

HS Orka hf.

Condensed Interim Financial Statements  
for the Six months ended 30 June 2014  
ISK

HS Orka hf.  
Brekkuvegur 36  
260 Reykjanesbær

Reg. no. 680475-0169

# Contents

---

Endorsement by the Board of Directors and Management .....	3
Independent Auditors' Review Report .....	4
Statement of Comprehensive Income (Loss) .....	5
Statement of Financial Position .....	6
Statement of Changes in Equity .....	7
Statement of Cash Flows .....	8
Notes to the Financial Statements .....	9

# Endorsement by the Board of Directors and the Management

---

The condensed interim financial statements of HS Orka hf. (the Company) for the period from 1 January to 30 June 2014 are prepared in accordance with the International Accounting Standard, IAS 34, *Interim Financial Reporting*.

According to the statement of comprehensive income, the Company's operating revenue amounted to ISK 3,582 million for the period 1 January - 30 June 2014 (2013: ISK 3,590 million) and the profit for the period amounted to ISK 740 million (2013: ISK 1,415 million loss). Total comprehensive income amounted to ISK 715 million (2013: ISK 1,480 comprehensive loss). According to the statement of financial position, the Company's assets amounted to ISK 44,387 million at the end of June 2014 (at year end 2013: ISK 44,873 million). Equity amounted to ISK 26,516 million at the end of June 2014 (at year end 2013: ISK 26,021 million) or 59.7% of total capital (at year end 2013: 58.0%).

To the best knowledge of the Board of Directors and the Management, the Company's condensed interim financial statements are in accordance with International Financial Reporting Standards as adopted by the EU and it is the opinion of the Board of Directors and the Management that the condensed interim financial statements give a true and fair view of the Company's assets, liabilities and financial position as at 30 June 2014, and its financial performance and changes in cash flows in the period from 1 January to 30 June 2014.

Furthermore, it is the opinion of the Board of Directors and the Management that the condensed interim financial statements and endorsement by the Board of Directors and the Management contain a fair overview of the Company's financial development and performance, its position and describe the main risk factors and uncertainties faced by the Company.

The Board of Directors and the Management of HS Orka hf. have today approved the Company's condensed interim financial statements for the six months ended 30 June 2014 and confirmed by means of their signatures.

Reykjanesbær, 12 August 2014.

The Board of Directors:

Ross Beaty  
Chairman of the board

Gylfi Árnason

John Carson

Anna Skúladóttir

Lynda Freeman

Managing Director:  
Ásgeir Margeirsson

Assistant Managing Director:  
Albert Albertsson

# Independent Auditors' Review Report

---

To the Board of Directors of HS Orka hf.

We have reviewed the accompanying statement of financial position of HS Orka hf. as at 30 June 2014 and the related statements of comprehensive income, changes in equity and cash flows for the six-month period then ended, and notes to the interim financial information. Management is responsible for the preparation and fair presentation of this condensed interim financial information in accordance with IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on this condensed interim financial information based on our review.

## Scope of review

We conducted our review in accordance with International Standard on Review Engagements 2410 *Review of Interim Financial Information Performed by the Independent Auditor of the Entity*. A review of interim financial information consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with International Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly, we do not express an audit opinion.

## Conclusion

Based on our review, nothing has come to our attention that causes us to believe that the accompanying condensed interim financial information is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting*.

Reykjavík, 12 August 2014

**KPMG ehf.**

Sæmundur Valdimarsson  
Margret G. Flóvenz

# Statement of Comprehensive Income (Loss) for the six months ended 30 June 2014

	Note	2014 Q2	2013 Q2	2014 H1	2013 H1
Operating revenue .....	5	1.683.049	1.642.827	3.582.157	3.590.097
Production cost and cost of sales .....		( 1.403.908)	( 1.393.715)	( 2.695.434)	( 2.711.825)
<b>Gross profit</b> .....		279.141	249.112	886.723	878.272
Other operating expenses .....	6	( 102.641)	( 62.449)	( 220.977)	( 235.951)
<b>Results from operating activities</b> .....		176.500	186.663	665.746	642.321
Finance income .....		79.973	291.745	383.837	1.314.176
Finance costs .....		( 99.798)	( 113.051)	( 201.008)	( 275.108)
Changes in fair value of swap contracts .....		20.049	81.275	41.218	334.728
Changes in fair value of embedded derivatives .....		465.705	( 1.194.429)	( 242.063)	( 3.950.368)
<b>Net finance income (expense)</b> .....	7	465.929	( 934.460)	( 18.016)	( 2.576.572)
Share of profit of associates .....		136.064	93.636	222.269	132.411
<b>Profit (loss) before income tax</b> .....		778.493	( 654.161)	869.999	( 1.801.840)
Income tax (expense) recovery .....		( 128.486)	149.554	( 129.546)	386.850
<b>Profit (loss) for the period</b> .....		650.007	( 504.607)	740.453	( 1.414.990)
<b>Other comprehensive income (loss)</b>					
<b>Items that will never be reclassified to profit or loss</b>					
Remeasurement of defined benefit liability .....		( 19.827)	( 33.491)	( 12.825)	( 33.491)
Tax on items that will never be reclassified to profit or loss .....		3.965	6.698	2.565	6.698
		( 15.862)	( 26.793)	( 10.260)	( 26.793)
<b>Items that may be reclassified subsequently to profit or loss</b>					
Foreign currency translation difference on associates .....		6.060	( 6.665)	( 14.919)	( 38.480)
<b>Other comprehensive loss, net of tax</b> .....		( 9.802)	( 33.458)	( 25.179)	( 65.273)
<b>Total comprehensive income (loss) for the period</b> .....		640.205	( 538.065)	715.274	( 1.480.263)
<b>Earnings per share</b>					
Basic and diluted earnings (loss) per share .....		0,08	( 0,06)	0,09	( 0,18)

Notes on pages 9 to 13 are an integral part of these financial statements

# Statement of Financial Position as at 30 June 2014

<b>Assets</b>	<b>Note</b>	<b>30.6.2014</b>	<b>31.12.2013</b>
Operating assets .....		31.139.372	31.422.097
Operating assets under construction .....		3.798.915	3.841.191
Intangible assets .....		1.080.480	1.050.738
Investments in associates .....		759.620	863.619
Investments in other companies .....		27.075	27.075
Bonds .....		324.877	313.586
Embedded derivatives in power sales contracts .....		0	260.580
Prepaid lease and royalty fee .....		497.835	492.449
Long term receivable .....		344.655	331.364
Total non-current assets		<u>37.972.829</u>	<u>38.602.699</u>
Inventories .....		424.643	414.388
Bonds .....		84.468	81.532
Trade and other receivables .....		976.511	1.003.885
Short term investments .....		365.866	357.020
Cash and cash equivalents .....	8	4.562.553	4.413.403
Total current assets		<u>6.414.041</u>	<u>6.270.228</u>
<b>Total assets</b>		<u><u>44.386.870</u></u>	<u><u>44.872.927</u></u>
<b>Equity</b>			
Share capital .....		7.841.124	7.841.124
Share premium .....		7.038.855	7.038.855
Translation reserve .....		271.018	285.937
Revaluation reserve .....		5.995.442	6.142.790
Retained earnings .....		5.369.719	4.712.178
Total equity		<u>26.516.158</u>	<u>26.020.884</u>
<b>Liabilities</b>			
Loans and borrowings .....		11.131.347	12.299.097
Pension obligations .....		1.810.500	1.792.000
Deferred tax liability .....		758.945	631.964
Embedded derivatives in power sales contracts .....		30.843	0
Currency and interest rate swap contracts .....		215.333	263.495
Total non-current liabilities		<u>13.946.968</u>	<u>14.986.556</u>
Loans and borrowings .....		2.206.540	2.221.609
Trade and other payables .....		1.210.501	1.094.759
Embedded derivatives in power sales contracts .....		88.640	137.999
Currency and interest rate swap contracts .....		418.063	411.120
Total current liabilities		<u>3.923.744</u>	<u>3.865.487</u>
<b>Total liabilities</b>		<u>17.870.712</u>	<u>18.852.043</u>
<b>Total equity and liabilities</b>		<u><u>44.386.870</u></u>	<u><u>44.872.927</u></u>

Notes on pages 9 to 13 are an integral part of these financial statements

# Statement of Changes in Equity

## for the six months ended 30 June 2014

	Share capital	Share premium	Translation reserve	Revaluation reserve	Retained earnings	Total
<b>1 January - 30 June 2013</b>						
Equity at 1 January 2013 .....	7.841.124	7.038.855	334.465	6.443.110	4.947.149	26.604.703
Loss for the period .....					( 1.414.990)	( 1.414.990)
Other comprehensive loss .....			( 38.480)		( 26.793)	( 65.273)
Total comprehensive loss .....			( 38.480)		( 1.441.783)	( 1.480.263)
Revaluation reserve transferred to retained earnings .....				( 150.170)	150.170	0
Dividends declared ISK 0.02 per share ....					( 150.000)	( 150.000)
Equity at 30 June 2013 .....	7.841.124	7.038.855	295.985	6.292.940	3.505.535	24.974.440
<b>1 January - 30 June 2014</b>						
Equity at 1 January 2014 .....	7.841.124	7.038.855	285.937	6.142.790	4.712.178	26.020.884
Profit for the period .....					740.453	740.453
Other comprehensive loss .....			( 14.919)		( 10.260)	( 25.179)
Total comprehensive (loss) income .....			( 14.919)		730.193	715.274
Revaluation reserve transferred to retained earnings .....				( 147.348)	147.348	0
Dividends declared ISK 0.03 per share ....					( 220.000)	( 220.000)
Equity at 30 June 2014 .....	7.841.124	7.038.855	271.018	5.995.442	5.369.719	26.516.158

Notes on pages 9 to 13 are an integral part of these financial statements

# Statement of Cash Flows

## for the six months ended 30 June 2014

	2014 H1	2013 H1
<b>Cash flows from operating activities</b>		
Profit (loss) for the period .....	740.453	( 1.414.990)
Adjustments:		
(Profit) loss on sale of operating assets .....	( 1.637)	16
Increase in pension obligations .....	5.675	39.809
Depreciation and amortization .....	677.919	652.091
Net finance expenses .....	18.016	2.576.572
Share of profit of associates .....	( 222.269)	( 132.411)
Income tax expense (recovery) .....	129.546	( 386.850)
	1.347.703	1.334.237
Inventories, (increase) decrease .....	( 10.255)	18.179
Receivables, decrease .....	38.785	99.065
Current liabilities, increase (decrease) .....	129.706	( 65.082)
Net cash from operations before interest and taxes	1.505.939	1.386.399
Interest income received .....	109.467	98.942
Interest and indexation costs paid .....	( 190.642)	( 240.325)
Net cash provided by operating activities	1.424.764	1.245.016
<b>Cash flows from investing activities</b>		
Acquisition of operating assets and assets under construction .....	( 340.852)	( 734.676)
Proceeds from sale of operating assets .....	5.610	950
Acquisition of intangible assets .....	( 45.781)	( 10.460)
Acquisition of shares in associates .....	( 6.000)	( 10.000)
Dividend received from associates .....	317.349	217.100
Net cash used in investing activities	( 69.674)	( 537.086)
<b>Cash flows from financing activities</b>		
Paid dividends .....	( 220.000)	( 150.000)
Repayment of borrowings .....	( 983.038)	( 1.002.960)
Net cash used in financing activities	( 1.203.038)	( 1.152.960)
<b>Increase (decrease) in cash and cash equivalents</b> .....	152.052	( 445.030)
<b>Cash and cash equivalents at 1 January</b> .....	4.413.403	5.227.728
<b>Effect of exchange rate fluctuations on cash held</b> .....	( 2.902)	( 37.302)
<b>Cash and cash equivalents at 30 June</b> .....	4.562.553	4.745.396



# Notes to the Condensed Interim Financial Statements

---

## 1. Reporting entity

HS Orka hf. is a limited liability company domiciled in Iceland. The Company's registered office address is Brekkustígur 36, Reykjanesbær, Iceland. The Company generates and sells electricity and hot water for heating. The condensed interim financial statements as at and for the six months ended 30 June 2014 comprise of the Company and its interest in associates. The Company is a subsidiary of Magma Energy Sweden AB. The financial statements of the Company are part of the consolidated financial statements of the ultimate parent company Alterra Power Corp., headquartered in Canada.

The Company's financial statements can be found at its website [www.hsorka.is](http://www.hsorka.is) and at the website of the Icelandic Stock Exchange; [www.nasdaqomxnordic.com](http://www.nasdaqomxnordic.com).

## 2. Statement of compliance

This condensed interim financial report has been prepared in accordance with IAS 34 *Interim Financial Reporting*. Selected explanatory notes are included to explain events and transactions that are significant to an understanding of the changes in financial position and performance of the Company since the last annual financial statements as at and for the year ended 31 December 2013. This condensed interim financial report does not include all the information required for full annual financial statements prepared in accordance with International Financial Reporting Standards and should be read in conjunction with the Financial Statements of 31 December 2013.

These condensed interim financial statements were approved by the Board of Directors on 12 August 2014.

## 3. Significant accounting policies

Except as described below, the accounting policies applied by the Company in these condensed interim financial statements are the same as those applied by the Company in its financial statements as at and for the year ended 31 December 2013.

These condensed interim financial statements are prepared in Icelandic krona, which is the Company's functional currency and all amounts have been rounded to the nearest thousand. They are based on historical cost, except for the following:

- a part of operating assets is recognized at revalued cost, which was the fair value at the revaluation dates of 1.1.2008 and 31.12.2012
- derivative financial instruments are measured at fair value
- embedded derivatives in power sales contracts are measured at fair value
- financial instruments at fair value through profit or loss are measured at fair value

### a Changes in accounting policies

The Company has adopted all new standards and amendments to standards with a date of initial application prior to or on 1 January 2014 that have been adopted by the EU (European Union). None of those effective from 1 January 2014 had effects on these financial statements.

## 4. Use of estimates and judgments

The preparation of interim financial statements 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.

In preparing these condensed interim financial statements, the significant judgements made by management in applying the Company's accounting policies and the key source of estimation uncertainty were the same as those that applied to the financial statements as at and for the year ended 31 December 2013.

## Notes, continued

### 5. Segment reporting

The Company has three operating segments that are described below:

#### Power Production

Includes production and sale of electricity, heating water and fresh water from subterranean steam.

#### Electricity Sale

Includes purchases and sale of electricity to users other than mass users and power companies.

#### Other

Includes sale of service, rental of facilities and equipment, and other sales.

	<b>Power production</b>	<b>Electricity sale</b>	<b>Other</b>	<b>Total</b>
<b>1 January - 30 June 2014</b>				
External revenue .....	1.389.645	1.715.304	477.208	3.582.157
Inter-segment revenue .....	808.158			808.158
Total segment revenue .....	2.197.803	1.715.304	477.208	4.390.315
Segment operating results .....	474.005	150.633	41.108	665.746
<b>Unallocated items</b>				
Net finance expenses .....			( 18.016)	
Share of profit of associates .....				222.269
Income tax expense .....			( 129.546)	
Profit for the period .....				740.453
Segment assets .....	35.431.342	45.695	541.730	36.018.767
Unallocated assets .....				8.368.103
Total assets .....				44.386.870
Unallocated liabilities .....				17.870.712
Capital expenditures .....	352.393	5.196	29.044	386.633
Depreciation and amortization .....	649.009	3.308	25.602	677.919
<b>1 January - 30 June 2013</b>				
External revenue .....	1.537.286	1.542.578	510.233	3.590.097
Inter-segment revenue .....	779.500			779.500
Total segment revenue .....	2.316.786	1.542.578	510.233	4.369.597
Segment operating results .....	481.838	125.969	34.514	642.321
<b>Unallocated items</b>				
Net finance expenses .....			( 2.576.572)	
Share of profit of associates .....				132.411
Income tax recovery .....				386.850
Loss for the period .....			( 1.414.990)	
Segment assets .....	35.647.977	46.079	546.565	36.240.621
Unallocated assets .....				9.236.890
Total assets .....				45.477.511
Unallocated liabilities .....				20.503.072
Capital expenditures .....	738.258	999	5.879	745.136
Depreciation and amortization .....	632.546	2.902	16.643	652.091

## Notes, continued

### 5. Segment reporting, contd.:

#### Major customers

Revenues from one customer of the Company's power production segment represents approximately ISK 798 million of the Company's total revenues during the period (1.1.2013 - 30.6.2013: ISK 945 million).

Revenues from HS Veitur hf. Amounted to ISK 993 million during the period (1.1.2013 - 30.6.2013: ISK 986 million) and relates to segments as follows:

	Power production	Electricity sale	Other	Total
Revenues 1.1. - 30.6.2014 .....	393.158	154.795	444.561	992.514
Revenues 1.1. - 30.6.2013 .....	405.609	137.453	443.419	986.481

### 6. Other operating expenses

Operating expenses specifies as follows:

	2014 Q2	2013 Q2	2014 H1	2013 H1
Salaries and related expenses .....	49.828	37.811	103.023	83.663
Changes in pension fund commitment .....	4.210	( 8.850)	11.343	12.045
Administrative expenses .....	44.185	29.796	98.123	133.042
Depreciation and amortization .....	4.418	3.692	8.488	7.201
Total operating expenses .....	102.641	62.449	220.977	235.951

### 7. Net finance expenses

Net finance expenses specifies as follows:

	2014 Q2	2013 Q2	2014 H1	2013 H1
Interest income on cash, loans and receivables .....	72.775	87.925	139.553	152.860
Net foreign exchange (loss) gain .....	( 4.930)	189.530	220.770	1.125.805
Fair value changes on financial assets through profit or loss .....	12.128	14.290	23.514	35.511
Total finance income .....	79.973	291.745	383.837	1.314.176
Interest expense .....	( 87.892)	( 105.024)	( 178.757)	( 216.505)
Indexation .....	( 11.906)	( 8.027)	( 22.251)	( 58.603)
Total finance costs .....	( 99.798)	( 113.051)	( 201.008)	( 275.108)
Changes in fair value of swap contracts .....	20.049	81.275	41.218	334.728
Changes in fair value of embedded derivatives .....	465.705	( 1.194.429)	( 242.063)	( 3.950.368)
Net finance expenses .....	465.929	( 934.460)	( 18.016)	( 2.576.572)

### 8. Restricted cash

At the end of June 2014 cash in the amount of ISK 508 million (USD 4.5 million) (at year end 2013: ISK 520 million (USD 4.5 million)) was classified as restricted. The cash is dedicated to pay interest and loan payments on none ISK denominated loans in accordance with a collateral agreement concluded in March 2010 with the Company's lenders.

### 9. Agreement with banks

The Company has a temporary waiver with the European Investment Bank for the year 2014. All covenants were fulfilled by the Company at the end of June 2014.

## Notes, continued

### 10. Fair value of financial instruments

#### Fair value versus carrying amounts

The fair values of financial assets and liabilities, together with the carrying amounts shown in the statement of financial position, are as follows:

	30.6.2014		31.12.2013	
	Carrying amount	Fair value	Carrying amount	Fair value
Interest-bearing loans and borrowings .....	13.337.887	12.998.570	14.520.706	14.142.410

For other financial instruments their carrying amount equals their fair value.

#### Interest rates used for determining fair value

The interest rates used to discount estimated cash flows, where applicable, are based on the government yield curve at the reporting date in the case of ISK denominated debt, embedded derivatives and bonds. For foreign denominated debt the discount rates are based on interbank rates. All discount rates include an adequate credit spread, and were as follows.

Interest rates used for determining fair value:

	30.6.2014	31.12.2013
Embedded derivatives in power purchase agreements (USD) .....	0,83%-3,72%	1,64%-4,84%
Bonds .....	5.0%	5.0%
Interest bearing long term liabilities .....	Libor + 250 bp	Libor + 250 bp

Currency and interest rate swaps are discounted at swap rates for foreign currency denominated legs and the Housing Finance Fund curve for ISK CPI indexed legs.

#### Fair value hierarchy:

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

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

	Level 1	Level 2	Level 3	Total
<b>30 June 2014</b>				
Operating assets .....			30.946.415	30.946.415
Embedded derivatives .....	(	23.428)	( 96.055)	( 119.483)
Bonds .....		409.345		409.345
Currency and interest rate swap contracts .....	(	255.868)		( 255.868)
Investments in other companies .....			27.075	27.075
Short term investments .....	365.866			365.866
Total .....	365.866	130.049	30.877.435	31.373.350
<b>31 December 2013</b>				
Operating assets .....			31.422.097	31.422.097
Embedded derivatives .....	(	21.386)	143.966	122.580
Bonds .....		395.118		395.118
Currency and interest rate swap contracts .....	(	302.827)		( 302.827)
Investments in other companies .....			27.075	27.075
Short term investments .....	357.020			357.020
Total .....	357.020	70.905	31.593.138	32.021.063

Embedded derivatives that expire in the year 2026 are classified in level 3 due to the fact that the forward market for aluminium only extends to maximum of ten years.

## Notes, continued

---

### 11. Other matters

#### Litigations and claims

A foreign currency swap agreement entered into between Glitnir Bank hf. and HS Orka hf. on 19 November 2006 is in dispute. Glitnir has now served a subpoena against HS Orka. The subpoena will was filed with the District Court of Reykjanes on 26 March 2014. HS Orka wrote a statement of objections and has delivered to the court. HS Orka's primary claim with respect to Glitnir's payment claim will be that there are no payment obligations pursuant to swap agreement as Glitnir has unilaterally issued a letter circulated by the resolution committee of Glitnir to its customers on 27 October 2008, whereas it was stipulated that the aim is to "close and settle" all outstanding derivatives contracts, without referring to when that would take place. Furthermore it was stipulated that all derivative contracts would be automatically terminated would Glitnir be declared bankrupt, which would lead to all claims thereunder being matured. HS Orka opinion is that the Company has a strong case and rejects the claims made in the subpoena. There has not been set a date for the hearing to take place, but it is expected to be in the autumn of 2014.

HS Orka has commenced an arbitration to determine the validity of the Power Purchase Agreement between HS Orka and Nordural dated April 23, 2007. The proceeding was commenced on July 10, 2014.