

Farice hf.

Financial statements
2005

Farice hf.
Skógarhlíð 12
105 Reykjavík

kt. 580902-2190

Farice hf.

Financial statements 2005

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Auditor's Report

To the board of directors and shareholders of Farice hf.

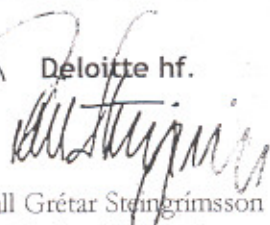
We have audited the accompanying balance sheet of Farice hf. as of December 31, 2005 and the related statement of income and cash flows for the year then ended. These financial statements are the responsibility of the company's management. Our responsibility is to issue a report on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards in Iceland. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the financial statements are free of material misstatement. An audit includes examining, on a test of basis, evidence supporting the amounts and disclosures in the financial statements. An audit includes assessing the accounting principles used and significant estimates made by the management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements give a true and fair view of the financial position of Farice hf. as of December 31, 2005 and of the results of its operations and its cash flows for the year then ended in accordance with the generally accepted accounting principles in Iceland applied on consistent basis.

Reykjavik, April 28, 2006

Deloitte hf.


Páll Grétar Steingrímsson
State Authorized Public Accountant

Report by the Board of Directors and Managing Director

It is the opinion of the Board of Directors and the Managing Director that these Financial Statements present all the information necessary to show the position of Farice hf. at year-end, the operating results for the year and the financial developments during the year 2005.

The Financial Statements of Farice hf. was prepared for the first time in the interim financial statement for June 30, 2005 in accordance with International Financial Reporting Standards (IFRS). The effects of the changes to IFRS are explained in note 17 in the Financial Statements.


The net loss of the year amounted to € 432.717. The Board recommends that the loss will be carried forward to next year. Owners equity at year-end amounted to € 11.390.596.


At year-end, shareholders in the company numbered 7. Two shareholders owned more than 10% of the shares in the Company, a total of 99%

The Board of Directors and Managing Director hereby confirm the Financial Statements for the year 2005 with their signatures.

Reykjavík, April 28, 2006

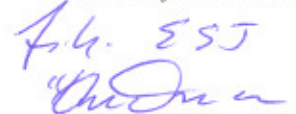
Board of Directors


Jón Birgir Jónsson
Chairman of the board


Andras Róin


Bjarni A. Bjarnason


Brynjólfur Bjarnason

Eiríkur S. Jóhannsson


Managing Director


Guðmundur Gunnarsson

Income Statement for the year 2005

	Notes	2005	2004
Operating revenue	3	6.657.622	5.355.500
Operating expenses		(1.886.940)	(1.803.042)
Administrative expenses		(858.435)	(711.139)
Depreciation	8	<u>(3.096.302)</u>	<u>(2.907.992)</u>
Net profit (loss) from operation		815.945	(66.672)
Financial expenses	6,13	(1.345.713)	(1.160.072)
Net loss before tax		(529.768)	(1.226.744)
Income tax	14	<u>97.051</u>	<u>225.404</u>
Net loss for the year		<u><u>(432.717)</u></u>	<u><u>(1.001.340)</u></u>

Balance Sheet

Asset	Notes	31.12.2005	1.1.2005
Fixed assets			
Point of Presence	8	202.964	225.241
Backhaul		3.516.725	3.768.261
Cable stations		815.519	904.944
International Waters		31.090.149	32.817.376
Common items		2.744.631	3.626.023
Deferred tax asset	14	409.570	312.519
Prepaid lease		405.792	449.873
		39.185.350	42.104.237
Current assets			
Accounts receivable	9	227.241	744.453
Other receivables		153.513	65.972
Market securities		4.000.000	1.000.000
Bank deposits and cash		1.022.779	1.607.749
		5.403.534	3.418.174
Total assets		44.588.883	45.522.411

December 31, 2005

	Notes	31.12.2005	1.1.2005
Equity and liabilities			
Shareholders' equity			
Share capital	10	13.689.662	13.689.662
Loss carry-forward	11	<u>(2.299.066)</u>	<u>(1.866.349)</u>
		<u>11.390.596</u>	<u>11.823.313</u>
 Liabilities			
Long term liabilities			
Long-term bonds	12	<u>29.366.667</u>	<u>32.300.000</u>
 Current liabilities			
Accounts payable		1.250.178	1.009.465
Current maturities	12	2.200.000	0
Other current liabilities		<u>381.442</u>	<u>389.633</u>
		<u>3.831.621</u>	<u>1.399.098</u>
 Total equity and liabilities		 <u><u>44.588.883</u></u>	 <u><u>45.522.411</u></u>

Statement of cash flows for the year 2005

	Notes	2005	2004
Cash flows from operating activities			
Net loss before other income and expenses		815.945	(66.672)
Items not affecting cash		3.096.302	2.907.992
Changes in current assets and liabilities		744.305	(795.156)
Net cash provided (used in) operating activities before interest		4.656.552	2.046.164
Paid in interest income		40.050	72.966
Paid interest expenses		(1.423.793)	(1.132.858)
Net cash provided (used in) operating activities		3.272.808	986.272
Cash flows from investing activities			
Investment in fixed assets		(124.445)	(4.281.828)
Net cash provided by (used in) investing activities		(124.445)	(4.281.828)
Cash flows from financing activities			
Long-term borrowings		0	32.300.000
Short-term liabilities repaid		0	(29.108.518)
Long-term liabilities repaid		(733.333)	0
Paid in capital stock		0	148.469
Net cash provided by (used in) financing activities		(733.333)	3.339.951
Increase (decrease) in cash and cash equivalents		2.415.030	44.395
Cash and cash equivalents at beginning of year		2.607.749	2.563.354
Cash and cash equivalents at end of year		5.022.779	2.607.749

Statement of changes in Equity for the year ended December 31, 2005

	Share capital	Loss carry-forward	Total equity
Balance at January 1, 2004.....	13.689.662	(952.126)	12.737.536
Deffered income tax.....	0	87.115	87.115
Net (loss) for the year.....	<u>0</u>	<u>(935.091)</u>	<u>(935.091)</u>
Balance at December 31, 2004.....	<u>13.689.662</u>	<u>(1.800.102)</u>	<u>11.889.560</u>
Balance at December 31, 2004.....	13.689.662	(1.800.102)	11.889.560
Effects of transition to IFRS.....	<u>0</u>	<u>(66.247)</u>	<u>(66.247)</u>
Balance at January 1, 2005.....	13.689.662	(1.866.349)	11.823.313
Net (loss) for the year.....	<u>0</u>	<u>(432.717)</u>	<u>(432.717)</u>
Balance at December 31, 2005.....	<u>13.689.662</u>	<u>(2.299.066)</u>	<u>11.390.596</u>

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. Summary of Significant Accounting Policies

Statement of compliance

The condensed financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS's) for financial statements (IAS 34). These are the company's first IFRS condensed consolidated financial statements and IFRS 1, First Time Adoption of International Financial Reporting Standards, has been applied.

An explanation of how the transition to IFRS has affected the reported financial position and financial performance of the company is provided in note 17. This note includes reconciliations of equity and profit or loss for comparative periods reported under Icelandic GAAP (previous GAAP) to those reported for the periods under IFRS.

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 IAS 34, Financial Reporting, 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

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.....	20%

Notes to financial statements

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 receivables 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

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:

	2005	2004
Lease of bandwidth - Farice 1	6.557.616	5.255.500
Other income	100.006	100.000
	<u>6.657.622</u>	<u>5.355.500</u>

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.....	1.302.620	5.355.002	6.657.622
Operating expenses	(430.153)	(1.456.787)	(1.886.940)
Administrative expenses.....	(182.341)	(676.094)	(858.435)
Depreciation.....	(506.358)	(2.589.944)	(3.096.302)
	<u>(1.118.852)</u>	<u>(4.722.825)</u>	<u>(5.841.677)</u>
Operating profit (loss).....	183.768	632.177	815.945
Net interest expence/income.....	(268.435)	(1.077.277)	(1.345.713)
Income tax.....	16.933	80.118	97.051
Net loss.....	<u>(67.735)</u>	<u>(364.982)</u>	<u>(432.717)</u>

Notes to financial statements

5. Salaries

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

	2005	2004
Salaries.....	198.144	172.371
Salary-related expenses.....	57.729	47.067
	255.874	219.438
 Average number of positions.....	 1,75	 1,90

6. Financial income / (expenses)

	2005	2004
Income from investments:		
Other interest income.....	76.326	72.966
 Finance costs:		
Other interest expenses.....	(1.449.008)	(1.207.055)
Exchange rate differences.....	26.970	(25.983)
	(1.345.713)	(1.160.072)

7. Earnings per share

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

	2005	2004
Net profit (loss) for the year.....	(432.717)	(1.001.340)
Total average number of shares including potential shares	13.689.662	13.689.662
Basic Earnings (loss) per Share	(0,03)	(0,07)

Notes to financial statements

8. Property, plant and equipment

	Point of presence	Backhaul	Cable stations	International Waters	Common Items
Cost					
At January 1, 2005.....	247.518	4.057.206	993.609	34.544.546	4.406.959
Additions.....	0	124.445	0	0	0
At December 31, 2005.....	<u>247.518</u>	<u>4.181.651</u>	<u>993.609</u>	<u>34.544.546</u>	<u>4.406.959</u>
Accumulated depreciation					
At January 1, 2005.....	22.277	288.945	88.665	1.727.170	780.935
Charge for the year.....	22.277	375.981	89.425	1.727.227	881.392
At December 31, 2005.....	<u>44.554</u>	<u>664.926</u>	<u>178.090</u>	<u>3.454.397</u>	<u>1.662.327</u>
Carrying Amount					
At December 31, 2005.....	<u>202.964</u>	<u>3.516.725</u>	<u>815.519</u>	<u>31.090.149</u>	<u>2.744.632</u>
At January 1, 2005.....	<u>225.241</u>	<u>3.768.261</u>	<u>904.944</u>	<u>32.817.376</u>	<u>3.626.024</u>

	Icelandic Branch Iceland	Icelandic Branch Scotland	Foreyja Branch	International Waters	Common Items
Cost					
At January 1, 2005.....	112.876	4.437.910	747.547	34.544.546	4.406.959
Additions.....	100.000	24.445	0	0	0
At December 31, 2005.....	<u>212.876</u>	<u>4.462.355</u>	<u>747.547</u>	<u>34.544.546</u>	<u>4.406.959</u>
Accumulated depreciation					
At January 1, 2005.....	10.159	322.449	67.279	1.727.170	780.935
Charge for the year.....	19.159	401.245	506.358	1.381.954	787.586
At December 31, 2005.....	<u>29.318</u>	<u>723.694</u>	<u>573.637</u>	<u>3.109.124</u>	<u>1.568.521</u>
Carrying Amount					
At December 31, 2005.....	<u>183.558</u>	<u>3.738.661</u>	<u>173.910</u>	<u>31.435.422</u>	<u>2.838.438</u>
At January 1, 2005.....	<u>102.717</u>	<u>4.115.461</u>	<u>680.268</u>	<u>32.817.376</u>	<u>3.626.024</u>

9. Other financial assets

Accounts receivable:

	<u>31.12.2005</u>	<u>1.1.2005</u>
Nominal value.....	<u>227.241</u>	<u>744.453</u>

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
	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, 2005.....	(1.866.349)
Net loss for the year.....	(432.717)
Balance at December 31, 2005.....	(2.299.066)

12. Loans from credit institutions

	Remaining balances 31.12.2005
Loans in EUR	29.366.667
Current maturities.....	2.200.000
Loans from credit institutions.....	31.566.667
Aggregated annual maturities are as follows:	
Current maturities.....	2.200.000
Installments 2007.....	2.200.000
Installments 2008.....	2.200.000
Installments 2009.....	1.466.667
Installments 2010.....	5.640.000
Installments later.....	17.860.000
	31.566.667

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, 2005.....	312.519	0	312.519
Calculated tax for the year.....	97.051	0	97.051
At December 31, 2005.....	409.570	0	409.570

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

Fixed tangible assets.....	(1.401.115)
Loss carry-forward.....	1.810.685
	<u>409.570</u>

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

	Tax loss	Deferred tax
Available for 7 years	33.564	6.042
Available for 8 years	2.885.472	568.128
Available for 9 years	3.677.167	705.086
Available for 10 years	2.728.505	531.429
	<u>9.324.708</u>	<u>1.810.685</u>

15. Litigation

There are two issues which both involve Farice hf. and the EFTA Surveillance Authority in Brussels. The first issue concerns a formal request for information from the EFTA Surveillance Authority, of May 6, 2004, for information concerning the compatibility of the Farice project with the rules on competition in the EEA Agreement. This issue is still being processed and no formal investigation has been decided.

The second issue concerns State Aid matters. In May 2005 the EFTA Surveillance Authority decided to initiate a formal investigation into the issue of State Aid towards the Farice project. This investigation is expected to take quite a long time, even 1-2 years.

Notes to financial statements

16. Approval of financial statements

The Financial statements were approved by the board of directors and authorised for issue on April 10, 2006.

17. Transition to IFRS

As discussed in the note on accounting policies, this is the first time the company prepares its interim accounts in accordance with International Financial Reporting Standards (IFRS).

Amounts in the opening balance sheet as of January 1, 2005 have been changed in accordance with IFRS but were previously presented in accordance with legislation on annual accounts and Icelandic GAAP. The following tables and notes show the effects the change from Icelandic GAAP to IFRS has had on the financial position of the company, its financial results and cash flows.

Shareholder's equity January 1, 2006:

Equity according to accounting policies December 31, 2004.....	11.889.560
Equity according to accounting policies January 1, 2005.....	<u>11.823.313</u>
Decrease from former accounting policies	(66.247)

Notes to financial statements

	Previous GAAP 31.12.2004	Effects of transition to IFRS	IFRS 1.1.2005
Asset			
Fixed assets			
Point of presence	222.766	2.475	225.241
Backhaul	3.736.155	32.106	3.768.261
Cable stations	1.640.207	(735.263)	904.944
International waters	32.817.376	0	32.817.376
Common items	3.626.023	0	3.626.023
Prepaid lease	0	449.873	449.873
Deferred tax asset	296.918	15.601	312.519
	<u>42.339.445</u>	<u>(235.208)</u>	<u>42.104.237</u>
Current assets			
Accounts receivable	744.453	0	744.453
Other receivables	65.972	0	65.972
Market securities	1.000.000	0	1.000.000
Bank deposits and cash	1.607.749	0	1.607.749
	<u>3.418.174</u>	<u>0</u>	<u>3.418.174</u>
Total assets	<u>45.757.619</u>	<u>(235.208)</u>	<u>45.522.411</u>

Notes to financial statements

	Previous GAAP 31.12.2004	Effects of transition to IFRS	IFRS 1.1.2005
Stockholders' equity and liabilities			
Stockholders' equity			
Capital stock	13.689.662	0	13.689.662
Loss carry-forward	(1.800.102)	(66.247)	(1.866.349)
Stockholders' equity	<u>11.889.560</u>	<u>(66.247)</u>	<u>11.823.313</u>
 Liabilities			
Long-term liabilities			
Long-term bonds	<u>32.300.000</u>	<u>0</u>	<u>32.300.000</u>
 Current liabilities			
Accounts payable	1.247.831	(238.366)	1.009.465
Derivative financial instrument		83.653	83.653
Other current liabilities	320.228	(14.248)	305.980
	<u>1.568.059</u>	<u>(168.961)</u>	<u>1.399.098</u>
 Total equity and liabilities	 <u><u>45.757.619</u></u>	 <u><u>(235.208)</u></u>	 <u><u>45.522.411</u></u>