

HS Orka hf.

Condensed Interim Financial Statements  
three months ended 31 March 2012  
ISK

HS Orka hf.  
Brekkuftigur 36  
260 Reykjanesbær

Reg.no. 680475-0169

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## Endorsement by the Board of Directors and the Management

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The condensed interim financial statements of HS Orka hf. (the Company) for the period from 1 January to 31 March 2012 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 1,841 million for the first three months of 2012 (2011: ISK 1,953 million) and the loss for the period amounted to ISK 8 million (2011: ISK 2,231 million profit). Total comprehensive income amounted to ISK 17 million (2011: ISK 2,249 million). According to the statement of financial position, the Company's assets amounted to ISK 44,948 million at end of March 2012 (at year end 2011: ISK 39,904 million). Equity amounted to ISK 21,113 million at the end of March 2012 (at year end 2011: ISK 16,397 million) or 47.0% of total capital (at year end 2011: 41.1%).

Icelandic shareholder Jardvarmi slhf. informed Magma Energy Sweden AB, on 10 February 2012 of their decision to exercise its option to increase its stake in HS Orka from 25.0% to 33.4%, according to an agreement between Jardvarmi and Magma Energy Sweden AB. Jardvarmi slhf. paid ISK 4.7 billion for the new shares at the end of February 2012 that increased HS Orka hf. equity by the same amount. Nominal value of the share capital increased by ISK 878 million to ISK 7.8 billion.

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 31 March 2012, its financial performance, and the changes in cash flows in the period from 1 January to 31 March 2012.

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 period from 1 January to 31 March 2012 and confirmed by means of their signatures.

Reykjanesbær, 14 May 2012.

The Board of Directors:

Ásgeir Margeirsson  
Chairman of the board

Gylfi Árnason

John Carson

Anna Skúladóttir

Ross Beaty

Managing Director:

Július Jónsson

Assistant Managing Director:

Albert Albertsson

# Independent Auditors' Review Report

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To the Board of Directors of HS Orka hf.

We have reviewed the accompanying statement of financial position of HS Orka hf. as of 31 March 2012 and the related statements of comprehensive income, changes in equity and cash flows for the three-month period then ended. Management is responsible for the preparation and presentation of this interim financial information in accordance with IAS 34 *Interim Financial Reporting*. Our responsibility is to express a conclusion on this 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 interim financial information is not prepared, in all material respects, in accordance with IAS 34 *Interim Financial Reporting*.

Reykjavík, 14 May 2012.

**KPMG ehf.**

Sæmundur Valdimarsson  
Margret G. Flóvenz

# Statement of Comprehensive Income for the three months ended 31 March 2012

	Note	2012 Q1	2011 Q1
Operating revenue .....	5	1.841.469	1.952.953
Production cost and cost of sales .....		<u>( 1.192.847)</u>	<u>( 1.282.087)</u>
<b>Gross profit</b> .....		648.622	670.866
Other operating expenses .....	6	<u>( 111.122)</u>	<u>( 164.880)</u>
<b>Results from operating activities</b> .....		537.500	505.986
Finance income .....		48.137	27.363
Finance costs .....		<u>( 913.194)</u>	<u>( 469.922)</u>
Changes in fair value of derivatives .....		<u>( 94.204)</u>	118.259
Changes in fair value of embedded derivatives in sales contracts .....		<u>461.861</u>	<u>2.607.744</u>
<b>Net finance (expenses) income</b> .....	7	<u>( 497.400)</u>	<u>2.283.444</u>
Share of loss of associates .....		<u>( 40.462)</u>	<u>( 683)</u>
<b>(Loss) profit before income tax</b> .....		( 362)	2.788.747
Income tax .....		<u>( 8.020)</u>	<u>( 557.749)</u>
<b>(Loss) profit for the period</b> .....		<u>( 8.382)</u>	<u>2.230.998</u>
<b>Other comprehensive income</b>			
Foreign currency translation difference of associates .....		25.228	18.401
<b>Other comprehensive income for the period, net of income tax</b> .....		<u>25.228</u>	<u>18.401</u>
<b>Total comprehensive income for the period</b> .....		<u><u>16.846</u></u>	<u><u>2.249.399</u></u>
<b>Earnings per share</b>			
Basic and diluted (loss) earnings per share .....		( 0,001)	0,320

Notes on pages 9 to 12 are an integral part of these condensed interim financial statements

# Statement of Financial Position as at 31 March 2012

<b>Assets</b>	<b>Note</b>	<b>31.3.2012</b>	<b>31.12.2011</b>
Operating assets .....		25.600.551	25.803.349
Operating assets under construction .....		3.564.007	3.544.465
Intangible assets .....		988.516	982.699
Investments in associates .....		635.519	655.608
Investments in other companies .....		27.075	27.075
Bonds .....		416.999	405.201
Embedded derivatives in power purchase agreements .....		4.638.099	4.294.623
Deferred tax asset .....		491.461	499.481
Prepaid lease and royalty fee .....		462.223	454.676
Long term receivable .....		206.260	200.926
<b>Total non-current assets</b>		<b>37.030.710</b>	<b>36.868.103</b>
Inventories .....		368.488	368.386
Bonds .....		72.478	70.428
Trade and other receivables .....		1.060.853	1.125.599
Embedded derivatives in power purchase agreements .....		285.168	166.784
Short term investments .....	8	466.035	0
Cash and cash equivalents .....	9	5.664.414	1.304.713
<b>Total current assets</b>		<b>7.917.436</b>	<b>3.035.910</b>
<b>Total assets</b>		<b>44.948.146</b>	<b>39.904.013</b>
<b>Equity</b>			
Share capital .....	11	7.841.124	6.962.919
Share premium .....	11	7.038.856	3.218.660
Translation reserve .....		322.770	297.542
Revaluation reserve .....		1.628.119	1.647.187
Retained earnings .....		4.281.645	4.270.960
<b>Total equity</b>		<b>21.112.514</b>	<b>16.397.268</b>
<b>Liabilities</b>			
Loans and borrowings .....		17.567.553	17.476.628
Pension obligations .....		1.579.500	1.576.500
Currency and interest rate swap contracts .....		843.598	761.614
<b>Total non-current liabilities</b>		<b>19.990.651</b>	<b>19.814.742</b>
Loans and borrowings .....		2.334.626	2.101.388
Trade and other payables .....		1.141.795	1.234.276
Currency and interest rate swap contracts .....		368.560	356.339
<b>Total current liabilities</b>		<b>3.844.981</b>	<b>3.692.003</b>
<b>Total liabilities</b>		<b>23.835.632</b>	<b>23.506.745</b>
<b>Total equity and liabilities</b>		<b>44.948.146</b>	<b>39.904.013</b>

Notes on pages 9 to 12 are an integral part of these condensed interim financial statements

## Statement of Changes in Equity for the three months ended 31 March 2012

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	Share capital	Share premium	Translation reserve	Revaluation reserve	Reserve for shares in associate	Retained earnings	Total
<b>Q1 2011</b>							
Equity at 1 January 2011 .....	6.962.919	3.218.660	296.634	1.723.505	( 37.157)	5.131.395	17.295.956
Total comprehensive income .....			18.401	0	0	2.230.998	2.249.399
Revaluation reserve transferred to retained earnings .....				( 19.080)		19.080	0
Equity at 31 March 2011 .....	<u>6.962.919</u>	<u>3.218.660</u>	<u>315.035</u>	<u>1.704.425</u>	<u>( 37.157)</u>	<u>7.381.473</u>	<u>19.545.355</u>
<b>Q1 2012</b>							
Equity at 1 January 2011 .....	6.962.919	3.218.660	297.542	1.647.187	0	4.270.960	16.397.268
Total comprehensive income .....			25.228			( 8.382)	16.846
Revaluation reserve transferred to retained earnings .....				( 19.068)		19.068	0
Share capital increase .....	878.205	3.820.196					4.698.401
Equity at 31 March 2012 .....	<u>7.841.124</u>	<u>7.038.856</u>	<u>322.770</u>	<u>1.628.119</u>	<u>0</u>	<u>4.281.645</u>	<u>21.112.514</u>

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# Statement of Cash Flows

## for the three months ended 31 March 2012

	Note	2012 Q1	2011 Q1
<b>Cash flows from operating activities</b>			
(Loss) profit for the period .....	(	8.382)	2.230.998
Adjustments:			
Gain on sale of operating assets .....	(	2.242)	0
Increase in pension obligations .....		3.000	80.400
Depreciation and amortization .....		248.817	258.015
Net finance expenses (income) .....		497.400	( 2.283.444)
Share of loss of associates .....		40.462	683
Income tax .....		8.020	557.750
		787.075	844.402
Inventories, increase .....	(	102)	( 13.423)
Receivables, decrease (increase) .....		59.412	( 110.453)
Current liabilities, increase .....		57.682	172.764
Net cash from operations before interest and taxes		904.067	893.290
Interest income received .....		26.760	4.722
Interest and indexation costs paid .....	(	121.577)	( 164.408)
Net cash from operating activities		809.250	733.604
<b>Cash flows from investing activities</b>			
Acquisition of operating assets during the period .....	(	61.319)	( 78.794)
Payments for operating assets acquired in prior year .....	(	174.394)	0
Proceeds from sale of operating assets .....		2.701	0
Acquisition of intangible assets .....	(	10.519)	( 554)
Dividend received from associate .....		4.855	4.855
Short term investments .....	(	466.035)	0
Proceeds from repayment and sale of bonds .....		0	634.164
Net cash (used in) provided by investing activities		( 704.711)	559.671
<b>Cash flows from financing activities</b>			
Share capital increase .....		4.698.401	0
Repayment of borrowings .....	(	486.674)	( 538.184)
Net cash provided by (used in) financing activities		4.211.727	( 538.184)
<b>Increase in cash and cash equivalents .....</b>		4.316.266	755.091
<b>Cash and cash equivalents at 1 January.....</b>		1.304.713	1.043.250
<b>Effect of exchange rate fluctuations on cash held.....</b>		43.435	( 5.107)
<b>Cash and cash equivalents at 31 March .....</b>		5.664.414	1.793.234

Notes on pages 9 to 12 are an integral part of these condensed interim financial statements



# Notes to the Condensed Interim Financial Statements

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## 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 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

The Company's condensed interim financial statements are prepared in accordance with IAS 34, *Interim Financial Reporting*. They do not include all of the information required for full annual financial statements and should be read in conjunction with the financial statements of the Company as at and for the year ended 31 December 2011.

These condensed interim financial statements were approved by the Board of Directors on 14 May 2012.

## 3. Significant accounting policies

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 2011.

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 31.12.2009
- derivative financial instruments are measured at fair value
- embedded derivatives in electric power sales contracts are measured at fair value
- financial instruments at fair value through profit or loss are measured at fair value
- financial assets available for sale are measured at fair value.

## 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 2011.

## 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 distilled 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.

	Power production	Electricity sale	Other	Total
<b>1 January - 31 March 2012</b>				
External revenue .....	830.507	758.371	252.591	1.841.469
Inter-segment revenue .....	468.415			468.415
Total segment revenue .....	1.298.922	758.371	252.591	2.309.884
Segment operating results .....	495.278	31.282	10.940	537.500
<b>Unallocated items</b>				
Net finance expenses .....				( 497.400)
Share of loss of associates .....				( 40.462)
Income tax .....				( 8.020)
Loss for the period .....				( 8.382)
Segment assets .....	29.528.000	51.359	573.715	30.153.074
Unallocated assets .....				14.795.072
Total assets .....				44.948.146
Unallocated liabilities .....				23.835.632
Capital expenditures .....	67.498	638	3.702	71.838
Depreciation and amortization .....	238.864	1.442	8.511	248.817
<b>1 January - 31 March 2011</b>				
External revenue .....	1.086.529	595.444	270.980	1.952.953
Inter-segment revenue .....	246.938			246.938
Total segment revenue .....	1.333.467	595.444	270.980	2.199.891
Segment operating results .....	566.004	( 75.818)	15.800	505.986
<b>Unallocated items</b>				
Net finance income .....				2.283.444
Share of loss of associates .....				( 683)
Income tax .....				( 557.749)
Profit for the period .....				2.230.998
Segment assets .....	29.678.471	54.214	598.210	30.330.895
Unallocated assets .....				13.630.907
Total assets .....				43.961.802
Unallocated liabilities .....				24.416.447
Capital expenditures .....	77.390	326	1.632	79.348
Depreciation and amortization .....	246.354	1.574	10.087	258.015

## Notes, continued

### 5. Segment reporting, contd.:

#### Major customers

Revenues from one customer of the Company's Production segment represents approximately ISK 547 million of the Company's total revenues during the period (1.1.2011 - 31.3.2011: ISK 821 million).

Revenues from HS Veitur hf. represents ISK 500 million during the period (1.1.2011 - 31.3.2011: ISK 462 million) and relates to segments as follows:

	Power production	Electricity sale	Other	Total
Revenues 1.1.2012 - 31.3.2012 .....	196.603	64.863	238.814	500.280
Revenues 1.1.2011 - 31.3.2011 .....	188.415	59.411	214.207	462.033

### 6. Other operating expenses

Operating expenses specifies as follows:

	2012 Q1	2011 Q1
Salaries and related expenses .....	43.733	37.960
(Decrease) increase in pension fund commitment .....	( 2.334)	36.381
Administrative expenses .....	66.201	86.302
Depreciation and amortization .....	3.522	4.237
Total operating expenses .....	111.122	164.880

### 7. Net finance (expenses) income

Net finance (expenses) income specifies as follows:

	2012 Q1	2011 Q1
Interest income on loans and receivables .....	33.020	13.040
Interest income on available for sale securities .....	0	3.428
Fair value changes on financial assets through profit and loss .....	15.117	10.895
Total finance income .....	48.137	27.363
Interest expense .....	( 147.569)	( 152.661)
Indexation .....	( 47.389)	( 21.860)
Net foreign exchange loss .....	( 718.236)	( 295.401)
Total finance costs .....	( 913.194)	( 469.922)
Fair value changes of currency and interest rate swap contracts .....	( 94.204)	118.259
Fair value changes of embedded derivatives in electric power sale contracts .....	461.861	2.607.744
Net finance (expenses) income .....	( 497.400)	2.283.444

## Notes, continued

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### 8. Short term investments

The company has invested in short term securities amounting to 466 million at the end of the period.

### 9. Restricted cash

At the end of March 2012 cash in the amount of ISK 568 million (USD 4.5 million) (at year end 2011: ISK 554 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.

### 10. Agreement with banks

At the end of the year 2009, the Company signed temporary agreements with its lenders with revised covenants and interest rates for the years 2009 and 2010. One of these temporary agreements was extended for the year 2011 by one of the banks (European Investment Bank) but further waivers were not needed for the other two banks. This waiver has now been extended for 2012. In early 2012, the Company amended its loan agreement with Nordic Investment Bank, which amended certain covenants and reset interest rates.

### 11. New equity

Icelandic shareholder Jardvarmi slhf. informed Magma Energy Sweden AB, on 10 February 2012 of their decision to exercise its option to increase its stake in HS Orka from 25.0% to 33.4%, according to an agreement between Jardvarmi and Magma Energy Sweden AB. Jardvarmi slhf. payed ISK 4.7 billion for the new shares at the end of February 2012 that increased HS Orka hf. equity by the same amount. Nominal value of the share capital increased by ISK 878 million to ISK 7.8 billion.

### 12. Other matters

#### Litigations and claims

HS Orka hf initiated on 16 December 2011 arbitration proceedings against Nordural Grundartangi concerning interpretation of clauses in the Power Purchase Agreement for Grundartangi concerning a minimum purchase of electricity. The full amount was accrued at end of March 2012. Results of the arbitration proceedings are expected in early 2013.

#### Trölladyngja

According to the first recommendation of the steering committee of "Rammaáætlun II" to the parliament, regarding categorizing the potential hydro and geothermal power sites in three groups: protected site, pending site and power developing site, the Trölladyngja area is categorized as a pending site where more information and data is required. The recommendation is now for dictums at all stake holders. HS Orka hf. has formerly opposed the recommendation with respect to Trölladyngja. If the recommendation is adopted HS Orka hf. would immediately assess the impact on the carrying value of Trölladyngja. The current carrying amount of those assets is ISK 675 million.