods ISK 740 million have been expensed. This action is in no way an admittance of the debt on Orkuveita Reykjavikur's behalf and the amount can either increase or decrease when the contracts are settled. The contracts are accounted for among other current liabilities. See in note 27.

Repair at headquarters

At the end of August 2015, severe water damage occurred at the company's headquarters on Bæjarháls 1. Various options are being considered for renovations of the house and the estimated cost for the different options are estimated ISK 1.500-2.380 million. No decision has been made on the different alternatives.

Litigation and claims

Gagnaveita Reykjavíkur submitted a claim on Mars 5th 2019 to Síminn hf. demanding compensation for damage allegedly suffered as a result of violation of the Media Act, which was the subject of Decision published by the Post and Telecom Administration on July 3 th 2018. The claim amounts to ISK 1.3 billion for loss of income, accrued cost and interest. A formal response was requested from Síminn. On March 19th 2019 a response came from Síminn where they rejected the claim entirely. Síminn hf. took legal action against the Post and Telecom Administration, Gagnaveitur Reykjavíkur hf., Sýn hf. and Mílu ehf. in respect of the Decision of the Administration regarding the alleged violation. Primary proceedings has been decided on February 27th 2020.

In light of the aforementioned events, Gagnaveita Reykjavíkur's attorneys are currently preparing a case for the Reykjavík District Court, on the basis of XII section of the Act on Private Procedures no. 91/1991, to have one or more count appointed Valuation specialists assess the financial loss that Gagnaveita Reykjavíkur considers itself to have suffered as a result of the actions of Síminn hf.

No entries have been made regarding this claim in the company's annual financial report for 2019.

29. Market risk, contd.

a. *Currency risk, contd.*

Balance sheet currency risk

The Group's exposure to currency risk is specified as follows:

31.12.2019	CHF	EUR	USD	JPY	SEK	ISK	Other currencies	Total
Loans and borrowings	(9.255.023)	(20.397.149)	(31.642.746)	(3.801.448)	(2.613.969)		(1.825.255)	(69.535.590)
Trade receivables (accounts payables)	1	(196.658)	451.163	(0)	713	(202.639)	(7.400)	45.181
Bank deposits	274.804	1.224.839	446.418	292.357	152.223	151.394	380.942	2.922.977
Embedded derivatives			(6.679.329)					(6.679.329)
Hedge contracts		(109.304)	(204.184)					(313.489)
Receivables/(payables) within the Group*		(105.950)	(2.939.110)			1.770.490		(1.274.570)
Loans and borrowings to related parties*			44.122.941					44.122.941
Risk of Financial instruments	(8.980.218)	(19.584.221)	3.555.153	(3.509.092)	(2.461.033)	1.719.246	(1.451.713)	(30.711.879)
Subsidiaries equity in USD**			51.029.008					51.029.008
Investments in other companies			5.160.587					5.160.587
Total risk in equity	(8.980.218)	(19.584.221)	59.744.748	(3.509.092)	(2.461.033)	1.719.246	(1.451.713)	25.477.716

(*) The functional currency of ON Power is in USD and exchange gains/losses from assets and liabilities in ISK are accounted for through P/L. In addition the exchange gains/losses for foreign assets and liabilities of the parent company towards it´s subsidiary, ON Power, are accounted through P/L .

(**) The functional currency of ON Power is in USD and translational differences due to changes in the USD/ISK exchange rate is accounted for in equity.

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 38 Amounts are in ISK thousand

29. Market risk, contd.

a. *Currency risk, contd.*

Balance sheet currency risk, contd.

31.12.2018	CHF	EUR	USD	JPY	SEK	ISK	Other currencies	
Loans and borrowings	(10.149.953)	(26.861.257)	(33.585.771)	(4.542.820)	(3.054.356)		(2.037.939)	(80.232.096)
Trade receivables (accounts payables)	3.981	216.994	496.436	(57)	(374)	311.724	3.769	1.032.473
Bank deposits	441.755	3.773.145	2.204.267	173.871	183.379	53.479	360.126	7.190.022
Embedded derivatives			(5.316.869)					(5.316.869)
Hedge contracts	398.965	(176.794)	(1.694.704)	411.140	305.925		376.506	(378.962)
Financial assets at fair value through P/L			0					0
Receivables/(payables) within the group*		(103.869)	(2.840.905)			(4.357.842)		(7.302.616)
Loans and borrowings to related parties*			44.615.774			13.603.353		58.219.127
Risk of Financial instruments	(9.305.252)	(23.151.781)	3.878.228	(3.957.866)	(2.565.426)	9.610.714	(1.297.538)	(26.788.921)
Subsidiaries equity in USD**			63.518.091					63.518.091
Investments in other companies			3.795.941					3.795.941
Total risk in equity	(9.305.252)	(23.151.781)	71.192.260	(3.957.866)	(2.565.426)	9.610.714	(1.297.538)	40.525.111

Sensitivity analysis

Appreciation by 10% of the Icelandic krona against the following currencies at year-end would have increased (decreased) equity and profit or (loss) by the amounts shown below, taking into account tax effects. This analysis assumes that all other variables, in particular interest rates and aluminium prices, remain constant. Depreciation by 10% of the Icelandic krona against the above currencies would have had the equivalent, but opposite effect on the above currencies to the amounts shown above, on the basis that all other variables remain constant.

	CHF	EUR	USD	JPY	SEK	ISK	Other currencies	Total
				Profit or (loss)				
The year 2019	898.022	1.958.422	(355.515)	350.909	246.103	(171.925)	145.171	3.071.188
The year 2018	930.525	2.315.178	(387.823)	395.787	256.543	(961.071)	129.754	2.678.892
				Equity				
The year 2019	898.022	1.958.422	(5.974.475)	350.909	246.103	(171.925)	145.171	(2.547.772)
The year 2018	930.525	2.315.178	(7.119.226)	395.787	256.543	(961.071)	129.754	(4.052.511)

Consolidated Financial Statements of Orkuveita Reykjavikur 2019 39 Amounts are in ISK thousand

Notes

39. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, and have been applied consistently by Group entities besides, these are the Group's first financial statements that apply IFRS 16. Changes in accounting policies are described in note 3.

a. *Basis of consolidation*

i) Subsidiaries

Subsidiaries are entities controlled by the Group. Control exists when the Group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

ii) Associates

Associates are those entities in which the Group has significant influence, but not control, over the financial and operating policies. Significant influence is presumed to exist when the Group holds between 20 and 50 percent of the voting power of another entity.

Associates are entered in the Group's financial statements by using the equity method.
Associated companies are reported at original cost, including business cost. After the original transaction the share of the Company is reported until significant influence ceases or joint control is concluded.

iii) Transactions eliminated on consolidation

Intra-group balances and transactions, and any unrealised income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements. Unrealised gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Group’s interest in the investee. Unrealised losses are eliminated in the same way as unrealised gains, but only to the extent that there is no evidence of impairment.

b. *Foreign currency*

i Trade in foreign currencies

Trade in foreign currencies is reported into each consolidation company at the rate of the business day. Monetary assets and debts in foreign currencies are reported in the rate of the reporting date. Other assets and debts reported at fair value in foreign currency are reported at the rate of the day the fair value was set. Exchange difference due to foreign trade is reported through P/L.

ii Subsidiary with other currencies than the Icelandic krona

Assets and debts in the operations of a company of the consolidated financial statements that has USD as its functional currency are calculated into Icelandic kronas at the rate of the reporting date. Income and expenses of this companies operation is calculated into Icelandic kronas at the average exchange rate of the year. The exchange difference due to this is reported in a special account in the statement of comprehensive income. When operations with another functional currency than the Icelandic krona are sold, partly or in full, the accommodating exchange difference is recognised in P/L.

c. *Financial instruments*

i) Non-derivative financial assets

Loans, receivables and cash in bank are recognised when received. All other financial instruments are recognised in the financial statements when the Company becomes a party of contractual provisions of the relevant financial instruments.

39. Significant accounting policies, contd.

c. Financial instruments, contd.

i) Non-derivative financial assets, contd.

Financial assets are eliminated from the financial statements if the Company's contractual right to cash flow due to the financial asset expires or if the Group transfers the assets to another party without retaining control or nearly all risk and gain inherent with their ownership. Any interest in transferred financial assets that is created or retained by the group is recognized as a separate asset or liability.

Non-derivative financial instruments comprise of; financial assets at fair value throught OCI, financial assets at fair value through P/L and financial assets at amortised cost.

Financial assets at fair value through OCI

The Group's investments in equity securities are classified as financial assets at fair value throught OCI. Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses and foreign exchange gains and losses for monetary items are recognised directly in equity. When an investment is derecognised, the cumulative gain or loss in equity is transferred to profit or loss. Fair value changes recognised under equity are derecognised when the financial asset at fair value through OCI is derecognised.

Financial assets at fair value through profit or loss

A Financial asset is classified at fair value through profit or loss if it is current asset or if it is designated as such upon initial recognition. Financial assets are designated at fair value through profit or loss if purchase and sale decisions are based on their fair value in accordance with the Company´s risk policy or investment plan. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss. Direct transaction cost is recognised in the income statement as it is incurred.

Financial assets af amortised cost

Financial assets at amortised cost are financial assets with certain or determinable payments and are not listed in active markets. Such assets are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition financial assets at amortised cost are measured at amortised cost using the effective interest method, less any impairment losses.

Financial assets at amortised cost comprise of receivables and other current assets.

Cash and cash equivalents comprise cash balances and call deposits.

ii) Non-derivative financial liabilities

Financial liabilities are eliminated from the financial statements when the contractual agreements of the instrument are no longer valid.

The Group classifies non-derivative financial liabilities as financial liabilities at amortised cost. Such liabilities are recognised initially at fair value plus, for instruments not at fair value through profit or loss, any directly attributable transaction costs. Subsequent to initial recognition financial liabilities are measured at amortised cost using the effective interest method.

Other non-derivative financial liabilities comprise of borrowings, accounts payable and other current liabilities.

iii) Derivative financial instruments

Derivatives are recognised initially at fair value; attributable transaction costs are recognised in profit or loss when incurred. Subsequent to initial recognition, derivatives are measured at fair value in the balance sheet and fair value changes are recognised in the income statement.

39. Significant accounting policies, contd.

c. *Financial instruments, contd.*

iv) Embedded derivatives

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured at fair value through profit or loss.

d. *Property, plant and equipment*

i) Recognition and measurement

Items of property, plant and equipment, except distribution and production systems, 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 asset to a working condition for its intended use, and the costs of dismantling and removing the items and restoring the site on which they are located. Purchased software that is integral to the functionality of the related equipment is capitalised as part of that equipment.

Interest expenses on loans used to finance cost of buildings in construction are capitalised over the construction period. Interest is not calculated on preparation cost. After the assets have been taken into use interest expenses are expensed in the income statement.

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

The Group's distribution- and production systems, are stated at revalued carrying amount in the balance sheet, which is their fair value at the revaluation date less additional depreciation from that date. Revaluation of those assets is made on a regular basis. Value surplus due to the revaluation is recognised in a revaluation reserve among equity after taking the effect on deferred tax liability into consideration. Depreciation on the revalued carrying amount is recognised in the income statement. Upon sale or discontinuance of the asset the part of the revaluation reserve belonging to the asset is transferred from the revaluation reserve to retained earnings after taking tax effect into consideration. No recognition takes place from the revaluation reserve to retained earning unless the relevant asset is sold or discontinued.

The fair value of these assets is determined on the basis of the depreciated replacement cost. This consists in that an assessment is made on changes in the construction cost of comparable assets and both cost and accumulated depreciations are revaluated in accordance with those changes. The calculation is based on official information and actual statistics from the Company's books on value changes of cost of items and takes into account an estimate on the weight of each cost item in the total cost of construction of comparable assets. Cost items and their proportional weight were determined by experts within and outside of the Company. The impairment test of assets is also taken into consideration and revaluation is not recognised beyond the expected future cash flow of the assets. Distribution systems for hot water, cold water, sewage and electricity are licensed operations and subject to official revenue targets that are based mostly on changes in the Construction cost index. This is taken into consideration when revaluating these systems.

Gains and losses on disposal of an item of property, plant and equipment are determined by comparing the proceeds from disposal with the carrying amount of property, plant and equipment and are recognised net within “other income” in the income statement. When revalued assets are sold, the amounts included in the revaluation surplus reserve are transferred to retained earnings.

ii) Subsequent costs

The cost of replacing part of an item of property, plant and equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Group and its cost can be measured reliably. All other cost is expensed in the income statement when incurred.

39. Significant accounting policies, contd.

d. *Property, plant and equipment, contd.*

iii) Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property, plant and equipment. Land is not depreciated. Estimated useful lives are specified as follows:

Production system	7-60 years
Electricity distribution systems	15-80 years
Heating distribution systems	15-60 years
Cold water distribution systems	15-90 years
Sewer distribution system	15-60 years
Fiber-optic distribution system	9-41 years
Other real estate	25-50 years
Other equipment	3-25 years

Depreciation methods, useful lives and scrap value are reviewed on the accounting date.

e. *Intangible assets*

i) Heating rights

Heating rights are recognised in the balance sheet at amortised cost as intangible assets. Heating rights are separated from land up on purchase.

ii) Other intangible assets

Other intangible assets are measured at cost less accumulated depreciation and impairment losses.

iii) Subsequent expenditure

Subsequent expenditure is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in profit or loss as incurred.

iv) Amortisation

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful lives of intangible assets from the date that they are available for use. The estimated useful lives is determined as follows:

Software	5-7 years

f. *Inventories*

Inventories are measured at the lower of cost and net realisable value. The cost of inventories is based on the first-in first-out principle, and includes expenditure incurred in acquiring the inventories, production or conversion costs and other costs incurred in bringing them to their existing location and condition. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

39. Significant accounting policies, contd.

g. *Impairment*

i) Financial assets

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

An impairment loss in respect of a financial asset measured at amortised cost is calculated as the difference between its carrying amount, and the present value of the estimated future cash flows discounted at the original effective interest rate. An impairment loss in respect of an available-for-sale financial asset is calculated by reference to its fair value at each time. The Group defines decrease in fair value below cost as a subjective indication of impairment of available-for-sale financial assets when:

- decrease is 15% below cost or
- fair value decrease lasts for at least six months.

Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

All impairment losses are recognised in profit or loss. Any cumulative loss in respect of an available-for-sale financial asset recognised previously in equity is transferred to profit or loss.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognised. For financial assets measured at amortised cost and available-for-sale financial assets that are debt securities, the reversal is recognised in profit or loss. For available-for-sale financial assets that are equity securities, the reversal is recognised directly in equity.

ii) Non-financial assets

The carrying amounts of the Group's non-financial assets, other than inventories and deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated.

Impairment is recognized if the carrying amount of an asset or a cash generating unit exceeds its estimated recoverable amount. A cash generating unit is the smallest separable group of assets that form a cash flow that is mostly independent of other units or groups of units. Impairment loss of revalued operating assets is recognized in equity under revaluation reserve.

The recoverable amount of an asset or cash-generating unit is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset´s carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

h. *Employee benefits*

i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised in the income statement when they are due.

ii) Defined benefit plans

The Group's net obligation in respect of defined benefit pension plans is calculated separately for each plan by estimating the amount of future benefit that current and former employees have earned in return for their service in the current and prior periods. The benefit is discounted to determine its present value and any unrecognised past service costs and the fair value of any plan assets are deducted. The calculation is performed annually by a qualified actuary using the projected unit credit method. Changes in the obligation are recognised in the income statement as incurred.

39. Significant accounting policies, contd.

i. *Obligations*

An obligation is recognised in the balance sheet when the Group has the legal right or has entered into an obligation due to previous events and it is likely that it will incur cost upon settling the obligation. The obligation is measured on the basis of the estimated future cash flow, discounted based on interests reflecting market interests, and the risk inherent with the obligation.

j. *Revenue*

i) Revenues from sale and distribution of electricity and hot water

Revenue from the sale and distribution of electricity and hot water is recognised in the income statement according to measured delivery to purchasers during the year plus a fixed fee.

The rate for the distribution of electricity has a revenue cap set by the National Energy Authority in accordance with laws on energy number 65/2003. The revenue cap is based on actual figures from prior years from the operation of distribution utilities, the depreciation of assets, real losses in the distribution system and return on equity. When setting the revenue cap financial income and expenses are not taken into account. The rate is decided from the revenue cap and projections of sale of electricity in the Group´s utilities area.

ii) Revenues from sale of cold water and sewage

Revenue from the sale of cold water and sewage are based on the size of properties plus a fixed fee and are set forth linearly in the income statement. In addition revenue is stated for cold water according to measurement from specific industries.

iii) Connection revenues

Upon connection of new users to distribution systems of electricity, water and sewage or upon renewal of connection an initial fee is charged. The initial fee meets cost due to new distribution systems or their renewal. Income on connection fees is recognised in the income statement upon delivery of the service.

iv) Rental income

Rental income is recorded as income in the income statement linearly over the lease term.

v) Other revenues

Other revenue is recognised when generated or upon delivery of goods or services.

39. Significant accounting policies, contd.

k. *Financial income and expenses*

Finance income comprises interest income on funds invested, dividend income, changes in the fair value of financial assets at fair value through profit or loss, foreign exchange gain and gains on hedging instruments that are recognised in the income statement. Interest income is recognised as it accrues in the income statement, using the effective interest method. Dividend income is recognised in the income statement on the date that the Group's right to receive payment is established.

Finance expenses comprise interest expense on borrowings, unwinding of the discount on provisions, foreign exchange losses, impairment losses recognised on financial assets, and losses on hedging instruments that are recognised in the income statement. Borrowing cost is recognised in the income statement based on effective interests.

Effective interest is the required rate of return used when discounting estimated cash flow over the estimated useful life of a financial instrument or a shorter period when applicable, so that it equals to the book value of the financial asset or liability in the balance sheet.

Currency gains and losses 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.

l. *Income tax*

Income tax expense comprises current and deferred tax. Income tax expense is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years. The income tax ratio for the parent company is 37,6% and the tax ratio for the subsidiaries is 20,0%. Cold water supply and sewage is exempt from tax.

Deferred tax is recognised 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 the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax was measured in accordance with the current tax rate, which is 37,6% for the parent company that is a partnership and 20,0% for the subsidiaries that are companies with limited liability.

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

m. *Segment reporting*

A segment is a distinguishable component of the Group that is engaged in business and is capable to earn revenues and accept cost, both within and outside of the Group. The return of all segments is overviewed by management to value their performance.

Segment results and their assets include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

Segment investments are investments in property, plant and equipment and intangible assets.
Inter-segment pricing is determined on an arm's length basis.

39. Significant accounting policies, contd.

n. *Determination of fair value*

A number of the Group's accounting policies and disclosures require the determination of fair value, for both financial and non-financial assets and liabilities.

The Group´s CFO is responsible for overseeing all significant fair value measurements, including Level 3 fair values. Risk management, led by the CFO, regularly reviews significant unobservable inputs and valuation adjustments. If third party information, such as broker quotes or pricing services, is used to measure fair values, then that information is used to support the conclusion that such valuations meet the requirements of IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

When measuring the fair value of an asset or a liability, the Group uses market observable data as far as possible.

Fair values are categorised into different levels in a fair value hierarchy based on the inputs used in the valuation techniques as follows.

Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

If the inputs used to measure the fair value of an asset or a liability might be categorised in different levels of the fair value hierarch, then the fair value measurement is categorised in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Group recognises transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred.

Further information about the assumptions made in measuring fair values can be found in relevant notes and in note 33 regarding fair value.

o. *Property, plant and equipment*

The fair value of production- and fiber-optic systems that have undergone a revaluation is determined on the basis of the depreciated replacement cost, which consists in the assessment of changes in construction cost of comparable assets and both cost and accumulated depreciation are revalued in accordance with those changes. The results of the impairment tests are also taken into consideration and revaluation is not recognised beyond the expected future cash flow of those assets.

p. *Investments in equity and debt securities*

The fair value of financial assets at fair value through profit or loss is determined on the basis of their market value at the reporting date. If the market value is not known the valuation is based on generally accepted valuation methods. Valuation methods can be based on known recent financial transactions between unrelated parties. In applying these valuation methods factors are considered which would be used in the respective market concerning calculation of fair value and the methods are in accordance with generally accepted methods concerning valuation of financial assets.

39. Significant accounting policies, contd.

q. *Derivatives*

The fair value of derivatives is based on their market value, if available. If the market value is not available the fair value is determined on the basis of generally accepted valuation methods.

Valuation methods may be based on prices in recent transactions between unrelated parties. The measurement is based on the value of other financial instruments comparable to the instrument in question, methods in order to evaluate the present value of cash flow or other valuation methods, which may be applied in order to reliably assess the real market value. When valuation methods are applied all factors are used, which market parties would use in price evaluations, and the methods are in accordance with generally accepted methods for the price evaluation of financial instruments. The Group verifies on a regular basis its valuation methods and tests them by using a price obtained in a transaction on an active market with the same instrument, without adjustments and changes, or are based on information from an active market.

The fair value of derivative agreements not listed in active markets is determined by use of valuation methods, which are regularly reviewed by qualified employees. All valuation models used must be approved and tested in order to ensure that the results reflect the data used.

The most reliable indication of the fair value of derivative agreements at the beginning is the purchase value, unless the fair value of the instruments is verifiable in comparison with other listed and recent market transactions with the same financial instrument or based on a valuation method where variables are only based on market data. When such data is available the Group recognises profit or loss at the initial registration date of the instruments.

The fair value of interest rate swaps is based on broker quotes. Those quotes are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

r. *Trade and other receivables*

The fair value of trade and other receivables, is estimated at the present value of future cash flows, discounted at the market rate of interest at the reporting date if applicable. This fair value is determined for disclosure purposes.

s. *Non-derivative financial liabilities*

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

t. *Leases*

The Group applied IFRS 16 using the modified retrospective approach, under which the cumulative effect of initial application is recognised in retained earnings at 1 January 2019. Accordingly, the comparative information presented for 2018 is not restated – i.e. it is presented, as previously reported, under IAS 17 and related interpretations. The details of the changes in accounting policies are disclosed below. Additionally, the disclosure requirements in IFRS 16 have not generally been applied to comparative information.

Policy applicable after 1 January 2019

At inception of a contract, the Group assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. To assess whether a contract conveys the right to control the use of an identified asset, the Group uses the definition of a lease in IFRS 16.

39. Significant accounting policies, contd.

t. *Leases, contd.*

Policy applicable after 1 January 2019, contd.

i As a lessee

At commencement or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of its relative stand-alone prices. However, for the leases of property the Group has elected not to separate non-lease components and account for the lease and non-lease components as a single lease component.

The Group recognises a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the end of the lease term, unless the lease transfers ownership of the underlying asset to the Group by the end of the lease term or the cost of the right-of-use asset reflects that the Group will exercise a purchase option. In that case the right-of-use asset will be depreciated over the useful life of the underlying asset, which is determined on the same basis as those of property and equipment. In addition, the right-of-use asset is periodically reduced by impairment losses, if any, and adjusted for certain remeasurements of the lease liability.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, the Group's incremental borrowing rate. Generally, the Group uses its incremental borrowing rate as the discount rate.

The Group determines its incremental borrowing rate by obtaining interest rates from various external financing sources and makes certain adjustments to reflect the terms of the lease and type of the asset leased.

Lease payments included in the measurement of the lease liability comprise the following:
– fixed payments, including in-substance fixed payments;
– variable lease payments that depend on an index or a rate, initially measured using the index or rate as at the commencement date;
– amounts expected to be payable under a residual value guarantee; and
– the exercise price under a purchase option that the Group is reasonably certain to exercise, lease payments in an optional renewal period if the Group is reasonably certain to exercise an extension option, and penalties for early termination of a lease unless the Group is reasonably certain not to terminate early.

The lease liability is measured at amortised cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, if there is a change in the Group's estimate of the amount expected to be payable under a residual value guarantee, if the Group changes its assessment of whether it will exercise a purchase, extension or termination option or if there is a revised in-substance fixed lease payment.
When the lease liability is remeasured in this way, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or is recorded in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.
Right-of-use assets and lease liabilities are listed in the balance sheet.

The Group has elected not to recognise right-of-use assets and lease liabilities for leases of low-value assets and short-term leases, including IT equipment. The Group recognises the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

39. Significant accounting policies, contd.

t. *Leases, contd.*
Policy applicable after 1 January 2019, contd.

ii As a lessor

At inception or on modification of a contract that contains a lease component, the Group allocates the consideration in the contract to each lease component on the basis of their relative stand-alone prices.

When the Group acts as a lessor, it determines at lease inception whether each lease is a finance lease or an operating lease.

To classify each lease, the Group makes an overall assessment of whether the lease transfers substantially all of the risks and rewards incidental to ownership of the underlying asset. If this is the case, then the lease is a finance lease; if not, then it is an operating lease. As part of this assessment, the Group considers certain indicators such as whether the lease is for the major part of the economic life of the asset.

The Group recognises lease payments received under operating leases as income on a straight-line basis over the lease term as part of 'other revenue'.

Generally, the accounting policies applicable to the Group as a lessor in the comparative period were not different from IFRS 16.

Policy applicable before 1 January 2019

For contracts entered into before 1 January 2019, the Group determined whether the arrangement was or contained a lease based on the assessment of whether:

– fulfilment of the arrangement was dependent on the use of a specific asset or assets; and

– the arrangement had conveyed a right to use the asset. An arrangement conveyed the right to use the asset if one of the following was met:

- the purchaser had the ability or right to operate the asset while obtaining or controlling more than an insignificant amount of the output;
- the purchaser had the ability or right to control physical access to the asset while obtaining or controlling more than an insignificant amount of the output; or
- facts and circumstances indicated that it was remote that other parties would take more than an insignificant amount of the output, and the price per unit was neither fixed per unit of output nor equal to the current market price per unit of output.

39. Significant accounting policies, contd.

t. *Leases, contd.*
Policy applicable before 1 January 2019, contd.

i As a lessee

In the comparative period, as a lessee the Group classified leases that transferred substantially all of the risks and rewards of ownership as finance leases. When this was the case, the leased assets were measured initially at an amount equal to the lower of their fair value and the present value of the minimum lease payments. Minimum lease payments were the payments over the lease term that the lessee was required to make, excluding any contingent rent. Subsequent to initial recognition, the assets were accounted for in accordance with the accounting policy applicable to that asset.

Assets held under other leases were classified as operating leases and were not recognised in the Group's statement of financial position. Payments made under operating leases were recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received were recognised as an integral part of the total lease expense, over the term of the lease.

ii As a lessor

When the group was a lessor it determinted at the beginning of the lease whether it was a finance lease or a operating lease.

To classify each lease, the Group made an overall assessment of whether the lease transferred substantially all of the risks and rewards incidental to ownership of the underlying asset. If this was the case, then the lease was a finance lease; if not, then it was an operating lease. As part of this assessment, the Group considered certain indicators such as whether the lease was for the major part of the economic life of the asset.

40. New accounting standards not yet adopted

A number of new standards are effective for annual periods beginning after 1 January 2019 and earlier application is permitted; however, the Group has not early adopted the new or amended standards in preparing these consolidated financial statements.

The following amended standards and interpretations are not expected to have a significant impact on the Group's consolidated financial statements.

– Changes in the refrences to the International Accoounting Standards.
– Definition on business (changes in IFRS 3).
– Definition á material effect (changes in IAS 1 and IAS 8).
– IFRS 17 Insurance Contracts.

Non-Financial Information (unaudited)

OR Values

The values of OR are foresight, efficiency and integrity and serve as the guiding principles of all of the activities of the company.

Environment

Orkuveita Reykjavíkur is trusted for the resources it utilizes. The responsibility involves working on the ideology of sustainable development and ensuring sustainable utilization, namely that generations have the same opportunities as present-day generations to exploit the resources and that it can be verified that this is done. OR commits itself to seeking successful solutions where public resource utilization is weighed and evaluated in relation to other interests. OR will protect the resources from hazards and imposition, due to the responsibility of the company. OR operates according to the environmental and the resource policy, published on the company's website, www.or.is, and is subject to independent certification under ISO 14001. A detailed article is prepared for environmental aspects of the operation in 2019 in the annual report of OR 2019, at the URL arsskyrsla2019.or.is.

Social issues

Orkuveita Reykjavíkur is a large company nationwide and has extensive knowledge and experience in the utilization of geothermal energy and other aspects of the company's operations. OR disseminates knowledge and encourages responsible environmental and positive impacts on society. Transparency is a key element in OR's business and makes the company fully aware of the social aspects of the business in 2019 in the annual report, OR 2019, at the URL arsskyrsla2019.or.is.

Human resources

At Orkuveita Reykjavíkur, people have the skills needed to perform the tasks that the company's activities require. On the OR web site, www.or.is, you can find employee policy, remuneration policy and the employee KPI. OR ensures that employees enjoy equal rights, in accordance with the Gender Equality Policy and Equal Opportunities. OR´s employee Policy is based on the company´s values and overall policies and is set in accordance with the Company's corporate governance policy. The company reports on human resources in 2019 in the annual report, OR 2019, at arsskyrsla2019.or.is

Corruption, bribery and human rights

At OR there are registered work procedures for the processing of issues when a staff member is alleged to have violated company rules or committed fraud at work. The rules of procedure are accessible to all employees on the company’s intranet. These specify what are considered to be deviations or violations at work. If an employee becomes aware of possible breaches committed by another employee(s) at work or there are grounds to suspect fraudulent activities or incidents, the immediate superior must be notified. It is also possible to notify the company's internal auditor of any potential breaches or frauds. Those who receive indications of possible violations or fraud have a duty to report it, but to treat the information with complete confidentiality. OR’s lawyer can also provide legal advice or assistance as the case may be. The management of OR, managing directors and directors are responsible for the internal supervision of their specific divisions. Quality Control is responsible for ensuring that OR’s internal monitoring system is effective. OR's quality control system is independently certified by external entities.
OR attaches great importance to gender equality, and the Equal Opportunities Policy of the Company implements a commitment for continuous improvement on equality at the workplace. The company adopts the human rights provisions of the Constitution on the basis of the equality policy aimed at evaluating individuals for their own merit and for equal rights. The equality policy is based on OR values and overall policies and is set in accordance with the company's corporate governance policy.

More information on non-financial information

In conjunction with the annual accounts, OR publishes the Annual Report 2019, which includes More detailed information about non-financial information. The report is available at arsskyrsla2019.or.is