Deloitte.

Farice hf.

Financial Statements

2007

Farice hf.
Skógarhlíð 12
105 Reykjavík
kt. 580902-2190

Farice hf.

Financial Statements

2007

Table of contents

Independent Auditor's Report

To the Board of Directors and shareholders of Farice hf.

We have audited the accompanying financial statements of Farice hf., which comprise the balance sheet as at December 31, 2007, and the income statement, cash flow statement and statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

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

Auditor's Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion
In our opinion, the financial statements give at rue and fair view of the financial position of Farice hf. as of December 31, 2007, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Kópavogi May 13, 2008

Deloitte hf.

Páll Grétar Steingrímsson
State Authorized Public Accountant

Report by the Board of Directors and Managing Director

The Financial Statements of Farice hf. for the year 2007 are prepared in accordance with International Financial Reporting Standards (IFRS), as adopted by the European Union, and additional Icelandic disclosure requirements for listed companies.

The loss of the year amounted to EUR 804.256. According to the Balance Statement the Company's assets amount to EUR 38.026.145, the year's end book value of equity is EUR 10.311.684 and the Company's equity ratio is 27%.

At year-end, shareholders in Farice hf. numbered seven. Two shareholders owned more than 10% of the shares in the Company at year-end: Eignarhaldsfélagið Farice ehf., with 79,9% and Telefonverkið P/F 19,9%. The Board of Directors recommends that the loss of the year should be brought forward to the next year. As regards changes in the equity of the Company, the Board of Directors refers to the Notes attached to the Financial Statements.

It is the opinion of the Board of Directors and the Managing Director that the accounting policies used are appropriate and that these Financial Statements present all the information necessary to give a true and fair view of the company's assets and liabilities, financial position and operating performance, as well as describing the principal risk and uncertainty factors faced by the company.

The Board of Directors and the Managing Director hereby confirm the Consolidated Financial Statements for the year 2007 with their signatures.

Reykjavík, April, 23 2008

Board of Directors

Sigurður G. Guðjónsson
Chairman of the Board

Kristian R. Davidsen

Brynjólfur Bjarnason

Bjarni A. Bjarnason

Arni Pétur Jónsson

Managing Director

Guðmundur Gunnarsson

Income Statement for the year 2007

	Notes	2007	2006
Operating revenue	3	6.117.718	6.957.600
Operating expenses		(2.076.300)	(2.049.465)
Administrative expenses		(491.946)	(914.755)
Depreciation	8	(3.257.365)	(3.062.001)
Net profit (loss) from operation		292.107	931.379
Financial income	6	46.538	76.326
Financial expenses	6,13	(1.318.798)	(1.422.038)
Net loss before tax		(980.152)	(414.334)
Income tax	14	175.896	97.051
Net loss for the year		(804.256)	(317.283)

Balance Sheet

Assets	Notes	31.12.2007	31.12.2006
Non-current assets			
Point of Presence	8	271.121	182.670
Backhaul	8	4.975.809	4.540.927
Cable stations	8	636.669	726.094
International Waters	8	27.635.695	29.362.922
Common items	8	1.341.479	2.026.787
Deferred tax asset	14	655.930	480.034
Prepaid lease		314.932	359.912
		35.831.635	37.679.346
Current assets			
Accounts receivable	9	80.357	390.203
Related parties receivables		1.581.326	0
Other receivables		287.061	282.188
Market securities		0	2.000.000
Bank deposits and cash		245.766	691.522
		2.194.510	3.363.913
Total assets		38.026.145	41.043.259

December 31, 2007

Equity and liabilities	Notes	31.12.2007	31.12.2006
Equity			
Share capital	10	13.689.662	13.689.662
Loss carry-forward	11	(3.377.978)	(2.618.231)
		10.311.684	11.071.431
Liabilities			
Non-current liabilities			
Long-term bonds	12	24.966.666	27.166.667
Current liabilities			
Accounts payable		179.859	153.156
Current maturities	12	2.200.000	2.200.000
Other current liabilities		367.936	452.006
		2.747.794	2.805.162
Total equity and liabilities		38.026.145	41.043.259

Statement of cash flows for the year 2007

	Notes	2007	2006
Cash flows from operating activities			
Net loss before other income and expenses		292.107	931.379
Items not affecting cash		3.248.540	3.062.001
Changes in current assets and liabilities		(1.331.674)	(1.223.142)
Net cash provided (used in) operating activities before interest		2.208.973	2.770.238
Paid in interest income		136.861	17.510
Paid interest expenses		(1.321.677)	(1.387.592)
Net cash provided (used in) operating activities		1.024.157	1.400.156
Cash flows from investing activities			
Investment in fixed assets		(1.287.011)	(1.531.413)
Car sold		17.098	0
Net cash provided by (used in) investing activities		(1.269.913)	(1.531.413)
Cash flows from financing activities			
Long-term liabilities repaid		(2.200.000)	(2.200.000)
Net cash provided by (used in) financing activities		(2.200.000)	(2.200.000)
Increase (decrease) in cash and cash equivalents		(2.445.756)	(2.331.257)
Cash and cash equivalents at beginning of year		2.691.522	5.022.779
Cash and cash equivalents at end of year		245.766	2.691.522

Statement of changes in Equity
for the year ended December 31, 2007

	Share capital	Loss carry-forward	Total equity
Balance at January 1, 2007	13.689.662	(2.618.231)	11.071.431
Other changes in equity		44.510	44.510
Net (loss) for the year	0	(804.256)	(804.256)
Balance at December 31, 2007	13.689.662	(3.377.978)	10.311.684

Notes to financial statements

1. Operations

Farice hf. is a limited company incorporated in Iceland. The addresses of its registered office and a principal place of business can be found on page 1.

These financial statements are presented in euros since that is the functional currency in which the majority of the company´s transactions are denominated.

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

2. Significant Accounting Policies

Statement of compliance

The financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS as adopted by the EU.

Basis of preparation

The financial statements are prepared under the historical cost convention except for revaluation of certain financial instruments.

The preparation of the financial statements in conformity with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The principal accounting policies adopted are set out below.

Revenue recognition

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

Interest income is accrued on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset to that asset's net carrying amount.

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

Notes to financial statements

2. Significant Accounting Policies (continued)

Foreign currencies

Transactions in currencies other than euros are recorded at the rates of exchange prevailing on the dates of the transactions. At each balance sheet date, monetary assets and liabilities that are denominated in foreign currencies are retranslated at the rates prevailing on the balance sheet date. Non-monetary assets and liabilities carried at fair value that are denominated in foreign currencies are translated at the rates prevailing at the date when the fair value was determined.

Taxation

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

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

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

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

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

Property, plant and equipment

Property, plant and equipment are recognised as an asset when it is probable that future economic benefits associated with the asset will flow to the company and the cost of the asset can be measured in a reliable manner.

Property, plant and equipment which qualifies for recognition as an asset is initially measured at cost.

The cost of the property, plant and equipment comprises its purchase price and any directly attributable cost of bringing the asset to working condition for its intended use.

The depreciable amount of the asset is allocated on a straight-line basis over its useful life. The depreciation charge for each year is recognised as an expense, on the following bases:

Point of Presence (PoP)	10%
Backhaul	10%
Cable stations	10%
International waters	5%
Common items	10-20%

2. Significant Accounting Policies (continued)

Impairment of tangible and intangible assets excluding goodwill

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

Recoverable amount is the greater of net selling price and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

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

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

Accounts receivable

Accounts receivable are valued at nominal value less an allowance for doubtful accounts. The allowance is deducted from accounts receivable in the balance sheet and does not represent a final write-off. Accounts receivable in other currencies than euro have been entered at the exchange rates prevailing on the balance sheet date.

Long-term liabilities

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

Accounts payable

Accounts payable are valued at nominal value and accounts payable in other currencies than euro have been booked at the exchange rates prevailing on the balance sheet date.

Derivative financial instruments

The Company uses derivative financial instruments to hedge its risk for changes in interest rates. Those financial instruments are interest rate swap contracts.

The use of financial derivatives is governed by the Company's policies approved by the Board of Directors, which provide written principles on the use of financial derivatives.

Notes to financial statements

2. Summary of Significant Accounting Policies (continued)

Provisions

Provision is recognised when an enterprise has a present obligation as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

Provisions for restructuring costs are recognised when the company has a detailed formal plan for the restructuring which has been notified to affected parties.

3. Revenue

Net sales are specified as follows:

	2007	2006
Lease of bandwith - Farice 1	6.020.299	6.853.776
Discount of bandwith	(11.414)	(3.684)
Other income	108.833	107.508
	6.117.718	6.957.600

4. Geographical segments

The company uses geographical markets as its primary segments. Segment information is presented below, according to location of customers:

Segment information

	Faroe Islands Branch	Iceland Branch	Farice hf.
Operating revenue	1.520.299	4.500.000	6.020.299
Discount of bandwith	(11.414)		
Other income	20.000	80.008	100.008
Sales gain		8.825	8.825
	1.528.885	4.588.833	6.129.132
Operating expenses	(583.026)	(1.493.274)	(2.076.300)
Administrative expenses	(98.631)	(393.315)	(491.946)
Depreciation	(566.180)	(2.691.185)	(3.257.365)
	(1.247.836)	(4.577.774)	(5.825.611)
Operating profit (loss)	281.049	11.059	303.521
Net interest expence/income	(254.452)	(1.017.808)	(1.272.260)
Income tax	(5.319)	181.215	175.896
Net gain (loss)	21.278	(825.534)	(804.256)

Notes to financial statements

5. Salaries

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

	2007	2006
Salaries	127.542	148.057
Board fees	45.202	0
Salary-related expenses	45.617	40.665
	218.360	188.722
Average number of positions	1,25	1,90

6. Financial income / (expenses)

	2007	2006
Income from investments:		
Other interest income	46.538	76.326
Finance costs:		
Other interest expenses	(1.397.526)	(1.449.008)
Exchange rate differences	78.728	26.970
	(1.318.798)	(1.422.038)
	(1.272.260)	(1.345.713)

7. Earnings per share

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

	2007	2006
Net loss for the year	(804.256)	(317.283)
Total average number of shares including potential shares	13.689.662	13.689.662
Basic Earnings (loss) per Share	(0,06)	(0,02)

Notes to financial statements

8. Property, plant and equipment

	Point of presence	Backhaul	Cable stations	International Waters	Common Items
Cost					
At January 1, 2007	249.678	5.710.904	993.609	34.544.546	4.406.958
Additions	115.991	1.128.049	0	0	42.971
Eliminated on disposal					(38.181)
At December 31, 2007	365.669	6.838.953	993.609	34.544.546	4.411.748
Accumulated depreciation					
At January 1, 2007	67.008	1.169.977	267.515	5.181.624	2.380.171
Charge for the year	27.540	693.167	89.425	1.727.227	720.006
Eliminated on disposal					(29.908)
At December 31, 2007	94.548	1.863.144	356.940	6.908.851	3.070.269
Carrying Amount					
At December 31, 2007	271.121	4.975.809	636.669	27.635.695	1.341.479
At January 1, 2007	182.670	4.540.927	726.094	29.362.922	2.026.787

8. Property, plant and equipment by location

	Icelandic Branch Iceland	Icelandic Branch Scotland	Foreyja Branch	International Waters	Common Items
Cost					
At January 1, 2007	212.876	5.687.485	1.053.830	34.544.546	4.406.958
Additions	83.719	923.927	236.394	0	42.971
Eliminated on disposal					(38.181)
At December 31, 2007	296.595	6.611.412	1.290.224	34.544.546	4.411.748
Accumulated depreciation					
At January 1, 2007	48.477	1.226.655	229.368	5.181.624	2.380.171
Charge for the year	22.494	658.657	128.981	1.727.227	720.006
Eliminated on disposal					(29.908)
At December 31, 2007	70.971	1.885.312	358.349	6.908.851	3.070.269
Carrying Amount					
At December 31, 2007	225.624	4.726.100	931.875	27.635.695	1.341.479
At January 1, 2007	164.399	4.460.830	824.462	29.362.922	2.026.787

9. Other financial assets

Accounts receivable:

	31.12.2007	31.12.2006
Nominal value	80.357	390.203

Bank balances and cash:

Bank balances and cash comprise cash and short-term deposits held by the company treasury function. The carrying amount of these assets approximates their fair value.

Notes to financial statements

10. Share capital

Common stock is as follows:

	Shares	Ratio	Nominal value
Total share capital at year-end	13.689.662	100,0%	13.689.662

Each share of one euro carries one vote.

11. Loss carry-forward

	Loss carry-forward
Balance at January 1, 2007	(2.618.231)
Other changes in equity	44.510
Net loss for the year	(804.256)
Balance at December 31, 2007	(3.377.978)

12. Loans from credit institutions

	Remaining balances 31.12.2007
Loans in EUR	24.966.666
Current maturities	2.200.000
Loans from credit institutions	27.166.666
Aggregated annual maturities are as follows:	
Current maturities	2.200.000
Installments 2009	7.106.666
Installments 2010	5.640.000
Installments 2011	2.820.000
Installments 2012	2.350.000
Installments 2013	2.350.000
Installments 2014	2.350.000
Installments 2015	2.350.000
	27.166.666

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

Notes to financial statements

13. Derivative financial instruments

Interest Rate Swaps

The Company uses interest rate swaps to manage its exposure to interest rate movements on its bank borrowings. Contracts with nominal values of 23,5 million euros have fixed interest payments at an average rate of 4,72 per cent for periods up until 2015 and have floating interest rate at 0,59 per cent plus LIBOR and the differences amounts to swap rates.

14. Deferred tax

	Deferred tax asset	Deferred tax liabilities	Total
At January 1, 2007	1.849.806	(1.369.772)	480.034
Calculated tax for the year	121.638	54.259	175.896
At December 31, 2007	1.971.443	(1.315.514)	655.930

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

Fixed tangible assets	(1.315.513)
Loss carry-forward	1.971.442
	655.930

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

	Tax loss	Deferred tax
Available for 5 years	33.564	6.041
Available for 6 years	1.863.456	363.725
Available for 7 years	3.677.167	705.086
Available for 8 years	2.728.505	531.429
Available for 9 years	754.569	135.822
Available for 10 years	1.274.103	229.338
	10.331.364	1.971.443

15. Approval of financial statements

The Financial Statements were approved by the Board of Directors and authorised for issue on April 23, 2008.