Orkuveita Reykjavíkur

Condensed Consolidated

Interim Financial Statements

1 January to 30 September 2008

Orkuveita Reykjavíkur
Bæjarhálsi 1
110 Reykjavík

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Endorsement by the Board of Directors and the Director

Orkuveita Reykjavíkur is a partnership that complies with the Icelandic Act No. 139/2001 on founding the partnership Orkuveita Reykjavíkur. The Company is an independent service company that produces and distributes electricity, distributes geothermal water for heating, cold water for consumptions and operates fibre-optic cable systems in its service area.

The condensed consolidated interim financial statements for the period 1 January to 30 September 2008 are prepared on the basis of the International Financial Reporting Standards. The financial statements comprise the consolidated interim financial statements of Orkuveita Reykjavíkur and subsidiaries. The financial statements have been reviewed by the independent auditor of the Company.

Loss of the operations of Orkuveita Reykjavíkur during the period amounted to ISK 39,588 million. According to the balance sheet the Company's assets amount to ISK 231,289 million, book value of equity at the end of the period amounted to ISK 48,218 million and the Company's equity ratio is 20,8%.

At the beginning and the end of the period the Company's shareholders were the following three:	Share
Reykjavíkurborg	93,539%
Akraneskaupstaður	5,528%
Borgarbyggð	0,933%

The Icelandic Parliament passed changes to several Acts affecting the energy sector in its spring session this year, which will come into effect 1 July 2009. These changes involve among other things that the Company must be split so that exclusive licence operations and competitive operations will be operated in separate entities. Preparations for these changes have begun.

Statement by the Board of Directors and the Director

The development of the ISK has been quite different in the period than were set forth in the financial schedules of the Company. This development causes significant increase in financial expenses during the period which consequently reduces the Company's equity.

According to the best knowledge of the Board of Directors and the Director of Orkuveita Reykjavíkur, the Company's condensed consolidated interim financial statements are in accordance with International Financial Reporting Standards as adopted by the EU. It is the opinion of the Board of Directors and the Director that the condensed consolidated interim financial statements give a fair view of the Company's assets, liabilities and financial standing at 30 September 2008 and the Company's operating return and changes in cash and cash equivalents for the period then ended.

It is furthermore the opinion of the Board of Directors and the Director that the condensed interim financial statements give a fair view of the Company's operating development and results, its standing and describe the main risk factors and uncertainties faced by the Company.

The Board of Directors and the Director of Orkuveita Reykjavíkur hereby confirm the Company's condensed consolidated interim financial statements for the period 1 January to 30 September 2008.

Reykjavík, 21 November 2008.

The Board of Directors:

Guðlaugur G. Sverrisson
Kjartan Magnússon
Júlíus Vífill Ingvarsson
Svandís Svavarsdóttir
Sigrún Elsa Smáradóttir
Gunnar Sigurðsson

Director:

Hjörleifur B. Kvaran

Independent Auditor´s Review Report

To the Board of Directors and owners of Orkuveita Reykjavíkur.

We have reviewed the accompanying condensed financial statements of Orkuveita Reykjavíkur, which comprise the interim balance sheet as at 30 September 2008 and the interim income statement, interim statement of changes in equity and interim cash flow statement for the nine-month period then ended, and a summary of significant accounting policies and other explanatory notes. Management is responsible for the preparation and fair presentation of this interim financial information in accordance with International Financial Reporting Standards as adopted by the EU. 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 does not give a true and fair view of the financial position of the Company as at 30 September 2008, and of its financial performance and its cash flows for the nine-month period then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Reykjavík, 21 November 2008.

KPMG hf.

Hlynur Sigurðsson
Auðunn Guðjónsson

Interim Income Statement for the period 1 January to 30 September 2008

	Notes	2008 1.1.-30.9.	2007 1.1.-30.9.
Operating revenue		16.816.467	15.414.145
Energy purchase		(3.074.377)	(2.999.907)
Salaries and salary related expenses	4	(2.882.002)	(2.445.905)
Other operating expenses		(2.677.567)	(2.658.336)
Depreciation and amortisation	5	(4.990.143)	(4.150.798)
Results from operating activities		3.192.378	3.159.199
Interest income		736.787	135.122
Interest expenses		(4.873.883)	(2.311.541)
(Expenses) income on financial assets and liabilities		(46.566.922)	6.846.243
Total financial income and expenses	6	(50.704.018)	4.669.824
Share of loss of associated companies		43.597	0
(Loss) profit before income tax		(47.468.043)	7.829.023
Income tax	7	7.879.900	(1.458.027)
(Loss) profit for the period		(39.588.143)	6.370.996

Attributable to:

Equity holders of the Company		(39.536.430)	6.367.993
Minority interest in subsidiaries		(51.713)	3.003
(Loss) profit for the period		(39.588.143)	6.370.996

Amounts are in ISK thousand

Interim Balance Sheet 30 September 2008

	Notes	30.9. 2008	31.12. 2007
Assets			
Property, plant and equipment	8	180.827.614	163.453.087
Intangible assets	9	677.171	403.838
Investments in associated companies		894.406	831.339
Investments in other companies		10.296.294	9.923.322
Embedded derivatives in electricity sales contracts	10	24.909.295	8.154.304
Other financial assets		222.856	140.848
Deferred tax assets	11	3.343.301	190.443
Total non-current assets		221.170.937	183.097.181
Inventories		1.633.841	969.092
Trade receivables		2.926.587	2.750.350
Other financial assets		113.169	226.494
Other receivables		1.303.255	697.023
Cash and cash equivalents		4.141.640	3.751.013
Total current assets		10.118.492	8.393.972
Total assets		231.289.429	191.491.153
Equity			
Revaluation reserve		23.374.919	23.374.919
Retained earnings		24.783.998	65.490.687
Equity attributable to equity holders of the Company		48.158.917	88.865.606
Minority interest		59.051	122.764
Total equity		48.217.968	88.988.370
Liabilities			
Loans and borrowings	13	171.391.803	88.032.626
Retirement benefit obligation		408.135	395.338
Other financial liabilities		80.947	60.550
Deferred tax liabilities	11	0	4.716.084
Total non-current liabilities		171.880.885	93.204.598
Accounts payable		3.867.747	2.692.213
Loans and borrowings	13	4.855.642	4.608.003
Other financial liabilities		543.880	122.474
Current tax liabilities		211	11.169
Other current liabilities		1.923.096	1.864.326
Total current liabilities		11.190.576	9.298.185
Total liabilities		183.071.461	102.502.783
Total equity and liabilities		231.289.429	191.491.153

Amounts are in ISK thousand

Interim Statement of Equity for the period 1 January to 30 September 2008

	Revaluation reserve	Retained earnings	Attributable to equity holders of the Company	Minority interest	Total equity
1.1. - 30.9. 2008					
Equity at 1 January 2008	23.374.919	65.490.687	88.865.606	122.764	88.988.370
Loss for the period		(39.536.430)	(39.536.430)	(51.713)	(39.588.143)
Other changes				(12.000)	(12.000)
Dividends paid		(1.170.259)	(1.170.259)		(1.170.259)
Equity at 30 September 2008	23.374.919	24.783.998	48.158.917	59.051	48.217.968
1.1. - 30.9. 2007					
Equity 31 december 2006	8.731.162	57.823.705	66.554.867	115.896	66.670.763
Changes due to adoption of IFRS		2.687.759	2.687.759		2.687.759
Equity at 1 January 2007, IFRS	8.731.162	60.511.464	69.242.626	115.896	69.358.521
Profit for the period		6.367.993	6.367.993	3.003	6.370.996
Increase in capital				430.560	430.560
Dividends paid		(1.145.751)	(1.145.751)		(1.145.751)
Equity at 30 September 2007	8.731.162	65.733.706	74.464.868	549.459	75.014.326

Amounts are in ISK thousand

Interim Statement of Cash Flows for the period 1 January to 30 September 2008

	2008 1.1.-30.9.	2007 1.1.-30.9.
Cash flows from operating activities		
(Loss) profit for the period	(39.588.142)	6.370.996
Financial income and expenses	50.704.018	(4.669.824)
Other items not affecting cash flow	(2.909.600)	5.405.354
Changes in operating assets and liabilities	(1.333.331)	(92.112)
Working capital from operation before interests and taxes	6.872.945	7.014.414
Received interest income	812.914	125.080
Paid interest expenses	(3.603.201)	(1.962.160)
Paid due to other financial income and expenses	347.033	117.427
Net cash from operating activities	4.429.691	5.294.761
Cash flows from investing activities		
Acquisition of property, plant and equipment and intangible assets	(21.409.204)	(14.492.007)
Acquisition of associated companies	(215.557)	(89.017)
Acquisition of other financial assets	(933.641)	(8.767.862)
Proceeds from sale of other assets	61.479	133.224
Net cash used in investing activities	(22.496.923)	(23.215.662)
Cash flows from financing activities		
Proceeds from new borrowings	13.789.204	14.174.418
Repayment of borrowings	(2.440.826)	(1.056.110)
Paid-in capital	0	500.000
Dividends paid	(1.170.259)	(1.145.751)
Credit facility	11.065.180	5.398.444
Current liabilities, (decrease) increase	(2.785.440)	2.027.384
Net cash from financing activities	18.457.859	19.898.385
Increase in cash and cash equivalents	390.627	1.977.484
Cash and cash equivalents at beginning of the period	3.751.013	253.171
Cash and cash equivalents at period end	4.141.640	2.230.655
Investments and financing without payment effects:		
Acquisition of property, plant and equipment	(1.228.216)	(464.432)
Proceeds from sale of property, plant and equipment	0	553
Other financial assets, change	0	(553)
Current liabilities, increase	1.228.216	464.432
Other information:		
Working capital from operation	4.635.887	5.345.310

Amounts are in ISK thousand

Notes to the Interim Financial Statements

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Amounts are in ISK thousand

Notes

1. Reporting entity

Orkuveita Reykjavíkur is a partnership that complies with the Icelandic Act No. 139/2001 on founding the partnership Orkuveita Reykjavíkur. The Company's headquarters are at Bæjarháls 1 in Reykjavik. The Company's consolidated interim financial statements include the interim financial statements of the parent company and its subsidiaries, (together referred to as "the Group") and a share in associated companies.

The Company is an independent service company that produces and distributes electricity, distributes geothermal water for heating, cold water for consumptions, sewer systems, and operates fibre-optic cable systems.

2. Basis of preparation

a. ***Statement of compliance***

These condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standard IAS 34 Interim Financial Reporting. They do not include all of the information required for a complete set of consolidated annual financial statements and should be read in conjunction with the consolidated financial statements of the Company as at and for the year ended 31 December 2007.

The interim financial statements were approved by the Board of Directors on 21 November 2008.

b. ***Basis of measurement***

The accounting policies applied by the Group in these condensed consolidated interim financial statements are the same as those applied by the Group in its consolidated financial statements as at and for the year ended 31 December 2007. The consolidated financial statements for the Group as at and for the year ended 31 December 2007 are available upon request from the Company's registered office at Bæjarháls 1, Reykjavík, at www.or.is or at The Nordic Stock Exchange website, www.omxgroup.com.

The consolidated interim financial statements have been prepared on the historical cost basis except for the following:

- A part of property, plant and equipment was revalued at fair value.
- Derivative agreements are stated at fair value.

c. ***Functional and presentation currency***

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

d. ***Use of estimates and judgements***

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

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

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

- Note 8; Property, plant and equipment
- Note 10; Embedded derivatives in electric power sale contracts

3. ## Segment reporting

Segment information is presented by the Group's business segments according to the Group's organisation and internal reporting. Business segments consist of production, distribution and sale, and other operation. In addition, information is provided on the Group's sectors, which are electricity, hot water, cold water, sewer and fibre-optic cable systems.

Business segments - divisons

	Production	Distribution	Sale	Other operation	Adjust-ments	Total
1.1. - 30.9. 2008						
Operation:						
External revenue	2.579.270	4.428.679	9.223.091	585.427	0	16.816.467
Inter-segment revenue	2.574.727	4.583.969	429.300	823.536	(8.411.532)	0
Total segment revenue	5.153.997	9.012.648	9.652.391	1.408.963	(8.411.532)	16.816.467
Segment result	511.798	2.906.486	336.655	(133.326)	0	3.621.613
Unallocated expenses						(429.235)
Results from operating activities						3.192.378
Financial income and expenses						(50.704.018)
Share of loss of associated companies						43.597
Income tax						7.879.900
(Loss) for the period						(39.588.143)
1.1. - 30.9. 2007						
Operation:						
External revenue	2.095.144	3.806.364	8.734.214	778.423	0	15.414.145
Inter-segment revenue	2.292.574	3.040.096	415.054	757.092	(6.504.816)	0
Total segment revenue	4.387.718	6.846.460	9.149.268	1.535.515	(6.504.816)	15.414.145
Segment result	773.238	1.425.059	1.284.399	225.417	0	3.708.113
Unallocated expenses						(548.914)
Results from operating activities						3.159.199
Financial income and expenses						4.669.824
Income tax						(1.458.027)
Profit for the period						6.370.996

Amounts are in ISK thousand

3. Segment reporting, contd.

Business segments - divisons, contd.

	Production	Distribution	Sale	Other operation	Unallocated	Total
1.1. - 30.9. 2008						
Balance sheet (30.9.2008):						
Property, plant and equipment .	90.280.550	80.064.065	19.441	427.258	10.036.300	180.827.614
Intangible assets	0	0	0	218.855	458.316	677.171
Other unallocated assets						49.784.644
Total assets						231.289.429
Unallocated liabilities						183.071.461
Investments:						
Property, plant and equipment .	16.283.572	5.566.931	0	86.915	373.677	22.311.095
Intangible assets	0	0	0	153.968	172.938	326.906
Depreciation:						
Property, plant and equipment .	2.119.736	2.405.779	3.889	0	360.334	4.889.738
Intangible assets	0	0	0	0	100.404	100.404
1.1. - 30.9. 2007						
Balance sheet (31.12.2007):						
Property, plant and equipment .	77.251.497	76.542.354	46.163	375.272	9.237.801	163.453.087
Intangible assets	0	0	0	64.888	338.950	403.838
Other unallocated assets						27.634.228
Total assets						191.491.153
Unallocated liabilities						102.502.783
Investments:						
Property, plant and equipment .	8.623.093	3.303.833	2.887	36.859	525.551	12.492.223
Intangible assets	0	0	0	75.313	84.626	159.939
Depreciation:						
Property, plant and equipment .	1.495.654	2.198.998	25.142	31	338.093	4.057.918
Intangible assets	0	0	0	0	92.880	92.880

Amounts are in ISK thousand

3. Segment reporting, contd.

Business segments - sectors

	Electricity	Hot water	Cold water	Sewer	Fibre-optic cable system	Adjust-ments	Total
1.1. - 30.9. 2008							
Revenue:							
External revenues	8.614.894	4.337.375	1.544.898	2.011.430	307.870	0	16.816.467
Inter-segment revenue	906.417	360.197	60.292	78.499	0	(1.405.405)	0
Total segment revenue	9.521.311	4.697.572	1.605.190	2.089.929	307.870	(1.405.405)	16.816.467
Assets (30.9.2008):							
Property, plant and equi	88.875.666	42.556.522	14.205.661	27.915.906	7.273.859	0	180.827.614
Intangible assets	235.575	329.767	37.582	74.247	0	0	677.171
Unallocated assets							49.784.644
Total assets							231.289.429
Investments:							
Property, plant and equi	15.774.450	4.579.836	622.739	1.122.458	211.612	0	22.311.095
Intangible assets	86.123	196.857	14.700	29.226	0	0	326.906
Depreciation:							
Property, plant and equi	1.852.510	1.583.425	379.180	800.441	274.182	0	4.889.738
Intangible assets	38.361	31.284	9.635	21.124	0	0	100.404
1.1. - 30.9. 2007							
Revenue:							
External revenues	7.894.989	3.938.760	1.502.222	1.674.019	404.155	0	15.414.145
Inter-segment revenue	916.417	371.325	71.922	93.641		(1.453.305)	0
Total segment revenue	8.811.406	4.310.085	1.574.144	1.767.660	404.155	(1.453.305)	15.414.145
Assets (31.12.2007):							
Property, plant and equi	73.487.182	41.741.690	14.090.805	27.715.907	6.417.503	0	163.453.087
Intangible assets	168.400	111.459	40.788	83.191	0	0	403.838
Unallocated assets							27.634.228
Total assets							191.491.153
Investments:							
Property, plant and equi	7.624.003	2.759.345	459.973	748.634	900.268	0	12.492.223
Intangible assets	35.289	98.670	8.547	17.433	0	0	159.939
Depreciation:							
Property, plant and equi	1.541.906	1.209.590	334.904	725.802	245.716	0	4.057.918
Intangible assets	29.994	32.024	9.798	21.064	0	0	92.880

Amounts are in ISK thousand

4. Salaries and salary related expenses

Salaries and salary related expenses are specified as follows:	2008 1.1.-30.9.	2007 1.1.-30.9.
Salaries	2.847.892	2.460.267
Defined contribution pension plan expense	388.368	330.171
Retirement benefit obligation, change	24.200	23.148
Other salary related expenses	217.292	181.221
Total salaries and salary related expenses	3.477.752	2.994.807

Salaries and salary related expenses are thus stated in the financial statements:

Expensed in the income statement	2.882.002	2.445.905
Capitalised on projects	595.750	548.902
Total salaries and salary related expenses	3.477.752	2.994.807

5. Depreciation and amortisation

Depreciation and amortisation is specified as follows:

Depreciation of property, plant and equipment, cf. note 8	4.889.739	4.057.918
Amortisation of intangible assets, cf. note 9	100.404	92.880
Depreciation and amortisation recognised in the income statement	4.990.143	4.150.798

6. Financial income and expenses

Financial income and expenses are specified as follows:

Interest income	736.787	135.122
Interest expenses	(4.671.034)	(2.200.521)
Guarantee fee to owners	(202.849)	(111.020)
Total interest expenses	(4.873.883)	(2.311.541)
Fair value changes of embedded derivatives in electricity sales contracts	16.773.696	1.507.723
Fair value changes of shares in other companies	(45.012)	0
Foreign exchange difference and forward currency swaps	(63.378.517)	5.239.080
Dividends	82.911	0
Profit from sale of shares in other companies	0	99.440
Total (expenses) income on financial assets and liabilities	(46.566.922)	6.846.243
Total financial income and expenses	(50.704.018)	4.669.824

Financing cost due to construction of a power plant to the amount of ISK 480,5 million is capitalised and has been recognised as reduction of financial expenses.

Financing cost due to construction of power plants and other projects is capitalized on the investment during the construction time or until the asset will give revenue to the Company. The financing cost is based on average interest rates on loans to OR and securitycharge to the owners of the Company. The rate is 4.26% on yearly basis. It is calculated from the total financial obligation at the given time.

Amounts are in ISK thousand

7. Income Tax

Orkuveita Reykjavíkur was exempt from taxation but with Act No. 50/2003 on the Tax Liability of Energy Companies the Company became tax liable in accordance with Article 2 of Act No. 90/2003 on Income Tax. The Act came into effect for the assessment of income tax in the year 2007 due to income in the year 2006. The part of the Company´s operation concerning operation of cold water supply and sewer remains though exempt from income tax.

In May 2008 the Icelandic Parliament approved a decrease in the income tax rate from 26% to 23.5% as of 1 January 2008. The effect of this amounts to ISK 456 million and the decrease is recognised in the interim income statement.

Income tax recognised in the income statement is specified as follows:	2008 1.1.-30.9.	2007 1.1.-30.9.
Change in deferred income tax	7.879.900	1.458.027

Reconciliation of effective tax rate:		2008 1.1.-30.9.		2007 1.1.-30.9.
(Loss) profit before income tax		(47.468.043)		7.829.023
Income tax according to current tax ratio	(23,5%)	11.154.990	(26,0%)	(2.035.546)
Changes in income tax rate	(1,0%)	455.557	0,0%	0
Non-taxable operation of water supply and sewer	7,4%	(3.513.541)	5,7%	446.507
Other items	0,5%	(217.106)	1,7%	131.012
Effective income tax	(16,6%)	7.879.900	(18,6%)	(1.458.027)

8. Property, plant and equipment

Property, plant and equipment is specified as follows:

1.1. - 30.9. 2008	Production system	Distribution system	Other real estates	Other equipments	Total
Cost or deemed cost					
Balance at beginning of the period ...	112.503.139	138.979.119	8.935.691	4.589.086	265.007.035
Reclassification of assets	272.626	(116.328)	(42.958)	(64.440)	48.900
Additions during the period	16.267.793	5.343.882	517.122	182.298	22.311.095
Balance at the end of the period	129.043.558	144.206.673	9.409.855	4.706.944	287.367.030
Depreciation					
Balance at beginning of the period ...	34.657.781	63.034.380	1.598.458	2.263.329	101.553.948
Reclassification of assets	91.051	34.849	(770)	(29.401)	95.729
Depreciated during the period	2.196.056	2.370.095	150.743	172.844	4.889.738
Balance at the end of the period	36.944.888	65.439.324	1.748.431	2.406.772	106.539.415
Carrying amounts					
At 1.1.2008	77.845.358	75.944.739	7.337.233	2.325.757	163.453.087
At 30.9.2008	92.098.670	78.767.349	7.661.424	2.300.172	180.827.614
Thereof ass. in constr. at period end .	24.537.076	0	0	0	24.537.076

Amounts are in ISK thousand

8. Property, plant and equipment, contd.

1.1. - 31.12. 2007	Production system	Distribution system	Other real estates	Other equipments	Total
Cost or deemed cost					
Balance at year beginning	75.661.692	127.517.196	8.614.674	4.246.748	216.040.310
Reclassification of assets	316.423	(421.864)	(3.584)	109.025	0
Additions during the year	15.049.991	5.671.345	324.601	233.313	21.279.250
Sold and disposed in the year	(646.876)	(1.474.000)	0	0	(2.120.876)
Revaluation	22.121.909	7.686.442	0	0	29.808.351
Balance at year end	112.503.139	138.979.119	8.935.691	4.589.086	265.007.035
Depreciation					
Balance at year beginning	25.380.305	57.352.782	1.412.551	1.925.861	86.071.499
Reclassification of assets	52.370	(154.307)	(3.772)	105.709	0
Depreciated during the year	2.090.770	2.896.048	189.679	231.759	5.408.256
Sold and disposed in the year	(128.182)	(740.514)	0	0	(868.696)
Revaluation	7.262.518	3.680.371	0	0	10.942.889
Balance at year end	34.657.781	63.034.380	1.598.458	2.263.329	101.553.948
Carrying amounts					
At 1.1.2007	50.281.387	70.164.414	7.202.123	2.320.887	129.968.811
At 31.12.2007	77.845.358	75.944.739	7.337.233	2.325.757	163.453.087
Thereof ass. in constr. at year end	11.004.598	0	0	0	11.004.598

Heating rights

The Group's lands are recognised among property, plant and equipment. Included in the land are heating rights. Those assets are recognised at cost value and have not been divided in heating rights, on the one hand, and land on the other. Carrying amount of those assets at the end of the period amounted to ISK 1,701 million (31.12.2007: ISK 1,675 million).

Revaluation

At year end 2006, a revaluation was made on heating, electricity and water supply distribution systems and sewer systems. The revaluation lead to an increase in the carrying amount of those assets to the amount of ISK 10,097 million. At year end 2007, this revaluation was reperformed and lead to an increase in the carrying amount of those assets to the amount of ISK 4,006 million.

At year end 2007, a revaluation was made on the Group's production systems, which included assets used in the production of electricity, hot and cold water. The revaluation lead to an increase in the carrying amount of those assets to the amount of ISK 14,859 million.

In the revaluation, the relevant asset groups are measured at fair value. The aforementioned increases are recognised in a revaluation reserve among equity taken into account effects of deferred income tax.

The fair value of production assets is determined on the basis of the depreciated replacement cost. This consists in that an assessment is made on changes in the construction cost of comparable assets and both cost and accumulated depreciations are revalued in accordance with those changes. The calculation is based on official information and real numbers from the Group's books on value changes of cost items and takes in account an estimate on the weight of each cost item in the total cost of construction of comparable assets. Cost items and their proportional weight was determined by experts within and outside of the Company.
The same method is applied in the determination of the fair value of distribution systems, accounted at fair value. Revalued distribution systems are used in operations subject to special licence and income limits are primarily based on changes in the building cost index. This is also taken into account when determining the fair value.

Amounts are in ISK thousand

8. Property, plant and equipment, contd.

Obligations

In May 2008 the Company entered into a contract concerning purchase of equipment for power plants. The equipment will be delivered in the years 2010 and 2011. The contract and other contracts regarding developments at Hellisheiði amount to ISK 34.8 billion as per exchange rate at the end of the period. Furthermore, the Company has entered into contracts and placed purchase orders with suppliers and developers concerning work on production and distribution systems. The balance of these contracts and purchase orders at 30 September 2008 is estimated at ISK 1,8 billion.

9. Intangible assets

Intangible assets are specified as follows:

	Preparation cost	Software	Total
1.1. - 30.9. 2008			
Cost			
Balance at beginning of the period	64.888	1.107.268	1.172.156
Reclassification of assets	0	11.350	11.350
Additions during the period	153.967	172.939	326.906
Balance at end of the period	218.855	1.291.557	1.510.412
Amortisation			
Balance at beginning of the period	0	768.318	768.318
Reclassification of assets	0	(35.481)	(35.481)
Additions during the period	0	100.404	100.404
Balance at end of the period	0	833.241	833.241
Carrying amounts			
At 1.1.2008	64.888	338.950	403.838
At 30.9.2008	218.855	458.316	677.171
1.1. - 31.12. 2007			
Cost			
Balance at year beginning	0	960.229	960.229
Additions during the year	64.888	147.039	211.927
Balance at year end	64.888	1.107.268	1.172.156
Amortisation			
Balance at year beginning	0	638.274	638.274
Additions during the year	0	130.044	130.044
Balance at year end	0	768.318	768.318
Carrying amounts			
At 1.1.2007	0	321.955	321.955
At 31.12.2007	64.888	338.950	403.838

Amounts are in ISK thousand

10. Embedded derivatives in electricity sales contracts

Three electricity sales contracts have been made to 20 years with Norðurál due to the aluminium plant at Grundartangi, in addition to a contract with Landsnet hf. on transmission of the electricity. Orkuveita Reykjavíkur and Norðurál have also made an electricity sales contract due to sale of electricity to a pending aluminium plant in Helguvík, and delivery of electricity is estimated to begin for the first stage in the year 2010. Those electricity sales contracts are made in USD and the price of the electricity is related to the world market price of aluminium.

The aforementioned electricity sales contracts include embedded derivatives as income thereon is subject to changes in the future world market price of aluminium. In accordance with provisions of IAS 39 on financial instruments, the fair value of those embedded derivatives regarding Grundartangi, have been measured and recognized in the interim financial statements.
As the market value of those embedded derivatives is not available their fair value has been measured with generally accepted evaluation methods. The expected net present value of the cash flow of an contract on the accounting date has been measured, based on the future price of aluminium on LME (London Metal Exchange) on the accounting date and expectations of price development of aluminium for the next 30 years according to the assessment of CRU, an independed evaluation party, as available on the accounting date. The expected net present value of cash flow of a contract on the accounting date has been deducted from this value based on premises on aluminium price on the initial date of the contract. The difference is the fair value change of the derivative. The valuation is based on the premises that the derivative has no value at the initial date of the contract.

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

The fair value of embedded derivatives due to electricity sales contracts, which have not yet been executed and that are uncertain, is calculated in the same way. Their fair value amounts to a total of ISK 11.659 million on 30.9.2008 (31.12.2007: ISK 2.885 million) and is not recognized in the interim financial statements.

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

	30.9.2008	31.12.2007
Fair value of embedded derivatives at the beginning of the year	8.154.304	3.699.990
Fair value changes during the period	16.754.991	4.454.314
Fair value of embedded derivatives at end of the period	24.909.295	8.154.304

11. Deferred tax assets and liabilities

Deferred tax assets and liabilities is specified as follows:

1.1. - 30.9. 2008	Tax assets	Tax liabilities	Net amount
Deferred tax assets/liabilities at the beginning of the year	190.443	4.716.084	(4.525.641)
Calculated income tax for the period	3.152.858	(4.727.042)	7.879.900
Other changes	0	10.958	(10.958)
Deferred tax assets/liabilities at the end of the period	3.343.301	0	3.343.301

Amounts are in ISK thousand

11. Deferred tax assets and liabilities, contd.

1.1. - 31.12. 2007	Tax assets	Tax liabilities	Net amount
Deferred tax assets/liabilities at the beginning of the year	1.480.889	0	1.480.889
Effects of a revaluation of non-current assets	0	4.221.705	(4.221.705)
Calculated income tax for the year	(1.290.446)	503.871	(1.794.317)
Current tax liabilities	0	(11.169)	11.169
Other changes	0	1.677	(1.677)
Deferred tax assets/liabilities at year end	190.443	4.716.084	(4.525.641)

Deferred tax assets and liabilities are attributable to the flollowing:

	30.9.2008		31.12.2007	
	Tax assets	Tax liabilities	Tax assets	Tax liabilities
Property, plant and equipment	(3.519.201)	0	156.362	3.845.752
Embedded derivatives	(5.853.684)	0	0	2.120.119
Other items	187.867	0	5.841	(140.765)
Effect of carry forward taxable loss	12.528.319	0	28.240	(1.109.022)
Deferred tax assets/liabilities at the end of the period	3.343.301	0	190.443	4.716.084

12. Equity

It is the Company's policy to maintain a strong equity standing in order to support stability and future development of the operations. Dividend payments have been determined as a percentage of retained earnings independent from the return of the relevant year. An owners' meeting makes decisions on dividend payments.

The Company's Board of Directors endeavours to maintain a balance between yield on equity, which can be increased by increased leverage, and benefits and safety, which can be obtained with a strong equity ratio. Return on equity is negative by 54.7% during the period 1.1. to 30.9. 2008 (1.1. to 30.9. 2007: positive by 12.5%).

The equity ratio of the Company at the end of the period is 20.8% (1.1. to 30.9.2008: 46.5%)

Amounts are in ISK thousand

13. Loans and borrowings

This note provides information about the contractual terms of the Group's interest-bearing loans and borrowings, which are measured at amortized cost. For more information about the Group's exposure to interest rate, foreign currency and liquidity risk, see note 14.

	30.9.2008	31.12.2007
Non-current liabilities		
Bank loans	154.043.712	83.695.057
Credit facility	14.714.314	0
Bond issuance	7.489.419	6.738.653
	176.247.445	90.433.710
Current portion on non-current liabilities	(4.855.642)	(2.401.084)
	171.391.803	88.032.626
Current liabilities		
Current portion on non-current liabilities	4.855.642	2.401.084
Current loans	0	2.206.919
	4.855.642	4.608.003
Total interest-bearing loans and borrowings	176.247.445	92.640.629

Terms of interest-bearing loans and borrowings

		30.9. 2008		31.12. 2007	
	Date of maturity	Average interest rate	Carrying amount	Average interest rate	Carrying amount
Liabilities in foreign currencies:					
Liabilities in CHF	26.6.2036	2.99%	26.617.175	2.94%	19.248.482
Liabilities in EUR	26.6.2036	5.21%	58.675.593	3.67%	34.751.351
Liabilities in USD	10.3.2028	3.11%	18.461.372	4.46%	11.738.228
Liabilities in JPY	26.6.2036	1.07%	12.906.829	1.05%	9.358.629
Liabilities in GBP	26.6.2036	6.36%	3.020.251	6.29%	2.463.379
Liabilities in SEK	5.10.2027	5.36%	10.788.992	4.35%	8.082.088
Liabilities in CAD	13.12.2011	3.59%	1.149.473	5.36%	65.658
			131.619.685		85.707.815
Liabilities in Icelandic kronas:					
Indexed	10.1.2037	5.16%	7.494.419	4.98%	6.932.814
Total interest-bearing loans and borrowings			176.247.445		92.640.629

Repayment on non-current liabilities are specified as follows on the next years:	30.9.2008	31.12.2007
Period 2008/2009	4.855.642	2.401.084
Period 2009/2010	3.135.819	3.012.120
Period 2010/2011	7.810.983	2.345.727
Period 2011/2012	22.989.144	5.055.364
Period 2012/2013	22.378.689	5.295.980
Later	115.077.168	72.323.435
Total non-current liabilities, including next 12 months repayment	176.247.445	90.433.710

Guarantees and pledges

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

Amounts are in ISK thousand

14. Risk management and financial instruments

a. ***Overview***

Orkuveita Reykjavíkur has approved a policy on objectives and execution of risk management. The main objectives with risk management according to the policy is to contribute to a stable return and limit financing cost by limiting fluctuations in currency exchange and aluminium prices and to contribute to a low interest rate.

The Group's currency risk is related to cash flow risk and risk in the balance sheet. Interest rate risk is related to the variance of variable interests and fixed interests and can relate to both cash flow and the balance sheet. Risk due to variance of aluminium prices is due to the relation between electricity price to industries and aluminium price level and relates to the cash on electricity sale to industry consumers.

The Group's currency risk is monitored both in cash flow and in the balance sheet with generally accepted calculation methods. Annual standards deviation and daily value at risk for liabilities and estimated cash flow in foreign currencies is measured. Risk in cash flow due to changes in aluminium prices and interests is measured based on the same method.

The policy defines risk and sets performance levels. The Company's Board of Directors receives on regular basis a statement on the standing and performance of the Group's risk management.

Decision making and control on the execution of the risk management is in the hands of a risk committee. The risk committee consists of the Managing Director, Director of finance, Superior of financial and risk management and Superior of the financial department.
Financial risk is divided into:
• Market risk
• Liquidity risk
• Credit risk

b. ***Market risk***

Market risk is the risk that changes in the market price of foreign currencies, aluminium price and interests will affect the Group’s income or the value of its financial instruments. This is the risk that weighs the most in the Group and is divided into:
• Currency risk due to liabilities in the balance sheet and cash flow in foreign currencies.
• Interest rate risk due to loans.
• Risk due to changes in the world market price of aluminium.

(i) ***Currency risk***

The Group is exposed to currency risk on sales, purchases and borrowings that are denominated in a currency other than Icelandic kronas (ISK). Those currencies mainly creating risk are Euro (EUR), Swiss Francs (CHF), Japanese Yens (JPY) and Swedish kronas (SEK).

Approx. 95.7% of the Group's non-current loans are in foreign currencies and thus creates currency risk. This currency risk is hedged in accordance with the Company's policy on risk management where the interest cost of the loans is assessed together with the currency risk. Interest rate of loans in foreign currencies was considerably lower than for loans in Icelandic kronas.

Foreign exchange rate of the main currencies during the year is specified as follows:

	Average exchange rate		Exchange rate at year end	
	2008	2007		
	1.1.-30.9	1.1.-31.12	30.9.2008	31.12.2007
CHF	71,794	53,339	94,745	55,503
EUR	115,502	87,601	149,270	91,955
USD	75,896	64,016	105,995	62,405
JPY	0,717	0,544	1,001	0,557
GBP	147,299	128,072	188,700	125,050
SEK	12,259	9,470	15,258	9,743
CAD	74,450	59,750	100,015	63,655
TWI	149,506	118,313	196,469	119,995

Amounts are in ISK thousand

14. Risk management and financial instruments, contd.

Exposure to currency risk

The Group's exposure to currency risk based on the nominal amounts is specified as follows (in ISK thousand):

30.9.2008	CHF	EUR	USD	JPY	GBP	Other currencies
Interest-bearing liabilities	(32.537.678)	(67.378.876)	(28.006.849)	(18.141.809)	(3.504.782)	(19.183.032)
Accounts payable			(22.949)		(686)	(40.159)
Trade receivable	10.008	24.482	707.601			15.722
Bank deposits	2.196	783.400	175.399	594	8.538	125.014
Aluminium deriv.			24.909.295			
Balance sheet risk	(32.525.474)	(66.570.994)	(2.237.503)	(18.141.215)	(3.496.930)	(19.082.455)
Est. sale in 2008			5.602.906			
Est. purch. in 2008 ...		(2.483.258)	(50.731)	(295.147)	(889)	(33.089)
Off balance sheet risk		(2.483.258)	5.552.175	(295.147)	(889)	(33.089)
Swaps	(891.402)	1.344.623		475.345	(813.845)	(102.684)
Forward agreem.	(28.855)	(946.520)	(549.206)	(116.622)	(288.554)	(456.440)
Net risk	(33.445.731)	(68.656.149)	2.765.466	(18.077.639)	(4.600.218)	(19.674.668)

31.12.2007	CHF	EUR	USD	JPY	GBP	Other currencies
Interest-bearing liabilities	(19.248.482)	(34.751.351)	(11.738.228)	(9.358.630)	(2.463.379)	(8.147.745)
Accounts payable	(143)	(123.224)	(27.021)	0	(670)	(11.589)
Trade receivable			275.299			1.559
Bank deposits	1.925	557.967	273.259	623	2.000	2.007
Aluminium deriv.			8.154.304			
Balance sheet risk	(19.246.700)	(34.316.608)	(3.062.387)	(9.358.007)	(2.462.049)	(8.155.768)
Est. sale in 2008			2.492.966			
Est. purch. in 2008 ...		(1.645.850)		(683.954)		
Off balance sheet risk		(1.645.850)	2.492.966	(683.954)		
Swaps	(468.225)	526.172	437.746	386.777	(1.037.912)	
Forward agreem.	(19)	(350)	(234)	(34)	(121)	(186)
Net risk	(19.714.944)	(35.436.636)	(131.909)	(9.655.218)	(3.500.082)	(8.155.954)

Sensitivity analysis

A 10 percent strengthening of the Icelandic krona against the following currencies at 31 December would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant. The analysis is performed on the same basis for 2007.

	Profit or (loss)	
	30.9.2008	31.12.2007
CHF	2.406.885	1.424.256
EUR	4.926.209	2.539.429
USD	165.575	226.617
JPY	1.342.450	692.493
GBP	258.773	182.192
Other currencies	1.412.102	603.527

14. Risk management and financial instruments, contd.

(ii) *Interest rate risk*

The Group's non-current loans and interest rate swaps are mainly based on variables interests.

Interest-bearing financial assets and liabilities are specified as follows at the end of the period:

Fixed rate instruments	30.9.2008	31.12.2007
Financial liabilities	13.525.231	10.775.934
Variable rate instruments		
Financial assets	120.394	37.590
Financial liabilities	162.824.975	82.052.627
	162.704.581	82.015.037

Fair value sensitivity analysis for fixed rate instruments

The Group does not account for any fixed rate financial assets and liabilities at fair value through profit or loss, and the Group does not designate derivatives (interest rate swaps) as hedging instruments under a fair value hedge accounting model. Therefore a change in interest rates at the reporting date would not affect profit or loss.

Cash flow sensitivity analysis for variable rate instruments

A change of 100 basis points in interest rates at the reporting date would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency rates, remain constant. The analysis is performed on the same basis for 2007.

	Profit or (loss)	
	100 p increase	100 p decrease
30.9.2008		
Variable rate instruments	(2.490.049)	2.638.901
31.12.2007		
Variable rate instruments	(958.175)	999.368

(iii) *Aluminium price risk*

The Group has entered into electricity sales contracts where the sales price of electricity is based on among other things the world market price of aluminium. The Group has not hedged specifically against aluminium price changes. Revenue from the electricity sales contracts related to aluminium price level amounted to 14.8% of the Group's total revenue for the period.

Sensitivity analysis

A change in the aluminium price level by 10% at year end, whether by increase or decrease, would have the following effect on the Group's profit or loss after taxes.

	Profit or (loss)	
	30.9.2008	31.12.2007
Increase by 10%	8.082.160	3.109.583
Decrease by 10%	(8.082.160)	(3.109.583)

Amounts are in ISK thousand

14. Risk management and financial instruments, contd.

(iv) ***Other market risk***

Other market risk is limited as investments in bonds and shares are an insubstantial part of the Group's operation.

c. ***Liquidity risk***

Liquidity risk is the risk that the Group will not be able to meet its financial obligations as they fall due. The Group’s approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking

Owners' guarantees for the Company's loans and a good credit rating have enabled the Company to obtain access to loans at good terms. The Company pays for owners' guarantee a 0.25% guarantee fee on the principal of the loans at each time. Power plant projects at Hellisheiði have primarily been financed with loans from the European Investment Bank (EIB), the Europe Development Bank (CEB) and the Nordic Investment Bank (NIB), but all of those banks have expressed an interest in continued participation in the financing of geothermal power plant projects, such as the power plant at Hellisheiði. The terms of the loans are long and have been determined in accordance with long term agreements on sale of electricity in order to limit the Company's risk inherent with refinancing.

The Group's cash and cash equivalents at year end amounted to ISK 4.1 billion. Furthermore, the Group had unused loan authorizations and an open credit line to the total amount of approx. ISK 18.0 billion. The Group had thus in total ensured capital at year end to the amount of approx. ISK 22.1 billion. The corresponding amount in 2007 amounted to ISK 23 billion.

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

	Carrying amount	Contractual cash flows	Less than 1 year	1 - 2 years	2 - 5 years	More than 5 years
30.9. 2008						
Non-derivative financial instruments						
Interest-bearing liabilities	176.247.445	(242.517.195)	(11.537.763)	(23.738.196)	(99.558.782)	(107.682.454)
Derivative financial instruments						
Currency swaps	12.037	(2.625)	19.990	27.034	(14.723)	(34.926)
	176.259.482	(242.519.820)	(11.517.773)	(23.711.162)	(99.573.505)	(107.717.380)
31.12.2007						
Non-derivative financial instruments						
Interest-bearing liabilities	92.640.629	(133.391.720)	(8.378.826)	(6.596.026)	(22.626.844)	(95.790.024)
Derivative financial instruments						
Currency swaps	155.442	(236.417)	(136.629)	(26.949)	(61.015)	(11.824)
	92.796.071	(133.628.137)	(8.515.455)	(6.622.975)	(22.687.859)	(95.801.848)

Non-current loans will presumably be refinanced in order to prolonge the loan term. Therefore, the distribution of the repayments will presumably be different from the above.

Amounts are in ISK thousand

14. Risk management and financial instruments, contd.

d. ***Credit risk***

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers. Losses due to unpaid receivables are insubstantial and have limited effect on the Group's return.

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

	30.9.2008	31.12.2007
Trade receivable	2.926.587	2.750.350
Other current receivables	1.303.255	697.023
Other financial assets	336.025	367.342
Cash and cash equivalents	4.141.640	3.751.013
	8.707.507	7.565.728

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

Trade receivable, industrial consumers	703.683	190.515
Trade receivable, retail	2.222.904	2.559.835
	2.926.587	2.750.350

Impairment

The aging of trade receivables and allowance for doubtful accounts at the reporting date was:

	30.9.2008		31.12.2007	
	Gross balance	Allowance	Gross balance	Allowance
Non-overdue receivables	2.099.039	42.407	2.080.247	49.096
Overdue receivables	931.709	61.754	769.599	50.400
	3.030.748	104.161	2.849.846	99.496

e. ***Fair value***

Fair values versus carrying amounts

The fair values of finacial assets and liabilities, together with the carrying amounts are specified as follows:

	30.9.2008		31.12.2007	
	Carrying amount	Fair value	Carrying amount	Fair value
Interest-bearing liabilities	(176.247.445)	(176.247.445)	(92.640.629)	(92.640.629)
Embedded derivatives in electicity sales contracts	24.909.295	24.909.295	8.154.304	8.154.304
Currency swaps	12.037	12.037	(155.442)	(155.442)
Forwards swaps	(516.470)	(516.470)	152.995	152.995

The fair value has not been determined for interest-bearing liabilities.

Interest rates used for determining fair value

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

	30.9.2008	31.12.2007
Embedded derivatives in electicity sales contracts	3.45%-6.87%	3.81%-5.03%

Amounts are in ISK thousand

15. **Group entities**

Shares in subisidiaries included in the consolidated financial statements are specified as follows:

			Share	
	Main operation	Nominal value	30.9.2008	31.12.2007
Gagnaveita Reykjavíkur ehf.	Data transfer	3.536.841	100,0%	100,0%
Hitaveita Akraness og Borgarfj	Heating supplyer		79,3%	79,3%
Hrafnabjargavirkjun	Preparation company	6.000	60,0%	60,0%
NCI fjarskipti og orka ehf.	No operation	3.000	100,0%	100,0%
Reykjavík Energy Invest ehf.	Investment company	3.004.723	100,0%	100,0%
Úlfljótsvatn frítímabyggð ehf.	Preparation company	225.000	100,0%	100,0%
REYST hf.	Energy school	10.500	99,9%	

Main changes in the Group during the year

In february 2008 Orkuveita Reykjavíkur, University of Iceland and Reykjavik University founded REYST hf. The purpose is to bring to the society an excellent expertise in the field of sustainable energy through education and research worldwide.

16. **Subsequent events**

Considerable changes have occurred in the Icelandic economy after the collapse of the Icelandic banks in the beginning of October. These changes have led to difficulties in funding for Icelandic companies. In spite of this situation the Company´s liquidity position is strong.

17. **Other issues**

Orkuveita Reykjavíkur purchased in the year 2007 a 16.58% share in Hitaveita Suðurnesja hf. According to an agreement between Orkuveita Reykjavíkur and Hafnarfjarðarbær, the Company entered into an obligation to purchase in addition all of the shares of Hafnarfjarðarbær in Hitaveita Suðurnesja amounting to the total of ISK 1,133,356,000 nominal value at the rate 7. The town council of Hafnarfjörður agreed on a meeting on 18 December 2007 to sell 95% of the municipality's share in Hitaveita Suðurnesja to Orkuveita Reykjavíkur. In a decision by the Competitive Authority No. 23/2008 it said that according to Article of the Competition Act No. 44/2005, the Competitive Authority instructs OR that the Company is not allowed to own more than 10% of Hitaveita Suðurnesja hf. The Board of Directors of Orkuveita Reykjavíkur intends to appeal this decision by the Competitive Authority.

With reference to the decision of Competitive Authority, the Board of Directors of Orkuveita Reykjavíkur is of the opinion that Orkuveita Reykjavíkur can not fulfill its obligation under the contract with Hitaveita Suðurnesja hf. to buy 95% of the municipality's shares in Hitaveita Suðurnesja hf. Hafnarfjörður has subpoenaed Orkuveita Reykjavíkur for the amount payable under the contract and the case was registered with the District Court of Reykjavík on 28 April 2008.

Amounts are in ISK thousand